Citation: R. v. Felderhof ONCJ 345
Old City Hall, 60 Queen St. W.,
Toronto, Ontario
DATE: 2007·07·31

ONTARIO COURT OF JUSTICE

07 214 008

B E T W E E N :

HER MAJESTY THE QUEEN

— AND —

JOHN BERNARD FELDERHOF

Before Justice Peter Hryn
Reasons for Judgment released on July 31, 2007

Offences:
Securities Act, RSO 1990, c.S.5, as am., ss 76(1)and 122(1)(c) (4 Counts)
Securities Act, RSO 1990, c.S.5, as am., ss 122(3) (4 Counts)

Emily C. Cole (March 2004-July 2007), Frank N. Marrocco Q.C. (March 2004-November 2005), Jay Naster (December 1999-April 2001), Ian Smith (December 1999-April 2001).....for the Crown

Joseph P.P. Groia, Jennifer K. Badley, Kevin Richard, Nicholas A. Richter, Janice Wright (until 2001), Donald Park (until 2001)..... for the defendant John Bernard Felderhof

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INTRODUCTION

Charges: Information and Particulars

John Bernard Felderhof is charged with eight counts of violating the *Securities Act*, R.S.O. 1990 c.S.5. The Ontario Securities Commission (O.S.C.) charged the Defendant with four counts of insider trading and four counts of authorizing misleading press releases.

Information

The Information states:

JOHN BERNARD FELDERHOF:

1. On or between the 24th day of April, 1996 and the 16th day of May, 1996, at the City of Toronto and elsewhere, being a person in a special relationship with Bre-X Minerals Ltd. ("Bre-X"), a reporting issuer in the Province of Ontario listed and posted for trading on the Toronto Stock Exchange, did sell securities of Bre-X, to wit: 100,000 shares (pre-split) for $21,053,951 more or less, with knowledge of a material fact with respect to Bre-X that had not been generally disclosed contrary to ss. 76(1) and 122(1)(c) of the *Securities Act*, R.S.O. 1990, c.S.5, as am. .

2. On or between the 24th day of June, 1996 and the 26th day of July, 1996, at the City of Toronto and elsewhere, being a person in a special relationship with Bre-X Minerals Ltd. ("Bre-X"), a reporting issuer in the Province of Ontario listed and posted for trading on the Toronto Stock Exchange, did sell securities of Bre-X, to wit: 991,800 shares for $22,649,558 more or less, with knowledge of a material fact with respect to Bre-X that had not been generally disclosed contrary to ss. 76(1) and 122(1)(c) of the *Securities Act*, R.S.O. 1990, c.S.5, as am. .

3. On or between the 1st day of August, 1996 and the 16th day of August, 1996, at the City of Toronto and elsewhere, being a person in a special relationship with Bre-X Minerals Ltd. ("Bre-X"), a reporting issuer in the Province of Ontario listed and posted for trading on the Toronto Stock Exchange, did sell securities of Bre-X, to wit: 714, 900 shares for $17,376, 205 more or less, with knowledge of a

material fact with respect to Bre-X that had not been generally disclosed contrary to ss. 76(1) and 122(1)(c) of the *Securities Act*, R.S.O. 1990, c.S. 5, as am. .

4. On or between the 26th day of August, 1996 and the 10th day of September, 1996, at the City of Toronto and elsewhere, being a person in a special relationship with Bre-X Minerals Ltd. ("Bre-X"), a reporting issuer in the Province of Ontario listed and posted for trading on the Toronto Stock Exchange, did sell securities of Bre-X, to wit: 913,800 shares for $22,875,955 more or less, with knowledge of a material fact with respect to Bre-X that had not been generally disclosed contrary to ss. 76(1) and 122(1)(c) of the *Securities Act*, R.S.O. 1990, c.S. 5, as am. .

5. On or about June 20, 1996, at the City of Toronto and elsewhere, being an officer and director of Bre-X Minerals Ltd. ("Bre-X"), did authorize, permit or acquiesce in Bre-X making a statement, in a press release dated June 20, 1996 to wit: announcing measured, indicated and inferred resources for the Central and Southeast Zones of the Busang properties in the Province of East Kalimantan, Republic of Indonesia, totalling 39.15 million ounces of gold, which press release was required to be filed or furnished under Ontario securities law, that in a material respect and at the time and in the light of the circumstances under which it was made, was misleading or untrue or did not state a fact that was required to be stated or that was necessary to make the statement not misleading contrary to s.122(3) of the *Securities Act,* R.S.O., 1990, c.S.5, as am..

6. On or about July 22, 1996, at the City of Toronto and elsewhere, being an officer and director of Bre-X Minerals Ltd. ("Bre-X"), did authorize, permit or acquiesce in Bre-X making a statement, in a press release dated July 22, 1996 to wit: announcing measured indicated and inferred resources for the Central and Southeast Zones of the Busang properties in the Province of East Kalimantan, Republic of Indonesia, totalling 46.92 million ounces of gold, which press release was required to be filed or furnished under Ontario securities law, that in a material respect and at the time and in the light of the circumstances under which it was made, was misleading or untrue or did not state a fact that was required to be stated or that was necessary to make the statement not misleading, contrary to s.122(3) of the *Securities Act*, R.S.O., 1990, c.S.5, as am..

7. On or about December 3, 1996, at the City of Toronto and elsewhere, being an officer and director of Bre-X Minerals Ltd. ("Bre-X"), did authorize, permit or acquiesce in Bre-X making a statement, in a press release dated December 3, 1996 to wit: announcing measured indicated and inferred resources for the Central and Southeast Zones of the Busang properties in the Province of East Kalimantan, Republic of Indonesia, totalling 57.33 million ounces of gold, which press release was required to be filed or furnished under Ontario securities law, that in a material respect and at the time and in the light of the circumstances under which

it was made, was misleading or untrue or did not state a fact that was required to be stated or that was necessary to make the statement not misleading, contrary to s.122(3) of the *Securities Act*, R.S.O., 1990, c.S.5, as am..

8. On or about February 17, 1997, at the City of Toronto and elsewhere, being an officer and director of Bre-X Minerals Ltd. ("Bre-X"), did authorize, permit or acquiesce in Bre-X making a statement, in a press release dated February 17, 1997 to wit: announcing measured indicated and inferred resources for the Central and Southeast Zones of the Busang properties in the Province of East Kalimantan, Republic of Indonesia, totalling 70.95 million ounces of gold, which press release was required to be filed or furnished under Ontario securities law, that in a material respect and at the time and in the light of the circumstances under which it was made, was misleading or untrue or did not state a fact that was required to be stated or that was necessary to make the statement not misleading, contrary to s.122(3) of the *Securities Act*, R.S.O., 1990, c.S.5, as am..

Particulars

The Particulars to the Information are as follows:

Particulars to the Information of Michael Hubley

1. The "*material fact*" referred to in count 1 of the information is:

a) that due to a failure to comply with contractual obligations owed to the Indonesian government and the shareholders of PT Westralian Atan Minerals ("PT WAM"), Bre-X had not secured its interest in the property known as Busang I; and/or

b) that Bre-X had misled the Indonesian government respecting the acquisition of an 80% interest in PT WAM; and/or

c) that Bre-X had unjustly excluded PT Krueng Gasui ("PT KG"), and/or PT Sungai Atan Perdana ("PT SAP"), and/or Jusuf Merukh, from obtaining an interest in the property known as Busang II.

2. The "*material fact*" referred to in count 2 of the information is:

a) that due to a failure to comply with contractual obligations owed to the Indonesian government and the shareholders of PT WAM, Bre-X had not secured its interest in the property known as Busang I; and/or

b) that Bre-X had misled the Indonesian government respecting the acquisition of an 80% interest in PT WAM; and/or

c) that Bre-X had unjustly excluded PT KG, and/or PT SAP, and/or Jusuf Merukh, from obtaining an interest in the property known as Busang II; and/or

d) that PT KG, and/or PT SAP, and/or Jusuf Merukh, had issued a complaint to the Indonesian government and Bre-X respecting their exclusion from obtaining an interest in the exploration of the property known as Busang II.

3. The "*material fact*" referred to in count 3 of the information is:

a) that Bre-X had misled the Indonesian government respecting the acquisition of an 80% interest in PT WAM; and/or

b) that Bre-X had unjustly excluded PT KG, and/or PT SAP, and/or Jusuf Merukh, from obtaining an interest in the property known as Busang II; and/or

c) that PT KG, and/or PT SAP, and/or Jusuf Merukh, had issued a complaint to the Indonesian government and Bre-X respecting their exclusion from obtaining an interest in the property known as Busang II.

4. The "*material fact*" referred to in count 4 of the information is:

a) that Bre-X had misled the Indonesian government respecting the acquisition of an 80% interest in PT WAM; and/or

b) that Bre-X had unjustly excluded PT KG, and/or PT SAP, and/or Jusuf Merukh, from obtaining an interest in the property known as Busang II; and/or

c) that PT KG, and/or PT SAP, and/or Jusuf Merukh, had issued a complaint to the Indonesian government and Bre-X respecting their exclusion from obtaining an interest in the exploration of the property known as Busang II; and/or

d) that the Indonesian government had cancelled the preliminary survey permit respecting the property known as Busang II.

Securities Act

The relevant sections of the *Securities Act* are found in the parts of these reasons where they are discussed. With respect to Counts 1 to 4, s.76(1), 122(1)(c) and the definition of

"*material fact*" are found at page 391 of these reasons. With respect to Counts 5 to 8, s.122(1)(b), (2) and (3) are found at page 17 of these reasons.

Brief Outline of Facts

David Walsh incorporated Bre-X in Alberta in 1989. Bre-X was a penny stock listed on the Alberta Stock Exchange. Walsh was the President, Chairman and Chief Executive Officer of Bre-X.

In late March 1993 Walsh contacted John Felderhof asking about copper deposits available for acquisition by Bre-X. Felderhof suggested a number of properties including Busang I, a gold deposit, (also referred to as the Central Zone or Block V) with which Felderhof had had some involvement and experience.

Walsh agreed and various attempts were made to obtain an interest in Busang I commencing in July of 1993.

Whether Bre-X secured its interest in Busang I (Particular 1) and whether Bre-X misled the Indonesian government about its interest in Busang I (Particular 2) are a part of the material facts alleged in the insider trading counts (1 to 4).

On May 1, 1993 Bre-X hired John Felderhof as its General Manager in charge of Bre-X's Indonesian exploration. On October 5, 1994 Felderhof was appointed Bre-X Vice-President of Exploration. On May 10, 1996 Felderhof joined the Bre-X Board of Directors as Vice-Chair.

In August and September 1993 Bre-X conducted further exploration which led to the discovery of a new prospect area in Busang II (also referred to as the South East Zone). On September 14, 1994 Bre-X applied for a new Contract of Work (COW) from the Indonesian government for Busang II separate from the existing COW over Busang I. Eventually it turned out that Busang I contained only a small proportion of Bre-X's resource calculations for Busang I and II. Busang I contained less than 3 million ounces of gold out of a total of 70.95 million ounces as of the date of the final February 7, 1997 resource calculation press release.

Whether Bre-X unjustly excluded an existing partner in the Busang I COW (Jusuf Merukh) from obtaining an interest in Busang II (Particular 3) and Merukh's complaint to the Indonesian government that he had been excluded (Particular 4) are a part of the material facts alleged in the insider trading counts.

Bre-X never obtained final approval for the COW over Busang II. As part of the process of applying for a COW, Bre-X was allowed to apply for a preliminary survey permit (SIPP) and on June 6, 1995 Bre-X applied for a SIPP over Busang II. On July 20, 1995 a SIPP was granted for one year and on July 20, 1996 extended for a further year to end on July 19, 1997.

On August 15, 1996 the Indonesian government cancelled the SIPP.

The cancellation of the SIPP for Busang II (Particular 5) is the final part of the material facts alleged in the insider trading counts.

In May 1995 Bre-X started drilling in Busang II. The results were positive.

On April 23, 1996 Bre-X was listed on the Toronto Stock Exchange (T.S.E.). By then Bre-X was no longer a penny stock. The opening price of Bre-X shares on the T.S.E. was $187.50.

Because of jurisdictional reasons the charge periods commence after Bre-X was listed on the T.S.E.. The insider trading counts commence on April 24, 1996 and end on September 10, 1996, the date of Felderhof's last trade.

The press release counts begin on June 20, 1996, the date of the first resource calculation press release after Bre-X's T.S.E. listing and end on February 17, 1997, the date of the last resource calculation press release before the salting was discovered.

The resource estimates continued to grow after Bre-X's T.S.E. listing.

The four press releases which are the subject matter of Counts 5 to 8 continued to put out ever increasing resource estimates as follows:

- June 20 1996: 39.15 million ounces of gold
- July 22, 1996: 46.92 million ounces of gold
- December 3, 1996: 57.33 million ounces of gold
- February 17, 1997: 70.95 million ounces of gold

At least one analyst was of the view that Busang would become one of the largest if not the largest gold deposit in the world.

In August 1996 Bre-X was also listed on the Montreal Stock Exchange and on NASDAQ. On December 16, 1996 Bre-X was added to the T.S.E. 100 Index and the T.S.E. 300 Composite Index.

Bre-X became the "*darling*" of the capital markets. The share price rose above $270.00 or $27.00 after the 10 to 1 stock split.

In addition to ordinary investors buying Bre-X stock, large mining companies wanted to enter into joint venture agreements or other arrangements with Bre-X to develop Busang. These included Barrick Gold, Placer Dome, Tech Corp., Newmont Mining and Freeport-McMoRan. As the amount of gold in Busang grew the Indonesian government became involved in determining who would have a share of Busang and the size of that share.

Barrick spent years and many millions of dollars and used its very substantial connections, a former American President, a former Canadian Prime Minister, a businessman married to a member of the royal family of Jordan and others to influence events and the Indonesian government to get a share of Busang.

This was at a time when newspapers were reporting that the Suharto government in Indonesia was "*one of the world's most famously corrupt governments*" and reporting that Barrick had formed an association with one of Suharto's daughters and Bre-X with one of Suharto's sons.

In the end on February 17, 1997 Bre-X entered into a joint venture agreement, not with Barrick, but with Freeport in an arrangement that was more profitable for Indonesian interests who received 40% of Busang.

As part of its due diligence program Freeport drilled several twin holes at Busang II. On March 10, 1997 Freeport began receiving negative assay results that showed almost no gold.

On March 19, 1997 the T.S.E. halted trading in Bre-X stock after news that de Guzman (the exploration manager for Bre-X) had fallen to his death from a helicopter as he was returning to Busang to investigate why Freeport was getting negative results.

Bre-X agreed to conduct a confirmation drilling program as suggested by Freeport. Strathcona Mineral Services was retained. Strathcona's drilling results were negative.

Bre-X issued a press release on May 4, 1997 confirming Strathcona's negative results. The price of Bre-X fell to 90 cents. Market capitalization of $6.1 billion at Bre-X's height was gone. A gold deposit that a Toronto newspaper had at one point reported may be worth as much as $44 billion was now worthless.

Exhibit S5 Volume I: paragraphs 1-123
R. v. Felderhof, July 31, 2007, Reasons for Judgement

Submission Exhibits And The Exhibit Chart

Submission Exhibits

Following roughly 160 days of trial commencing December 1999, and the marking of 1687 exhibits, the O.S.C. and Defence filed substantial written submissions with respect to the Charter application and separate submissions with respect to the merits. The Defence also filed separate replies.

Following the two weeks of oral closing submissions, at my request the O.S.C. and Defence filed supplementary written submissions commenting on each others original written submissions except as follows: the O.S.C. did not comment on the Defence Charter submissions nor the Defence replies nor the Defence separate submissions with respect to the law for Counts 1 to 4 and 5 to 8. The Defence did not comment on the O.S.C. Charter submissions except with respect to those paragraphs which the O.S.C. repeated in the O.S.C. merit submissions.

Where in these reasons I state that the Defence or O.S.C. agrees with paragraphs of opposing counsels submissions, I base that on the admissions in the supplementary written submissions.

The various written submissions have been entered as exhibits, not as part of the trial exhibits but as part of or in addition to the oral submissions for convenience of reference in this judgement.

These written submissions have been marked as Exhibits S1 through to S15.

These exhibits are:

S1: Written Defence Argument on Charter Application
S2: Written Defence Reply Charter Application
S3: Written Closing Argument of the Defence
S4: Written Reply of the Defence
S5: Defence Comments on the Submissions of the Ontario Securities Commission Volumes I and II
S6: Defence Comments on the "Respondent's Factum (Charter Application)"
S7: Letter to Justice Hryn, dated December 21, 2006, from Joseph Groia
S8: Respondent's Factum (Charter Application)
S9: Submissions of the Ontario Securities Commission Volume I
S10: Submissions of the Ontario Securities Commission Volume II
S11: Appendices to the Submissions of the Ontario Securities Commission Volumes I and II
S12: Ontario Securities Commission Admissions and Denials to the Written Closing Argument of the Defence Facts Relating to Counts 1 and 4
S13: Ontario Securities Commission Admissions and Denials to the Written Closing Argument of the Defence Facts Relating to Counts 5 and 8
S14: Letter to Justice Hryn, dated October 25, 2006, from Emily Cole
S15: Letter to Justice Hryn, dated October 27, 2006, from Emily Cole (without attachments)

In Exhibit S5 and S6 the Defence comments with respect to the O.S.C. submissions appear in bold following each O.S.C. paragraph.

In Exhibit S12 and S13 the O.S.C. comments with respect to the Defence submissions are contained in boxed areas following each Defence paragraph.

Footnotes are generally omitted when any of the written submissions are incorporated into these reasons.

Exhibit Chart And Use That May Be Made Of Exhibits

After 70 days of trial, the O.S.C. applied for prohibition and certiorari. After the application and appeals were dismissed the matter returned before me for completion. Before the date set for recommencing the hearing of evidence the parties concluded a case management process before Madame Justice Lane.

One of the results of that process was the creation of an Exhibit Chart. That Exhibit Chart listed every exhibit entered in the trial up to that point in time, Exhibits 1-552, along with six columns denoting the different categories of documents entered and a column denoting which documents were or were not in dispute. For most exhibits, the Exhibit Chart discloses the agreement of the parties as to the use that may be made of each exhibit. That is the use I have made of them in this judgement.

Some of the documents in dispute in the Exhibit Chart and other documents tendered after the trial recommenced that were also in dispute were part of the O.S.C. Business Records Application. My ruling with respect to that application is R. v. Felderhof [2005] O.J. No. 4151 (QL).

After the trial recommenced all exhibits, except those included in the Business Records Application, were entered on consent with an agreement that except where otherwise stated they could be used for any purpose including the truth of their contents. The O.S.C. and Defence comments on this matter are noted below:

MR. MARROCCO: No. The agreement Mr. Groia and I had was if a document was admitted on consent it could be used for any purpose. We had this discussion a long time ago. So if it goes in on consent, it can be used for proof of the facts, contained in it.

...

MR. MARROCCO: And as we went through the different witnesses, you know, you'll recall, we tendered documents on consent at the end and that's because we're operating on that principle, so –with Normet and all that, we were consenting – we were just putting those documents in on consent, without trying to decide, without trying to categorize them as a business record, or whatever, we went and put it in on consent. You can make whatever use of it. It's capable of proving the facts contained in it, but it's in on consent. No one's agreed to the categorization of it. That's how we avoided having the debate, the business records debate, before now.

...

MR. GROIA: I would say that the chart has everything up to the point in time we're now discussing, and the chart has the admissions, and then as we've gone along in the post-adjournment era, then my friend's right, most documents have gone in on consent.

Transcript: August 16, 2005, pages 37-38

For convenience the Exhibit Chart is marked Exhibit S16.

Reference Materials

Located within various exhibits are useful reference materials:

Exhibit 208: page 4 –Location Map Busang

Exhibit 208: page 15 –Regional Tectonics and Gold Deposits Map

Exhibit 681: Pocket –Busang General Location Map

Exhibit 681: pages 5-11 –Glossary of Geological Terms

Exhibit 1202: pages 319-338; Exhibit 1328A: pages 89-100; Exhibit S3: Appendix A

-Glossary of Geological and Metallurgical Terms

Exhibit S11: Tab 1 –List of Individuals

Exhibit 828 (also found at Exhibit S11: Tab 2) –Ownership Chart of PT WAM

Exhibit 1001: pages 1-20 –Indonesian Mining Law

Exhibit 858: pages 1-6 –Mining Titles In Indonesia. (see Disclaimer on page 6 of Exhibit 858 and see page 454 of these reasons)

Outline Of These Reasons

In these reasons I deal first with the Notice of Application and Constitutional Question and then with the merits. The Application is only relevant to Counts 5 to 8. Following my reasons with respect to the Application, I give my reasons with respect to Counts 5 to 8 and then my reasons with respect to Counts 1 to 4.

Notice of Application And Constitutional Question (Charter Application)

In the Notice of Application and Constitutional Question the Defence submits that if I do not find that s.122(3) of the Securities Act requires the O.S.C. to prove mens rea; that is, if I find that s.122(3) is a strict liability offence, then the Defence argues that s.122(3) violates s.7 and 11(d) of the Charter and asks that I declare s.122(3) to be of no force and effect.

I disagree with the Defence and I find that s.122(3) is a strict liability offence and I find that it is not inconsistent with the provisions of the Constitution.

The Application is dismissed.

Counts 5 to 8

I find that the O.S.C. has proven the actus reus of these offences beyond a reasonable doubt.

I find, as was conceded, that Bre-X issued the press releases set out in Counts 5 to 8.

I find, as was conceded, that these press releases were required to be filed by Bre-X under Ontario Securities law.

I disagree with the Defence and I find that these press releases contained statements announcing resource calculations that, in a material respect and at the time and in the light of the circumstances under which they were made, were misleading or untrue.

I find, as was conceded, that Felderhof was a director and officer of Bre-X.

I disagree with the Defence and I find that Felderhof did authorize, permit or acquiesce in the issuance of these press releases.

The defence of due diligence is available to Felderhof. Where everyone else saw gold only Strathcona with hindsight saw red flags. I disagree with the O.S.C. and I find that I am satisfied on a balance of probabilities that Felderhof has proven that he took all reasonable care. In the circumstances of this case that means that I prefer the Defence evidence over the O.S.C. evidence with respect to the Red Flags alleged by the O.S.C. .

Felderhof is found not guilty of counts 5 to 8.

Counts 1 to 4

I find that the O.S.C. has not proven the actus reus of these offences beyond a reasonable doubt.

I find, as was conceded, that Felderhof was in a special relationship with Bre-X a reporting issuer listed and posted for trading on the T.S.E. .

I disagree with the Defence and I find that Felderhof sold Bre-X shares as alleged.

I disagree with the O.S.C. and I find that the O.S.C. has not proven beyond a reasonable doubt that the alleged material facts were in fact material.

Felderhof is found not guilty of counts 1 to 4.

The Defendant is found not guilty of all counts.

NOTICE OF APPLICATION AND CONSTITUTIONAL QUESTION (CHARTER APPLICATION)

Application

The Applicant, John Bernard Felderhof (referred to as the Defendant) served the Ontario Securities Commission (O.S.C.) and the Ministry of the Attorney General (Ontario) and the Ministry of the Attorney General (Canada) with a Notice of Application and Constitutional Question dated September 29, 2000. The Ministries of the Attorney General for Ontario and Canada were re-served in 2006. There was no indication they intended to appear and they have not appeared nor taken a position.

The Notice states in the introductory paragraph:

> TAKE NOTICE that the applicant, John Bernard Felderhof, will bring an application before the Honorable Mr. Justice Peter Hryn of the Ontario Court of Justice at 10:00 a.m. on the 16th day of October, 2000, or so soon thereafter as the application can be heard, at Courtroom 126, Old City Hall, 60 Queen Street West, Toronto, for an order pursuant to section 24(1) of the *Canadian Charter of Rights and Freedoms* (the "*Charter*") declaring that section 122(3) of the Ontario *Securities Act* (The "*Securities Act*") is inconsistent with the *Charter* and is therefore of no force or effect.

The Defence position has since evolved adding an alternative found at paragraphs 6 and 24 of the Written Defence Argument On Charter Application, Exhibit S1:

> Para. 6. The defence therefore renews the *Charter* Application and once again asks for an order that section 122(3) of the *Securities Act* (as it then was) be declared to be of no force or effect and that Counts 5 to 8 of the Information of Michael Hubley sworn on May 11, 1999 be dismissed. In the alternative, the defence asks that this Court rule that in order for section 122(3) of the *Securities Act* not to be inconsistent with the *Charter*, the OSC must prove that Mr. Felderhof knew that the impugned Bre-X Minerals Ltd. ("Bre-X") press releases were false or misleading or that he was reckless in not knowing that they were false or misleading before he could possibly be convicted under section 122(3) of the *Securities Act*.
>
> ...
>
> Para. 24. The issue for determination on the *Charter* Application can now be put quite simply: if the OSC is correct, and all that the OSC needs to show for a conviction is that Mr. Felderhof knew that Bre-X was putting out press releases, which are then subsequently found to be false or misleading, then it is submitted that section 122(3) is contrary to the *Charter* and cannot stand. If, on the other hand, this Court determines that Mr. Felderhof must have had knowledge that the Press Releases were false, misleading or materially incomplete before he can be convicted, then section 122(3) does withstand *Charter* scrutiny and ought not to be declared to be of no force or effect.

Securities Act And Charter

The relevant sections of the Ontario *Securities Act*, R.S.O. 1990, c. S.5, are sections 122(1)(b), 122(2), and 122(3):

122. (1) **Offences, general.** -Every person or company that,

(b) makes a statement in any application, release, report, preliminary prospectus, prospectus, return, financial statement, information circular, take-over bid circular, issuer bid circular or other document required to be filed or furnished under Ontario securities law that, in a material respect and at the time and in the light of the circumstances under which it is made, is misleading or untrue or does not state a fact that is required to be stated or that is necessary to make the statement not misleading; ...

is guilty of an offence and on conviction is liable to a fine of not more than $1,000,000 or to imprisonment for a term of not more than two years, or to both.

(2) **Defence.**- Without limiting the availability of other defences, no person or company is guilty of an offence under clause (1) (a) or (b) if the person or company did not know and in the exercise of reasonable diligence could not have known that the statement was misleading or untrue or that it omitted to state a fact that was required to be stated or that was necessary to make the statement not misleading in light of the circumstances in which it was made.

(3) **Directors and officers.**- Every director or officer of a company or of a person other than an individual who authorizes, permits or acquiesces in the commission of an offence under subsection (1) by the company or person, whether or not a charge has been laid or a finding of guilt has been made against the company or person in respect of the offence under subsection (1), is guilty of an offence and is liable on conviction to a fine of not more than $1,000,000 or to imprisonment for a term of not more than two years, or to both.

The relevant sections of the *Canadian Charter of Rights and Freedom*, Part I of the Constitution Act, 1982, being Schedule B to the *Canada Act 1982* (U.K.), 1982, c.11, are sections 1, 7, 11(d) and 52(1).

s. 1. The *Canadian Charter of Rights and Freedoms* guarantees the rights and freedoms set out in it subject only to such reasonable limits prescribed by law as can be demonstrably justified in a free and democratic society.

s.7. Everyone has the right to life, liberty and security of the person and the right not to be deprived thereof except in accordance with the principles of fundamental justice.

s. 11. Any person charged with an offence has the right

d) to be presumed innocent until proven guilty according to law in a fair and public hearing by an independent and impartial tribunal;

s. 52(1). The Constitution of Canada is the supreme law of Canada, and any law that is inconsistent with the provisions of the Constitution is, to the extent of the inconsistency, of no force or effect.

Defence Position

In Exhibit S1 the Defence sets out the following under the heading "*Overview*":

Para. 8. To properly develop the *Charter* argument, it is necessary to first discuss the precise nature of Counts 5 to 8 and the OSC's position concerning those Counts. The starting point is to first consider the primary and underlying offence alleged to have been committed by Bre-X. The OSC alleges that Mr. Felderhof authorized, permitted or acquiesced in the commission of that offence...

...

Then under the subheading "*(i) The Primary Bre-X Offences*":

Para. 9. The provisions of section 122(3) of the *Securities Act* impose a burden upon the OSC to prove the culpability for the primary offence against Bre-X before the derivative charges against Mr. Felderhof of 'authorize, permit or acquiesce' can be considered.

...

Para. 10. The defence concedes that the primary or underlying offence alleged against Bre-X under section 122(1)(b) is a strict liability offence...

...

Para. 16. If the Court believes that the OSC has satisfied the burden of proving Bre-X's *actus reus* in this case, then Bre-X at common law and under the

Securities Act, has a due diligence defence to be proven on the balance of probabilities (which turns it from an absolute liability to a strict liability offence).

Then under the subheading "*(ii) The Derivative Offence Under Section 122(3)*":

Para. 17. Only if the Court is satisfied that the OSC has proven beyond a reasonable doubt the elements of the alleged Bre-X's offences under section 122(1)(b) and that Bre-X or anyone else has failed to make out Bre-X's defence of due diligence under section 122(2), does the need arise to consider Mr. Felderhof's derivative offences under section 122(3). To succeed against Mr. Felderhof, if they have successfully proven the commission of an offence by Bre-X, the OSC must now prove, beyond a reasonable doubt, that Mr. Felderhof "authorized, permitted or acquiesced" in the issuance of the Press Releases. Those words are intended to tie a defendant into the commission of a Bre-X offence and create a special 'party to an offence' regime under the *Securities Act*.

...

Para. 26. In considering the constitutionality of section 122(3), the defence asks that this Court give careful consideration to the import of the words "in the commission of an offence". Those words appear on their face, and the cases cited below have held, that they require an element of *mens rea*. In some other public welfare statutes, the statutory language chosen is such that an accused can be charged where he authorized, permitted or acquiesced in the act or omission that constitutes the offence thereby tying the knowledge of the accused more closely to the mere act of the corporation as opposed to the provisions of the *Securities Act* which ties the knowledge to the commission of an offence. Even, however, in those other cases, the Court has held *mens rea* to be a requirement of the offence.

***R.* v. *Peterson*, [2006] A.J. No. 286 (Alta. Prov. Ct.)**

Then under the heading "*Section 7 of the Charter*" para.105 to 110:

Para. 105. The cases make it clear that in order to not cause an infringement of section 7 of the *Charter*, there must be an element of moral blameworthiness or personal fault that attaches to a culpable aspect of the *actus reus*.

Para. 106. In *DeSousa*, the Court said at para. 21:

> *It is axiomatic that in criminal law there should be no responsibility with [sic, without] personal fault. A fault requirement was asserted to be a fundamental aspect of our common law by this Court in R. v. Sault Ste. Marie (City), (1978) 40 C.C.C. (2d) 353, 85 D.L.R. (3d) 161, [1978] 2 S.C.R. 1299, and as a matter of constitutional law under s. 7 of the Charter in Reference re: s. 94(2) of Motor Vehicle Act (1985), 23 C.C.C. (3d) 289, 24 D.L.R. (4th) 536, [1985] 2 S.C.R. 486. As a matter of statutory*

interpretation, a provision should not be interpreted to lack any element of personal fault unless the statutory language mandates such an interpretation in clear and unambiguous terms.

Para.107. Without some degree of guilty knowledge as part of either the *actus reus* or the *mens rea*, section 122(3) would be converted from "a strict liability offence into something more and just short of an absolute liability offence" since defendants would be held liable for the mere fact that they were directors of the issuing corporation during the material time.

Para. 108. It will likely be common ground that when a defendant, such as Bre-X, is charged with a strict liability offence arising under Section 122(1)(b) of the *Securities Act*, the OSC has the burden of proving beyond a reasonable doubt the *actus reus* of the offence. The onus then shifts to the defendant to prove on a balance of probabilities the defence of due diligence or reasonable mistake of fact.

Para. 109. To prove that Mr. Felderhof is liable under section 122(3) it is not necessary for the OSC to charge or convict Bre-X of the underlying offence. The OSC must prove, however, that Bre-X was culpable of the underlying offence essentially proving that had Bre-X been charged under section 122(3), it would have been convicted. This arises from the clear wording of section 122(3) of the *Securities Act.*

Para. 110. In order not to infringe section 7 of the *Charter*, the OSC must prove that Mr. Felderhof had the requisite knowledge of the primary Bre-X offence to support a conviction on the derivative section 122(3) offence. The OSC must go beyond the mere fact that he was a director of Bre-X who knew that press releases were being disseminated since that alone could not make him liable and still survive *Charter* scrutiny. The OSC must also provide evidence of actions or inactions of Mr. Felderhof during the material time that show he either knew, or was reckless in not knowing that Bre-X's press releases were false or misleading.

In oral submissions the Defence expands upon the written submissions, in part, as follows starting at page 7 of the August 21, 2006 transcript:

MR. GROIA: The argument, reduced to its core, is that to convict Mr. Felderhof, and to potentially to incarcerate him as a result of that conviction, for someone else's negligence – in this case, the negligence of Bre-X Minerals - violates the Charter; and that more directly, to convict Mr. Felderhof for his negligence, or alleged negligence, in ensuring that Bre-X properly discharged its duty, is a violation of s.7 and a violation of the Supreme Court's reasoning in De Sousa.

As a result, the way we intend to approach the argument is to try and demonstrate that what s.122(3) requires is essentially what the parties to the offence provisions of the Criminal Code require, or the POA, and that is the Commission would have to show that Mr. Felderhof knew that these press releases were false or misleading at the time that Bre-X issued them in order for there to be a conviction of a provision that does not violate s.7.

...

If you're persuaded by the Commission, as they argued in 2000, that Mr. Felderhof could be convicted simply because he knew that Bre-X was going to issue press releases, but had no knowledge that those press releases were false or misleading, then we say that that violates s.7 and s.122(3) ought to be declared to be of no force and effect. But I'm going to make the primary argument that s.122(3) actually imports a mens rea requirement first.

...

Yes. Firstly, Your Honour, it's my submission that a useful way of looking at these charges is to distinguish between the Bre-X offence and the allegations against Mr. Felderhof. And you'll see that in our factum we refer to them as "primary" and "derivative" charges.

The press releases that were issued – I believe there's no debate – were as a result of the conduct of Bre-X and a number of its senior officers and directors. And the requirement to issue a press release under the Securities Act is a requirement that existed only with Bre-X. These are not Mr. Felderhof's documents. And the Statute which makes it an offence to issue a false press release is s.122(1). On its face, s.122(1) can only apply to Bre-X in the circumstances of this case.

The charge that we're considering this morning is a derivative charge, it's a charge that makes Mr. Felderhof liable for the actions of another, in this case the company, and that's s.122(3).

...

And so what this section, I believe, says is that the first inquiry that one begins to have to undertake to understand this section, is whether there has been by, in this case Bre-X, the commission of an offence under ss. (1). In other words, you can't be guilty of "authorizing, permitting or acquiescing" of something that is not an offence.

Now, I agreed with the Commission that you don't have to find Bre-X guilty; indeed, I daresay you couldn't find them guilty because they were never charged. But it's my submission that you have to find that Bre-X committed an offence

under ss. 122(1) before there's any need to go on and look at the activities of Mr. Felderhof.

...

Secondly, Ms. Cole and I are in agreement that in examining whether or not there was the commission of an offence by Bre-X, that's a strict liability offence.

...

We then turn to what the Statute requires in order to convict Mr. Felderhof for the derivative offence. This is really the heart and soul of the Charter application. We say that the Statue requires that the Commission show that Mr. Felderhof firstly "authorized, permitted, and acquiesced", which are all part of the actus reus. But the critical issue becomes he "authorized, permitted, and acquiesced" in what? That's where Ms. Cole and part company.

The Commission's position is that if they can show that Mr. Felderhof "authorized, permitted, or acquiesced" in the issuance of a press release by Bre-X, then he can be convicted and incarcerated. And we say that's not sufficient.

...

To be fair to the Commission, they would say he would have a due diligence defence on that issue; in other words, that this is also a strict liability offence. And we say that that's not sufficient, but what is sufficient is that they must show Mr. Felderhof knew the facts which gave rise to the commission of the offence. In other words, he has to know that the facts –the press releases, rather, were false or misleading.

...

The Fell decision is at Tab 32. The quote of G. Arthur Martin is to be found at page six. Fell was a case under the Competition –what was then the Combines Investigation Act, and a prosecution where the Court of Appeal clearly said the primary offence against the company, in this case the company was Kenitex Canada, was a strict liability offence.

They then turn to the derivative prosecution against Mr. Fell, who was a director and officer of Kenitex.

...

And after some discussion, you'll see that at the bottom of page four, the Court considered that the only basis upon which the Crown was alleging that Mr. Fell could be convicted was under the party to the offence provision of s.21 of the 1970 Criminal Code. And there's a long discussion on pages four, five about the

requirements for someone to be a party. And I say s.122(3) of the Securities Act is essentially a parties to the offence type provision.

...

So my argument today is that unless the Crown is able to show you, unless the Commission is able to show you that Mr. Felderhof knew the true facts, in other words, knew that the press releases were false or misleading, that the results had been somehow tampered with, then I say, under s.122(3), he ought to be acquitted.

Transcript: August 21, 2006, pages 7-14

In the oral reply the Defence readdresses some of these issues. Starting at page 40 of the

August 22, 2006 transcript with a response to an inquiry from me:

THE COURT: ....you are not saying that the requirement under s.122(3) is for the Crown to simply prove that it was negligence, you are saying that the Crown should be required to prove that Mr. Felderhof knew that the press release was misleading. In fact, you are suggesting a full mens rea.

MR. GROIA: Yes.

...

So in order for me to succeed on the first part of the offence, the question of whether Bre-X committed an offence, I have to meet the Sault Ste. Marie burden. So Ms. Cole, on behalf of the Commission, calls the evidence that would establish that the press releases were false or misleading, and I have to take what would otherwise have been Bre-X's obligation to show on the balance of probabilities that due diligence had been performed on the part of Bre-X. So that's stage one of the inquiry. In Wholesale Travel and the rationale in 205 is absolutely applicable to that part of the analysis.

Now, if at the end of that you were to conclude that had Bre-X been charged, you would make a finding that they've committed an offence, then you go to the second part of the inquiry.

...

Now, if we then come to the second inquiry, the Charter issue for your decision is whether I'm right that a director has to be shown to have known that the press release was false or misleading, or Ms. Cole's right, that if it can be shown that he

was negligent in not stopping the company from being negligent, then essentially the strict liability law would apply at stage one.

...

...I think where we get a bit confused is Ms. Cole's notion that she urges upon you that somehow this is a primary offence against Mr. Felderhof; in other words, she's trying to argue that Mr. Felderhof has a direct responsibility in law to ensure that Bre-X's press releases are not untrue or misleading. She says that as a director, he has a duty to ensure that the corporation did not put out misleading disclosure or inaccurate disclosure, I think is the way she noted it. And she would have the two stage inquiry be amalgamated in the one. And I say with respect to the argument, that's simply not the law.

...

It's not his statement and he's not required to file. The representation that's alleged to be false is the company's representation.

...

My next point is that you asked Ms. Cole about the requirement for authorizing, permitting or acquiescing. I think the issue really gets crystallized at that point. You can look at those words and say if Mr. Felderhof was negligent in not knowing that the press releases were misleading, and he can't make a due diligence defence, you're essentially saying 122(3) is a strict liability offence and therefore he can be convicted unless he meets the burden. I think that's a fair way of putting the Commission's argument. We're saying that's not high enough, because how can you unknowingly authorize, permit or acquiesce?

Those words, by their very nature, include a knowledge component and the Commission has agreed that they have a knowledge component, but they say the knowledge component is he had to know that Bre-X was putting out press releases, and he had to participate somehow, to some degree, in putting out the press releases. We're saying he had to know they were putting out false press releases, and in saying that, we rely on all the cases I told you about, but also we rely on the Wholesale Travel because if one can be convicted simply of knowing that the company was putting out a press release, and have no knowledge there's anything wrong with it, then we say it doesn't meet the minimum requirements of s.7 for all the reasons we've discussed.

I think the argument really does come down at the end to Ms. Cole and the Commission saying 122(3) is strict liability, it's a negligence standard and Mr. Felderhof has to show you that he didn't –he wasn't negligent. We're saying it's a

mens rea requirement and they have to show you that he knew or was willfully blind in not knowing that the press releases were false.

Transcript: August 22, 2006, pages 40, 42, 43, 44, 52, 53

The Defence makes these further submissions when addressing the merits of Counts 5 to 8 on August 28, 2006 starting at page 36:

> MR. GROIA: I am talking about the company, but it also applies to Mr. Felderhof who is one step removed. Otherwise what you are going to have is that companies are guarantors of the information in the press release. You do the best you can. You have an honest belief that what you are saying is true. But for some reason, unbeknownst to you, you are mistaken. Just like Kilborn was mistaken. Barrick was mistaken. The analysts were mistaken. All these people obviously believed in these results. I say press release charges against the company are only intended to apply where the company puts out a press release knowing the true state of affairs to be different. ...But where all the evidence in this case points towards this being a valid gold deposit and the company releases an estimate that subsequently with the benefit of hindsight, turns out to have been wrong, I say that unless you are satisfied that they knew that they were putting out a false release, or were willfully blind to something like the Harper situation, I say the law requires that you dismiss the charge.
>
> ...
>
> Well, it works this way in strict liability. Strict liability says the Crown has to prove the actus reas. What is the actus reas? The actus reas is putting out a press release that is false or misleading at the time and in the circumstances under which it was made. What do the words "at the time" and "in the circumstances under which it was made" do, it imports into the actus reas a requirement that the company know the press release is false or misleading?
>
> ...
>
> The real question is, what does the Crown have to prove? Clearly, I cannot argue on the basis of Sault St. Marie that this offence for Bre-X is anything other than strict liability. And therefore, I also cannot argue that there is a mens rea component. So I am not arguing that and I am trying to stay away from arguing that. But the actus reas requires you to find that the press release was false, untrue or misleading at the time and in the light of the circumstances under which it was

made. So what I am saying that does is it simply says as part of the actus reus you have got to find the company put out the press release and when they did so they had evidence, they had circumstances or facts which would have made it known to them that the press release was either untrue or was misleading. A press release disclosure count by its nature deals with knowledge.

Transcript: August 28, 2006, pages 36, 37, 38, 39

O.S.C. Position

Below I set out some of the O.S.C. submissions with respect to the constitutionality of s.122 (3) as found in the O.S.C. Respondent's Factum (Charter Application) Exhibit S8 starting at paragraph 174:

> Para. 174. At issue in this application is the level of *mens rea* that is constitutionally required under section 122(3) of the Act.
>
> Para. 175. The Crown takes the position that it is not required to prove subjective *mens rea* where an accused is charged with an offence under section 122(3) of the Act.
>
> Para. 176. The Supreme Court of Canada has held that where an offence is punishable by imprisonment, the minimum *mens rea* that will meet constitutional scrutiny is negligence in that a defence of due diligence is available. In other words, the Crown is not required to prove negligence as one of the elements of the offence, but the due diligence defence is available to the accused to prove an absence of negligence...
>
> Para. 177. Section 122(3) of the Act meets the minimum constitutional requirement because it offers a defence of due diligence.
>
> ...
>
> Para. 182. The Crown is not required to prove subjective *mens rea* under section 122(3) of the Act because the stigma attached to the offence is not as great as that attached to a criminal offence.
>
> ...
>
> Para. 184. *R. v. Sault Ste. Marie* (City), the Supreme Court of Canada recognized three categories of offences: full *mens rea*, strict liability and absolute liability.

The Supreme Court held that strict liability offences do not require the Crown to prove *mens rea*...

...

Para. 188. Regulatory offences are *prima facie* strict liability offences. The fundamental importance of regulation and its enforcement justifies the reverse onus...

Para. 189. Regulatory measures are the "primary mechanisms employed by governments in Canada to implement public policy objectives". Without regulatory offences, governments would not be able to regulate potentially harmful conduct and protect the public.

Para. 190. In *Wholesale Travel Group Inc.*, Justice Cory stated that there are two justifications for the different treatment of regulatory offences and true crimes: the licensing concept and the protection of the vulnerable.

...

Para. 193. The *Securities Act*, through licensing those who participate in the capital markets and protecting the public, meets both justifications outlined by Justice Cory. In this case, Bre-X was the market participant as a public company offering its shares to the investing public. Felderhof was an officer and director of Bre-X and was therefore regulated by the Act.

Para. 194. The purpose of the Act is to protect investors from unfair, improper or fraudulent practices and to foster fair and efficient capital markets and confidence in capital markets.

...

Para. 197. The primary means of achieving the purposes of the Act include "requirements for timely, accurate and efficient disclosure of information", "restrictions on fraudulent and unfair market practices and procedures" and "requirements for the maintenance of high standards of fitness and business conduct to ensure honest and responsible conduct by market participants".

...

Para. 200. Full, true and plain disclosure is the foundation of the capital markets system. The final report of the Toronto Stock Exchange Committee on Corporate Disclosure stated that information is really the "lifeblood" of the capital markets...

...

Para. 202. It is widely known and accepted that the securities industry is well regulated and why.

Para. 203. Participants engage in the securities industry voluntarily, for their own profit, and in exchange must comply with Ontario securities laws to ensure the protection of the public...

Para. 204. Directors and officers of publicly traded corporations voluntarily accept their positions in the corporation, and are generously compensated for their experience and expertise. In exchange, directors and officers assume duties and obligations.

...

Para. 207. Directors and officers of public corporations accept their positions with the knowledge that they have heightened responsibilities because of the regulated nature of the securities industry. The duties and obligations imposed on directors and officers require a high level of care and active steps to ensure compliance with the Act.

...

Para. 209. The protection of the investing public and the highly regulated nature of the securities industry justify strict liability offences against officers and directors, and the reverse onus provision contained in section 122(3) of the Act.

...

Para. 213. The imposition of strict liability with a defence of due diligence is necessary and appropriate. It is virtually impossible in most regulatory cases for the Crown to prove negligence beyond a reasonable doubt because the accused alone has the knowledge and ability to prove he or she took reasonable care...

...

Para. 215. The Defence argues that:

> 110.In order not to infringe section 7 of the *Charter*, the OSC must prove that Mr. Felderhof had the requisite knowledge of the primary Bre-X offence to support a conviction on the derivative section 122(3) offence. The OSC must go beyond the mere fact that he was a director of Bre-X who knew that press releases were being disseminated since that alone could not make him liable and

> still survive *Charter* scrutiny. The OSC must also provide evidence of actions or inactions of Mr. Felderhof during the material time that show he either knew, or was reckless in not knowing that Bre-X's press releases were false or misleading.

> Para. 216. This would import a full subjective *mens rea* element into the strict liability offence set out in section 122(3) of the Act contrary to the jurisprudence developed by the Supreme Court of Canada in *R. v. Sault Ste. Marie*, *Reference re Motor Vehicle Act (British Columbia)*, *R. v. Vaillancourt* and *R. v. Wholesale Travel Group Inc.* The Defence is asking this Court to criminalize this regulatory conduct, contrary to the Supreme Court of Canada's dicta emphasizing the critical importance of the regulatory structure.

Written and oral submissions of the Defence and O.S.C. made on the Charter Application which are more relevant to the case on its merits will be dealt with in that part of the judgement.

As noted above the Defence position is that if the offence in s.122(3) in a strict liability offence then it "*...is contrary to the Charter and cannot stand...*" but if I find it to be a full *mens rea* offence then it "*does withstand Charter scrutiny and ought not to be declared of no force or effect.*" I will begin by first determining the *mens rea* requirement of s.122(3) and then determine the section's constitutionality if necessary.

Interpretation of S.122(3)

R. v. Sault St. Marie

The starting point for an analysis of "*public welfare*" or "*regulatory*" offences is the Supreme Court of Canada decision in R. v. Sault Ste. Marie (City) [1978] 2 S.C.R. 1299

(S.C.C.) (QL). Starting at page 6 under the heading '*The Mens Rea Point*' the Court states:

> The Mens Rea Point
>
> The distinction between the true criminal offence and the public welfare offence is one of the [sic] prime importance. Where the offence is criminal, the Crown must establish a mental element, namely, that the accused who committed the prohibited act did so intentionally or recklessly, with knowledge of the facts constituting the offence, or with wilful blindness toward them. Mere negligence is excluded from the concept of the mental element required for conviction. Within the context of a criminal prosecution a person who fails to make such enquiries as a reasonable and prudent person would make, or who fails to know facts he should have known, is innocent in the eyes of the law.
>
> In sharp contrast, "absolute liability" entails conviction on proof merely that the defendant committed the prohibited act constituting the actus reus of the offence. There is no relevant mental element. It is no defence that the accused was entirely without fault. He may be morally innocent in every sense, yet be branded as a male factor [sic, malefactor] and punished as such.
>
> Public welfare offences obviously lie in a field of conflicting values. It is essential for society to maintain, through effective enforcement, high standards of public health and safety. Potential victims of those who carry on latently pernicious activities have a strong claim to consideration. On the other hand, there is a generally held revulsion against punishment of the morally innocent.
>
> ...
>
> The unfortunate tendency in may [sic, many] past cases has been to see the choice as between two stark alternatives; (i) full mens rea; or (ii) absolute liability.
>
> ...
>
> Dr. Glanville Williams has written: "There is a half-way house between mens rea and strict responsibility which has not yet been properly utilized, and that is responsibility for negligence," (Criminal Law (2d ed.): The General Part, p. 262).
>
> ...
>
> The correct approach, in my opinion, is to relieve the Crown of the burden of proving mens rea, having regard to Pierce Fisheries and to the virtual impossibility in most regulatory cases of proving wrongful intention. In a normal case, the accused alone will have knowledge of what he has done to avoid the

breach and it is not improper to expect him to come forward with the evidence of due diligence. This is particularly so when it is alleged, for example, that pollution was caused by the activities of a large and complex corporation. Equally, there is nothing wrong with rejecting absolute liability and admitting the defence of reasonable care.

In this doctrine it is not up to the prosecution to prove negligence. Instead, it is open to the defendant to prove that all due care has been taken. This burden falls upon the defendant as he is the only one who will generally have the means of proof. This would not seem unfair as the alternative is absolute liability which denies an accused any defence whatsoever. While the prosecution must prove beyond a reasonable doubt that the defendant committed the prohibited act, the defendant must only establish on the balance of probabilities that he has a defence of reasonable care.

I conclude, for the reasons which I have sought to express, that there are compelling grounds for the recognition of three categories of offences rather than the traditional two:

1. Offences in which mens rea, consisting of some positive state of mind such as intent, knowledge, or recklessness, must be proved by the prosecution either as an inference from the nature of the act committed, or by additional evidence.

2. Offences in which there is no necessity for the prosecution to prove the existence of mens rea; the doing of the prohibited act prima facie imports the offence, leaving it open to the accused to avoid liability by proving that he took all reasonable care. This involves consideration of what a reasonable man would have done in the circumstances. The defence will be available if the accused reasonably believed in a mistaken set of facts which, if true, would render the act or omission innocent, or if he took all reasonable steps to avoid the particular event. These offences may properly be called offences of strict liability. Mr. Justice Estey so referred to them in Hickey's case.

3. Offences of absolute liability where it is not open to the accused to exculpate himself by showing that he was free of fault.

Offences which are criminal in the true sense fall in the first category. Public welfare offences would prima facie be in the second category. They are not subject to the presumption of full mens rea. An offence of this type would fall in the first category only if such words as "wilfully," "with intent," "knowingly," or "intentionally" are contained in the statutory provision creating the offence. On the other hand, the principle that punishment should in general not be inflicted on those without fault applies. Offences of absolute liability would be those in

respect of which the Legislature had made it clear that guilt would follow proof merely of the proscribed act. The overall regulatory pattern adopted by the Legislature, the subject matter of the legislation, the importance of the penalty, and the precision of the language used will be primary considerations in determining whether the offence falls into the third category.

...

There is another reason, however, why this offence is not subject to a presumption of mens rea. The presumption applies only to offences which are "criminal in the true sense", as Ritchie J. said in the Queen v. Pierce Fisheries (supra), at p. 13. The Ontario Water Resources Commission Act is a provincial statute. If it is valid provincial legislation (and no suggestion was made to the contrary), then it cannot possibly create an offence which is criminal in the true sense.

The present case concerns the interpretation of two troublesome words frequently found in public welfare statutes: "cause" and "permit". These two words are troublesome because neither denotes clearly either full mens rea nor absolute liability. It is said that a person could not be said to be permitting something unless he knew what he was permitting. This is an over-simplification. There is authority both ways, indicating that the courts are uneasy with the traditional dichotomy.

...

The conflict in the above authorities, however, shows that in themselves the words "cause" and "permit", fit much better into an offence of strict liability than either full mens rea or absolute liability. Since s. 32(1) creates a public welfare offence, without a clear indication that liability is absolute, and without any words such as "knowingly" or "wilfully" expressly to import mens rea, application of the criteria which I have outlined above undoubtedly places the offence in the category of strict liability.

Proof of the prohibited act prima facie imports the offence, but the accused may avoid liability by proving that he took reasonable care. I am strengthened in this view by the recent case of R. v. Servico Limited, supra, in which the Appellate Division of the Alberta Supreme Court held that an offence of "permitting" a person under eighteen years to work during prohibited hours was an offence of strict liability in the sense which I have described. It also will be recalled that the decisions of many lower courts which have considered s. 32(1) have rejected absolute liability as the basis for the offence of causing or permitting pollution, and have equally rejected full mens rea as an ingredient of the offence.

R. v. Sault Ste. Marie (City): pages 6,7,8, 14, 15, 16

The Defence submissions that s. 122(3) is a full mens rea offence and/or requires the O.S.C. to prove as either a part of the actus reas or mens rea, that the Defendant knew the press releases were misleading or untrue may be divided under three headings:

1. The Meaning Of "Authorizes, Permits or Acquiesces In" in s.122 (3)
2. The Import of Section 122 (2)
3. The Meaning of "At The Time And In The Light Of The Circumstances" In s.122(1)(b)

1. THE MEANING OF "AUTHORIZES, PERMITS OR ACQUIESCES IN" IN S.122(3)

The Defence points to various cases which the Defence submits assist in understanding the words "*authorizes, permits or acquiesces*" in s.122(3) as encompassing full *mens rea*: R. v. F.W. Woolworth 18 C.C.C. (2d) 23 (Ont. C.A.) (QL), R. v. Fell (1981), 64 C.C.C.(2d) 456 (Ont. C.A.) (QL), R. v. Helsdon 2007 ONCA 53, R. v. Posner [1966] 1 O.R. 388 (Ont. H.C.J.) (QL), R. v. Rogo Forming Ltd. (1980), 56 C.C.C. (2d) 31 (Prov. Ct. (Crim. Div.)) (QL), R. v. Swendson [1987] A.J. No. 247 (Alta. Q.B.) (QL), Faulds v. Harper (1886) 11 S.C.R. 639 (QL), R. v. Armaugh Corp. [1993] O.J. No. 4360 (Ont. Ct.J.) (QL), R..v. Boyle [2001] A.J. No. 70 (Alta. Prov. Ct. (Crim. Div.)) (QL), and R. v. Peterson [2006] A.J. No. 286 (Alta. Prov. Ct. (Crim.Div.)) (QL), R. v. Gilson [1989] O.J. No. 1339 (Ont. Dist. Ct.), R. v. Gilson [1993] O.J. No. 4529 (Ont. Dist. Ct.)

R. v. F.W. Woolworth

In R. v. F.W. Woolworth, supra, the Ontario Court of Appeal states at page 8:

> As has been stated by Lord Reid in Sweet v. Parsley, [1970] A.C. 132, there is a presumption that mens rea is an essential element of every offence unless some reason can be found for holding that it is not necessarily so; when Parliament has chosen to create an offence of absolute liability the Courts must carry out its will but only to the extent that Parliament's intention to displace the presumption is clearly stated. In enacting s. 33 Parliament had the option of including in the Act provisions extending culpability for the infraction of the section to those other than the actual perpetrators in which even the Courts would have been called upon to interpret the scope of the words used by Parliament to convey its intention. However, instead of so doing Parliament has chosen to rely upon the extension by s. 21 imported into any offence created by statute.
>
> ...
>
> It is sought to make Woolworth a party as having done or omitted to do something for the purpose of aiding Healey and McPhee to commit the substantive offence.
>
> There are two principal reasons for holding that Woolworth was not a party to the offence charged:
>
> > 1. Even with respect to offences of strict liability the alleged aider must know that he is aiding. Although it is not necessary that it be proven that he know that the conduct he is aiding constitutes an offence it is necessary that the accused be proven at least to have known the circumstances necessary to constitute the offence he is accused of aiding.

R. v. Fell

In R. v. Fell, supra, the Ontario Court of Appeal relying on R. v. F.W. Woolworth states at page 6:

> The trial Judge correctly held that even where the offence is one of strict liability in so far as the liability of the principal is concerned, the liability of an aider or abettor to be convicted of the offence requires the existence of mens rea on the part of the aider or abettor. Mens rea in this context means knowledge of the circumstances which make up or constitute the offence, that is, in this case,

> knowledge on the part of the respondent that the representations were made and knowledge of the true facts. It was, of course, not necessary for the prosecution to prove that the respondent knew that those circumstances constituted an offence: see R. v. F. W. Woolworth Co. Ltd. (1974), 16 C.P.R. (2d) 272, 46 D.L.R. (3d) 345, 18 C.C.C. (2d) 23, and particularly at pp. 280-3 C.P.R., pp. 32-4 C.C.C.

As stated in R. v. F.W. Woolworth, Parliament had the option of including in the *Combines Investigation Act*, R.S.C. 1970, c.C-23, "*provisions extending culpability for the infraction of the section to those other than the actual perpetrators*" but instead chose to rely on s.21 of the *Criminal Code*.

In the case at bar the Legislature chose to include a charging section in the *Securities Act*, s. 122(3), for a director or officer who 'authorizes, permits, or acquiesces in' the commission of an offence under subsection (1) and did not rely on the "*Parties to Offence*" section of the *Provincial Offences Act, R.S.O. 1990, c.33*, which is section 77. The Defendant is not charged as a party to Bre-X's alleged commission of an offence under subsection (1). The Defendant is charged with a separate offence of 'authorizing, permitting or acquiescing in' the alleged commission of an offence by Bre-X.

In any event, s.21 of the *Criminal Code* which creates a true criminal offence requiring full *mens rea* is not applicable to a charge under s.122(3). *Criminal Code* provisions do not apply to the *Securities Act*.

R. v. Helsdon

The same analysis applied to Woolworth and Fell above is applicable to the more recent Ontario Court of Appeal decision in R. v. Helsdon, supra.

The Defence in Exhibit S1 (page 41) groups R. v. Posner, R. v. Rogo, and R. v. Swendson as tax cases interpreting language similar to the language in s.122(3).

R. v. Posner

In R. v. Posner, supra, in the Ontario High Court of Justice, the Court states starting at page 1:

> On January 18, 1965, the accused, Samuel Posner, was found guilty of the following offence against the Excise Tax Act, R.S.C. 1952, c. 100, and amendments thereto, namely, that he, being an officer and director or agent of Violet Sportswear Limited, did direct, authorize, condone or participate in the commission of an offence by the said Violet Sportswear Ltd...
>
> ...
>
> I would think that the state of mind of Samuel Posner at the time of the conduct giving rise to the charge is vital. Do not the very words "direct, authorize, participate or condone" imply the existence of a state of mind which can be described as intending to do some act which the accused Posner knew to be illegal, namely, as president of the company participated in its failure to pay? I therefore must say that mens rea is a necessary ingredient of the offence, and my answer to Q. 3(a) will be -- "Yes".

R. v. Posner: pages 1, 4

This decision is not one under the *Ontario Securities Act* but under the *Excise Tax Act*, R.S.C. 1952, c. 100, a federal statute.

The decision is dated 27 July, 1965 or some thirteen years prior to the decision in R. v. Sault Ste. Marie where as noted above the Supreme Court of Canada states at page 8:

> The unfortunate tendency in may [sic, many] past cases has been to see the choice as between two stark alternatives; (i) full mens rea; or (ii) absolute liability.

If that statement is applied to Posner than that court did not have the benefit of Sault Ste. Marie and the middle option of strict liability. Without the middle option of strict liability, the language used in the *Excise Tax Act* would rule out an absolute liability offence leaving only the option of a full mens rea offence. In Posner the court describes the accused's required state of mind "*as intending to do some act which the accused Posner knew to be illegal*" which is contrary to the Ontario Court of Appeal decisions in Woolworth and Fell where the court states it was not necessary for the prosecution to prove that the Defendant knew that the circumstances constituted an offence. The *Excise Tax Act* has similar wording to the *Securities Act* but does not include the word "*permit*" which the Supreme Court of Canada in Sault Ste. Marie states fits much better an offence of strict liability.

R. v. Rogo

In R. v. Rogo, supra, in the Ontario Provincial Court (Criminal Division) the court states starting at page 2:

> The individual accused are charged pursuant to s. 242 of the Income Tax Act which reads:
>
> > Where a corporation is guilty of an offence under this Act, an officer, director or agent of the corporation who directed, authorized, assented to, acquiesced in, or participated in, the commission of the offence is a party to and guilty of the offence and is liable on conviction to the punishment

provided for the offence whether or not the corporation has been prosecuted or convicted.

...

Into which of the three categories of offences described in R. v. City of Sault Ste. Marie, supra, does the offence created by ss. 153(1) and 238(2) of the Income Tax Act fall which makes it an offence for an employer to fail to remit in the time prescribed to the Receiver-General the amount of money withheld from employees' salaries on account of their tax obligations? Prior to the decision in that case it was considered to be an offence of absolute liability. Consistent with the judgment of Dickson J. (for the Court) I am satisfied that this offence falls within the category of offences of strict liability. That is the substantive offence in this case. Different considerations apply however where individuals are charged as directors, officers or agents of an employer that is a corporation under s. 242 of the Act. This section provides for liability of individuals as parties to the substantive offence committed by others. It has a scope and operation equivalent to s. 21 of the Criminal Code which provides for the liability of individuals as parties to substantive offences committed by others in the case of Criminal Code offences.

Crown counsel cited to me two cases decided prior to the decision in the case of the City of Sault Ste. Marie. The first in point of time is a decision of the Montreal Court of Sessions of the Peace in R. v. Caron (1946), 91 C.C.C. 389, where it was held that mens rea was not a necessary element of an offence under s. 111(3) of the Special War Revenue Act, R.S.C. 1927, c. 179, a provision worded similarly to s. 242 of the present Income Tax Act. To contrary effect is the second case which is a decision of the Supreme Court of Ontario in R. v. Posner, [1965] 4 C.C.C. 312, [1966] 1 O.R. 388, 46 C.R. 321. On a stated case, Lieff J. held that mens rea was an ingredient of the offence which an officer and director commits under a section of the Excise Tax Act containing a wording similar to s. 242 of the Income Tax Act. In that case the controlling words were "direct, authorize, participate or condone". He held that those very words imply the existence of a state of mind requisite to the offence charged against the individuals.

...

However, as to the liability under s. 242 of an officer, director or agent as a party to the substantive offence committed by a corporation. the ingredient of mens rea is imported or implied by the very words "who directed, authorized, assented to, acquiesced in, or participated in" the commission of the offence. These words include in themselves a mental element. It should be remembered that traditionally the problem whether mens rea is an ingredient of a statutory offence arose where the statute is silent as to mens rea and merely sets out the offence in terms of the prohibited act or omission. In criminal and some penal cases it was

held that a mental element is nevertheless an ingredient of the offence, requiring proof that the accused did the prohibited act intentionally or recklessly, with knowledge of the facts constituting the offence, or with wilful blindness toward them. Where the statute specifies a particular state of mind, such as "maliciously," "wilfully" or "recklessly", the problem generally does not arise; the case is one requiring proof of mens rea but the description of the offence itself includes an ingredient of specific or express mens rea. As mentioned above this was the view of Lieff J. in Posner which I adopt and apply. Alternatively, the words "who directed, authorized, assented to, acquiesced in, or participated in", the commission of the offence are part of the actus reus of the offence. This is consistent with the approach of Dickson J. in R. v. City of Sault Ste. Marie, supra, where he dealt with the words "discharging", "causing", or "permitting" being the key words of the actus reus of the offence charged in that case: see p. 376 of the report above cited.

However the matter is regarded, the Crown is bound to prove beyond a reasonable doubt all the elements of the offence as set out in the statute. As against an individual charged under s. 242, this includes proof of the substantive offence by the corporation, and in addition proof that he is (1) an officer, director or agent of the corporation, and (2) who directed, authorized, assented to, acquiesced in, or participated in the commission of the offence.

...

However, with respect to the individual accused, I hold that the offence charged against them under s. 242 of the Act as parties to the offence committed by the company is an offence requiring proof of mens rea as expressed in the governing words "who directed, authorized, assented to, acquiesced in, or participated in" the commission of the offence; or alternatively that those words form part of the actus reus of the offence; and at all events the onus of proof is upon the Crown to prove all the ingredients of the offence beyond a reasonable doubt including the elements of active or passive participation in the substantive offence within the meaning of those key words. Upon the evidence I am unable to find that funds were available to the company from which to pay the employees' tax deductions in due time and were diverted to other purposes or, if they were, that the accused knew [sic] about it.

R. v. Rogo: pages 2, 5,6,7,8

This case interprets the *Income Tax Act*, R.S.C. 1952, c.148, a federal statute and not the Ontario *Securities Act*. The *Income Tax Act* does not include the word "*permit*" which as

noted above, the Supreme Court of Canada in Sault Ste. Marie found fits much better an offence of strict liability. This case discusses Sault Ste. Marie but also relies on Posner, which as noted above was decided prior to Sault Ste. Marie. The court in Rogo finds s.242 has the "*scope and operation equivalent to s.21 of the Criminal Code*" but as I found above in the discussion of Woolworth and Fell, s. 21 is not applicable to an offence under s.122(3) of the *Securities Act*. Section 242 is different from s. 122(3) in that s.242 states that the officer or director is a party to the offence committed by the corporation while s.122(3) creates a separate offence for the officer or director.

R. v. Swendson

In R. v. Swendson, supra, in the Alberta Court of Queen's Bench, the court states starting at page 2:

> In my view Section 242 is not a charging section. The offence was a failure to comply with Section 1S3(1) [sic] and the offence is created by Section 238(2) of the Act.
>
> Section 242 sets out the various ways by which an officer, director or agent of a corporation may become a party to an offence committed by a corporation. The section requires that such person "direct, authorize, assent to, acquiesce in or participate in the commission of the offence" before guilt may attach to him. These requirements prevent the fixing of automatic penal liability upon officers, directors or agents of a guilty corporation.
>
> The substantive offences committed by the corporation are in my view properly characterized as strict liability offences. I adopt the reasoning in R. v. Rohan's Rock Pile Ltd. 57 C.C.C. (2d) 388. It follows therefore that if the respondent is guilty of the same offences their characterization does not change. A party to an offence faces the same offence as that committed by the principal. The real question before me is whether or not the Crown discharged the onus of proving that the respondent was a party within the meaning of Section 242 of the Act.
>
> ...

> In the present case the actus reus of the substantive offence was the failure by the corporation to remit sums it had deducted and withheld from salaries and wages of its employees to the Receiver General. The Crown was not required to prove mens rea in order to saddle the corporation with guilt under Section 238(2) of the Act. Where it sought to affix guilt to the respondent by virtue of Section 242, it was necessary to prove not only the guilt of the corporation but in addition that the respondent "directed, authorized, assented to, acquiesced in or participated in", the commission of the offence. The Crown chose to particularize the charge by alleging that the respondent "participated" in the failure to remit the funds to the Receiver General.
>
> ...
>
> In my opinion, the words "directed, authorized, assented to, acquiesced in, or participated in" are essential factual conditions requiring the Crown to prove at least one of them before a person specified in Section 242 can be held to be a party to and guilty of an offence committed by a corporation contrary to Sections 153(1) and 238(2) of the Act.

R. v. Swendson: pages 2,3,4

This case is not the decision of an Ontario Court. The decision confirms that s.242 of the *Income Tax Act* is not a charging section and simply sets out the various ways by which an officer or director may become a party to an offence committed by the corporation unlike s.122(3) which, as noted above, creates a separate offence for directors and officers. The approach in Swendson is similar to the analysis in Rogo where s.242 was compared to s.21 of the *Criminal Code*. The Court in Swendson quotes passages from Posner and Rogo but in the third paragraph quoted above concludes that if the company is guilty of a strict liability offence then an officer or director that is guilty of the same offence is also guilty of a strict liability offence and not a full mens rea offence as the Defence argues in the case at bar.

As noted above the court concludes the "*words 'directed, authorized, assented to, acquiesced in, or participated in' are essential factual conditions requiring the Crown to*

prove at least one of them..." The O.S.C. in this case does intend to prove that the defendant 'authorized, permitted or acquiesced in' the commission of an offence under subsection 122(1).

As noted above in the discussion of Rogo the *Income Tax Act* does not contain the word "*permit*".

Faulds v. Harper

The Defence also refers to Faulds v. Harper, supra, where the Supreme Court of Canada states at page 7:

> Now, in order to constitute equitable acquiescence it is incumbent on the party who relies on it to prove, not merely that there was some vague suspicion of wrong, but that actual knowledge of the facts were brought home to the party to be affected by it.

The discussion of equitable acquiescence in that case is in a different context of a civil suit to redeem lands where the plaintiffs had not been aware of the fraudulent character of the sale and so could not be said to have acquiesced in the possession of the defendants. This is not a case of director or officer liability in a provincial public welfare legislation prosecution.

R. v. Armaugh

In paragraph 112 of Exhibit S1 the Defence suggested R. v. Armaugh, supra, was a "*good starting point for understanding the words authorize, permit or acquiesce*". In Armaugh the court states starting at page 2:

Robert Daniel Fraser and Robert Patrick Joseph Kelly, at all material times officer and/or directors of Armaugh Corporation, were charged with six counts each of authorizing, permitting or acquiescing in the commission of the offences described above by Armaugh Corporation and thereby committing offences, contrary to section 118(3) (now section 122(3)) of the Securities Act.

...

Justice of the Peace MacPherson concluded that the combination of ss.52(1)(b) and 118(1)(c) created an absolute liability offence and therefore offended s.7 of the Charter by imposing imprisonment either directly or in combination or in default. ...

The terms "authorized", "permitted" and "acquiesce" imply, in the opinion of this court, an intentional act which would appear to be what is suggested by the reasoning and conclusions of Mr. Justice Dickson in R. v. Sault Ste. Marie, supra.

In *Websters New World Dictionary*, 3rd college edition acquiesce means to agree or consent quietly without protest. Authorize is defined in part as to give official approval or permission, to give power or authority, to give justification for and permit is defined as to allow, consent to tolerate, to give permission, authorize permission especially in writing, a document granting permission, licence, warrant.

In my opinion, the definition of all three words implies a knowing or an intentional act and therefore the defence of due diligence or mistake of fact would properly be available in accordance with the common law.

The case of R. v. Sault Ste. Marie, supra, is especially appropriate in considering those issues because of the fact that the legislation considered in that case, that is R. v. Sault Ste. Marie, included the words cause and permit and the word permit is found in section 118(3) accompanied with the synonyms authorized and acquiesced.

Quoting from the case of R. v. Sault Ste. Marie at p. 375 of that decision Mr. Justice Dickson stated as follows:

> The present case concerns the interpretation of two troublesome words frequently found in public welfare statutes: "cause" and "permit". These two words are troublesome because neither denotes clearly either full mens rea nor absolute liability. It is said that a person could not be said to be permitting something unless he knew what he was permitting.

> This is an over-simplification. There is authority both ways, indicating that the Courts are uneasy with the traditional dichotomy. Some authorities favour the position that "permit" does not import mens rea ...

Further down on p. 375 he continues:

> The conflict in the above authorities, however, shows that in themselves the words "cause" and "permit" fit much better into an offence of strict liability than either full mens rea or absolute liability.

...

As stated earlier in this judgment this court finds that the Legislature by using the words authorized, permitted, or acquiesced in section 118(3) imply a degree of mens rea. Therefore, as the case of R. v. Sault Ste. Marie was decided primarily concerning the interpretation of the words cause and permit, I, likewise, decide this matter on the interpretation of the word authorized, permitted or acquiesced. Therefore, while the intention of the Legislature is not free from doubt, as stated by Mr. Justice Saunders in R. v. Richardson at p. 359:

> more than a judicial determination of intention is required to find absolute liability. To meet the test laid down in the Sault Ste. Marie case, the Legislature must by its language make it clear that guilt follows proof merely of the proscribed act. In my opinion, the Legislature has not done so and the prima facie category of strict liability has not been displaced.

The court arrives at the same conclusions for the same reasons.

R. v. Armaugh: pages, 2, 4, 5, 6, 7

At paragraph 113 of Exhibit S1 the Defence submits:

> Para. 113. The Court in *Armaugh* found that each of these words implied an element of knowledge, or intentional act, into the offence. Therefore, it said that the OSC had to go beyond merely proving that the defendant was an officer or director of the company that committed the main offence. If that is all that would have been required, then Mr. Francisco, Dr. Kavanagh and Mr. McAnulty could all have been charged and found guilty under section 122(3).

I do not see how this case helps the Defence position that s.122(3) is a full *mens rea* offence. The case determines the same issue that is before me: the constitutionality of s.122(3). The case overturns a lower court decision that found s.122(3) to be an absolute liability offence and rules that s.122(3) is a strict liability offence.

The O.S.C. in this case concedes that it must go beyond simply proving that the defendant is an officer or director. At paragraph 218 of Exhibit S8 the O.S.C. states:

> Para. 218. The Crown concedes that section 122(3) requires a knowing or intentional act. In the context of this case, the knowing or intentional act is knowledge that Bre-X was issuing press releases that were required to be filed or furnished under Ontario securities law, of which there is an abundance of evidence beyond a reasonable doubt. The Crown is not required, contrary to what the Defence argues, to prove that Felderhof knew that the press releases were misleading or untrue, although this Court may find on the evidence of this case that he did.

As the O.S.C. has submitted, the court in Armaugh also points out, as discussed above, that the Supreme Court of Canada in Sault Ste. Marie considered the word "*permit*" which is also found in s.122(3) and decided that "*permit*" fits much better into an offence of strict liability than either full *mens rea* or absolute liability.

R. v. Boyle

In Exhibit S1 at paragraph 14, the Defence relies on the following quote from page 15 of R. v. Boyle, supra, an Alberta Provincial Court (Criminal Division) decision, arising out of a prosecution under s. 161(4) of the *Securities Act*, S. A. 1981, c.S.6.1. which has similar language to s.122(3):

> In my opinion, the Crown's argument, premised upon proof of the third party impugned acts coupled with simply being a Director, ignores both the inclusion of action and the encapsulation of knowledge contained within "authorized, permitted or acquiesced" as used in s. 161(4)(a) of the Act. To put it simply, one must know in order to authorize, permit or acquiesce.
>
> The mere fact that one is listed as a Director does not convey or communicate to that person knowledge of acts which are then to be either authorized, permitted or to which acquiescence is accorded.
>
> If I accept the reasoning and conclusion of Armaugh, and if I accept that the reasoning in both Fells and Woolworth is persuasive, I would reach a conclusion that the use of "authorized, permitted or acquiesced" in s. 161(4)(a) of the Act required the Crown to establish that there was some evidence of knowledge or of intentional act by either or both of Brian Boyle and Jason Boyle in regard to the primary acts of Kevin Boyle upon which the Crown rely to both establish there is some evidence in respect of the allegations against Kevin Boyle and which evidence informs the allegations against Brian Boyle and Jason Boyle. This conclusion would also comport with the interpretation of similar but not identical language in s. 242 of the Income Tax Act as noted in Swendsen.
>
> The language "authorized, permitted or acquiesced" in s. 161(4)(a) of the Act as part of the legislative scheme to regulate securities transactions within the Province of Alberta means that before a conviction can be registered against a Director or senior officer, the Crown must establish some evidence that the Director or senior officer had some knowledge of the acts or circumstances of another person which other person's acts are alleged constitute breaches of the Act for which the Director is liable under s. 161(4)(a).

This case from the Alberta Provincial Court is not binding on me. The O.S.C. submission in paragraph 221 of Exhibit S8 sets out the difference between Boyle and the case at bar:

> Para. 221. In that case, the Crown took the position that it was not required to prove that the director or officer was even aware of the alleged acts of a fellow director that constituted the offence by the company. The Court held that liability did not flow to directors based on the mere fact that they were listed as directors. In the case at bar, the Crown concedes that it must prove beyond a reasonable doubt that Felderhof authorized, permitted or acquiesced in the issuance of the statutorily required press release that contained misleading or untrue statements.

Further the court in Boyle approves of Armaugh which as noted above held that s.122(3) was a strict liability offence. Significantly in Boyle, contrary to the Defence position in the case at bar, the court accepts the position of the Crown and Defence that the charges in that case were strict liability offences and not full *mens rea* offences.

At page 8 the court states:

> In respect of charges under the Act, the Crown accepts that the offences with which these accused stand charged are not full mens rea offences, but are offences of strict liability to which a defence of due diligence is available to the accused. This position, accepted as well by the accused, removes any suggestion that the offences created by the Act are full mens rea offences, or absolute liability offences, for which liability flows simply from proof by the Crown of the legislatively impugned act.

R. v. Peterson

In paragraph 121 of Exhibit S1, the Defence sets out the following quote from R. v. Peterson, supra, at page 23, also from the Alberta Provincial Court (Criminal Division):

> In my view, the words "authorized...assented to or acquiesced or participated in the act or omission ", found in section 165(1) of the Fair Trading Act, all imply a degree of mens rea, or knowledge, on the part of an accused as Director, of the act or omission constituting the offence.
>
> Although the offence is a regulatory, public welfare offence, the Legislature by enacting section 165(1) of the Act, has by the language employed implicitly made mens rea an essential element in the Crown's case, if a "principle, director, manager, employee or agent of the corporation" is to be made a party to the offence.
>
> In my view, where a Director is charged, the offences are not strict liability offences falling in the second category of offences specified in Sault Ste. Marie (supra) but full mens rea offences, falling in the first category, requiring the Crown to prove knowledge on the part of the accused beyond a reasonable doubt, with no reverse onus on the accused to prove due diligence. If the Crown adduces evidence of knowledge, and that the accused did nothing, the Court may draw the

> inference that the accused, at minimum, acquiesced in the act or omission constituting the offence under the Act, absent some evidence to the contrary.

This case is not binding on me. It is an Alberta Provincial Court decision with respect to different legislation. This case, like Boyle is also a case where the director is charged as a party as was the case in Fell, Woolsworth, Rogo and Swendson and unlike s.122(3) which charges officers and directors with a separate offence.

In paragraph 222 of Exhibit S8 the O.S.C. correctly distinguishes this case:

> Para. 222. The Defense also relies on *R.* v. *Peterson*, a 2006 decision of the Alberta Provincial Court. This case can be distinguished because the accused in that case was a director of the company in name only. He had no knowledge of the acts or omissions that constituted the offence, nor was there any evidence that he assented to, acquiesced or participated in the act that constituted the offence.

Significantly, after an extensive review of the case law including Boyle, the court agreed with the opinion expressed in Boyle but as noted above Boyle found the offence in that case to be a strict liability offence and not a full *mens rea* offence contrary to the finding in Peterson.

The "*Fair Trading Act*" section under discussion in Peterson does not contain the word "*permit*" and so the direction of the Supreme Court of Canada in Sault Ste. Marie as to its significance was not applicable.

FINDING

I am not persuaded by the authorities cited by the Defence above that the words "*authorities, permits or acquiesces in*" import knowledge into the offence that the press releases were misleading or untrue either as part of the *mens rea* or *actus reus*.

Sault Ste. Marie states public welfare offences are prima facie strict liability offences, not subject to the presumption of full *mens rea*.

Section 122 (3) does not use such words as "*willfully*", "*with intent*", "*knowingly*", or "*intentionally*" which Sault Ste Marie states would make it a *mens rea* offence.

Contrary to the Defence position that the words "*authorize, permits or acquiesces*" dispel the statement in Sault Ste. Marie that welfare offences are prima facie strict liability offences, as noted above, Sault Ste. Marie finds that "*the words 'cause' and 'permit' fit much better into an offence of strict liability than either full mens rea or absolute liability.*"

Section 122(3) is a strict liability offence.

R. v. Gilson

At paragraph 217 of Exhibit S8 the O.S.C. states:

> Para. 217. The Crown was only able to find one decision in which the Court interpreted the words "authorized, permitted or acquiesced" as they appear in section 122(3) of the Act.

The O.S.C. then quotes and cites Armaugh.

But at paragraph 187 the O.S.C. also states:

> Para. 187. Ontario courts have held that whether a company is charged with trading in securities without filing a prospectus or an officer or director is charged with acquiescing in the same offence it is still a strict liability offence.
> *R.* v. *Gilson*, supra.
> *R.* v. *Armaugh*, supra.

The citation for R. v. Gilson, above, is found in paragraph 185 of Exhibit S8:

> *R.* v. *Gilson* [1989] O.J. No. 1339 (Ont. Dist. Ct.)

R. v. Armaugh is a decision of the Ontario Court of Justice (Provincial Division) and although persuasive it is not binding on me, but R. v. Gilson [1989] O.J. No. 1339 (Ont. Dist. Ct.), is an Ontario District Court decision sitting as a Summary Conviction Appeal Court and would be binding on me if it decided that s.122(3) was a strict liability offence as paragraph 187 above implies.

At page 2 of Gilson, supra, the court states:

> The essential issue at trial and on appeal, is with respect to the defence of due diligence. The offences as described in S. 118 of the Securities Act are strict liability offences. Upon proof of the actus reus, the accused may be convicted unless he proves on a balance of probabilities that he took all reasonable care, and the standard is set out in Regina v. City of Sault St. Marie (1978) 85 D.L.R. (3) 161, a decision of the Supreme Court of Canada and is described on Page 181 by Mr. Justice Dickson, "An offence to which there is no necessity for the prosecution to prove the existence of mens rea, the doing of a prohibited act prima facie imports the offence leaving it open to the accused to avoid liability by proving that he took all reasonable care."
>
> The court described three categories of offences and I am dealing with the second category referred to therein. This involves consideration of what a reasonable person would have done in the circumstances. The defence will be available if the accused reasonably believed in a mistaken set of facts which if true would render the act or omission innocent or if he took all reasonable steps to avoid the particular event. These offences may properly be called offences of strict Liability [sic].

The authors of *Securities Law and Practice*, 3rd Edition, Borden Ladner Gervais, Thompson Carswell, also state that the same case of R. v. Gilson, supra, held that s.122(3) is a strict liability offence at Volume 3, pages 22-9:

> Prior to the *Richardson* and *Sault Ste. Marie* decisions, the common law presumption of *mens rea* was held not to be a prerequisite to a summary conviction offence against directors of a corporation who acquiesced in the distribution of securities without prospectus, contrary to the ASA (*R.* v. *Burkinshaw*; *R.* v. *Zora* [1973] 5 W.W.R. 764, reversing (sub nom. *R.* v. *Burkinshaw*) [1973] 3 W.W.R. 150 (Alta. C.A.).

> This matter has been clarified by the *Sault Ste. Marie* and *Richardson* decisions. In *R.* v. *Gilson* (1989) 12 O.S.C.B. 3001, it was held that an offence under s.122(3) against an officer or director is a strict liability offence. The *mens rea* element is not required to be established by the Crown as a prerequisite to conviction. Conversely, a defence is available to the accused if he or she can prove that he or she took all reasonable care and the the [sic] accused had an honest and reasonable, but mistaken, belief as to the facts involved.

Both the O.S.C. and *Securities Law & Practice* refer to the same decision of Justice Corbett dated May 31, 1989.

My reading of that decision did not lead me to conclude that Gilson was charged as a director or officer under s.122(3). S.122 was previously S.118.

Upon further inquiry of the O.S.C. with respect to another R. v. Gilson at [1993] O.J. No. 4529, (1993), 16 O.S.C.B. 5297, a judgement of Justice Loukidelis of the Ontario Court of Justice (General Division) dated October 22, 1993, the O.S.C. agreed that the cite in paragraph 187 is incorrect and that it is the 1993 decision which deals with a prosecution under s.122(3).

It is a brief judgement and reads in full as follows:

> 1. LOUKIDELIS J. (endorsement): - The appeal against conviction is dismissed.
>
> 2. It was open to the trial judge to convict upon the evidence.
>
> 3. The first ground of appeal was that the trial judge found that the appellant had knowledge of the press release of September 18, 1987. Knowledge is not the operative word but rather the verbs authorize, permit or acquiesce. Further it is argued there is no evidence of knowledge at the relevant time charged. At the same time there was evidence to show that the accused as an officer and director came within the operative words of the section.

4. Insofar as identity is concerned, there was evidence upon which the trial judge could find identity had been proven.

5. The appellant having abandoned the appeal against sentence, the appeal is consequently dismissed. The conviction and sentence are affirmed.

As noted above, I was not persuaded by the authorities cited by the Defence. Neither the O.S.C. nor the Defence referred to Justice Loukidelis judgement in their written submissions nor the oral submissions that followed.

Regardless of the Defence submissions and Defence authorities I am of course bound by Justice Loukidelis' ruling that "*Knowledge is not the operative word but rather the verbs authorize, permit or acquiesce.*"

2. THE IMPORT OF SECTION 122(2)

Another Defence argument for interpreting s.122(3) as a *mens rea* offence is found in paragraph 136 of Exhibit S1. Also at pages 43 and 46 of the August 21, 2006 transcript the Defence argues:

> MR. GROIA: But in any event, 122, sub 2 is there and available for Bre-X. It's not available for Mr. Felderhof. And I would ask the Court to ask the question, why is that the case? Mr. Felderhof – or if the legislature intended Mr. Felderhof to have only a due diligence defence, in other words, if it had intended that (3) be a strict liability offence as opposed to a mens rea offence, it would have made infinitely more sense to have the defence in (2) available for persons charged under (3).

> It cannot be said that the legislature intended that a person charged with a derivative offence, a person charged with the commission of an offence by another, should have fewer defences than the company which committed the offence in the first place. And I say that that supports the argument that 122(3) was intended to have either full mens rea, or was intended to have the Crown prove that the person knew or was willfully blind, and that, of course, makes the whole due diligence issue irrelevant. Due diligence doesn't come up in a full mens rea prosecution in my submission.

...

> Well, I think the point is that if the legislature had intended the two sections to be dealt with in the same way, they would have either had no 122(2) and left it all to the common law remedy, or they would have had 122(2) apply to 122(1) and 122(3). Putting the statutory due diligence defence in the middle, in my submission supports the argument that the legislature intended something different for those two charging sections, and I say what they intended was that that (3) be a mens rea and they emphasized that they intended the (1) to be strict liability. They could have just left it out altogether if there's no difference, or they could have made it apply to both if there's no difference. When you apply it to one and not the other, that's a difference.

That argument was rejected by the Court in Armaugh which overturned a lower court that had decided:

> ...why give subsections 1(a) and (b) a due diligence defence and not subsection 1(c)? I am forced to consider that the Legislature did not intend the same strict liability offences to apply to subsection 1(c).

R. v. Armaugh: page 4

The Court in Armaugh relied on the Ontario Court of Appeal decision in R. v. Martin 2 O.R. (3d) 16. An appeal to the Supreme Court of Canada was dismissed at [1992] 1 S.C.R. 838. Armaugh also relied on the Ontario Divisional Court decision of R. v. Richardson [1981] O.J. No. 2511. The appeal to the Ontario Court of Appeal was dismissed at (1982), 39 O.R. (2d) 438 on other grounds.

In R. v. Martin the Court states at page 24:

> Further, it is asserted that because s.21 of the Act expressly provides for the defence of due diligence when it uses the words "failing to exercise due diligence", the absence of those words in s.13 indicates an intention that such a defence was not intended.

...

> As to the argument that the provision for the defence of due diligence in s. 21 must lead to the conclusion that s. 13 was intended to be an absolute liability offence, I accept the proposition that contextual analysis of other sections of the statute may in some instances provide an aid to construction. In my view, however, such analysis should not be considered conclusive. The decision of *Sault Ste. Marie* mandates that a court start with the general proposition that public welfare offences are strict liability offences and that the common law defences of due diligence and mistake of fact are available to the accused. I am prepared to assume that the due diligence provision of s. 21 was inserted by the legislature without consideration of the implications to other offences. Section 21 addresses a very specific situation and, in my view, its provision for the defence of due diligence was not intended to operate exclusively in the circumstances of that section.
>
> I am of the view, then, that the express provision of due diligence in s. 21 does not manifest an intent of the legislature to preclude raising the defence under s. 13.

In R. v. Richardson, separate reasons were delivered by the three Justices in the Divisional Court concurring in the result.

At page 5 Justice Steele states:

> The position of the Crown was, basically, that offences under the Act would be strict liability offences if it were not for the provisions of s-s. (2) of s.137 which specifically provide for a defence of due diligence in offences under cls. (a) or (b) of s-s. (1) and by inference, it contends, made all other offences in the Act absolute liability offences. I do not accept this proposition.

At page 9 Justice Saunders states:

> I am troubled by the language of s. 137. The Crown contends that as s-s. (2) specifically provides for a due diligence defence for prosecutions under s. 137(1)(a) and (b), it follows that no such defence is available for prosecutions under s. 137(1)(c) and (d) and that, therefore, the latter offences are ones of absolute liability within the meaning of R. v. City of Sault Ste. Marie, [1978] 2 S.C.R. 1299, 85 D.L.R. (3d) 161, 40 C.C.C. (2d) 353.
>
> ...
>
> Section 137(1) and (2) were enacted in their present form in 1966 and, prior to that time, there had been no provision similar to s-s. (2). The legislation was introduced following the submission to the then Attorney-General for Ontario of

> the report of a committee chaired by the late J. R. Kimber, Q.C. At that time, in prosecutions for statutory offences, the choice in Canada was between (1) a mens rea offence where the Crown is required to prove the state of mind of the accused as well as the actus reus; and, (2) an absolute liability offence where the actus reus only need be proved to obtain a conviction. In 1965, some courts in other jurisdictions and legal writers were seeking a middle ground where the Crown would not be required to show mens rea, but where an accused could establish a defence of due diligence or an honest, non- negligent mistake of fact.
>
> The middle ground was subsequently labelled "strict liability" and was finally established by the decision in the Sault Ste. Marie case, supra. From 1966 to the present, the wording of what is now s. 137(1) and (2) has not changed. The legislation was recently re-enacted after the decision in the Sault Ste. Marie case was issued and after the information was laid in the case at bar. It is possible that the language of what is now s. 137(2) was first introduced to make clear that mens rea was not a necessary element of an offence involving false or misleading statements. The Crown now submits that as the Legislature has re-enacted the section without change, the omission to provide a due diligence defence for prosecutions under s. 137(1)(c) and (d) by implication means that such defence is not available and that the offence is and always has been one of absolute liability.
>
> While the intention of the Legislature is not free from doubt, in my opinion, more than a judicial determination of intention is required to find absolute liability. To meet the test laid down in the Sault Ste. Marie case, the Legislature must by its language make it clear that guilt follows proof merely of the proscribed act. In my opinion, the Legislature has not done so and the prima facie category of strict liability has not been displaced.

I follow the above authorities and I am not persuaded by this Defence submission.

3. THE MEANING OF "AT THE TIME AND IN LIGHT OF THE CIRCUMSTANCES" IN S.122(1)(B)

The Defence also argues that the qualifier "*at the time and in light of the circumstances*" in s. 122(1)(b) imports into the *actus reus* a requirement that the company and the director or officer knew the press release was misleading or untrue. Section 122(1)(b) and s.122(3) are strict liability offences. There is no knowledge component. The qualifier "*at the time and in the light of the circumstance*" refers to whether factually the statement is misleading or untrue. It does not refer to the defendant's knowledge and it does not

require the O.S.C. to prove the defendant had knowledge the statement was misleading or untrue.

It does not require the O.S.C. to prove red flags beyond a reasonable doubt. Whether or not the evidence establishes the existence of any red flags is not relevant to whether the press releases were in fact misleading or untrue but relevant to a defence of reasonable care. The press releases may be misleading or untrue whether or not there were any red flags.

Change in Defence Position

Contrary to the Defence position taken in the Charter Application, in written submissions with respect to the merits the Defence agrees s.122(3) is a strict liability offence in its commentary to paragraph 4 of Exhibit S5 Volume II.

In paragraph 4 of Exhibit S5 Volume II the O.S.C. states:

> Para. 4. The offence of a director or officer authorizing, permitting or acquiescing in a company issuing statutorily required press releases that contain misleading or untrue statements is a strict liability offence. The burden is on the Crown to prove the *actus reus* of the offence and then it is open to Felderhof to avoid liability by proving that he took all reasonable care.

The Defence comments are:

> **The Defence agrees, and notes that the burden on the Crown is to prove the *actus reus* of the offence beyond a reasonable doubt.**

Alleged Charter Breach

Having determined that s.122(3) is a strict liability offence with no knowledge component, I now will deal with the Defence submission that if I find, as I have, that the O.S.C. does not have to prove the Defendant knew (or was reckless or willfully blind)

that the impugned press releases were misleading or untrue, then s.122(3) is in breach of the Charter and of no force or effect.

There was no Constitutional Question before Justice Loukidelis in Gibson and so this issue was not determined by the court.

R. v. Sault Ste. Marie

I reviewed R. v. Sault Ste. Marie above. Sault Ste. Marie was a pre-Charter case.

Reference Re M.V.A. (B.C)

Reference re M.V.A (B.C.) s.94(2) [1985] S.C.J. No. 73 (QL), is a post-Charter case in the Supreme Court of Canada which sets out the minimum *mens rea* required for a regulatory offence. Reference re M.V.A. (B.C.) is reviewed in R. v. Vallaincourt below.

R. v. Vallaincourt

In R. v. Vallaincourt [1987] S.C.J. No 83 (S.C.C.) (QL) the Supreme Court of Canada states at page 11:

> This Court's decision in Re B.C. Motor Vehicle Act stands for the proposition that absolute liability infringes the principles of fundamental justice, such that the combination of absolute liability and a deprivation of life, liberty or security of the person is a restriction on one's rights under s. 7 and is prima facie a violation thereof. In effect, Re B.C. Motor Vehicle Act acknowledges that, whenever the state resorts to the restriction of liberty, such as imprisonment, to assist in the enforcement of a law, even, as in Re B.C. Motor Vehicle Act, a mere provincial regulatory offence, there is, as a principle of fundamental justice, a minimum mental state which is an essential element of the offence. It thus elevated mens rea from a presumed element in Sault Ste. Marie, supra, to a constitutionally required element. Re B.C. Motor Vehicle Act did not decide what level of mens rea was constitutionally required for each type of offence, but inferentially decided that even for a mere provincial regulatory offence at least negligence was required, in

that at least a defence of due diligence must always be open to an accused who risks imprisonment upon conviction.

...

But, whatever the minimum mens rea for the act or the result may be, there are, though very few in number, certain crimes where, because of the special nature of the stigma attached to a conviction therefore [sic] or the available penalties, the principles of fundamental justice require a mens rea reflecting the particular nature of that crime. Such is theft, where, in my view, a conviction requires proof of some dishonesty. Murder is another such offence.

R. v. Wholesale Travel

In R. v. Wholesale Travel [1991] S.C.J. No. 79 (S.C.C.) (QL), the Supreme Court of Canada continues the analysis of public welfare legislation and the application of the Charter. Justice Cory states starting at page 35:

There is no doubt that regulatory offences were originally and still are designed to protect those who are unable to protect themselves.

...

The Sault Ste. Marie case recognized strict liability as a middle ground between full mens rea and absolute liability. Where the offence is one of strict liability, the Crown is required to prove neither mens rea nor negligence; conviction may follow merely upon proof beyond a reasonable doubt of the proscribed act. However, it is open to the defendant to avoid liability by proving on a balance of probabilities that all due care was taken. This is the hallmark of the strict liability offence: the defence of due diligence.

...

The objective of regulatory legislation is to protect the public or broad segments of the public (such as employees, consumers and motorists, to name but a few) from the potentially adverse effects of otherwise lawful activity. Regulatory legislation involves a shift of emphasis from the protection of individual interests and the deterrence and punishment of acts involving moral fault to the protection of public and societal interests. While criminal offences are usually designed to condemn and punish past, inherently wrongful conduct, regulatory measures are generally directed to the prevention of future harm through the enforcement of minimum standards of conduct and care.

...

In short, regulation is absolutely essential for our protection and well being as individuals, and for the effective functioning of society. It is properly present [page 222] throughout our lives. The more complex the activity, the greater the need for and the greater our reliance upon regulation and its enforcement.

...

The appellant has argued that conviction for the offence of false advertising carries a stigma of dishonesty, with the inference that the accused falsely advertised for the purposes of obtaining economic advantage. It is said that nothing could be more damaging to a business than the implication that it has made dishonest representations. In my view, however, the offence does not focus on dishonesty but rather on the harmful consequences of otherwise lawful conduct. Conviction suggests only that the defendant has made a representation to the public which was in fact misleading and that the defendant was unable to establish the exercise of due diligence in preventing the error. This connotes a fault element of negligence rather than one involving moral turpitude. Thus, any stigma that might flow from a conviction is very considerably diminished.

...

A Contextual Approach to Charter Interpretation

A. The Importance of Considering Charter Rights in Context

...

It is now clear that the Charter is to be interpreted in light of the context in which the claim arises. Context is relevant both with respect to the delineation of the meaning and scope of Charter rights, as well as to the determination of the balance to be struck between individual rights and the interests of society.

A contextual approach is particularly appropriate in the present case to take account of the regulatory nature of the offence and its place within a larger scheme of public welfare legislation. This approach requires that the rights asserted by the appellant be considered in light of the regulatory context in which the claim is situated, acknowledging that a Charter right may have different scope and implications in a regulatory context than in a truly criminal one.

...

In the present case, the contextual approach requires that regulatory and criminal offences be treated differently for the purposes of Charter review. Before proceeding to the substantive analysis, however, it is necessary to consider the

justifications for differential treatment. They are two-fold: the first relates to the distinctive nature of regulatory activity, while the second acknowledges the fundamental need to protect the vulnerable through regulatory legislation.

...

1. The Licensing Justification

...

The licensing argument is directed to this question of choice. Thus, while in the criminal context, the essential question to be determined is whether the accused has made the choice to act in the manner alleged in the indictment, the regulated defendant is, by virtue of the licensing argument, assumed to have made the choice to engage in the regulated activity. The question then becomes not whether the defendant chose to enter the regulated sphere but whether, having done so, the defendant has fulfilled the responsibilities attending that decision.

The licensing justification is based not only on the idea of a conscious choice being made to enter a regulated field but also on the concept of control. The concept is that those persons who enter a regulated field are in the best position to control the harm which may result, and that they should therefore be held responsible for it.

...

2. The Vulnerability Justification

The realities and complexities of a modern industrial society coupled with the very real need to protect all of society and particularly its vulnerable members, emphasize the critical importance of regulatory offences in Canada today. Our country simply could not function without extensive regulatory legislation. The protection provided by such measures constitutes a second justification for the differential treatment, for Charter purposes, of regulatory and criminal offences.

...

It follows that a contextual approach is required in the present case in order that the distinctive nature of regulatory offences and their fundamental importance in Canadian society may be considered. Both licensing and vulnerability considerations justify differential treatment for the purposes of Charter interpretation, of crimes and regulatory offences. This, then, is the basis upon which the present case must be approached.

...

The Constitutionality of Strict Liability

...

A. Section 7: The Mens Rea Issue

...

The question which must now be determined is as follows: in situations where imprisonment is available as a penalty, does s. 7 require proof of a degree of fault greater than negligence? That is to say, must a positive mental state be established in order to justify a conviction?

...

Does section 7 require in all cases that the Crown prove mens rea as an essential element of the offence? The resolution of this question requires that a contextual approach be taken to the meaning and scope of the s. 7 right. Certainly, there can be no doubt that s. 7 requires proof of some degree of fault. That fault may be demonstrated by proof of intent, whether subjective or objective, or by proof of negligent conduct, depending on the nature of the offence. While it is not necessary in this case to determine the requisite degree of fault necessary to prove the commission of particular crimes, I am of the view that with respect to regulatory offences, proof of negligence satisfies the requirement of fault demanded by s. 7. Although the element of fault may not be removed completely, the demands of s. 7 will be met in the regulatory context where liability is imposed for conduct which breaches the standard of reasonable care required of those operating in the regulated field.

...

It must be remembered that regulatory offences were historically developed and recognized as a distinct category precisely for the purpose of relieving the Crown of the burden of proving mens rea. This is their hallmark. The tremendous importance of regulatory legislation in modern Canadian industrial society requires that courts be wary of interfering unduly with the regulatory role of government through the application of inflexible standards. Under the contextual approach, negligence is properly acceptable as the minimum fault standard required of regulatory legislation by s. 7.

...

For these reasons, I conclude that the appellant's claim that strict liability offences violate s. 7 of the Charter cannot succeed. The requirements of s. 7 are met in the

regulatory context by the imposition of liability based on a negligence standard. Therefore, no violation of s. 7 results from the imposition of strict liability.

B. Section 11(d): Onus and the Due Diligence Defence

Wholesale Travel argues that the placing of a persuasive burden on the accused to establish due diligence on a balance of probabilities violates the presumption of innocence as guaranteed by s.11(d) of the Charter. As the due diligence defence is the essential characteristic of strict liability offences as defined in Sault Ste. Marie, the appellant's s.11(d) claim represents a fundamental challenge to the entire regime of regulatory offences in Canada.

...

The reasons for ascribing a different content to the presumption of innocence in the regulatory context are persuasive and compelling. As with the mens rea issue, if regulatory mechanisms are to operate effectively, the Crown cannot be required to disprove due diligence beyond a reasonable doubt. Such a requirement would make it virtually impossible for the Crown to prove regulatory offences and would effectively prevent governments from seeking to implement public policy through regulatory means. ...

This rationale is no less compelling today. Quite simply, the enforcement of regulatory offences would be rendered virtually impossible if the Crown were required to prove negligence beyond a reasonable doubt. The means of proof of reasonable care will be peculiarly within the knowledge and ability of the regulated accused. Only the accused will be in a position to bring forward evidence relevant to the question of due diligence.

R. v. Wholesale Travel: pages 35, 36, 37, 39, 40, 41, 42, 43, 44, 46, 47, 48, 49, 50

In the QuickLaw headnote a summary of the decisions is set out:

The issues are decided as follows:

1. It is not an infringement of s. 7 of the Charter to create an offence for which the mens rea component is negligence, so that a due diligence defence (s. 37.3(2)(a) and (b)) is available. Unanimous.

2. The timely retraction provisions (s. 37.3(2)(c) and (d)) infringe s. 7, are not justified under s. 1, and are accordingly unconstitutional. Unanimous.

3. (a) On a majority reasoning by Lamer C.J. (and La Forest, Sopinka, Gonthier, McLachlin, Stevenson and Iacobucci JJ.), the reverse onus provision ("he establishes that" in s. 37.3(2)) infringes s. 11(d) of the Charter; L'Heureux-Dubé and Cory JJ. (dissenting on this issue) would find no infringement, and would in any event, have found an infringement justified under s. 1.

(b) Per Gonthier, Stevenson and Iacobucci JJ.: The provision is justified under s. 1 of the Charter.

(c) Per Lamer C.J. and La Forest, Sopinka and McLachlin JJ. (dissenting on this issue): The provision is not justified under s. 1 of the Charter.

(d) Per L'Heureux-Dubé, Gonthier, Cory, Stevenson and Iacobucci JJ. (Lamer C.J. and La Forest, Sopinka and McLachlin JJ. dissenting in the result): The reverse onus provision is constitutional.

4. The matter is therefore remitted to trial on the bases that:

(a) a negligence mens rea regulatory offence is constitutional;

(b) the timely retraction provisions are unconstitutional; and

(c) the reverse onus provision is constitutional. [Page 3]

B.C.S.C. v. Branch

The regulating nature of securities legislation is discussed by the Supreme Court of Canada in British Columbia Securities Commission v. Branch [1995] S.C.J. No. 32 (S.C.C.) (QL) where the Court states starting at page 14.

We must determine the predominant purpose of such an inquiry at which a witness is compelled to attend. In Pezim v. British Columbia (Superintendent of Brokers), [1994] 2 S.C.R. 557, Iacobucci J., writing for the Court referred to the regulatory nature of the Securities Act (at p. 589):

> It is important to note from the outset that the [Securities Act] is regulatory in nature. In fact, it is part of a much larger framework which regulates the securities industry throughout Canada. Its primary goal is the protection of the investor but other goals include capital market efficiency and ensuring public confidence in the system: David L. Johnston, Canadian Securities Regulation (1977), at p. 1. [Emphasis added.]

The goal of protecting our economy is a goal of paramount importance. In Pezim, the preeminence of securities regulation in our economic system was emphasized (at pp. 593 and 595)...

...

Clearly, this purpose of the Act justifies inquiries of limited scope. The Act aims to protect the public from unscrupulous trading practices which may result in investors being defrauded. It is designed to ensure that the public may rely on honest traders of good repute able to carry out their business in a manner that does not harm the market or society generally.

...

There are areas of business, for example, that are subject to regulation as a matter of course. Persons who carry on the business of trading in securities realize that the industry is heavily regulated and for good reason. It is a crucial part of our economy that is at stake. In Pezim, supra, at pp. 592-93, this Court relied on the following position articulated by Fauteux J. in Gregory & Co. v. Quebec Securities Commission, [1961] S.C.R. 584, at p. 588:

> The paramount object of the Act is to ensure that persons who, in the province, carry on the business of trading in securities or acting as investment counsel, shall be honest and of good repute and, in this way, to protect the public, in the province or elsewhere, from being defrauded as a result of certain activities initiated in the province by persons therein carrying on such a business.

It is widely known and accepted that the industry is well regulated. Similarly, it is well known why the industry is so regulated. The appellants in this case were well aware of the dictates of the Securities Act.

In a concurring decision dismissing the appeal, Justice L'Heureux-Dube writes at page 25:

> Second, although activity in the securities sphere is of immense economic value to society generally, it must be remembered that participants engage in this licensed activity of their own volition and ultimately for their own profit. In return for permitting persons to obtain the fruits of participation in this industry, society requires that market participants also undertake certain corresponding obligations in order to safeguard the public welfare and trust. Participants must conform with the extensive regulations and requirements set out by the provincial securities commissions. Many of these requirements are fundamental to maintaining an efficient, competitive market environment in a context where imperfect information is endemic. They are also essential to prevent and deter abuses of such asymmetries of information, and therefore to maintain the integrity of the securities system and protect the public interest.

British Columbia Securities Commission v. Branch: pages 14, 20, 25

There is no issue the securities industry is highly regulated in Ontario.

Securities Act

The "*purposes*" of the *Securities Act* are set out in s.1.1:

> **Purposes of Act**
>
> 1.1 The purposes of this Act are,
>
> (a) to provide protection to investors from unfair, improper or fraudulent practices; and
>
> (b) to foster fair and efficient capital markets and confidence in capital markets.

The "*principles to consider*" are set out in s.2.1 which reads in part:

> **Principles to consider**
>
> 2.1 In pursuing the purposes of this Act, the Commission shall have regard to the following fundamental principles:

1. Balancing the importance to be given to each of the purposes of this Act may be required in specific cases.

2. The primary means for achieving the purposes of this Act are,

   i. requirements for timely, accurate and efficient disclosure of information,

   ii. restrictions on fraudulent and unfair market practices and procedures, and

   iii. requirements for the maintenance of high standards of fitness and business conduct to ensure honest and responsible conduct by market participants.

National Policy Statement 40 –Timely Disclosure

National Policy Statement 40 –Timely Disclosure made pursuant to s. 143.8 of the *Securities Act* under the heading "*Basic Principle –Disclosure of Material Information*" states:

> It is a cornerstone principle of securities regulation that all persons investing in securities have equal access to information that may affect their investment decisions. Public confidence in the integrity of the securities markets requires that all investors be on an equal footing through timely disclosure of material information concerning the business and affairs of reporting issuers and of companies whose securities trade in secondary markets. Therefore, immediate disclosure of all material information through the news media is required.

Erikson v. Ontario (Securities Commission)

In Erikson v. Ontario (Securities Commission), [2003] O.J. No. 593 the Ontario Superior Court of Justice refers to their earlier decision in Manning v. Ontario (Securities Commission) [1996] O.J. No. 3414 and states at page 10:

> Participation in the capital markets is a privilege, not a right.

RULING

S. 122(3) is public welfare legislation as defined in Sault Ste. Marie and Wholesale Travel in a highly regulated field as described in Pezim and Branch. The licensing and vulnerability justifications discussed by Justice Cory in Wholesale Travel are applicable to securities legislation as is the discussion about stigma.

The Defence relies on R. v. DeSousa [1992] S.C.J. No. 77 (S.C.C.) (QL), in its s.7 argument where the Supreme Court of Canada states at page 7:

> It is axiomatic that in criminal law there should be no responsibility without personal fault. A fault requirement was asserted to be a fundamental aspect of our common law by this Court in R. v. City of Sault Ste. Marie, [1978] 2 S.C.R. 1299, and as a matter of constitutional law under s. 7 of the Charter in Re B.C. Motor Vehicle Act, [1985] 2 S.C.R. 486. As a matter of statutory interpretation, a provision should not be interpreted to lack any element of personal fault unless the statutory language mandates such an interpretation in clear and unambiguous terms.

De Sousa is concerned with the fault requirement in criminal law. But it is to Sault Ste. Marie, B.C. Motor Vehicle, Vaillancourt and Wholesale Travel that I must look to determine the fault requirement in a public welfare offence.

Section 122(3) satisfies the fault requirement set out in those cases. The Supreme Court of Canada in Wholesale Travel refers to the Vallaincourt and B.C. Motor Vehicles and states that the level of *mens rea* constitutionally required for a provincial regulatory offence is negligence:

> The requirements of s.7 are met in the regulatory context by the imposition of liability based on a negligence standard. Therefore, no violation of s.7 results from the imposition of strict liability.

R. v. Wholesale Travel Group Inc: pages 47-48

Section 122(3) meets the minimum constitutional *mens rea* requirement. It is a strict liability offence where the defendant has a common law defence of due diligence.

Section 122(3) does not breach s.7 of the Charter.

Any breach would be saved by s.1 for the reasons discussed above.

Any Defence argument relying on s.11(d) of the Charter is answered by the decision in Wholesale Travel.

Section 122(3) of the Ontario Securities Act is not inconsistent with the Charter.

The Notice of Application and Constitutional Question is dismissed.

REQUIREMENTS OF S.122(3)

Contrary to the Defence position, the determination that s.122(3) is a strict liability offence does not mean that officers and directors are "*liable for the mere fact that they were directors of the issuing corporation during the material time*" (Paragraph 107 of Exhibit S1).

The O.S.C. must prove beyond a reasonable doubt that the defendant was a director or officer of the company and that the defendant 'authorized, permitted or acquiesced in' the commission of an offence under subsection (1) by that company.

Authorize, permit and acquiesce have their ordinary dictionary meaning.

Those words are defined in *The Canadian Oxford Dictionary* in part as follows:

> **Authorize:** "*sanction formally*", "*give authority* "
>
> **Permit:** "*give permission or consent to*", "*authorize*", "*allow*", "*give an opportunity to*", "*admit*", "*allow for* "
>
> **Acquiesce:** "*agree, esp. tacitly*", "*raise no objection*", "*accept*"

Because s.s.122(1)(b) creates a strict liability offence, then to prove the commission of an offence under subsection (1) of s.122 as required by s.s.122(3), the O.S.C. must prove only the *actus reus* of that offence; that is, that Bre-X made a statement in a press release required to be filed under Ontario securities law that, in a material respect and at the time and in the light of the circumstances under which it was made, was misleading or untrue or did not state a fact that was required to be stated or that was necessary to make the statement not misleading.

If the company commits the *actus reus* set out in s.s. 122(1)(b) then s.s.122(1) continues and states that the company "*is guilty of an offence...*"

The company due diligence defence is then contained in a separate subsection; that is, s.s.122(2).

Subsection 122(3) charging the officer or director refers to "*the commission of an offence under subsection(1) by the company*".

Once the O.S.C. proves the *actus reus* of s.s.122(1)(b) beyond a reasonable doubt, the O.S.C. has proved the company "*is guilty of an offence*" which satisfies the requirement of s.s. 122(3), that the director or officer authorizes, permits or acquiesces in "*the commission of an offence under subsection (1)*".

"*Material*" has its ordinary dictionary meaning. The relevant part of the meaning found in *The Canadian Oxford Dictionary* is: "*pertinent, essential, relevant (at the material time)*", "*serious, important, of consequence*", "*Law (of evidence, a fact, etc.) significant,*

influential, esp. to the extent of determining a cause, affecting a judgment, etc, (a material witness)".

"*At the time and in the light of the circumstances under which it is made*" means that the statement is factually misleading or untrue at the time and in the circumstances under which it is made whether or not it was true at some other time or in other circumstances. Or to put it in the reverse, a statement is not misleading or untrue if at the time and in the circumstances under which it is made it is not misleading or untrue even if at another time or under other circumstances it had been or becomes misleading or untrue.

Without limiting the availability of other defences, subsection 122(2) gives Bre-X a statutory defence of due diligence. If there is evidence of due diligence by Bre-X established on a balance of probabilities then Felderhof is entitled to an acquittal. Felderhof has a defence of due diligence at common law. If Felderhof proves on a balance of probabilities that he was not negligent or that he was duly diligent or took reasonable care that the press releases that he 'authorized, permitted or acquiesced in' were not misleading or untrue, then he is entitled to an acquittal on that basis as well. As noted above the Charter Application is dismissed and I now proceed to deal with Counts 5 to 8.

COUNTS 5 TO 8: AUTHORIZING MISLEADING PRESS RELEASES

Counts 5 to 8 of the information are set out at page 2 of these reasons. Sections 122(1)(b), (2) and (3) of the *Securities Act* are set out at page 17.

The Defence agrees with paragraphs 1, 4 and 5 of Exhibit S5 Volume II as follows:

> Para. 1. John Bernard Felderhof is charged with four counts of authorizing, permitting or acquiescing in issuing statutorily required press releases that contained misleading or untrue statements contrary to sections 122(1)(b) and (3) of the Act.
>
> **The Defence agrees.**
>
> ...
>
> Para. 4. The offence of a director or officer authorizing, permitting or acquiescing in a company issuing statutorily required press releases that contain misleading or untrue statements is a strict liability offence. The burden is on the Crown to prove the actus reus of the offence and then it is open to the accused to avoid liability by proving that he took all reasonable care.
>
> **The Defence agrees, and notes that the burden on the Crown is to prove the *actus reus* of the offence beyond a reasonable doubt.**

As noted earlier in my discussion of the Charter application, the Defence agreement here that s. 122(3) is a strict liability offence is not consistent with the Defence position in the Charter application but is consistent with my findings in that application.

> Para. 5. The Crown must prove beyond a reasonable doubt the elements of issuing statutorily required press releases which contain misleading or untrue statements:
>
> | | |
> |---|---|
> | Element A | A company made a statement in a press release; |
> | Element B | The press release was required to be filed by the company under Ontario securities law; |

Element C	The press release contained a statement that, in a material respect and at the time and in the light of the circumstances under which it was made, was misleading or untrue or did not state a fact that was required to be stated or that was necessary to make the statement not misleading; and
Element D	The defendant, director or officer authorized, permitted or acquiesced in the issuance of the statutorily required press release that contained misleading or untrue statements.

The Defence Agrees.

It is convenient to follow the breakdown of the elements of the offence under s.122 (3) set out above by the O.S.C. and agreed to by the Defence.

Element A: Bre-X Made Statements In Press Releases

There is no issue that Bre-X issued the press releases dated June 20, 1996, July 22, 1996, December 3, 1996 and February 17, 1997 which are the subject matter of Counts 5 to 8.

The Defence states at page 5 of the Introduction to Exhibit S5 Volume II:

> Again, the Defence and the OSC disagree as to the inferences and conclusions that can be drawn from the documentary evidence and testimony as to Mr. Felderhof's role in the alleged 'authorization', 'permission', or 'acquiescence' in the issuance of the Press Releases. While clearly Bre-X issued them, the limited extent of Mr. Felderhof's involvement is clearly insufficient for a conviction to be registered.

The Defence agrees with paragraph 9 of Exhibit S5 Volume II:

> Para. 9. Felderhof concedes that Bre-X made the statements in the subject press releases.

The Defence Agrees.

The Defence also agrees with paragraphs 8, 200, 210 and 220:

> Para. 8. On June 20, 1996, Bre-X issued a press release disclosing a resource calculation of 39.15 million ounces of gold, an increase of more than 57% from the previous resource calculation disclosed by Bre-X on April 17, 1996. This was the first resource calculation disclosed by Bre-X after it became a reporting issuer in Ontario.
>
> **The Defence agrees.**
>
> ...
>
> Para. 200. On July 22, 1996, Bre-X issued a press release disclosing a resource calculation of 46.92 million ounces of gold; an increase of more than 20% from the previous resource calculation disclosed by Bre-X on June 20, 1996.
>
> **The Defence agrees.**
>
> ...
>
> Para. 210. On December 3, 1996, Bre-X issued a press release disclosing a resource calculation of 57.33 million ounces of gold; an increase of more than 22% from the previous resource calculation disclosed by Bre-X on July 22, 1996.
>
> **The Defence agrees.**
>
> ...
>
> Para. 220. On February 17, 1997, Bre-X issued a press release disclosing a resource calculation of 70.95 million ounces of gold; an increase of more than 24% from the previous resource calculation disclosed by Bre-X on December 3, 1996.
>
> **The Defence agrees.**

Element B: The Press Releases Were Required To Be Filed By Bre-X Under Ontario Securities Law

There is no issue that the press releases were required to be filed by Bre-X under Ontario securities law. That is conceded by the Defence on page 4 of Exhibit S5 Volume II:

The Defence has conceded that the impugned Press Releases were required to be filed and will not comment further on this requirement.

Even without the above noted Defence concession, the evidence establishes that the press releases which are the subject matter of Counts 5 to 8 were required to be filed by Bre-X under Ontario securities law.

I agree with the Crown's submissions set out in paragraphs 11 to 16 which follow the Defence concession above:

> Para. 11. Section 75 of the Act imposes an obligation on a reporting issuer to issue a press release where a material change occurs in its affairs:
>
> > Subject to subsection (3), where a material change occurs in the affairs of a reporting issuer, it shall forthwith issue and file a news release authorized by a senior officer disclosing the nature and substance of the change.
>
> Para. 12. The press release must be authorized by a senior officer and disclose the nature and substance of the material change.
>
> Para. 13. "Material change" is defined in section 1.1 of the Act as:
>
> > ....when used in relation to the affairs of an issuer, means a change in the business, operations or capital of the issuer that would reasonably be expected to have a significant effect on the market price or value of the securities of the issuer and includes a decision to implement such a change made by the board of directors of the issuer or by senior management of the issuer who believe that confirmation of the decision by the board of directors is probable.
>
> Para. 14. Bre-X was required to issue a press release where a material change occurred in its affairs.

Para. 15. In *The Superintendent of Brokers v Pezim*, the Supreme Court of Canada held that a change in assay and drilling results can amount to a material change.

> In the mining industry, mineral properties are constantly being assessed to determine whether there is a change in the characterization of the property. Thus, **from the point of view of investors, new information relating to a mining property (which is an asset) bears significantly on the question of that property's value.** Accordingly, I agree with the approach taken by the Commission, namely that **a change in assay and drilling results can amount to a material change depending on the circumstances.**

Para. 16. The changes in Bre-X assay results and corresponding increases in its resource calculations were material changes in Bre-X's affairs.

As discussed later in these reasons (pages 81-84), the Supreme Court of Canada finding in The Superintendent of Brokers v. Pezim [1994] S.J.C. No. 58 (S.C.C.) (QL) (paragraph 87), "*that a change in assay and drilling results can amount to a material change depending on the circumstances*" is equally applicable to resource calculations.

Also as discussed later in these reasons (pages 84-85) I find that the discussion of forecasts found in Kerr v. Danier Leather Inc. [2005] O.J. No. 5388 (Ont. C.A.)(QL) is not applicable to resource calculations which are not forecasts.

Element C: The Press Releases Contained Statements That, In A Material Respect And At The Time And In The Light Of The Circumstances Under Which They Were Made, Were Misleading Or Untrue or Did Not State Facts That Were Required To Be Stated Or That Were Necessary To Make The Statements Not Misleading

The Impugned Press Releases State Resource Calculations And Not Drill Hole Results

The Defence agrees with paragraphs 20, 21, 25 to 28 of the O.S.C. submissions, Exhibit S5 Volume II. Paragraph 29 states:

> Para. 29. On February 17, 1997, Bre-X disclosed that there were 58 millions ounces of gold between lines 44 and 66. In March 1997, Strathcona drilled in the SEZ between lines 49 and 66.5. Representatives from Bre-X, Freeport and the Indonesian military were present during the drilling program. Strathcona confirmed Freeport's negative results and that there was no gold of economic interest in the SEZ.

With respect to that paragraph the Defence states:

> **The Defence disagrees. Bre-X never disclosed that there was 58 million ounces of gold.**

I agree with the Defence that the February 17, 1997 Bre-X press release (Exhibit RF 006) does not state "*there were 58 million ounces of gold*". It states that between section lines SEZ-44 and SEZ-69 (69 and not 66.5 as stated in paragraph 29) there were 30.49 million ounces "*Measured and Indicated*" and 27. 20 million ounces "*Inferred*" which totals approximately 58 million ounces "*measured and indicated*" and "*inferred*".

But the remainder of paragraph 29, in particular that "*Strathcona confirmed Freeport's negative results that there was no gold of economic interest...*" is correct.

In paragraph 24 the O.S.C. states:

> The subject press releases were misleading or untrue on the dates they were issued because the additional gold resources in the SEZ that Bre-X disclosed were simply not there. There is little to no gold in the SEZ. There is no gold of economic value in the CZ.

The Defence disagrees and states:

The Defence disagrees. The OSC has chosen to charge Mr. Felderhof with authorizing, permitting or acquiescing in the alleged commission of offences by Bre-X in the issuance of press releases that announce resource estimates. They consciously chose not to charge Mr. Felderhof with any press releases relating to the drill-hole results. Accordingly, the OSC must meet the burden that lies upon it to show that the resource estimates done by Kilborn and reported in the impugned Press Release were false or misleading. The burden of proof beyond a reasonable doubt is not satisfied by merely stating that there was no gold of economic value in the SEZ.

On that same issue of differentiating and contrasting press releases announcing resource calculations and press releases announcing drill hole results, the Defence states as follows starting at paragraph 3 of Tab E of Exhibit S3:

> Para. 3. The critical issues for consideration by this Honourable Court are:
>
> > (i) At the time of each press release, and in the light of the circumstances under which each press release was made, was each press release in a material respect:
> >
> > (a) misleading; or
> > (b) untrue; or
> > (c) incomplete because it did not state a fact that was required to be stated, or that was necessary, to make the statement not misleading?
>
> Each of these points are denied by the defence. Each resource estimate was a true resource estimate, performed by a well-known and reputable independent advisor to Bre-X, Kilborn, and in accordance with normal and accepted industry standards. Accordingly, they also were not misleading as they fairly set out the results of the work done by Kilborn in accordance with industry standards.
>
> ...
>
> Para. 6. The Court held [R. v. Maxwell, [1996] O.J. No 4832 (Ont. Ct. J.) (QL)]:
>
> > *Section 122(1)(b) prohibits making statements in financial statements that "in material respects" were misleading and untrue. The Securities Act does not define "material respect". The Oxford Dictionary defines "material" as "important, essential". Because it is not defined in the legislation I have concluded that the legislature intended it to have its ordinary dictionary meaning.*
>
> ...

Para.4. The *Securities Act* does not define "material respect", "misleading" or "untrue". The Canadian Oxford Dictionary defines these terms as follows:

> ***Material:*** *5. (Law) (of evidence, a fact etc.) significant, influential, esp. to the extent of determining a cause, affecting a judgment, etc.*
>
> ***Misleading:*** *giving the wrong idea or impression*
>
> ***Untrue:*** *contrary to what is the fact*

...

Para. 15. The statements contained in the Press Releases were not misleading, untrue or incomplete but were based upon all of the relevant facts known to Bre-X, its advisors and Mr. Felderhof when they were issued. They fairly set out the results of the work done by Kilborn in accordance with industry standards. The Press Releases do not purport to claim the existence of an actual gold reserve, nor do they promise a certain number of ounces of gold in the ground. Rather they provide the results of measured, indicated and inferred resource calculations, performed by Kilborn, a reputable independent advisor to Bre-X in accordance with accepted industry standards.

...

Para. 20. It is respectfully submitted that the Bre-X Press Releases were prepared using reasonable care and skill, were believed by the Board, and Mr. Felderhof to be reasonable and did not conceal any known fact that might have undermined the forecast. An estimate of a resource calculation can be considered to be true and correct even if it ultimately proves to be an incorrect estimate provided that, at the time the estimate is made, there was no reason to doubt the accuracy of the estimate. Neither Bre-X nor Mr. Felderhof is charged with having released false drill hole results. Mr. Felderhof is charged with authorizing, permitting or acquiescing in the release of a false or misleading resource calculation. Therefore, the critical issue is whether the Press Releases contained an assurance or representation by Bre-X that the gold is actually in the ground, in the amount set out in the press release, or whether it is merely an estimate that is reasonably based on Kilborn's work...

At paragraphs 11 to 14 of Exhibit S1:

Para. 11. In choosing to charge only Mr. Felderhof with authorizing, permitting or acquiescing in Bre-X's alleged commission of offences that relate to announcing false or misleading resource estimates, as opposed to any charges related to false or misleading drill hole results, the OSC must now prove that the resource estimate calculations done by Kilborn/SNC Lavalin ("Kilborn") were false or misleading. There is a strong argument that whether or not the drill hole data was false or misleading should be irrelevant. The OSC cannot argue that

Bre-X and Mr. Felderhof knew or ought to have known that the drill results were false or misleading- because they chose not to charge him with the January 13, 1997 press release or those portions of the July 22, 1996 press release that disclosed drill hole results.

Para. 12. This case is therefore very different from the facts and circumstances which underlay the Supreme Court of Canada's decision in *Pezim v. British Columbia (Superintendent of Brokers)*, as in that case the Court was asked to consider whether the drill hole results themselves could constitute material facts or material changes.

Para. 13. The OSC could have followed the same path as *Pezim* but chose to ignore the Bre-X press releases that disclosed the actual drill hole results and instead focused solely on the press releases that disclosed Kilborn's resource estimates. It is respectfully submitted that this choice fundamentally changes the nature and assessment of the underlying requirements for the commission of an offence by Bre-X as it relates to Counts 5 to 8.

Para. 14. Although Mr. Felderhof's detailed argument on the underlying primary "charges" against Bre-X will be made in the Main Argument, for present purposes it is sufficient to say that there is no evidence that the resource estimates were wrong- indeed based upon the information that Bre-X and Kilborn had at the time they are true and correct in all material respects. The analysis of the primary "charges" will require a determination by this Court of the simple but fundamental question: what exactly are the Press Releases saying? The OSC must argue that in pith and substance the Press Releases contain an express or implied representation by Bre-X that a certain amount of gold was actually in the ground at Busang and that such an unexpressed statement can be a material fact or material change of such certainty that charges can be brought based on it. The Court now knows that the Press Releases accurately and carefully set out Kilborn's estimates and calculations. In addition, as it is not known how much gold is yet to be found in Busang, there is no way to know with certainty if the resource estimates are wrong and, if so, how wrong they might actually have been.

At paragraph 38 of Exhibit S2:

Para. 38. The OSC also never puts forward an argument as to why the Bre-X Press Releases were misleading or untrue when all they do is fairly and accurately report the Kilborn estimates. They also do not address the argument that the resource estimates prepared by Kilborn are, in fact, true.

The Superintendent of Brokers v. Pezim

In Pezim, supra, the Supreme Court of Canada states at paragraphs 85 to 89:

> Para. 85. The Commission's conclusion that s. 67 was violated in the context of the share options transactions can be subdivided into two parts. The first element of the conclusion is that undisclosed drilling results can constitute a material change in the affairs of a reporting issuer. Locke J.A. of the Court of Appeal agreed. Lambert J.A., however, writing for the majority of the Court of Appeal, was of a different view. He held at p. 268 that information obtained from assay results cannot constitute a material change:
>
> > In my opinion, geological information obtained from observations of visible matter and geological information from drill cores in the form of assay results, or in the form of a properly plotted plan prepared from the results of a number of assays, are all capable of being material facts. Let us assume that the geological information relied upon by the commission constituted material facts in this case. That does not mean that the same geological information constituted material changes. In my opinion, geological information of the nature obtained on a continuing basis as a result of a planned drilling program does not constitute a change in the business, the operations, the assets or the ownership of the issuer, no matter what information is obtained from the drilling results. Such information may constitute a basis for a perception that there has been a change in the value of an asset. But that is a far different thing than a change in an asset. [Emphasis added]
>
> Para. 86. As already mentioned, the determination of what constitutes a material change for the purposes of general disclosure under s. 67 of the Act is a matter which falls squarely within the regulatory mandate and expertise of the Commission. Consequently, when the majority of the Court of Appeal rejected the Commission's findings on this matter, it fell into error. Furthermore, the majority's view on this point is, in my opinion, clearly wrong and is inconsistent with the economic and regulatory realities the Act sets out to address. Counsel for the respondents conceded this point, during the hearing of this appeal, and stated that "information from a drilling program can be tantamount to a material change".
>
> Para. 87. In the mining industry, mineral properties are constantly being assessed to determine whether there is a change in the characterization of the property. Thus, from the point of view of investors, new information relating to a mining property (which is an asset) bears significantly on the question of that property's value. Accordingly, I agree with the approach taken by the

Commission, namely that a change in assay and drilling results can amount to a material change depending on the circumstances.

Para. 88. George C. Stevens and Stephen D. Wortley, authors of "Murray Pezim in the Court of Appeal: Draining the Lifeblood from Securities Regulation" (1992), 26 U.B.C.L. Rev. 331, are of the same view. In commencing on the above quoted passage, they stated the following at pp. 336-37:

> To the geologist or the mining property valuator, Lambert J.A.'s statement is astonishing. Every mine starts from host rock. Every drill hole leads not merely to a change of perception of the asset: it is a piece in the puzzle that ultimately determines whether the asset is moose pasture or ore. Each new result may change the characterization of the asset from rock, to mineral deposit, to inferred ore, to probable ore and ultimately, with enough holes supported by a feasibility study, to proven ore.
>
> Even more astonishing was the Court's conclusion, without receipt of any evidence, that drilling results would never constitute a change in the operations or assets of an issuer.
>
> ...
>
> Can the Court really suggest that there has not been a change in a company's assets when, following adequate sampling, a discovery is made on a portion of its property that had been previously categorized as having no known mineralization? Surely, given the basic aim of the Act – to protect the investing public through full, true and plain disclosure of all material facts relating to securities –one could conclude (as did Mr. Justice Locke, the dissenting judge) that the Commission did not make a "plain and vital mistake" in the application of the words in s. 67 of the Act to the facts before it...

Para. 89. Consequently, I am of the view, as found by the Commission and Locke J.A., that the assay results constituted a change with respect to or in the companies' assets and is "material" for the purposes of the Act.

In Pezim the Supreme Court of Canada is dealing with assay and drilling results.

The Defence argues the case at bar is different because the Defendant is not charged with offences related to misleading or untrue drill holes results but with offences related to

misleading or untrue resource calculations and as the press releases accurately set out Kilborn's resource calculation they are not misleading or untrue.

The Supreme Court of Canada above quotes Stevens and Wortley with approval and I repeat that quote here:

> Every drill hole leads not merely to a change of perception of the asset: it is a piece in the puzzle that ultimately determines whether the asset is moose pasture or ore. Each new result may change the characterization of the asset from rock, to mineral deposit, to inferred ore, to probable ore and ultimately, with enough holes supported by a feasibility study, to proven ore.

Stevens and Wortley referred to *"inferred"*, *"probable"*, and *"proven ore"* while the Bre-X press releases referred to *"measured"*, *"indicated"* and *"inferred resources"* but they are both references to resource calculations. The investing public is not protected by the work done by Kilborn even though done to industry standards, if that work is based on incorrect assay results as a consequence of salting of the core samples resulting in misleading or untrue resource calculations.

If a drill hole result is material then a resource calculation based on that drill hole result is material. If a drill hole result is misleading or untrue then a resource calculation based on that drill hole result is misleading or untrue.

Of note here is the evidence of Paul Semple (see page 143 of these reasons), Vice President Mining and Metallurgy at Kilborn:

> Q. And you would agree with me that the quality of Kilborn's resource calculations could only be as good the data that Bre-X provided?
>
> A. Yes.

Q. And you would agree with me it's garbage in/garbage out?

A. Yes.

Transcript: January 25, 2006, page 80

Although as noted above Pezim specifically deals with assay and drilling results, the Supreme Court of Canada states in paragraph 87 that "*new information relating to a mining property (which is an asset) bears significantly on the question of that property's value.*" The reference is to "*new information*" generally which would include resource calculations.

I find no merit in this Defence submission.

Kerr v. Danier

The Defence relies on Kerr v. Danier, supra, in the Ontario Court of Appeal, as set out in paragraphs 7 to 20 of Tab E of Exhibit S3. Kerr is a case with respect to substantially different and distinguishable sections of the Ontario *Securities Act*. Kerr is a case with respect to s. 130(1) which deals with statutory civil liability for prospectus "*misrepresentation*". The definition of "*misrepresentation*" in s.1.(1) was central to the appeal. In 1994, s. 122(1)(b) was amended to take out the prior reference to misrepresentation. The significance of that is set out by Reinhardt J. in R. v. Maxwell [1996] O.J. No. 4832 (Ont.Ct.J.)(QL), at paragraphs 119 and 120:

> Para. 119. The defence argues that the 1990 Act in Section 122(1)(b) requires a "misrepresentation", which is defined as an "untrue statement of material fact or an omission to state a material fact." Material fact in turn is defined as "a fact that

> significantly affects, or would reasonably be expected to have a significant effect on, the market price or value of such securities".
>
> Para. 120. The 1994 Act in Section 122(1)(b) requires a lesser standard, namely, a statement "that in a material respect and at the time and in the light of the circumstances under which it is made, is misleading or untrue or does not state a fact that is required to be stated or that is necessary to make the statement not misleading".

Kerr deals with a forecast in a prospectus. The Defence submits a resource estimate is similar to a forecast. I disagree. The press releases are not forecasts but statements of present, not future, resource calculations based on tampered drill hole results. They are statements which are misleading or untrue at the time they are released and not forecasts of future results.

In Kerr, (at paragraph 157) the Court applied the business judgement rule because as that case states *"[a] forecast is a quintessential example of the exercise of business judgement*". As noted above the case at bar does not deal with a forecast but with the prosecution of a strict liability offence of releasing a misleading or untrue statement.

FINDING

I find that the four impugned Bre-X press releases contained statements about resource calculations that, in a material respect and at the time and in the light of the circumstances under which they were made, were misleading or untrue.

Element D: The Defendant Director Or Officer Authorized, Permitted Or Acquiesced In The Issuance Of The Press Release

Felderhof Was An Officer And Director Of Bre-X

There is no issue that the Defendant was an officer and director of Bre-X at the material times.

The Defence agrees with paragraph 35 of Exhibit S5 Volume II:

> Para. 35. As also previously discussed in Count 1, Element A, Felderhof was an officer and director of Bre-X during the relevant time.

The Defence agrees.

With respect to this issue I accept the O.S.C. statements at paragraphs 7 to 11 of Exhibit S8:

> **(a) Felderhof was a director and officer of Bre-X during the relevant period**
>
> Para. 7. Bre-X became a reporting issuer in Ontario under the Act on April 23, 1996, when it began trading on the Toronto Stock Exchange.
>
> > "reporting issuer" means an issuer,
> >
> > (c) any of whose securities have been at any time since the 15th day of September 1979 listed and posted for trading on any stock exchange in Ontario recognized by the Commission, regardless of when such listing and posting for trading commenced.
>
> Para. 8. On May 1, 1993, Bre-X hired Felderhof as its General Manager for a term of five years. As a General Manager, Felderhof became an officer under the Act:

> "officer" means the chair, any **vice-chair of the board of directors**, the president, any vice-president, the secretary, the assistant secretary, the treasurer, the assistant treasurer, and the **general manager** of a company, and any other person designated an officer of a company by by-law or similar authority, or any individual acting in a similar capacity on behalf of an issuer or registrant;

Para. 9. On October 5, 1994, Felderhof was appointed Senior Vice-President of Exploration.

Para. 10. On May 10, 1996, he joined the Bre-X Board of Directors as Vice-Chairman. As Vice-Chairman of the board, Felderhof became a director under the Act.

> "director", where used in relation to a person, includes a person acting in a capacity similar to that of a director of a company

Para. 11. Felderhof concedes that he was an officer and director for Counts 5 to 8.

The Defendant was senior vice-president of exploration and the general manager and the only director and senior officer in Indonesia. See page 110 of these reasons.

As noted above there is no issue that Bre-X issued the press releases which are the subject matter of Counts 5 to 8.

The issue is whether the evidence of the Defendant's involvement proves beyond a reasonable doubt that the Defendant 'authorized, permitted or acquiesced in' the commission of an offence by Bre-X under subsection (1) of section 122. In the context of this discussion the issue is whether the Defendant 'authorized, permitted or acquiesced in' Bre-X's issuance of the press releases.

The submissions with respect to the evidence of the Defendant's involvement in the issuance of the four press releases is found almost exclusively in the written rather than the oral submissions.

They are found at:

Exhibit S1-paragraphs 29 to 101.
Exhibit S8- paragraph 6 to 172.
Exhibit S2 -paragraphs 1 to 28.
Exhibit S5 Volume II –paragraphs 6 to 229.

These written submissions set out in detail the general background facts with respect to the issuance of the gold resource press releases at Bre-X and the specific facts with respect to the four press releases in issue.

It is not necessary to review in detail all of these submissions except to say that in coming to my conclusions I have given substantial consideration to them. They tell a story even where counsel disagree on interpretations. They form the background to my reasons.

DID FELDERHOF AUTHORIZE, PERMIT OR ACQUIESCE IN THE PRESS RELEASES

I will now consider the evidence whether Felderhof 'authorized, permitted or acquiesced in' issuing a press release which is specific to each of the four impugned press releases.

The June 20, 1996 Press Release

There is no doubt that the Defendant was involved in the preparation of a resource calculation press release for sometime in June 1996 with the intention of issuing it. See Exhibit S1 paragraphs 35 to 47 and Exhibit S5 Volume II, paragraphs 88-105.

The Defence disagrees with parts of paragraph 101 of Exhibit S5 Volume II, which states:

> Para. 101. On June 18, 1996, McAnulty sent a draft press release to Felderhof for his changes and exclusions. McAnulty testified that the geological data for this press release or the draft press release itself came from Felderhof.

The Defence disagrees with the O.S.C. position that geological data for the press release came from the Defendant:

> **The Defence disagrees. As the OSC stated in the previous paragraph, the resource calculations were forward by Kilborn to Bre-X. The actual exchange relied upon by the OSC in support of their argument in this paragraph that the information actually came from Mr. Felderhof is instructive of the care that must be given in relying upon the evidence of Mr. McAnulty in isolation.**

McAnulty was a Bre-X executive in Investor Relations working in the Calgary head office.

In cross-examination McAnulty appears to agree with the Defence position that the data originally came from Kilborn in a fax to David Walsh with copies to Felderhof and others and that that fax was turned into a press release and sent to Felderhof for review.

Transcript: August 17, 2005, pages 25-26

That is not an important distinction for the purposes of s. 122(3). If an officer or director authored a press release than he or she would certainly be found to have 'authorized, permitted, or acquiesced in' the press release. But an officer or director could certainly 'authorize, permit or acquiesce in' a press release without having authored it or provided the data for it.

What is important and conclusive is the Defendant's approval of the draft press release in a fax from the Defendant to McAnulty dated June 18, 1996 (Exhibit 1146). The Defendant wrote "*Your calculations are correct*" with respect to the resource calculations which are the same resource calculations that appear in the press release issued two days later on June 20, 1996 announcing measured, indicated and inferred resources totalling 39.15 million ounces of gold as set out in Count 5.

In commentary with respect to paragraph 108 of Exhibit S5 Volume II, the Defence states in part:

> **The O.S.C. must prove that Mr. Felderhof authorized, permitted or acquiesced in the Press Release that was issued; not some earlier or draft version.**

In Exhibit S1 the Defence also states at paragraph 44 and 47:

> Para. 44. Mr. McAnulty testified that he sent a draft of the press release via fax to Mr. Felderhof for his "changes and/or exclusions, inclusions, whatever...". Mr. McAnulty said that Mr. Felderhof's handwritten response appears on a return fax dated June 18. Mr. Felderhof's handwriting states that Mr. McAnulty's calculations in the resource estimate summary table were correct. Mr. Felderhof also requested that the press release state that Bre-X was using the cyanide leach assay method. Mr. McAnulty testified that Mr. Felderhof's request to refer to the cyanide leach assay method appears in the June 20 press release. There are, however, significant differences between the one page June 19 draft commented on by Mr. Felderhof and the actual June 20 two page press release that was issued, including the title and the entire second page.

...

> Para. 47. As there was no evidence that Mr. Felderhof ever saw, or commented on the June 20, 1996, press release in its final form, and as there were significant changes from the draft he saw, it cannot fairly be said that he authorized, permitted or acquiesced in the release of Bre-X's June 20 press release. Even on the OSC's view of the case, "you can't consent to something about which you don't know".

The Defence position noted above is different than the position taken in oral submissions at pages 46 to 48 of the transcript of August 22, 2006:

> MR. GROIA: At the beginning of her argument, Ms. Cole took you to the charges and she said that she wanted you to look at the press releases as well as the charges, and that the press releases had other things in them that she mentioned were – I think she called them "context" on one occasion and "background" on another. And if that's all that the press releases contain, other than the representation about the amount of gold, then we're exactly at the same place and there's no disagreement between us.
>
> But if there's something more, then what I'd ask Your Honour to consider is that way back at the beginning of this case we went in front of Justice Hogan asking for particulars and one of the things that happened was on August 25, 1999, the charges were amended, counts 5 to 8 were amended and the amendment made clear, was intended to make clear, that the only aspect of the press releases that is the subject matter of the statement, so the only thing that we're arguing about is true or untrue, are the "measured, indicated and inferred" calculations that were done by Kilborn. So to the extent, for example, that some drill hole results were announced in the press release, those are not part of the charges before the Court, even though they're in a press release which is part – which forms part of the basis for a charge before the Court. S [sic] I wanted to emphasize that, and if there's any issue about it, then I'll develop those submissions further.
>
> But the charges make it clear that it's Bre-X made a statement in a press release, to wit, announcing measured, indicated and inferred. So the charges are limited only to those parts of the press releases announcing measured, indicated and inferred calculation. And that was – somewhere we have the transcript in front of Judge Hogan, and that was the basis of the amendment and I just want to make sure that I emphasize that.

I'm not objecting in any way of course to looking at the whole press release for whatever other reason. That's not the charge that we're dealing with.

THE COURT: But the other side of the coin there is that in terms of proving authorizing, permitting and acquiescing, the Crown then only has to prove that Mr. Felderhof authorized or permitted this statement –

MR. GROIA: Correct.

THE COURT: - as opposed to –

MR. GROIA: - the other statement.

THE COURT: - The other statements in the press releases.

MR. GROIA: It doesn't matter who authorized them.

THE COURT: So when I am looking at the facts [sic, faxes] as they are going back and forth – because you are arguing he did not authorize and the Crown says he did authorize – when I am looking at those faxes, then I only have to be concerned about the discussion about the resource calculation.

MR. GROIA: And whether he approved or agreed to have the press release go out. Because in one press release he says "I want to talk to Mike about it", so he's saying don't put out any press release. But I agree, if there was –

THE COURT: Just to give you an example, if there was a first draft which had the resource calculation in it and Mr. Felderhof saw that and agreed to that, but then there were a second, and third and fourth and fifth draft which may have changed other things, and which Mr. Felderhof may never – there may not be evidence that he actually saw the second, third and fourth, but he had agreed to the resource calculation in the first draft, and the final draft, with whatever other variations it has, has that resource calculation –

MR. GROIA: And it hasn't been changed.

THE COURT: - and the resource calculation is the same resource calculation, that is all the Crown has to prove.

MR. GROIA: I would agree with that as long as, at the very beginning, he also approved putting that resource calculation out. I agree with that.

In the submissions above the Defence agrees that if the Defendant agreed to a resource calculation in a draft press release, it did not matter if the Defendant did not see the final press release if the resource calculation was the same and the Defendant had agreed at the beginning to release the resource calculation.

I find that is the correct test to apply. The Defendant is charged with 'authorizing, permitting or acquiescing in' the commission of an offence by Bre-X of making a misleading or untrue statement announcing measured, indicated and inferred resources totaling 39.15 million ounces of gold (See Count 5). There is no allegation with respect to what is stated on page two of the press release (the resource calculation is on page one) and the O.S.C. is not required to prove the Defendant 'authorized, permitted or acquiesced in' what is on page two with respect to which the Defendant is not charged.

When a director or officer 'authorizes, permits or acquiesces in' the company making an alleged misleading or untrue statement, it is not relevant that thereafter, before release, the statement is edited, or the format is changed or other information is added or taken out if it does not alter the meaning of the impugned part of the statement or is unrelated to the allegations. The test is whether the misleading or untrue impugned statement made by the company is in substance and in essence the statement 'authorized, permitted or acquiesced in' by the director or officer.

In paragraph 16 of Exhibit S2 the Defence submits:

> Para. 16. By focusing solely on Mr. Felderhof's role, the OSC argues that he was responsible for 'initiating', 'monitoring', 'planning' and 'authorizing' the June 20,

> 1996 press release. In doing so they do not fairly present the participation by the various members of Kilborn, and the roles that Mr. McDonald, Dr. Kavanagh and Mr. McAnulty played in this press release. For example, Mr. McAnulty admitted that for this press release, he had a series of fairly extensive discussions with Dr. Kavanagh, that were "editorial in nature".

As noted earlier who authored the press release and who else participated in drafting the press release is not determinative of the culpability of the director or officer. The issue is whether the director or officer 'authorized, permitted or acquiesced in' the making of the statement.

I have set out the dictionary definitions of '*authorize*', '*permit*' and '*acquiesce*' at page 69 of these reasons.

FINDING

Given the evidence of Felderhof's participation in the creation for release of the June 20, 1996 press release and his approval of the resource calculation in Exhibit 1146, I find Felderhof 'authorized, permitted or acquiesced in' the issuance of the June 20, 1996 press release.

The July 22, 1996 Press Release

The Defence submissions with respect to this press release are found at paragraphs 48 to 64 of Exhibit S1 and paragraphs 18 to 20 of Exhibit S2. The O.S.C. submissions and Defence comments are at paragraphs 110 to 139 of Exhibit S5 Volume II.

In paragraph 132 of Exhibit S5 Volume II the O.S.C. states and the Defence comments as follows:

Para. 132. Felderhof clearly knew that July 22, 1996 press release was going to be issued as evidenced by his fax to Barbara Horn, the Registered Representative in his Nesbitt Burns trading account. On July 20, 1996 in Jakarta, Felderhof told Horn that he had telephoned Natasha the day before to suspend any trading until further notice because Bre-X was issuing a press release on Monday (July 22, 1996) or Tuesday (July 23, 1996) and that he would notify them when to resume trading.

> "*Dear Barbara*
>
> *Yesterday, I phoned Natasha to suspend any further trading until further notice as we will be issuing a press release Monday or Tuesday. I will notify when to resume.*
>
> *Best Regards,*
> *J.B. Felderhof*"

The Defence agrees that fax is accurately quoted.

In stating "***we** will be issuing a press release*" (emphasis added) in Exhibit 1047 Tab 1275 above, the Defendant is referring to a press release being issued by Bre-X including himself as a director and officer.

This is a statement by the Defendant that he is 'authorizing, permitting or acquiescing in' the issuance of a press release on July 22 or 23, 1996.

The Defence submits there is some doubt as to the contents of the press release the Defendant in fact 'authorized, permitted or acquiesced in'.

Starting in late June 1996, the Defendant wanted Bre-X to issue another resource press release. See paragraphs 49 to 52 of Exhibit S1 and paragraphs 110 to 118 of Exhibit S5 Volume II.

On July 13, 1996 Kilborn faxed the resource calculation for SEZ-44 to SEZ-69, which was included in the July 22, 1996 press release to David Walsh with copies to Felderhof, de Guzman and M. Puspos. See paragraphs 53 and 54 of Exhibit S1, paragraph 119 of S5 Vol. II and Exhibit 1106 Tab 41.

On July 18, 1996 MacDonald sent Francisco a fax stating "*Rolly: Final draft of Monday's press release follows. JBF has checked it.*" See paragraph 121 of Exhibit S5 Volume II and Exhibit 1115. That fax, after other portions were expunged, was admitted as a business record for the truth of its contents in my business records ruling of September 22, 2005.
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Exhibit 672 is a draft of the July 22, 1996 press release titled "*very FINAL DRAFT – REVIEWED BY JBF*". The Defence submits there is no evidence that Exhibit 672 is the version of the press release referred to in Exhibit 1115 above and that in any event it is different than the final press release issued on July 22, 1996. See paragraph 57 of Exhibit S1 and paragraphs 122 to 124 of Exhibit S5 Volume II.

Although Exhibit 1115 refers to the "*Final draft*", on the next day July 19, 1996, MacDonald (Exhibit 1158), in response a fax from McAnulty dated July 18, 1996 (Exhibit 1157), sent McAnulty corrections to the final press release. See paragraph 56 of Exhibit S1 and paragraphs 125 to 127 of Exhibit S5 Volume II. Also on July 19, 1996

MacDonald (Exhibit 239) faxed McAnulty further changes from Felderhof. This shows that the "*Final draft*" (Exhibit 1115) was not in fact "*Final*".

What is of more significance though is that the total of the measured, indicated and inferred resources of 46.92 million ounces of gold alleged in Count 6 and found in the final press release is also found in Exhibit 672 ("*very FINAL DRAFT-REVIEWED BY JBF*") and in the draft press release sent by McAnulty (Exhibit 1157) and in the corrections by MacDonald (Exhibit 1158).

Felderhof takes no issue with Kilborn's resource calculations in this or any of the other press releases or their drafts which contained the same resource calculations as the final press releases. Kilborn prepared the resource calculations which then went into the draft press releases and eventually into the final press releases. Misleading or untrue resource calculations are the substance of Counts 5 to 8.

Also of significance is that at the time of Felderhof's fax to Horn on July 20, 1996 that "*we will be issuing a press release*", the press release was already finalized and a copy already sent to the Toronto Stock Exchange on July 19, 1996. See paragraph 134 of Exhibit S5 Volume II and Exhibit 1159.

As noted above on July 19, 1996 (Exhibit 239) MacDonald faxed further changes from Felderhof to McAnulty. McAnulty put in a paragraph requested by Felderhof but did not

take out the individual drill hole results as Felderhof also requested. See paragraphs 58 to 63 of Exhibit S1 and paragraphs 128 to 130 of Exhibit S5 Volume II.

The Defence position is that if the Defendant did not want the individual drill hole results included in the press release and the final press release included the individual drill hole results, as it did, then the Defendant did not 'authorize, permit or acquiesce in' the July 22, 1996 press release.

The Defence submits that McAnulty's evidence that Felderhof acquiesced in including the individual drill hole results in the press release is uncertain and equivocal. See paragraph 130 of Exhibit S5 Volume II.

I agree that McAnulty's evidence is not as clear as it could have been but there is other evidence of Felderhof's acquiescence found in his fax to Barbara Horn where on the day after the request to take out the drill hole results the Defendant stated (Exhibit 1047, Tab 1275) "*we will be issuing a press release*" and a press release is issued on July 22, 1996 including the individual drill hole results.

But as noted above (at page 89-93) in the discussion of the June 20, 1996 press release what is important is the Defendant's acquiescence in making the statement that is the basis of the charge, the resource calculations, and not whether the Defendant acquiesced or not in making a statement about another matter, for example here the drill hole results which are not part of the charge.

What is significant is that in Exhibit 239 Felderhof is not asking for a change to the total resource calculations of 46.92 million ounces of gold found in Count 6 and in the final press release and in all of the draft press releases but asking for a change to information not related to the allegations, that is, not to include individual drill hole results.

FINDING

I find Felderhof 'authorized, permitted or acquiesced in' the issuance of the July 22, 1996 press release.

I would add that where a director or officer 'authorizes, permits or acquiesces in' a specific press release as here ("*we will be issuing a press release Monday or Tuesday*") and the O.S.C. proves the press release was issued as the O.S.C. has done here, the O.S.C. does not have to prove anything further. It is not open for the director or officer to argue that although he or she 'authorized, permitted or acquiesced in' the issuance of the press release, he or she is not culpable because he or she did not fulfill his or her duties as a director and officer and did not review the contents of the press release that was in fact released.

The December 3, 1996 Press Release

The Defence submissions with respect to this press release are found at paragraphs 65 to 73 of Exhibit S1 and paragraphs 21 to 23 of Exhibit S2. The O.S.C. submissions and Defence comments are at paragraphs 141 to 162 of Exhibit S5 Volume II.

At paragraphs 65, 67 and 72 of Exhibit S1 the Defence submits:

Para. 65. There was very little evidence presented at this trial about the December 3, 1996 press release. There is no evidence that Mr. Felderhof played any role in the drafting or reviewing of the December 3, 1996 press release or that he authorized, permitted or acquiesced in its issuance.

...

Para. 67. Mr. McAnulty reviewed a fax from Mr. Felderhof containing "add ons" for a news release on December 1, 1996, which was sent to Mr. McAnulty and Mr. Walsh. Mr. McAnulty testified that the December 3, 1996 press release issued by Bre-X does not reflect Mr. Felderhof's draft.

...

Para. 72. During cross-examination, Mr. McAnulty was asked to confirm that no faxes were sent to Mr. Felderhof concerning this press release. Mr. McAnulty replied that he could not comment on what transpired with every press release. There was no evidence called by the O.S.C. to indicate that Mr. Felderhof saw this press release before it was issued.

The Defence agrees with O.S.C. paragraphs 153 to 155:

Para. 153. On November 15, 1996, Kilborn issued the Intermediate Feasibility Study. The same 57.33 million ounces of gold resource calculation that Bre-X disclosed in the December 3, 1996 press release is on pages 2 to 4.

The Defence agrees.

Para. 154. On December 1st, 1996, Felderhof sent to Walsh and McAnulty four pages of "*add ons*" for a press release. Felderhof's "*add ons*" about his team's review of the Kilborn Intermediate Feasibility Study and the resource calculation table were included in the December 3, 1996 press release.

The Defence agrees that the fax referred to contains Mr. Felderhof's suggested add ons for the December Press Release and that comments about the Kilborn Intermediate Feasibility Study and a resource calculation table were included.

Para. 155. The remainder of Felderhof's "*add ons*" were about his concerns about a November 29, 1996 Globe and Mail article that reported that Bre-X shareholders were concerned about the negotiations between Bre-X and Barrick. Felderhof felt the news story ridiculed Bre-X and publicly insulted Sigit Harjojudanto of PT Panutan Duta. Sigit Harjojudanto is the son of Indonesia's President Suharto.

The Defence agrees that Mr. Felderhof's "add ons" also addressed some of his concerns arising from the Globe & Mail article.

There is no issue that the Defendant had knowledge of the Kilborn resource calculation found in the Intermediate Feasibility Study or that he knew they were included in the draft and final December 3, 1996 press releases. The Defendant's "*add ons*" in Exhibit 462 dated December 1, 1996 are "*add ons*" to a draft press release containing the measured, indicated and inferred resources totaling 57.33 million ounces of gold originally released by Kilborn on November 15, 1996 and found in Count 7 and in the final press release.

FINDING

It is not important that the Defendant's "*add ons*" were not included in the press release. What is important is that the Defendant was actively participating in the issuance of the press release without questioning the resource calculation. See discussion above at pages 89-93 with respect to the June 20, 1996 press release and at pages 98-99 with respect to the July 22, 1996 press release.

I find Felderhof 'authorized, permitted or acquiesced in' the issuance of the December 3, 1996 press release.

The February 17, 1997 Press Release

The Defence submissions with respect to this press release are found at paragraphs 74 to 101 of Exhibit S1 and paragraphs 24 to 28 of Exhibit S2. The O.S.C. submissions and Defence comments are at paragraphs 163 to 199 of Exhibit S5 Volume II.

Paragraphs 182 to 185 of Exhibit S5 Volume II state:

Para. 182. On January 23, 1997, Kilborn sent de Guzman an updated resource calculation for the SEZ based on the exploration drilling results available as of January 15, 1997. Felderhof, MacDonald and Francisco were copied on this fax. The 70.95 million ounces of gold resource calculation Kilborn sent to Bre-X on January 23rd, 1997 is the same as the one disclosed in the February 17, 1997 press release.

The Defence agrees that Kilborn forwarded the updated resource calculation and that the Kilborn resource estimate in the February 17, 1997 Press Release is 70.95 million ounces.

Para. 183. On January 28, 1997, de Guzman sent Felderhof an "URGENT NOTE" in which he stated that the latest resource calculation was on Felderhof's desk. He faxed it to Villa Capri, Fisher Island in Florida where Felderhof was vacationing. Clearly he thought the information he had to convey, including the fact that the resource calculation had arrived, was significant enough to disturb Felderhof while he was on vacation.

> Dear John,
>
> Sorry to disturb you, but I need to relay info – item A.
>
> A. Our Geology building + 3 other units got burned last week at Busang base camp. No one informed me because I was at the hospital.
>
> I will travel tomorrow morning to size up the damage and keep up the spirit of our personnel
>
> I will be back 1 February. No need to worry, my health OK.
>
> B. Placer Dome – 2 sets of reports available to be delivered by Kilborn by 2 p.m. today. Only 1 set copy left at the mess which is my working copy with notations.
>
> C. Latest resource calculation report by Sophie now available, 2 copies at your desk and 1 copy on my file.
>
> All other matters upon you arrival in Jakarta.
>
> Best regards,
> Mike de Guzman

The Defence agrees that the fax as quoted is accurate, but notes that the likely reason for the urgency of the fax was the fire at Busang, not the resource calculations as suggested by the O.S.C.

Para. 184. In paragraph 87 of the Defence factum, the Defence suggests that there is no direct evidence that Felderhof received the January 23, 1997 letter from Kilborn enclosing the resource calculation and in any event, he was in the Cayman Islands on January 15 and then in Florida on January 27, 1997.

The Defence agrees.

Para. 185. On February 5, 1997, Felderhof returned to Indonesia for one month. In paragraph 92 of the Defence factum, the Defence concedes that Felderhof was in Jakarta on February 5, 1997.

The Defence agrees that it states that Mr. Felderhof was in Jakarta on February 6 (not 5) 1997. There is no evidence cited in support of the contention of the OSC that Mr. Felderhof was in Indonesia for one month, so the Defence cannot comment.

On January 23, 1997 Kilborn sent de Guzman the updated resource calculation of 70.95 million ounces of gold which is also found in the February 17, 1996 press release and in Count 8. Kilborn sent copies to Felderhof, MacDonald and Francisco. See Exhibit 181. On January 28, 1997 de Guzman faxed Felderhof who was on vacation in Florida, that the latest resource calculation was on Felderhof's desk. See Exhibit 1188. On February 6, 1997 Felderhof returned to Jakarta. See paragraph 185.

There is a strong circumstantial case that Felderhof received the Kilborn resource calculation. In any event as discussed later there is evidence the Defendant reviewed at least a draft press release which would have contained the Kilborn resource calculation.

Paragraphs 189 and 190 of Exhibit S5 Volume II state:

> Para. 189. On February 7, 1997, McAnulty sent Felderhof a fax asking him to review a draft press release for February 17, 1997 with particular reference to

accuracy in the table. The table contains the same 70.95 million ounces of gold resource calculation that was discussed in the February 17, 1997 press release.

The Defence agrees that Mr. Felderhof was asked by Mr. McAnulty to review the draft and the table for accuracy. The 70.95 million ounce resource calculation is handwritten on the draft.

Para. 190. McAnulty testified that he thought that Felderhof phoned him in response. He speculated that perhaps Felderhof did not have a fax machine where he was. Felderhof was at Busang from February 7 to 9, 1997.

> *A.* Well, it appears that way, yeah. I don't know whether I'm sending him the unmarked or unchanged document and then I got the changes over the phone because they're in my handwriting. You know, but I mean obviously we're trying to get this release out and I probably sent him the copy that has not been changed yet. He's either given me the changes verbally over the phone what's confusing about this is it's his handwriting on the top and my handwriting in the table.
>
> Q. Okay.
>
> A. I don't quite remember how that would have occurred. The only thing I can think of is he sent it back to me and then phoned me and said here change this, change that. Maybe he didn't have a fax machine where he was. I don't know. But you know, obviously he sent it back to me. He does say to Steve per DW, so DW is David Walsh, so obviously things were communicated to me verbally and David faxed the press release to me. That's all I can think of.

The Defence agrees that this is an accurate quote from the transcript.

In the comments to paragraph 189 the Defence agrees Felderhof was asked by McAnulty to review the draft press release and table for accuracy although in paragraphs 26 and 27 of Exhibit S2 the Defence submits that that fax (Exhibit 1106 Tab 112, Exhibit 1191) was sent to the Cayman Islands (see fax number on Exhibit 1106 Tab 112) while

Felderhof was in Indonesia (See paragraph 185 and 190 of Exhibit S5 Volume II and Exhibit 1052 Tab 1609) and that the evidence of McAnulty was vague and that there was no other evidence cited that Felderhof ever received the draft press release.

There is corroboration that Felderhof reviewed a draft press release in Exhibit 1192 where in a fax from McAnulty to MacDonald dated February 7, 1997 there is a reference to "*per John: draft P.R.*". See paragraph 191 of Exhibit S5 Volume II.

Also in the fax dated February 12, 1997 from Felderhof to Walsh (Exhibit 1052 Tab 1613) Felderhof states:

> Mike de Guzman is still in Singapore for a health check up as he had a major malaria attack last week. Therefore, please do not put out the release until I have gone over it with Mike. He should be back this Friday. Sorry for the inconvenience.

I find that in this fax Felderhof is referring to a release in his possession which he wants to review with de Guzman and which would have had the resource calculation of 70.95 million ounces of gold. It is significant that the resource calculation from Kilborn and the draft press releases and the final press release all refer to the 70.95 million ounces of gold which is the total set out in Count 8.

The Defence submits that there is no evidence that Felderhof 'authorized, permitted or acquitted in' the issuance of the February 17, 1997 press release but that in fact the evidence is the opposite and that Bre-X issued the press release contrary to Felderhof's request "*not [to] put out the release*" in the fax above (Exhibit 1052 Tab 1613) to Walsh.

The O.S.C. submissions and Defence comments are found at paragraphs 194 to 196 of Exhibit S5 Volume II. The Defence submissions are at paragraphs 95 to 101 of Exhibit S1 and paragraph 28 of Exhibit S2. I agree with the Defence that McAnulty's evidence does not assist the O.S.C. .

I rely on the following evidence. Felderhof's fax is dated February 12, 1999 asking that the release not be put out until Felderhof has gone over it with de Guzman who "*should be back this Friday*". Friday was February 14 and the release was put out on Monday, February 17.

Exhibit 1196 is a fax from de Guzman in Busang dated February 17, 1997 at 10:51 a.m. This fax is important for several reasons. It indicates that at least by the morning of February 17, 1997 (February 16, 1997 in Canada, the day before the press release was issued) de Guzman was back from Singapore and had traveled to Busang. The fax refers to previously placing a note through MacDonald's door which would have occurred in Jakarta. The request in the note was for a copy of the "*latest press release*". De Guzman takes no issue with the contents of the press release nor is there any suggestion that it is not the final press release. De Guzman simply wanted to quote the press release in an abstract.

In Exhibit 1052 Tab 1613 above Felderhof apologizes for asking to delay putting out the release. I infer from his statements that he intended to delay it no longer than necessary and that he would review it with de Guzman as soon as de Guzman got back. I infer from

Exhibit 1196 that de Guzman was back in Jakarta before February 17, 1997 (February 16, 1997 in Canada) given the time it would then have taken to travel from Jakarta to Busang which is from where de Guzman sent the fax, Exhibit 1196 on February 17,1997. The press release was issued in Canada on February 17, 1997 (February 18, in Indonesia).

On the basis of the circumstantial evidence set out above, I find the press release was not released contrary to Felderhof's request.

FINDING

On the basis of the circumstantial evidence set out above. I find Felderhof 'authorized, permitted or acquiesced in' the issuance of the February 17, 1997 press release.

In summary I find, the O.S.C. has proved beyond a reasonable doubt that Felderhof 'authorized, permitted or acquiesced in' the issuance of each of the impugned press releases dated June 20, 1996, July 22, 1996, December 3, 1996 and February 17, 1997.

THE DEFENCE OF DUE DILIGENCE AND THE RED FLAGS

Defence Of Due Diligence

The Defence concedes that if I find, and I do find, that the O.S.C. has proven the elements of the offence beyond a reasonable doubt then the onus shifts to the Defence to establish on a balance of probabilities that Felderhof exercised due diligence.

> Para. 230. The Crown submits that based on the foregoing evidence, it has satisfied the burden on it to prove the elements of the offence beyond a reasonable

> doubt. If this Court finds that the Crown has met that burden, then the onus shifts to the accused to establish on a balance of probabilities that he exercised due diligence.
>
> **The Defence disagrees that the OSC has met the burden of proving the elements of the offences charged beyond a reasonable doubt, but agrees that if this Court finds that it has the onus shifts to the accused to establish a defence or due diligence on the balance of probabilities.**

Exhibit S5 Volume II: paragraph 230

My function is to determine whether Felderhof has established that he took all reasonable care on a balance of probabilities.

I am not required to go so far as to determine that, for example, the theory of "*depletion of gold at surface*" relied on by Felderhof is geologically correct (Red Flag 2) but to determine whether Felderhof under the circumstances acted reasonably in relying on that theory.

Case Law

The test is set out in R.v. Sault Ste. Marie (City) [1978] 2 S.C.R. 1299 (S.C.C.) (Q.L.) at page 15:

> Offences in which there is no necessity for the prosecution to prove the existence of mens rea; the doing of the prohibited act prima facie imports the offence, leaving it open to the accused to avoid liability by proving that he took all reasonable care. This involves consideration of what a reasonable man would have done in the circumstances. The defence will be available if the accused reasonably believed in a mistaken set of facts which, if true, would render the act or omission innocent, or if he took all reasonable steps to avoid the particular event. These offences may properly be called offences of strict liability.

In R v. Gonder (1981), 62 C.C.C. (2d) 326 (Yuk. Terr. Ct.), the court in addressing the question of reasonable care states at pages 4 and 5:

> The approach consists of two stages. First, the existence of any general standard of care common to the business activity in question must be determined. Is there a standard practice of care commonly acknowledged as a reasonable level of care and did the accused act in accord with that standard? The second stage examines any special circumstances of the case which might require a different level of care other than the level suggested by the standard practice. Evidence of a standard practice is only one important component of that test, the ultimate test is the degree of due diligence required in the circumstances of each case.
>
> ...
>
> Reasonable care implies a scale of caring. The reasonableness of the care is inextricably related to the special circumstances of each case. A variable standard of care is necessary to ensure the requisite flexibility to raise or lower the requirements of care in accord with the special circumstances of each factual setting. The degree of care warranted in each case is principally governed by the following circumstances.
>
> (a) Gravity of potential harm.
> (b) Alternatives available to the accused.
> (c) Likelihood of harm.
> (d) Degree of knowledge or skill expected of the accused.
> (e) Extent underlying causes of the offence are beyond the control of the accused.

In R. v. Bata Industries Ltd. [1992] O.J. No. 236 (Ont. Ct. (Prov. Div.)) (QL) it was held that a court will consider whether an accused is an officer and director and also has a co-existing management position.

The Defence agrees with the O.S.C.'s general statement of law with respect to the duties of directors and officers which include:

i) a fiduciary duty, often described as a duty to act "honestly and in good faith with a view to the best interests of the corporation;" and

ii) the duty of care, which is set out in most statutes as requiring the "care, diligence and skill that reasonably prudent person would exercise in comparable circumstances."

Exhibit S5 Volume II: paragraph 235

John Felderhof

Felderhof had a degree in geology from Dalhousie University. Felderhof was an experienced geologist in the Pacific Rim. Felderhof was a director and officer of Bre-X. He was the General Manager in Indonesia. He was promoted to Senior Vice-President of Exploration on October 5,1994. He joined the Bre-X Board of Directors as Vice-Chair on May 10, 1995. Felderhof was the top technical officer and only senior Bre-X officer and director in Indonesia. Felderhof had overall responsibility for Bre-X's Indonesian operations. See pages 86-87 of these reasons.

Transcript: March 15, 2005, page 51
Transcript: December 4, 2005, pages 82-83
Exhibit 11: 1995 Bre-X Annual Report, page 147

Felderhof's duties set out in his 1993 Employment Agreement include:

2.1 Felderhof shall serve the Corporation and its parent and any subsidiaries in such capacity or capacities and shall perform such duties and exercise such power pertaining to the management and operation of the Corporation as may be determined from time to time by the board of directors of the Corporation.

2.1.1 devote his full time and attention and his best efforts and as may be required by the nature and operation of the Corporation and its business to the business and affairs of the Corporation;

2.1.2 perform the duties that may be assigned to him diligently and faithfully to the best of his abilities and in the best interests of the Corporation and its parent and subsidiaries;

2.1.3 use his best efforts to promote the interests and goodwill of the Corporation; and

2.1.4 without limiting the generality of the foregoing and for the exclusive benefit of the Corporation:

2.1.4.1 to seek and identify in Indonesia and elsewhere potential mining and mineral properties and for that purpose to carry out the appropriate field work therefor;

2.1.4.2 pursuant to clause 2.1.4.1., to personally attend at the potential properties and both before and after such attendance, to conduct such investigations, examine such documents, reports and analyses as are necessary and proper in accordance with accepted professional practice in the industry and to report thereon to the Corporation;

2.1.4.3 to identify other economic opportunities for the benefit of the Corporation;

2.1.4.4 to report thereon where such properties and economic opportunities are identified to the President of the Corporation forthwith and to take such steps as are necessary and legally required to preserve and protect the properties so identified;

2.1.4.5 to work together with David Walsh, the President of the Corporation and the Corporation to meet and discuss with other parties who may become interested in financing, joint venturing, participating with, promoting and otherwise acting for the benefit of the Corporation and its shareholders including without limitation, investment and stock brokers, mining and exploration companies, promoters and such other persons, firms and corporations as the President determines is in the interest of the Corporation; ...

Exhibit 576

DEFENCE POSITION ON DUE DILIGENCE

The Defence position is that Felderhof acted with reasonable care, for example, in retaining reputable professionals such as Kilborn to calculate the gold resources and M.R.D.I. to evaluate the gold deposit and work that Bre-X was doing at Busang. That evidence also goes to rebutting the red flag allegations.

The Defence position with respect to due diligence is found in the August 28, 2006 transcript at pages 46-49:

> MR. GROIA: ...I am not sure there is much difference between Mr. Felderhof's due diligence defence and Bre-X's due diligence defence. [page 46]
>
> ...
>
> MR. GROIA: And then lastly, my third point is that in due diligence terms I think when one looks at the red flags they are intended to try and show essentially the negative. In other words, the due diligence inquiry is not about red flags; it's about whether Mr. Felderhof and Bre-X exercised all due care and attention in the circumstances. And knocking down the red flags is the attempt on our part to show why the Commission's expert Mr. Farquharson was wrong. But that's not the central inquiry. The central inquiry was did Mr. Felderhof and Bre-X exercise all due care and attention to ensure that the drill core that went to Indo Assay was properly assayed and those results were properly given to Kilborn so the estimates could properly be prepared. And so the evidence, for example of M.R.D.I., the auditor, goes to the due care and attention question. It indirectly goes to showing why the red flags were not red at all.
>
> So I want to turn to the due diligence issue. I want to turn to Mr. Felderhof's knowledge and whether he should have foreseen that there had been tampering or, in other words, did he exercise all due care and attention. And the answer is, in my submission, unequivocally that, yes, he did. This was a once in a lifetime event even on the testimony of the Commission's expert and the law does not require in due diligence a council [sic] of perfection. What we say the evidence has disclosed is, beyond any reasonable conclusion, this was a world class exploration project being conducted by world class experts and all the evidence suggested that the results were plausible and reasonable and exactly what you'd expect.

Transcript: August 28, 2006, pages 46-49

THE O.S.C. POSITION ON DUE DILIGENCE

The O.S.C. submits that the issue of John Felderhof's due diligence that I must resolve "*is really quite simple*". In the O.S.C.'s submission Felderhof was not duly diligent because he did not recognize the red flags and he did not make enquiries.

On August 30, 2006 at page 87 the O.S.C. states:

> Now, Your Honour, I'm going to suggest again that due diligence in this case is really quite simple. All Mr. Felderhof had to do was to alert to the flags and make inquiries.

Transcript: August 30, 2006, page 87

At paragraph 315 of Exhibit S5 Volume II, the O.S.C. states:

> Para. 315 Therefore, this Court may find that Felderhof did not exercise due diligence, if it finds that the evidence proved any of the bright red flags that would have required Felderhof to make inquiries. Alternatively, this Court may find that Felderhof did not exercise due diligence based on evidence of any combination of the red flags listed in the Strathcona October 20, 1997 letter to Walsh that collectively point in the same direction and would have required Felderhof to make inquiries.
>
> **The Defence disagrees.**

Another way of stating the O.S.C. position is that Felderhof was not duly diligent because he did not recognize the red flags and/or ignored the red flags and/or did not investigate the red flags and/or did not resolve the red flags before authorizing, permitting or acquiescing in the four impugned press releases.

TEST OF DUE DILIGENCE IN THIS CASE

The Defence's articulation of the due diligence issue above sets out the test found in Sault Ste. Marie, supra and in the case law that followed.

Given the evidence in his case, the way in which the parties approached the evidence and the submissions, the O.S.C. articulation above sets out in practical terms the central issue that I must determine; that is, do I prefer the Defence evidence over the O.S.C. evidence with respect to the red flags. There is no onus on the O.S.C. that I prefer the O.S.C.

evidence but of course if I do then Felderhof has not met his onus. If I find the O.S.C. and Defence evidence equally compelling then again Felderhof would not have met his onus. As noted the onus is on the Defendant to establish due diligence on a balance of probabilities.

In addition to determining the central issue above, I do not ignore that the green flags or acts of reasonable care by Felderhof go not only to rebut the evidence of red flags but are also positive pieces of evidence of due diligence by Felderhof.

Red Flags

Graham Farquharson And Strathcona Mineral Services Limited

The O.S.C. called an expert, Graham Farquharson, President of Strathcona Mineral Services Limited to prove the red flags alleged by the O.S.C. .

Strathcona's experience and Farquharson's curriculum vitae are set out in Exhibit 676.

Strathcona's experience in litigation and arbitration assignments is set out in Exhibit 677.

In the last paragraph of my ruling of March 17, 2005 I qualified Farquharson as follows:

> This is a ruling with respect to admissibility of expert evidence and not as to its weight and certainly not as to my final determination. In conclusion, Graham Farquharson is qualified to give expert evidence in both areas set out above, red flags at Busang and whether such red flags should have been apparent to an experienced geologist.

R v. Felderhof [2005] O.J. No. 6002 (QL)

October 20, 1997 Letter From Strathcona To Bre-X

Strathcona set out "*a list of the concerns or warning signs, or 'red flags' as they came to be called, that [Strathcona] noted upon [their] initial review of the Busang data and during the first few days of [their] visit to Busang*" in a letter to Bre-X dated October 20, 1997. Strathcona listed 20 red flags. For convenience of reference and as an overview of the O.S.C. allegations that letter which is found in Exhibit 681, Appendix VII is reproduced in full:

Red Flags at Busang

> At a meeting with Howard Gorman of Macleod Dixon and Bryan Coates of Bre-X Minerals we were asked if we could compile a list of the concerns or warning signs, or "red flags" as they came to be called, that we noted upon our initial review of the Busang data and during the first few days of our visit to Busang. This letter responds to that request and identifies most of the red flags that became apparent to us in the initial phase of our audit assignment. Some of the red flags are more significant and more obvious than others. Some of them, individually, on their own, might not create any doubt or questions to the casual observer but, collectively, they all point in the same direction.
>
> All of the red flags require the observer to have some experience in the mining industry and particularly in gold and the more experienced the observer the more numerous the red flags that become evident. However, the observer need not be a highly specialized scientist as the red flags do not involve any sophisticated technology but rather, if the observer is familiar with the exploration and evaluation of gold projects then that background should be sufficient to have identified most of the red flags, given the opportunity to become reasonably familiar, as we did, with the project.
>
> Following then is a list of the red flags that we identified during our initial period at Busang and in Jakarta and they are listed in a sequence commencing with the logical steps for the discovery of the deposit, the carrying out of the drilling program, treatment of the samples etc.
>
> **1. No gold geochemical anomaly over the Southeast Zone**
>
> We asked the question of whether or not there was a geochemical expression on surface of the major deposit that was said to be located in the Southeast Zone, having been aware that there was a geochemical expression for the gold

mineralization that had been identified in the Central Zone by the Australian group that carried out exploration at Busang prior to Bre-X. There really was no satisfactory explanation given as to why there was no geochemical anomaly over the Southeast Zone.

2. **No gold in outcrop samples –"it had been leached"**

   We also asked why there was no gold in samples of outcrop over the Southeast Zone as indicated by an outcrop map in the office at Busang, particularly given that the orebody as projected by Kilborn, and based on the drill core assays, extended right through to surface. The answer came back that the gold on surface had been leached and probably was concentrated a few metres below surface which, of course, was not the case.

3. **Location of new drill holes was never influenced by results of previous drilling**

   We noted on our arrival at Busang that the spotting of new drill holes was simply done by the surveyor according to a predesigned grid without any consideration by the geologists as to whether or not the hole locations might change because of drilling results from surrounding holes.

4. **Busang geologists never went to drill sites**

   When we were working with the drilling company in spotting our audit holes the remark was made that they never saw a geologist from Bre-X at any of the drill sites, despite six drills being in operation at the time. It became apparent that the Busang geologists were not really interested in watching what came out of the hole as the core was stored for many weeks after drilling prior to going through the logging, sampling process etc.

5. **Drill core not split –all 14 kilograms of core from each two-metre sample "required for accurate assays"**

   Many observers have commented on this particular red flag and with good reason. A sample weighing 14 kilograms, and representing but two metres is a very large sample and most people with any experience in the gold industry would have recognized that a seven-kilogram sample would have been just as representative of that two-metre interval.

6. **Selected intervals designated visually as "mineralized" and received different sample treatment.**

   We were amazed that the geologist logging the core could designate which areas were likely to contain gold mineralization and which would be barren,

simply based upon visual observations. The geology of the Southeast Zone is such that the only way one can tell if there is gold present is to sample the interval. There are some obvious areas that are unlikely to have any gold mineralization but based upon the geological theory for the existence of gold at Busang any of the host andesite rock, or dacite as the Busang geologists preferred to call it, was prospective for gold, with the degree of alteration having an impact on the degree of prospectiveness.

The other common description that the Busang geologists used in logging core was a frequent reference to silicification which our geologists could not identify and any competent observer could have readily refuted this description by applying the penknife scratch test for silica.

7. **In over 60 000 metres of core logging no reports of visible gold**

The nature of the gold found at Busang Southeast zone had generally been reported to be coarse in nature and, therefore, one would have thought that in over 60 000 metres of drill core some evidence of visible gold would have been reported in the drill logs but when we asked the question we were told that there were no reports of visible gold. This conflicts with the statement "gold dominantly occurs in free native form" in the technical paper presented in early 1996 (?) entitled Busang Gold Deposit by Felderhof, de Guzman, Puspos and Nassey.

Also, it would be normal practice for the person responsible for a major project such as Busang to have requested thin-sections be prepared from the core in some of the higher grade areas to be able to visually confirm the presence of the gold and its association. This was not done and we are not aware if others asked if this procedure had been done.

8. **The geology of the 10-centimetre "skeletons" from reported high-grade intervals did not appear to support such assays.**

We looked at some of the skeletons remaining from those intersections that had grades of 20 grams per tonne or more fully expecting to see geology typical of high-grade epithermal deposits but the high-grade areas looked no different and were just as tight and solid as those areas reported as being very low grade or barren.

9. **No gold identified in 103 petrographic samples selected to represent the deposit**

Anne Thompson of PetraScience Consultants in Vancouver was given 103 samples on which to do different petrographic studies, in other words to identify the component minerals and mineral associations in the Southeast

Zone with the samples being selected by the Busang geologists to be representative of the Southeast Zone. Somewhere in that minute detailed work that she did there should have been some evidence of gold if it was present but she commented in her report that she was unable to find any gold in those samples.

10. An excellent sample preparation facility at Busang was under-utilized despite large backlog of core waiting to be sampled

We were impressed with the excellent sample preparation facility that had been erected at Busang but during the two weeks that we were there were equally impressed by the fact that the crew had nothing to do during our period of residence at Busang and no samples were given to them to process despite a very large backlog of drill core waiting to be sampled.

11. Only "in-fill samples" designated as "non-mineralized" could be prepared at Busang.

We queried why only "non-mineralized" samples were allowed to be crushed and prepared for assaying at Busang and the response was that they wanted to be sure there was no opportunity for "sample contamination" of the areas considered likely to have potential for gold and that samples from those areas would only be treated by an independent laboratory.

12. All sample bags delivered to Samarinda had to be opened to "check for bag breakage" and "confirm core logging description"

We were astonished to hear on two or three occasions at Busang when the sample treatment process was being described that it was readily acknowledged that the sample bags were opened at Samarinda in order to check that there had not been any deterioration in the fiberglass bags during the few weeks that it took to get the samples from Busang to Samarinda and to allow Cesar Puspos, as the chief geologist, to have a final check on whether or not the core logs properly described the sample interval. It is, of course, standard practice in the industry that once a sample bag has been closed it should never be opened again until in the assay laboratory.

13. Despite a large accumulation of samples at Samarinda and assaying capacity available at Indo Assay, no samples were shipped unless Michael de Guzman or Cesar Puspos released the samples

This particular red flag was one that we became aware of at a later date but we did hear from John Irvin at Indo Assay Laboratories that frequently he had capacity and was waiting for samples and knew that there was a large accumulation of samples at Samarinda but they would not be released until they had been through the "final inspection".

14. Poor reproducibility of assays

All of the laboratories that have done test work for the metallurgical investigations and the check assays that have been done for Barrick, Placer Dome etc, have indicated problems in reproducing assays from the same sample and while coarse gold always does present some problem in attaining acceptable reproducibility the variations at Busang were extreme.

15. Screen analyses of sample rejects indicate almost all gold in plus 106 microns (150 mesh) fraction

One of the first items of documentation that we received before leaving Toronto was some assay results of samples taken by Barrick. We had never seen such a distribution of gold before because all of the gold was located in a particular coarse fraction and for a primary deposit, such as Busang was reported to be, the gold should have been distributed throughout all size fractions.

16. Mineralogical studies identified gold in metallurgical samples as being "coarse, rounded and with gold-rich rims"

This particular red flag had received much attention in the press and we were certainly not the first to point it out. In fact, we were the fourth group to have commented on this. Included in the feasibility studies assembled by Kilborn were mineralogical studies carried out by Hazen Research in Colorado and Roger Townend working for Normet in Perth, Australia and both identified the nature of the gold which an observer with a gold industry background should recognize as being placer gold in origin. Freeport made the same observations and we confirmed the nature of the gold with our work at Lakefield.

17. Metallurgical testwork indicated more than 90 percent gold recovery in gravity concentrates of one percent to six percent of feed

When reviewing the Kilborn feasibility study in the hotel room in Jakarta on our first day there this particular item caught my attention and I initially thought that there must be a typographical error but both Hazen and Normet commented on the remarkable ease with which the gold could be recovered in a gravity concentrate. In the case of the Hazen report only one percent of the millfeed would be required to drop into a gravity trap to recover more than 90 percent of the gold and this was a characteristic that we had never seen nor has anyone else in a so called "primary deposit".

18. Metallurgical recovery was independent of fineness of grind

Both the Hazen and Normet reports went on to comment on a remarkable lack of effect on gold recovery in changing the grind when processing the Busang material. Normally one would expect when treating a primary ore that the recovery would increase with a finer grind but in this case, apparently, no grinding was required at all as the gold was already liberated.

19. Request for drill holes exclusively for metallurgical testwork was denied

We only became aware of this red flag when we arrived in Perth and the Normet metallurgist advised that their request for complete core from drill holes to carry out metallurgical test work was denied on the basis that all the drills had to be kept working to expand the ore reserves as that was what the investors and the market were looking for at the time.

20. Could one deposit contain as much as eight percent of the known gold resources of the world

This of course is a red flag that is easy to point out in hindsight but with all the experienced observers that had been to Busang perhaps someone should have asked is it really possible, that considering there are thousands of gold deposits in the world, that one could be on such a larger scale than any of the others and why would nature be so generous as to endow Busang with such a large proportion of the world's gold resources.

There are other lesser flags that we could add to this list but the foregoing represents the more significant ones that we think could have been identified at some stage by the many others that preceded us to visit and report on Busang. The query has been made to us on several occasions as to why Strathcona was able to identify the problem in such a short period of time whereas other observers had not. Our response has been that we had two major advantages over those who had been involved with or had followed and reported on the developments at Busang.

One was that when we arrived in Jakarta on March 24 we had been forewarned that there might be a problem with the estimated gold resources at Busang and as a consequence we went looking for trouble and examined every document, comment and action very critically. The second advantage that we had was that we received an excellent two-hour verbal presentation from Freeport in the morning of March 26 during which they summarized the work that they had done but during which they were very careful to not

state that they did not believe that there was no gold at Busang. In fact, their parting line was that there must be gold at Busang somewhere with all the work that has been done by Bre-X and they were ready to work with Strathcona to help us find it. A shorter version of their presentation had been given to John Felderhof a few days earlier.

We trust all of the foregoing will be of some use for your present requirements and if there are any questions on these various red flags we would be pleased to respond.

Exhibit 681: Appendix VII

Strathcona's Expert Opinion, Exhibit 681

In their Expert Opinion to the O.S.C., Exhibit 681, Strathcona summarizes their observations and lists eight red flags at pages 2 and 3:

> The following summarizes our observations on the geological facts to which warnings were attached and which are discussed in this report.
>
> **Absence of gold surface anomalies in the Southeast Zone**
>
> - The absence of gold in sediments in streams draining the Southeast Zone indicated that the rocks eroded by those streams contained no gold.
> - The presence of base metals in surface samples over the Southeast Zone and the lack of gold in those samples disproves any claim that gold had been leached or depleted at surface, as gold, if present and being the most noble of all metals, would be the last to be leached or put into solution and transported elsewhere.
> - The Central Zone, which has a small erratic in-situ gold content, does have the typical surface expression of that gold content in soil samples and surface outcrops.
>
> **The physical nature of the gold and absence in drill core**
>
> - Metallurgical studies in 1995 and 1996 on samples of crushed core reported coarse, liberated gold, with physical characteristics not of

gold from a primary hardrock deposit but rather of alluvial gold. Felderhof has claimed in a July 25, 1997 public statement that the type of gold found in the metallurgical samples is not unusual for an oxidizing environment in the tropics. However, at Busang, oxidation is confined to a thin surface layer with an average depth of nine metres in the Southeast Zone, but coarse alluvial gold was found in most holes to a depth of 400 metres.

- No visible gold was observed in all the core drilled by Bre-X. Considering the coarse gold found in the samples used for assaying and subsequently for metallurgical testing and mineralogical studies and the amount of core drilled in the Southeast Zone (130 000 metres) and in the Central Zone (over 18 000 metres), visible gold should have been frequently found in the core samples had the gold been part of the original rock and not added later.

- Examination under a microscope of 75 core specimens from the Central Zone was done in 1995 and traces of very fine gold associated with quartz veins were found in only four samples. In 1996, no gold was found under the microscope in 103 representative core and rock samples from the Central Zone and from the large gold deposit reported for the Southeast Zone. The results of these petrographic studies were incompatible with the coarse alluvial gold found and reported in samples used for metallurgical tests and which had been derived from core samples sent for assaying and upon which gold estimates for the Busang property were based.

- Because of the alluvial gold added to the samples metallurgical testwork achieved exceptional gold recoveries by gravity methods that would be unachievable and incompatible with hardrock gold deposits as Busang was reported to be.

- Duplicate assays, assays with different methods, and check assays at other laboratories, all done for Bre-X, confirmed large variations for gold values of individual data pairs. While coarse gold always does present some problem in attaining acceptable reproducibility, the variations at Busang were extreme. This poor assay repeatability indicated coarse free gold in the samples, which was completely at odds with the mineralogical-petrographical evidence. Also, a decline in gold values in subsequent repeat assays of certain assay batches pointed to poor gold homogenization in the samples, and should have raised concern as to the cause of this problem.

> A competent geologist acting reasonably would have identified the red flags or warning signs arising from the sampling results and studies carried out during the Busang program and would have realized that they are incompatible with basic geological principles and with the results being publicly reported by Bre-Minerals Ltd.

The opinion then focuses on the three most striking areas of red flags at Busang at page 5:

> Our discussion in this report on the warning signs that would point to the massive sample tampering that occurred will focus on the three most striking areas of red flags at Busang, i.e.
>
> - the lack of gold at surface in the Southeast Zone, and
> - the discrepancy that existed between the very few specks of fine gold detected under the microscope in rock samples from only the Central Zone with none at all being detected by Bre-X in samples from the Southeast Zone, and the coarse liberated alluvial gold found and reported in all crusher core samples from the Central and Southeast Zones used for metallurgical tests and mineralogical studies.
> - the total absence of any visible gold in more that one hundred kilometers of drill core, which is completely contrary to the reasoning offered by Bre-X for the requirement to assay all of a core sample because of the reported coarse nature of the gold at Busang.

Strathcona's detailed opinion is found at pages 11-32 of Exhibit 681.

Farquharson's Re-Examination About "Most Striking Areas Of Red Flags"

In re-examination Farquharson testified as follows about the "*most striking areas of red flags*" or "*big flags*" on April 7, 2005, pages 4-7:

> MR. MARROCCO: Mr. Farquharson, I think you said yesterday and if you didn't say it yesterday you certainly said it in your report that some of the red flags were

most striking, or that there were most striking areas of red flags and one of them you mentioned yesterday was the absence of a geochemical anomaly in the Southeast Zone. What were the other most striking areas of red flags?

MR. FARQUHARSON: Well considering the list that Mr. Groia has on the score card there and looking at it from the point of view of the red flags that would be most evident to a geologist involved with the property, or having an opportunity to review the geological data on the property, compare it to all the metallurgical test work that was done and the petrographical work and so on, but in addition to the lack of the gold geochem' surface anomaly over the Southeast Zone that would correspond with the anomaly over the Central Zone for the similar type geology. The other big flags would be the absence of physical gold in all of the core that was drilled in the Southeast Zone over two to three years of drilling and coming from a deposit that was reported to have coarse gold and the fact that other than the one exception that Mr. Groia was able to find in the drill logs there really was no other legitimate references to visible gold. And so a geologist coming to the property, one of the first things he always does is he wants to look at core. And the fact that there was no core there to demonstrate visible gold would be a concern. And the fact that there was no visible gold reported in the drill logs, if he had looked at the drill logs. And the third one sort of follows on from that. Given that the geologist would not be able to look at any drill core because all of the drill core had been consumed for the analytical work, for the assaying with the exception of the skeletons then he would very quickly go to the library of skeletons to look at what could be observed in the skeletons. Again, he would always say well let's look at the high grade intervals and the skeletons that remain from the high grade intervals. And he would rapidly come to the same conclusion that we did and that Leach and Corbett did that those skeletons for the high grade intervals looked just as dry and barren as the rest of the core where there was very little, if any, gold reported. So that would be a big red flag as to why in these skeletons – and there were many of them—and he would look at a number of the skeletons and he wouldn't be able to see in any of those skeletons any evidence of the high grade mineralization that was reported in the assays. And finally, the fourth flag that I would sort of categorize in the list of major flags would be the one where the Bre-X staff reported to us on two occasions while I was there, their geologist and their project manager, that the sample bags after they left Busang and before they got to the assay laboratory were opened for inspection and that is just absolutely contrary to all of the rules and procedures for security of samples that apply anywhere in the mining industry. I don't know if visitors to the property would be aware of that, but when we asked the question it was very forthcoming, matter of fact, nothing unusual about it. And, of course, to us that set the alarm bells ringing in a major way when we heard those statements from two separate individuals in the Bre-X organization at our time on site.

So those four items I think would be—any one on their own would cause a geologist, somebody familiar with exploration, to say what is going on here and how can that be and do further work.

> The other flags, one on its own, you might sort of shrug your shoulders and say well maybe there is a reason for that, but it might not set the alarm bells ringing in a loud manner. If you had several of those other flags appearing that are related to each other then you would have a cause for saying something is not right here.

Transcript: April 7, 2005, pages 4-7

O.S.C. Evidence

There are other witnesses and hundreds of exhibits on which the O.S.C. relies on in its case that Felderhof did not exercise due diligence but in the main the O.S.C. case is based on the evidence of Graham Farquharson.

Examples of other witnesses that the O.S.C. relies on with respect to some of their evidence are: Dr. Paul Kavanagh, Alexander Mihailovich, called by the O.S.C. and Defence witnesses such as Dr. Phillip Hellman, Terry Leach, Paul Semple and Peter Munk.

Defence Evidence

As noted above the Defence called the following witnesses on the issue of due diligence: Dr. Hellman, Terry Leach, Paul Semple and Peter Munk. The Defence also relies on Dr. Kavanagh.

The Defence also relies on evidence that reflected the participation of many others in the development of Busang; for example Kilborn, Normet, Hazen, Oretest, Mintek, Petra Science, R. Pooley, Roger Townend, John Borner, Anne Thompson, Martha Schwartz, Sophie Ashby, M.R.D.I., Indo Assay Laboratories (I.A.L.), John Irvin, J.P. Morgan, Republic National Bank.

The Defence also relied on comparisons to other gold properties; for example, Kelian, OK Tedi, Mirah, Mount Muro, Mount Kare, Munyup, Gunung Mas, Ampalit, Eddie Creek, Hidden Valley and others.

Dr. Hellman (Exhibit 1202) and Terry Leach (Exhibit 1328A and Exhibit 1328B) prepared expert reports which addressed Farquharson's red flags and added green flags. Farquharson was not asked to and did not look for green flags.

Dr. Hellman

Dr. Hellman's qualifications are found at pages 5-11 of Exhibit 1202. Dr. Hellman was qualified to testify as an expert without objection in the three areas requested by the Defence:

> I'm asking him to be qualified in three areas. These areas may sound familiar because I essentially borrowed Mr. Marrocco's area for Mr. Farquharson, with a couple of small changes. So the first area will be I'm asking that Doctor Hellman be permitted to give opinion evidence or expert evidence as to the existence of non-existence of certain red and green flags. Secondly, to give expert or opinion evidence as to whether those red and green flags should have been apparent to an experienced geologist such as Mr. Felderhof. I think Mr. Marrocco put it to a geologist having the background and experience of Mr. Felderhof. And then thirdly, I'm going to ask him to give some very brief expert evidence as to the meaning and understanding of resource estimates and ore reserves which is the small section at Tab 6.

Transcript: November 2, 2005, page 4

In Dr. Hellman's opinion the red flags "*did not exist*".

Dr. Hellman's overview and opinion about the red flags is found at pages 1-3:

1. ***Overview***

No evidence of tampering, contradictions, irregularities or any substantive issues relating to the validity of the exploration drilling data are known to have been reported by any of Bre-X's directors, employees, officers, experts, consultants or visitors to the site prior to Freeport's due diligence drilling activities. This is despite numerous visits to Busang by representatives of many large and respected mining and exploration companies.

It is fundamental principle in mineral exploration that actual results from drill holes constitute the ultimate and final test of reconnaissance exploration activities such as surface geochemical sampling of soils or trenches. This is because these samples are subject to a variety of processes, many of which are poorly understood, including oxidation, erosion, water movement and glacial activity. The veracity of drill hole assay results is also not judged by geophysical results such as from magnetic or gravity surveys.

Drill hole results are the final test of the many, often contradictory, exploration surface results. The drill hole results from Busang were consistent with the geology of the core. This was acknowledged by Strathcona:

"There is a close correlation between those core intervals identified in the logging process as 'mineralized' with those intervals subsequently found to have gold values." (Strathcona, May 1997, p 51) [6]

Once drill results have been received, all other data assume less importance.

An independent, extensive and detailed review by one of North America's best known and respected minerals auditing groups, MRDI Inc., was commissioned by Bre-X in October 1996 specifically to assess its work at Busang. That review stated:

> "*Our principal conclusion is that the exploration work is being done to a high standard.*"

It is difficult to reconcile this and the many other positive comments about Bre-X with the numerous criticisms made by Strathcona who states:

> "A competent geologist acting reasonably would have identified the red flags or warning signs arising from the sampling results and studies carried out during the Busang program and would have realized that they are incompatible with basic geological principles and with the results being publicly reported by Bre-X Minerals Ltd." (Strathcona, 2000, p 3) [37]

The MRDI review did not identify any of the 20 red flags that Strathcona alleges should have been obvious to an observer "*familiar with the exploration and evaluation of gold projects*". The MRDI review was authored by four highly qualified and experienced people who specialized in the geology of mineral deposits, coarse gold sampling, resource estimation, technical audits and reviews, analytical chemistry, Quality Control issues and even fatal flaw audits. As such, all were well familiar with the exploration and evaluation of gold projects.

The MRDI review does not have the characteristics of a "rubber-stamping" exercise. It includes a number of useful and constructive recommendations and suggested improvements. It strongly contrasts in both tone and content with the reports of Strathcona.

Mr. John Felderhof, as well as the many professionals who worked on the Busang project, either as employees or consultants did not fail to recognize or ignore the alleged warning signs of Strathcona. These professionals included specialists in mineralogy, metallurgy, mining engineering, petrology, resource estimation, sampling and assaying. The reason why Strathcona's red flags were not recognized is because they did not exist.

As with Strathcona, I recognize that the most probable explanation of the negative Freeport results was tampering. I advised Mr. Felderhof of this opinion. During numerous discussions with him, I found that he had solid geological reasons underpinned by extensive exploration experience to believe that Busang was a real gold deposit.

Busang was a rare instance of a determined and intelligently planned fraud that had been cleverly disguised in the context of real mineralization that withstood the close scrutiny of many experienced practitioners from the minerals industry. It was achieved with

> "...a scale and over a period of time and with a precision that, to our knowledge, is without precedent in the history of mining anywhere in the world."

Exhibit 1202: pages 1-3

Dr. Hellman's detailed analysis of the 20 red flags in Strathcona's October 1997 letter is found at pages 43-62 of Exhibit 1202 and at pages 100-273 of Appendix III.

In the executive summary Dr. Hellman sets out his opinion of the 20 red flags on pages 21-24 as follows:

Flag	**Description**	Comment
1	No gold geochemical anomaly over the SEZ	(1) There was anomalous gold over the SEZ but of a magnitude less than the CZ. (2) Strathcona did not take into account a whole map of geochemical results over the SEZ many of which were anomalous. (3) Strathcona did not appear to consider the contrasting geology between the CZ and the SEZ which Mr. Felderhof believed explained differences in surface expression between the CZ and the SEZ.
2	No gold in outcrop samples - "It had been leached:	(1) Gold in drill core was depleted towards the surface in the SEZ as demonstrated by the data that I gathered, as well as the data disclosed by Strathcona. (2) The depletion of gold at surface was consistent with the immediate past experience of Mr. Felderhof at the gold deposit of Mirah, Kalimantan. (3) Strathcona's view on the mobility of gold appears to be a unique view unsupported by published geochemical research with which I am aware.
3	Location of new drill holes was never influenced by results of previous drilling	(1) No evidence has been presented to support this allegation. (2) Drilling to a predesigned grid is not a red flag. (3) Routine infill drilling is standard procedure.
4	Busang geologists never went to drill sites	No evidence has been provided to support this allegation which is based on "*a remark*"
5	Drill Core not split – all 14 kilograms of core from each two-metre	(1) Bre-X's practice conformed to that recommended by one of the world's leading sampling experts and is entirely

	sample "required for accurate assays"	sensible for coarse gold. (2) Skeleton core was stored for future verification and core photos were archived.
6	Selected intervals designated visually as "mineralized" and received different sample treatment	This is a sensible practice and not a red flag.
7	In over 60,000 metres of core logging no reports of visible gold	This is false because there are more mentions of visible gold in the core logs than at Kelian.
8	The geology of the 10 centimetre "skeletons" from reported high-grade intervals did not appear to support such assays	I have not considered this because whilst on site I did not examine the relationship of the skeleton core with the assays. That was part of Terry Leach's scope of work for the Sheraton project.
9	No gold identified in 103 petrographic samples selected to represent the deposit	(1) The identification of gold grains was not the aim of this study. (2) No gold was also identified in samples from the CZ which Strathcona acknowledges contained gold mineralization and which is known to contain coarse visible gold.
10	An excellent sample preparation facility at Busang was under-utilized despite large backlog of core waiting to be sampled.	(1) The on-site sample preparation facility was not used because of the likelihood of segregation of gold in pulps during transport from site to IAL in Balikpapan. (2) The protocol of having an independent laboratory responsible for sample preparation of core is not a red flag and is widely used in the industry.
11	Only "in-fill" samples designated as "non-mineralised" could be prepared at Busang	Bre-X could have been criticized for using the sample preparation at Busang for the mineralized core because it was not an independent laboratory.
12	All sample bags delivered to Samarinda had to be opened to "check for bag breakage" and "confirm core logging description"	Checking of sample bags is not a red flag and is good practice.
13	Despite a large accumulation of samples at Samarinda and assaying capacity	It is a standard industry practice for senior staff to authorize dispatch of samples. This is not a red flag and would normally be commended as a demonstration of management control.

	available at Indo Assay, no samples were shipped unless Michael de Guzman or Cesar Puspos released the samples.	
14	Poor reproducibility of samples	(1) Samples with coarse gold are well known to produce sampling and reproducibility issues. (2) It would be a red flag if the samples had excellent reproducibility.
15	Screen analyses of sample rejects indicate almost all gold in plus 106 microns (150 mesh) fraction.	(1) This allegation is not supported by the evidence. (2) Indo Assay Labs, who performed Bre-X's screened assays, were experienced in these types of assays. It is unlikely that the results would attract no adverse comment or questioning if they were a red flag.
16	Mineralogical studies identified gold in metallurgical samples as being "coarse, rounded and with gold-rich rims"	(1) This description was never used by the mineralogists who studied the gold grains. (2) No mineralogist expressed any concerns.
17	Metallurgical testwork indicated more than 90 percent gold recovery in gravity concentrates of one percent to six percent of feed	(1) These results are not unusual. (2) A 27-tonne pilot plant test on SEZ achieved only a 49% recovery. (3) Strathcona confused recoveries achieved in the laboratory with those from actual operations.
18	Metallurgical recovery was independent of fineness of grind	(1) This was the same as for Kelian (2) Some tests showed a relationship of metallurgical recovery with grind size.
19	Request for drill holes exclusively for metallurgical testwork was denied	(1) This allegation is unreasonable. (2) Even if the allegation was correct it would not be a red flag.
20	Could one deposit contain as much as eight percent of the known gold resources of the world	(1) This allegation is based on incorrect data. (2) The South Deep deposit, 50% of which is owned by Placer Dome, had a reported resource plus reserve of 98 million ounces which is greater than that reported for Busang and has not been reported by Farquharson to be a red flag while he has been a director of Placer Dome.

Dr. Hellman's opinion of Strathcona's summary of red flags in Exhibit 681, pages 2-3, is found at pages 17-20 of Exhibit 1202.

Dr. Hellman and Leach were both involved with the Sheraton Project which investigated Freeport's negative results and Busang and which both describe in their expert reports.

Dr. Hellman states:

> Mr. Felderhof sought the advice of a group of consultants who were familiar with exploration in tropical environments such as those that are typically found in Indonesia and who were also familiar with the geology of epithermal gold deposits. This was due to Mr. Felderhof's reservations about the experience of Strathcona. Accordingly, Dr. Greg Corbett, Mr. Terry Leach and I undertook, in consultation with Normet and Kilborn, various geological studies which included a field visit to Busang.
>
> The representatives of Normet and Kilborn, as well as Mr. Felderhof and Mr. J. Alo met at the Sheraton Hotel in Perth, Western Australia, in April 1997. At that meeting it was clear that all who had been involved in Busang fervently shared Mr. Felderhof's belief in the validity of the project.
>
> Dr. Corbett and Mr. Leach had just returned from Busang and described the findings of their geological work at the meeting. After reviewing the various reports, I advised that I believed the most likely explanation for the negative Freeport results was salting.
>
> ...
>
> A number of tasks were agreed upon to test the belief that the gold mineralization at Busang was real, which was a belief that was shared by Mr. Felderhof and Mr. Alo from Bre-X and the representatives from Kilborn and Normet.

Exhibit 1202: pages 12-16
Exhibit 1328A: pages 17-25
Exhibit 1328B: pages 17-32

Terry Leach

As noted above, Leach's qualifications are found at pages 12-16 of Exhibit 1328A and pages 5-11 of Exhibit 1328 B.

Leach was qualified to testify as an expert without objection in the three areas requested by the Defence:

> MR. GROIA: So, Your Honour, I am going to ask that Mr. Leach be qualified on three areas. Firstly, to give expert testimony as to the existence or non-existence of certain red flags and green flags. And if you look, Your Honour, at the table of contents to Volume 1 of the report you will see that Mr. Leach is going to comment only on red flags 1, 2, 6, 8, and 9. So the other red flags I am not asking to qualify him to comment on those, simply the ones that are referred to in the report. And the green flags, you will see, Your Honour, are referred to in Section 5 and again I will only be asking for his testimony concerning those green flags that are listed in the report.
>
> And then, secondly, I am going to ask to qualify him as to whether or not the listed red flags should have been apparent to a geologist with Mr. Felderhof's background and training.
> And then, thirdly, I am going to ask him to give his opinion on the Strathcona suggestion that the tampering of the Busang results went back to BRH-3, as you have heard some evidence about. And in the report, Your Honour, that's the section to be found at Section 4, sub-section (g). "When Tampering Took Place" is what it is titled in the report.

Transcript: December 12, 2005, pages 10-11

As noted above, Leach's opinion on the red flags is limited to those that fall within his core expertise: Red Flags 1, 2, 6, 8, 9. Leach discusses these red flags at pages 41-60 of Exhibit 1328A and pages 33-139 of Exhibit 1328B.

Leach's opinion is that these are not red flags and that they are not red flags that should have been apparent to Felderhof.

Exhibit S11 –Tab 5

At tab 5 of Exhibit S11 the O.S.C. lists the "*Hellman and Leach References that were Not Admitted at Trial*". Where the opinions of Dr. Hellman (Exhibit 1202) or Leach (Exhibit 1328A and 1328B) rely on an item on that list then I have not considered that part of the opinion except to the limited extent permitted in Lavallee.

R. v. Lavallee: Expert Opinion Based On Hearsay

In the Supreme Court of Canada decision of R. v. Lavallee, [1990] 1 S.C.R. 852 (QL) Justice Wilson states at paragraph 74:

> If the majority of the Court of Appeal is suggesting that each of these specific facts must be proven in evidence before any weight could be given to Dr. Shane's opinion about the accused's mental state, I must respectfully disagree. Abbey does not, in my view, provide any authority for that proposition. The Court's conclusion in that case was that the trial judge erred in treating as proven the facts upon which the psychiatrist relied in formulating his opinion. The solution was an appropriate charge to the jury, not an effective withdrawal of the evidence. In my view, as long as there is some admissible evidence to establish the foundation for the expert's opinion, the trial judge cannot subsequently instruct the jury to completely ignore the testimony. The judge must, of course, warn the jury that the more the expert relies on facts not proved in evidence the less weight the jury may attribute to the opinion.

Definition of Red Flag

In paragraphs 288-307 of Exhibit S5 Volume II the O.S.C. submits that Hellman's and Leach's evidence about the red flags is of limited value because they did not use the same definition as Farquharson and because they "*attempted to lower the standard of due diligence required of a competent geologist acting reasonably.*" Upon review of those

paragraphs and the Defence comments I do not see that the definitions used by Farquharson, Hellman and Leach are different in any significant way. The issue is whether the evidence establishes that Felderhof was or was not duly diligent as defined by the Supreme Court of Canada in Sault Ste. Marie, supra.

Exhibit S5 Volume II: paragraphs 288-307

Felderhof Not Aware of Salting

In their opening address the O.S.C. stated:

> And it must be stressed that in connection with what we are seeing here, there is no demonstration of any indication in this material that Mr. Felderhof was aware of a salting operation.

Transcript: November 17, 2000, pages 52-53

The O.S.C. has since stated that on the evidence, I may find that Felderhof knew or was willfully blind that the press releases were misleading or untrue.

Exhibit S5 Volume II: paragraphs 33, 282-284
Exhibit S6: paragraph 218

But the O.S.C. has not stated that it is resiling from its original position.

The Defence submits that if by this the O.S.C. is saying that Felderhof was not a true believer in Busang then the best evidence to the contrary is Felderhof's conduct after Freeport's negative results.

Felderhof flew back to Indonesia and then flew to Busang by helicopter with his wife. This was after reports of the death de Guzman. De Guzman fell from a helicopter on his way to Busang after Freeport's negative results. The Defence submission is why would

Felderhof go back into the jungle with his wife at a time of great uncertainty and great danger unless he was a true believer and knew nothing about any salting. The second argument is why would Felderhof invest in the Sheraton project to determine what went wrong if he already knew and was not a true believer in Busang.

Transcript: August 28, 2006, pages 63-65

On the other hand the O.S.C. poses the question why was Felderhof selling so many of his Bre-X shares when the resource calculations were increasing and analysts were advising investors to buy not sell.

Issues In Weighing The Evidence

Before my review of the evidence of the red flag allegations there are a number of issues I wish to discuss that will impact on the evidence of the red flags and on the weight to be given that evidence.

Those issues include:

- Obvious Prospectivity Of Busang For Gold
- Tampering Was Unprecedented And Assay Results Were Believable
- Hindsight
- Mining Industry Rules Changed Because Of The Bre-X Fraud
- Drill Hole Results Trump Geological Puzzles
- Comparison With The Kelian Gold Mine
- The Changing Brightest Red Flags
- Professionals And Experts Involved With Busang
- Barrick Was Confident There Was Gold In Busang
- What Farquharson Knew Of Felderhof's Experience
- Felderhof's Extensive Experience In The Pacific Rim
- Farquharson's Lack Of Experience In The Pacific Rim
- Red Flags For Felderhof But Not For Strathcona's Clients
- Strathcona's Retainer And Impartiality
- Issues With Dr. Hellman's Evidence
- Issues With Terry Leach's Evidence

- Issues With Graham Farquharson's Evidence

OBVIOUS PROSPECTIVITY OF BUSANG FOR GOLD

The Defence agrees with the O.S.C. submissions in paragraphs 878-881 of Exhibit S5

Volume II:

> Para. 878. There is perhaps one agreed fact in this case. Busang was prospective for gold mineralization. Hellman stated that its prospectivity was obvious from its location in relation to other gold deposits in Kalimantan, Indonesia. All of the experts agreed that the Busang area was prospective.
>
> **The Defence agrees.**
>
> Para. 879. Many people with geological backgrounds who visited the site quickly identified its prospectivity.
>
> **The Defence agrees.**
>
> Para. 880. Leach described prospectivity as the "...potential to discover a major deposit..."
>
> **The Defence agrees.**
>
> Para. 881. Sharwood also a geologist described it as meaning "an area of geological interest"
>
> **The Defence agrees.**

In Exhibit 208, Strathcona's Busang Technical Audit, Farquharson states at page 20:

> Busang has characteristics favourable for gold deposition. These include its location on a major tectonic boundary – the Kalimantan Suture – which also hosts the Kelian maar diatreme gold deposit, classified as a carbonate-base metal gold deposit by Corbett and Leach (1997), and other gold occurrences, including Mt. Muro. The proposed maar diatreme setting and the type and large size of the alteration system at Busang are further positive indicators for gold mineralization. Available information indicates, that these conditions may have led to deposition of some gold in the Central Zone, while drilling of the Strathcona holes in the Southeast Zone proves that this zone, despite its strong alteration, contains traces of gold only.

And at page 51:

> The Busang geologic setting is such that there is no doubt that it represents a valid exploration target for gold. Discussions with the consulting geologists Greg Corbett and Terry Leach, brought to the Busang site at the time of our visit by John Felderhof, and who have an excellent background in the geologic environment of settings such as Busang confirm the highly prospective nature of the geology and thus, the site selected for a tampering program has been well chosen.

Westralian Results

Westralian drilled 19 holes in the Central Zone before Bre-X's involvement in Busang.

Farquharson testified that while Westralian "*had found gold in some of the drill holes, the continuity and the extent of the mineralization was not sufficient to indicate that there was an economic deposit.*" Farquharson based his opinion on the fact that Westralian "*did not continue on with further work on the Central Zone*".

In cross-examination Farquharson conceded that in fact he did not know why Westralian "*did not continue with further work.*"

He testified he was making an "*assumption*". He agreed he was "*guessing*" and he agreed "*guessing*" was not of assistance to the court.

Transcript: March 21, 2005, pages 26-27

Dr. Hellman

Dr. Hellman testified:

> The only opinion I can offer is that there is an undetermined component of the Central Zone that is real mineralization; in other words, the presence of the gold can only be explained by it being a genuine deposit.

Transcript: November 3, 2005, page 8

And:

> ...it occurred to me that there was only one explanation for certainly at least the Central Zone, and that was that there probably had been tampering upon genuine gold mineralization. How far that extended into the Southeast Zone, I still do not know.

Transcript: November 2, 2005, page 60

Dr. Hellman believed a drilling program in the Central Zone would be positive.

Transcript: November 2, 2005, page 62

The Central Zone only held only a small percentage of the total gold Bre-X reported in the press releases in Counts 5-8.

With respect to the Southeast Zone Dr. Hellman testified:

> MR. GROIA: Let's then turn our attention to the Southeast Zone. Have you been able, as a result of your work, to reach any conclusions about how much gold there may be in the Southeast Zone?
>
> MR. HELLMAN: No, I'm not aware of – no, I don't believe I can do that. I can only go on the assumption that the area that had been tested by Strathcona has been proved to be negative, and similarly with the area tested by Freeport, though I understand that there is a significant area between the Central Zone and the northern part of where those due diligence holes were drilled which would remain open.
>
> ...
>
> MR. GROIA: Is there any other evidence that you're aware of today that would suggest to you that there is reason at least to go and take another look at the Southeast Zone?
>
> MR. HELLMAN: Well, undoubtedly there has been genuine porphyry mineralization identified at depth. The area consists of the right geological environment; in other words, there had been a number of intrusives that have been extremely heavily altered and it could well be that the area of drill testing to date has been in the wrong place.

Transcript: November 2, 2005, pages 62-63

Terry Leach

Leach testified that after the first days at Busang he thought it was a valid deposit:

> MR. GROIA: Mr. Leach, when you were on the Busang property doing the work you did in April of 1997, are you able to comment on whether there was anything you saw, or any of the work you did that suggested that tampering had taken place?
>
> MR. LEACH: No, there wasn't. As I said, after the first four days that Greg and I were there looking at surface features in the Central Zone and the Southeast Zone and having gone through the core, the skeletal core from the Central Zone and the Southeast Zone, basically we thought it was a valid deposit.

Transcript: December 13, 2005, page 65

At page 25 of Exhibit 1328B Leach states:

> During the visit to Busang, the style of alteration, vein development and mineralization that I observed in the skeleton core was so similar to that in the East Prampus Zone at Kelian, that I was confident that the Central Zone at Busang was a valid carbonate-base metal gold system. At this time Corbett and I felt that both the South East Zone and the Central Zone at Busang were valid gold projects. This assessment was based on what Corbett and I had seen at the surface in the Central and South East Zone, the style of alteration and mineralization in core from the Central Zone drill holes, as well as the South East Zone drill holes BDH 05 and BSSE 275, and the gold that Corbett had panned from streams that drained the South East Zone. There was nothing at that point in time that indicated that the gold, which was reported in the assays from the Bre-X drilling, was not there.

Exhibit 1328B: page 25
Exhibit 1328A: page 21

Leach's later more detailed work and resulting issues are discussed under Red Flag 8.

Leach testified:

> MR. LEACH: Well basically with the samples that I collected I could see gold in it. And the same amount of gold I saw and the same frequency of gold in the samples I collected at Busang were exactly the same as the frequency of gold that I saw at Kelian. So I know there is gold there. I assayed the core from the veins that I took from the Central Zone. The vast bulk of them had significant amounts of mineralization and up to more than 2 ounces of gold in the vein samples. And I think of all of the vein samples that I took, they are averaging somewhere up in between 5 and 7 grams per tonne gold. So there is significant amounts of gold in the Central Zone.

Transcript: December 12, 2005, page 110

The O.S.C. admits that the samples from the Central Zone that Leach observed under the microscope were made from skeleton core and did not contain salted gold but was "*natural gold*".

Transcript: December 12, 2005, pages 85-87
Exhibit S13: paragraph 16

At page 117 of Exhibit 1328B Leach states:

> The Busang project area is located within a major gold district and has the same optimum tectonic and structural settings as the Kelian and Indo Muro gold mines and other major gold prospects in Kalimantan. It is also situated along the Kalimantan magmatic arc that hosts Carlin-style gold deposits in Sarawak, porphyry copper deposits in Sabah prospects in Central Kalimantan, and epithermal gold and massive sulphide prospects in East Kalimantan.
> The Busang project is located in an optimum geological setting for gold mineralization.

Exhibit 1328B: page 117

Dr. Kavanagh

Dr. Kavanagh obtained his Ph.D. in economic geology from Princeton University in 1954. He has worked as an exploration geologist, chief geologist and consulting geologist. He was President of Newmont Mining Corporation from 1973-1975 and Vice-President of Exploration for Rio Algoma Mines Limited from 1975 to 1986. He jointed American Barrick Resources Corporation in 1987 and was Senior Vice-President Exploration for Barrick when he retired in 1994. He joined the Bre-X Board of Directors as an outside director on April 28, 1994.

Transcript: April 4, 2001, pages 4-32

Dr. Kavanagh agreed "*The geological setting [at Busang] is such that there is no doubt in your mind that it represented a valid exploration target.*"

Transcript: March 14, 2005, page 39

Dr. Kavanagh continued to believe there was a substantial amount of gold at Busang until Strathcona's negative results.

Transcript: March 8, 2005, pages 33-34

Dr. Kavanagh testified Strathcona's negative results came as "*a great shock*" and "*a great disappointment*" to him.

Transcript: March 2, 2005, page 73

Dr. Kavanagh testified that the Central Zone "*even today could stand more work and possibly develop a mineable deposit of three million ounces.*"

Transcript: March 2, 2005, page 74

Paul Semple

Semple received a Bachelor of Science degree in Mining Engineering from Queen's University in 1983. He worked for Campbell Resources then Placer Dome and in 1987 he joined Kilborn Engineering Pacific. He first worked as a project metallurgist including the Kelian gold project where he worked on the final feasibility study. He was promoted to Vice-President of Mining and Metallurgy. He was involved in Kilborn's work for Bre-X from 1995 to 1997.

Transcript: January 23, 2006, pages 2-6

Semple testified:

> MR. GROIA: Had you reached any conclusions as to whether tampering had taken place on or about, well I should say, on or before May the 3rd, 1997.
>
> MR. SEMPLE: At that stage you have got to remember we had seen, we had seen all, we had seen Freeport information, we had seen additional information from Barrick. We had had, or I had had discussions with people at the Sheraton Project. At that stage I was, I was believing that salting the samples was more possible. I still – what I – if I was to predict results I would have, my prediction at that stage – and it was my prediction at that stage because I discussed it – was that I thought that the results from Strathcona would come in at something around 1.5 grams rather than at 2 grams. So there was gold there. There may have been some samples at the end of the programme that had been sweetened, I guess, rather than salted. But I was willing to – and still –you know, these were theories – I still believed there was a possibility that they would come back, you know, either as expected by Bre-X or as, you know, salted samples with little gold in them.
>
> ...

MR. GROIA: Do you have any view today, Mr. Semple, as to whether these results were sweetened or salted?

MR. SEMPLE: I am still surprised that all the Strathcona results came back as low as they did, that surprises me. But that doesn't mean that, you know, I believe the results of the independent programme done by Strathcona would prove if there was salting or not on the portion of the deposit that they drilled.

MR. GROIA: What about on the rest of the deposit?

MR. SEMPLE: The rest of the deposit, if it hasn't been looked at, in my opinion would still need, there would still be some question in mind especially some of the early stuff in the Central Zone I believe it was called.

MR. GROIA: And that question – what question in your mind would you be asking?

MR. SEMPLE: I guess, if you assume that the Strathcona results indicate tampering, I am not necessarily convinced that it started at day one.

Transcript: January 25, 2006, pages 70-71

TAMPERING WAS UNPRECEDENTED AND ASSAY RESULTS WERE BELIEVABLE

At paragraph 853, Exhibit S5 Volume II, the O.S.C. states "*that 25,000 or 30,000 samples were tampered with over a three and one half year period.*" That was unprecedented in the history of mining.

Farquharson

In the covering letter for Exhibit 208, Strathcona states:

> However, the magnitude of the tampering with core samples that we believe has occurred and resulting falsification of assay values at Busang, is of a scale and over a period of time and with a precision that, to our knowledge, is without precedent in the history of mining anywhere in the world.

Farquharson testified in cross-examination that he stood by that statement.

Transcript: March 23, 2005, pages 29-30

At page 50 of Exhibit 208 Strathcona states:

> When first requested by Bre-X to undertake this audit assignment, we were asked if it was possible to think of tampering with the Busang data to which we quickly replied that this would be most unlikely, given the number of samples that were involved.
>
> ...
>
> What has been difficult has been the acceptance of the evidence that this tampering has occurred for so long, on such a scale, and with such accuracy as to give the assay values and subsequent interpretation of those values, the appearance of being plausible.

And at page 52:

> The step in the tampering process postulated that we have the most difficulty to accept, but yet at the same time are impressed with its success, is the accuracy with which gold has been added to so many samples to result in assay values that, in the absence of other information and the observations we made previously, could be accepted as being a reasonable range of grades compatible with the geology.

At page 53:

> All of the foregoing suggests that those involved in the tampering process have had a very good understanding of the geology of the Busang property and have the knowledge required to determine the very small amounts of gold required to result in sample assays that would be compatible with the geological interpretation.

Farquharson testified in cross-examination that:

> MR. GROIA: ... And I am suggesting to you that the person or persons who salted these samples had to be incredibly sophisticated in order to allow this process to continue in the way that it did?
>
> MR. FARQUHARSON: Yes.

Transcript: March 23, 2005, page 29

Farquharson also testified "*that the tampering was done with a remarkable degree of consistency in terms of the assay value...*".

Transcript: March 16, 2005, page 91

On a different date in cross-examination Farquharson would not agree "*that the Busang results were plausible, reasonable and something that would fit with the geology.*"

It was then pointed out to him that when he had testified before Sheppard J. as an expert in R. v. Harper [2000] O.J. No. 2791 he volunteered exactly that about the Busang results:

> MR. GROIA: And then you volunteer this, I believe, Mr. Farquharson:
>
> "Again I emphasize that the difference there as compared with the Stenpad property is that the results that came out of the Busang property, the numbers looked plausible, reasonable and something that would fit with the geology."
>
> MR. GROIA: Do you recall being asked those questions and volunteering that answer?
>
> MR. FARQUHARSON: It is there in writing.
>
> MR. GROIA: And you were sworn to give evidence on that occasion under Oath?
>
> MR. FARQUHARSON: Yes.
>
> MR. GROIA: And those answers were true, were they not, as of that date?
>
> MR. FARQUHARSON: Yes.

Farquharson added a proviso in the case at bar:

> MR. GROIA: And they are true as of today's date?

MR. FARQUHARSON: Yes, with the proviso that I obviously made those statements on the basis that somebody had not looked at all of the detail data that we had looked at when we went to the property.

MR. GROIA: Where will I find that in the transcript, Mr. Farquharson?

MR. FARQUHARSON: It's not there.

MR. GROIA: No. You were trying on that occasion to assist the O.S.C. with its prosecution of Mr. Harper arising out of the Stenpad results, correct?

MR. FARQUHARSON: Yes.

Transcript: March 29, 2005, pages 47-48

That proviso was not part of his sworn evidence in Harper. On page 48, Farquharson agreed that in Harper he testified the Bre-X "*assay results were believable for [the Busang] geology.*"

Transcript: March 29, 2005, pages 44-48

If "*the Busang results were plausible, reasonable and something that would fit the geology*" and if "*the assay results were believable for that geology*" as Farquharson testified then that is in effect saying that there were no geological red flags.

Freeport/Colin Jones

Farquharson gave a video taped lecture in 2001 at the Colorado School of Mines for the Society of Economic Geologists where he made reference to Colin Jones who was the geologist for Freeport who went to Busang as part of their due diligence and drilled the first hole which came back negative.

In the video Farquharson said: "*So he [Colin Jones] got back the assay results with no gold in it. He thought for sure that the assay laboratory must have got his samples mixed up with some other property.*" This statement about Colin Jones would support the Defence position that there were no red flags at Busang and that Freeport, like Bre-X and Kilborn's Semple believed Bre-X's results even after drilling by Freeport began to show negative results.

Farquharson would not concede this and before the video was played in court Farquharson testified he had "*made that comment [about Colin Jones] in jest*".

> MR. GROIA: And perhaps so that we don't need to show you the video, would you agree with me that anyone attending the lecture would have come to the conclusion that you were quoting Mr. Jones rather than making something up and putting those words into his mouth?
>
> MR. FARQUHARSON: It was intended that it would be a light comment and I think the audience interpreted it as such.
>
> MR. GROIA: That he was so astonished by the results that he would have jumped to the conclusion that the samples must have been mixed up with some other property.
>
> MR. FARQUHARSON: As I said, Mr. Groia, I made that comment in jest. I don't believe Mr. Jones made that comment. When I made that talk I made that comment that probably Mr. Jones made the statement.

Transcript: March 23, 2005, pages 1-2

In the video which was then played in court Farquharson stated:

> THE WITNESS: (On tape) They were planning to lay out more drill ore holes. They didn't seem to be too concerned about what might have been found in the holes that they drilled previously. The fellow in the turquoise shirt is a fellow called Colin Jones and he was with Freeport Minerals and he is really the fellow that drilled the discovery hole on Busang because he put down the first hole for Freeport. So he got back the assay results with no gold in it. He thought for sure that the assay laboratory must have got his samples mixed up with some other property.

The video does not support Farquharson's position.

Farquharson's position is also not supported by his October 1997 letter to Bre-X where he states:

> The second advantage that we had was that we received an excellent two-hour verbal presentation from Freeport in the morning of March 26 during which they summarized the work that they had done but during which they were very careful to not state that they did not believe that there was no gold at Busang. In fact, their parting line was that there must be gold at Busang somewhere with all the work that has been done by Bre-X and they were ready to work with Strathcona to help us find it.

As noted above even after the negative results from Freeport, Semple still preferred to believe that there was gold and that the Strathcona results "*would come in at something around 1.5 grams*" per tonne or even "*as expected by Bre-X*".

Terry Leach

Leach testified about the tampering:

> ...then Freeport didn't find that much gold. I mean suddenly we felt that there was – and we couldn't describe, we couldn't explain it on a geological basis, then I think that we suddenly realized before we left Busang that there was something seriously wrong. And I think that we never kind of really thought that it would be possible that salting could have been done to such a degree. It matched all of the, you know – just basically on the geology. But I mean, you know, it looked valid. So I mean we didn't actually kind of, we didn't actually think that it would be possible to salt it that well and to that degree.

And:

> MR. GROIA: And other than the negative results from Freeport and the negative results from Strathcona, are you able to say, Sir, whether you are aware of any red flag that would have suggested tampering to a geologist such as Mr. Felderhof?

> MR. LEACH: I mean no. That's basically why I mean, you know, that I was more than happy to help him as a technical adviser because I mean I just totally felt that Mr. Felderhof had nothing that he could see at the time that he was doing the work that would tell him that it was tampering. I mean neither Greg nor myself could see it unless we did detailed work and that detailed work was way outside what would be expected of a general manager of a company. I mean general managers don't do that kind of work. And so, you know, I have been – I can't see anything that I could see that when Mr. Felderhof was working at Busang, given his position and also what was there, that he could have known. So I mean that's, I guess that's why I basically was happy to help him because I realized that there is nothing you could see. It was such a – the salting was done so well and the fact that it was done on a totally valid hydrothermal system with all the characteristics of mineralization, I can't see any way that he could have known.

Transcript: December 13, 2005, pages 66-68

In commenting on paragraph 37 in Exhibit S13, the O.S.C. states:

> On cross-examination Leach agreed that the salting at Busang was systematic; it was carried out over a long period of time; the salting was done on top of an existing deposit in the CZ and the SEZ; this salting on top of an existing gold deposit even if it wasn't a deposit of economic value would be a difficult thing to do. He agreed that this is a very sophisticated salting scheme; one that would have required a detailed knowledge of geology; an intimate knowledge of carbonate base metal systems and some understanding of the grade and distribution in carbonate based metal systems like Kelian.

Exhibit S13: paragraph 37
Transcript: December 15, 2005, pages 58-59

Dr. Hellman

At page 3 of Exhibit 1202 Dr. Hellman agrees with and quotes Strathcona's covering letter in Exhibit 208:

> Busang was a rare instance of a determined and intelligently planned fraud that had been cleverly disguised in the context of real mineralization that withstood the close scrutiny of many experienced practitioners from the minerals industry. It was achieved with

"...a scale and over a period of time and with a precision that, to our knowledge, is without precedent in the history of mining anywhere in the world."

Dr. Hellman testified:

> MR. HELLMAN: ...The material on the right-hand is the side of alteration that most geologists would be quite interested in in [sic] terms of its association with gold. The material on the left is reasonably boring in terms of a geologist's expectation that it might contain gold. But you can see every so often there are a pile of fragments within that.
> I was intrigued to see how the assays correlated with these two samples, and I was staggered to find that the sample on the right had elevated gold grades and the grades on the left were quite subdued. And it was at that particular moment when I saw that, that I realized how precise that the tampering had been, that the person responsible must have had a geological knowledge, they would have had access to very detailed geological logs, and had actually gone to the trouble of titrating their assays with the amount of alteration in the samples.
>
> MR. GROIA: What do you mean by titrating?
>
> MR. HELLMAN: Of adjusting. So if it was very altered and had all the characteristics of mineralization, for instance it might have had sulphides, pyrite, gilanous, pheterite, those sorts of things, maybe even stibnite.

...

And:

> MR. HELLMAN: ...[I]t gave me a new respect as to the way one should approach this whole business. I think I might have been somewhat arrogant in my approach beforehand, thinking how can anybody allow a fraud like this go on for so long. And it was only when I really gone down, in a sense, on my hands and knees with a hand lens and I looked at detail – in great detail at the results, not only these sorts of results, but at some of the metallurgical results, that I guess I had a respect, though that's the incorrect word, but certainly an understanding of the degree of precision that the perpetrators went to pull this off.

Transcript: November 2, 2005, pages 58-59

The O.S.C. denies paragraph 34 of Exhibit S13 but admits that Dr. Hellman testified that:

MR. GROIA: What factors can you recall that seemed to you at the time to be counter indicative of salting?

MR. HELLMAN: There were a number of results that I was genuinely perplexed by. The first one which was vivid in my mind was the results of the gravity pilot plant results, which came from a 27 tonne pilot plan [sic, plant] test.

COURT REPORTER: Tonne –

MR. HELLMAN: --pilot plan [sic, plant] test. And that had been performed by a laboratory called Amdel in Adelaide, Australia. And in the final monthly report, I believe of the whole project, which was February 1997, Kilborn predicted that the gravity recovery was likely to be 50 percent. To me that was incompatible with the gold being added, tampered.

The other result which was incompatible with tampering were some amalgamation results. The details of those I don't believe I had access to though in the meeting...

...

MR. HELLMAN: ...And those results were also incompatible with tampering. There are a number of other factors. One overriding factor was how was it possible that there could be so many groups of such a reputation, over such a length of time, and so many drill holes, how is it possible that this could have gone uncovered for so long?

There was one particular section which was 66.5, which is up on the board, which indicated to me there was good correlation from hole to hole. There were other results that were portrayed in microphotographs which showed that there were gold grains very much smaller than 100 microns, and if the hypothesis was that the salted gold was probably panned from an alluvial situation, it seemed to me unlikely that that gold could have been added to the samples because it was too fine and likely to have been lost from the pans.

Transcript: November, 2, 2005, pages 39-40
Exhibit S13: paragraph 34

Computer Data Mine Model

Kilborn believed the assay results. They lined up with their computer model used to estimate ore reserves for Busang.

Dr. Hellman testified with respect to Kilborn's use of the Data Mine software and model on Busang:

> MR. GROIA: You're familiar with Kilborn's use of the Data Mine software and Data Mine model on the Busang property?
>
> MR. HELLMAN: I'm aware that they used Data Mine to manipulate the drill hole data and to produce their model of the resource estimates, yes, I am.
>
> MR. GROIA: And are you familiar with how Data Mine works in general terms?
>
> MR. HELLMAN: Yes. We use Data Mine in our group. We also use a number of the other pieces of mining software. There are probably five or six pieces of mining software that are specifically used to quantify and to manipulate geological data. And this type of software is very specialized because it had to be able to import the files that I described before, the digital database of Kilborn, it has to be able to import that; it has to be able to plot cross sections, to plot plans, to create contour maps, and finally, in the case of advanced projects, it has to be able to calculate the resource estimates and also to be able to produce all reserves once the mining engineers get involved and start to design the actual mine plan.
>
> MR. GROIA: You said yesterday in your testimony, Doctor Hellman, that this salting or tampering program would have had to have been carried out with precision. Do you recall that?
>
> MR. HELLMAN: Yes, I do.
>
> MR. GROIA: If the program had not been carried out with precision, or with the precision that you were speaking of yesterday, if the tampering had been done in a way that was less precise, are you able to tell the Court what effect that would have had on Kilborn's ability to develop the Data Mine model and the work that it was doing to create that model by using all the drill core results?
>
> MR. HELLMAN: Well, very typically, Mr. Groia, the first assessment one does – and Data Mine has the capability of doing that –is to assess the statistics of the gold grades. One looks for the shape of the population, one looks at how skewed it is, how unusual variations occur in the gold grades, because the more extreme the grades, the more difficult it is to model. And from my review of the documents, Ms. Zofia Ashby, in her work, has a number of sections which describe the statics of the assays and that is a very typical part of the work that we do, and is typical of any group like ourselves. So her work was standard in that respect. One assesses the gold grades. There was nothing unusual about that and she reported that there was nothing unusual about that. Then that leads into looking at what's called the special variability and that consists of how predictable are the results from hole to hole, from section to section. And I was

able to verify that the special variability was very typical of real gold deposits and that process was something that Kilborn had gone through using Data Mine.

So basically if there'd been anything unusual at that stage, then I'm sure it would have been reported and drawn attention to. And I'm not aware in the work that I've done that there are any concerns, or any alarm bells ringing in the work that she did.

MR. GROIA: So can you then comment, Doctor Hellman, on whether the Data Mine work that was done by Kilborn allows you to draw any correlation between that work and the precision of the tampering scheme?

MR. HELLMAN: Well, in terms of precision of the tampering, the area that I was probably alluding to yesterday – I was alluding to yesterday was the relationship of the gold grades to the actual geology. And you might remember that I showed some photographs, I described some photographs, whereby the grades correlated with the degree of alteration of the rock, so that there was a consistency between the geology and the assays. And that was certainly commented on MRDI.

At the moment I don't recall any specific comments by Kilborn.

But that is a step of the process that any group would assist straightaway, and that is the way in which the geology correlates with the assays to make sure that when you produce your resource estimates, that you're not producing estimates that are unbelievable, or unreliable, or geologically implausible. The whole test of resource estimates is are they consistent with the geology, and there ae [sic, are] safeguards that – one safeguard I can remember that she took to ensure that she was not overstating the resource estimates. So as far as I recall, the steps that she used in the Data Mine process were adequate to identify anything unusual or aberrant.

MR. GROIA: So would it be your view that the use of the Data Mine program and the results of the Data Mine program would qualify as another form of a green flag at Busang?

MR. HELLMAN: By all means, yes.

Transcript: November 3, 2005, pages 39-42

Paul Semple

Semple's evidence with respect to prospectivity previously reviewed at pages 143-144 above includes some evidence about tampering.

The O.S.C. points out that in cross-examination Semple testified:

> MR. COLE: And again Mr. Groia asked you if there was anything in the various reports that caused you concern that the samples had been salted. First of all, I think you would agree with me that that wasn't something that was in your mind at that time?
>
> MR. SEMPLE: Our objective, our prime objective wasn't looking for tampering or salting, no. We were looking to design a mining operation.
>
> MR. COLE: And, in fact, looking for tampering or salting wasn't your mandate at all?
>
> MR. SEMPLE: That's correct.
>
> ...
>
> MR. COLE: And is it fair to say that tampering was, in fact, the furthest thing from your mind as you are working on this project?
>
> MR. SEMPLE: The furthest thing from my mind. There is lots of things that go through your mind. We weren't there to look for tampering.

Transcript: January 25, 2006, pages 72-73

Kilborn was not mandated to look for tampering, it was not their prime objective, they "*weren't there to look for tampering*".

Before the Bre-X fraud and the change in regulations that followed that fraud, the mining industry did not suspect that such sophisticated tampering on such a scale could occur and was not actively looking for it. Felderhof was in no different position.

Kilborn was not there to look for tampering but Kilborn was a well respected company and Kilborn wanted to develop Busang with Bre-X. Kilborn certainly would not want to invest in a scam and would not have ignored any signs of tampering or red flags.

In commenting on paragraph 42 of Exhibit S13 the O.S.C. submitted:

> The OSC admits that the draft minutes of the Bre-X board meeting, May 3, 1997, state "...The consensus from the metallurgical and mining people was that it was difficult to orchestrate such a fraud from a size magnitude perspective". Semple gave the following evidence about this excerpt of the minutes.
>
> THE WITNESS: "I think that when you look at all of the work that had been done, all the drilling that had happened and all the assays that had been done, it was easier for some of the mining and metallurgical people, including myself, to come to believe that a more plausible explanation would be that there was a problem at the lab during the Freeport, when the Freeport assays were done, than it was to look at how a tampering scheme had happened over that period of time on a low grade deposit."
> [Semple transcript, January 25, 2006, p. 60]

Exhibit S13: paragraph 42
Exhibit 207
Transcript: January 25, 2006, pages 60-62

Peter Munk

Munk testified:

> MR. MUNK: ...ever since I heard the name Bre-X and I followed the case quite closely, it never occurred to me once that a fraud of this magnitude could be possibly happening in a country as developed in the mining industry as Canada.

Transcript: December 7, 2005, page 65

Dr. Kavanagh

Dr. Kavanagh testified that the tampering was "*unprecedented*", "*sophisticated*" and required "*remarkable technical ability.*" Dr. Kavanagh was "*astonished*" and "*didn't believe it at first*" when the suggestion of salting was made.

> MR. GROIA: And so during the time that you were looking at these cross sections, the cross sections you were preparing.
>
> MR. KAVANAGH: Yes.
>
> MR. GROIA: Was there ever an occasion where you saw something that was inconsistent to your eye?
>
> MR. KAVANAGH: No, there was never a time.

Transcript: March 2, 2005, pages 28-29

...

> MR. GROIA: All right. There was never a red flag that you saw on the drilling results.
>
> MR. KAVANAGH: Never.
>
> MR. GROIA: So if we're going to assume for the moment that someone salted those results before you got them sent to you.
>
> MR. KAVANAGH: Salted the?
>
> MR. GROIA: The results, salted the core.
>
> MR. KAVANAGH: Yeah.
>
> MR. GROIA: Which then resulted in a false assay being summarized and sent to you, we assume that, would you agree with me that that person had to be quite sophisticated in the way they approached that work?
>
> MR. KAVANAGH: I would agree with that.
>
> MR. GROIA: Because what they had to do was to make sure that as they salted that one drill core from wherever they started to wherever they stopped, they had to salt in a manner that was not going to create a red flag to an experienced geologist like yourself.

MR. KAVANAGH: Yes.

MR. GROIA: That's not an easy thing to do, you would agree?

MR. KAVANAGH: I would agree with that.

Transcript: March 2, 2005, page 29

...

MR. GROIA: But did the fact that you were doing cross sections allow you to start to form an opinion as to the shape and location of the deposit?

MR. KAVANAGH: Yes.

MR. GROIA: And within that shape and location, there would be areas which in your opinion you started to believe to be mineralized, and other areas that you started to believe were not mineralized.

MR. KAVANAGH: Yes.

MR. GROIA: And the person or persons who allegedly salted the results would have to be able, throughout all of these drill holes and all of these intervals, to produce salted results consistent with that model, is that fair?

MR. KAVANAGH: Yes.

Transcript: March 2, 2005, page 33

...

MR. KAVANAGH: ...I don't think there's too much doubt that there would have to have been 25,000 two metre interval samples salted.

Transcript: March 2, 2005, page 34

...

MR. GROIA: Would you agree with me that it took remarkable technical ability to successfully tamper with 25,000 or 30,000 samples?

MR. KAVANAGH: Yes.

MR. GROIA: It's been said that that's unprecedented in mining circles. Would you agree with that statement.

MR. KAVANAGH: I think so, yes.

MR. GROIA: You were astonished when the suggestion of salting was made.

MR. KAVANAGH: Yes.

MR. GROIA: You didn't believe it at first.

MR. KAVANAGH: I did not.

Transcript: March 2, 2005, page 34

...

MR. GROIA: Would you also agree with me, sir, that there were a number of other positive indicators to suggest that the Busang results were legitimate, besides the plotting of the cross sections?

MR. KAVANAGH: Yes.

Transcript: March 2, 2005, page 35

...

MR. GROIA: So I'm not suggesting that they were so clumsy as to salt samples that had no mineralization, I'm suggesting that they were sophisticated enough to salt heavily mineralized sections to a higher grade, than lower mineralized hydro fractured sections.

MR. KAVANAGH: In a general way, that was the case. The results mirrored, if you will, the indicated –the indications of mineralized expressed in the drill logs and in the weekly time report.

MR. GROIA: And did so to such a successful degree, that it never set an alarm bell off in your review of any of the drill hole results.

MR. KAVANAGH: Yeah. That's right. And we're talking about large sections. We're talking about – within those sections there would be variations; in the next hole those variations might be in different places, but in the overall section there would be connectability.

Transcript: March 2, 2005, pages 94-95

...

MR. GROIA: And did it give you a certain degree of comfort or confidence that you were preparing your own cross sections?

MR. KAVANAGH: Yes, my own presentations mirrored the ones that were being done in Indonesia.

MR. GROIA: And they eventually, when Kilborn started to do cross sections, were mirrored by Kilborn's work too, were they not?

MR. KAVANAGH: Yes.

Transcript: March 7, 2005, pages 95-96

...

MR. GROIA: Do you agree with me that what has been the most difficult to accept in this case about the salting is the fact it had occurred for so long, and on such a scale, and with such accuracy, as to give the assay values the appearance of being positive?

MR. KAVANAGH: Yes.

MR. GROIA: Would you go so far as to agree with me that, to your knowledge, the Bre-X case is unprecedented in the history of gold exploration?

MR. KAVANAGH: Yes.

MR. GROIA: And in particular, never before has there been salting on such a scale or magnitude ever carried out anywhere in the world to your knowledge.

MR. KAVANAGH: To my knowledge.

Transcript: March 14, 2005, page 40

HINDSIGHT

Exhibit 755, Freeport's Site Visit Report dated March 6, 1997 has the following note dated April 18, 1997 added to the end of the text of the report:

> Note: The bulk of this report was written prior to receiving the results of the Due Diligence drilling Program. The negative results from that program have cast the Busang "Deposit" in a far different light than it was in at the time of this trip. In hind sight some of the comments in this report may seem a bit naïve but the reader is asked to remember that the author was viewing this as a golden (pun intended) opportunity and approached the task in an optimistic light. The bucket of cold water that quenched the fire of optimism was still some weeks in the future.
> DRP, Jakarta, April 18th, 1997

Exhibit 755: page 15

Farquharson was cross-examined about Exhibit 755.

> MR. GROIA: And he is saying that now with the benefit of hindsight, or I guess the value of hindsight, he has a very different view of those same results, right?
>
> MR. FARQUHARSON: Yes.

Transcript: April 4, 2005, pages 37-38

Freeport's original due diligence observations and findings remained the same. They did not in fact change but their interpretation changed from positive to negative with the benefit of hindsight.

Farquharson agreed with Groia's suggestion that,

> ...when one looks at the red flags that Strathcona claims to have identified it will be important for us to keep in mind that we all now have the benefit of hindsight which will cast a far different light on those red flag because of the results of the Strathcona drilling programme.

Transcript: April 4, 2005, page 38

Farquharson also agreed that if Strathcona had gotten positive results from their drilling program they would not have suspected their results had been tampered with. But the actual facts underpinning the alleged red flags would still have been the same, just not red. What I find that Farquharson is saying is that while Strathcona would not have suspected their own results they expected Felderhof to suspect Bre-X's results. Strathcona expected Felderhof to suspect Bre-X's results although Busang was

prospective, the tampering was unprecedented and other professionals working for Bre-X were not suspicious.

Transcript: April 4, 2005, pages 37-39
Exhibit 755

On page 6 of the October, 1997 letter Exhibit 681 Appendix VII Strathcona states:

> The query has been made to us on several occasions as to why Strathcona was able to identify the problem in such a short period of time whereas other observers had not. Our response has been that we had two major advantages over those who had been involved with or had followed and reported on the developments at Busang.
> One was that when we arrived in Jakarta on March 24 we have been forewarned that there might be a problem with the estimated gold resources at Busang and as a consequence we went looking for trouble and examined every document, comment and action very critically...

Exhibit 681: Appendix VII

With hindsight Strathcona "*went looking for trouble*". As noted above in Exhibit 755 Freeport first "*approached the task in an optimistic light*" and saw no red flags. After getting negative results, with hindsight, Freeport then interpreted things differently.

At page 40 of Exhibit 1328A Leach states.

> The Strathcona group involved in the Busang audit had the significant advantage of 20-20 hindsight in the identification of these 'red flags'. Prior to the Freeport due diligence, this hindsight was not available to anyone involved in the geological assessment of the Busang project.

Exhibit 1328A: page 40

M.R.D.I., Kilborn and all the other independent professionals retained by Bre-X did not have the benefit of hindsight.

Felderhof did not have the benefit of hindsight.

MINING INDUSTRY RULES CHANGED BECAUSE OF THE BRE-X FRAUD

New rules regulating the mining industry came into force after the tampering at Bre-X; for example, the now required Technical Report Form 43-101. Before Bre-X those involved in mining did not look for tampering on the scale and sophistication that occurred at Bre-X. Since Bre-X the industry is now only too painfully aware of and taking steps to protect itself from the possibility of such large scale fraud.

An example of a 43-101 Report in Exhibit 744.

Farquharson testified:

> MR.GROIA: And then in this presentation you talk a little bit about what could be done and then you come to the question that I am sure everyone wanted your answer on which is, can it happen again. And do you recall the answer you gave?
>
> MR. FARQUHARSON : It would have been something along the lines of this could never happen again because people had had the experience of being through the Bre-X story once and would obviously be much more critical and observant and careful in future. And, of course, subsequent to 1997 there were new regulations introduced for reporting on mineral properties with a high degree of independent reporting that would ensure that this process that occurred with Busang should not happen again.

Transcript: March 29, 2005, pages 55-56

Dr. Hellman testified:

> Generally speaking, at that time the necessity of auditing, tampering, security, all that sort of thing was basically not even thought about.

Transcript: December 5, 2005, page 15

In January 1999 the Toronto Stock Exchange and Ontario Securities Commission released the Final Report of the Mining Standards Task Force entitled "*Setting New Standards, Recommendations For Public Mineral Exploration And Mining Companies*". At page 7 the report states:

> The Bre-X scandal was the immediate impetus for the establishment of this Task Force. Bre-X was listed on the TSE, ME and ASE in Canada and on Nasdaq in the United States. In 1996, Bre-X announced what promised to be the greatest gold deposit ever discovered. Following months of heavy trading during which the share price skyrocketed, the Bre-X Busang deposit was proven to be a hoax. At its height, the market capitalization of Bre-X was $6.1 billion. Thousands of investors who sold before the hoax was uncovered profited while thousands of others lost as the stock price plummeted and the company was forced into bankruptcy.

At page 10 the report continues:

> This Report recommends a more coherent, standardized disclosure regime in which exploration and mining companies will be required to provide all material information on the state of their affairs and not merely what they wish to emphasize at any particular time. This new reporting regime will require exploration and mining companies to follow recognized industry best practices and to disclose their adherence to these practices. It is expected that with this enhanced disclosure, the absence of information in a press release or a departure from recognized industry standards will serve as a red flag to the recipients of the information.
>
> ...
>
> On adoption of NI 43-101 many of our recommendations will thereby be implemented.

Like Kilborn and all the other Bre-X professionals, Felderhof of course did not have the benefit of the new rules.

DRILL HOLE RESULTS TRUMP GEOLOGICAL PUZZLES

Dr. Hellman's opinion is found at pages 1, 126-127 of Exhibit 1202. At pages 126-127

Dr. Hellman states:

> It is a fundamental principle in mineral exploration that the ultimate and final test of reconnaissance geochemical sampling, geological mapping or geophysical surveys are the actual results from the drill holes. The veracity of the drill hole results is not judged by geochemical results from the surface soils or surface trenches. This is because these samples are subject to a variety of processes, many of which are poorly understood, including oxidation, erosion, water movement and glacial activity. The veracity of the drill hole results is also not judged by geophysical results such as from magnetic or gravity surveys.
>
> The drill hole results are the final test of the many (often contradictory) exploration surface results. The drill hole results were consistent with the geology of the core, as acknowledged by Mr. Farquharson who stated:
>
> > "There is a close correlation between those core intervals identified in the logging process as 'mineralized' with those intervals subsequently found to have gold values." (May 1997, p. 51) [6]
>
> Accordingly, once drill results have been received, all other data assume less importance. Mr. Felderhof's views regarding the surface results are well supported by the literature, the geology of Busang and, most importantly, the gold assays as provided in Kilborn's digital data.

Exhibit 1202: pages 126-127

Exhibit 685 is a PT Westralian Atan Minerals Summary Report On Exploration Activities Busang Project entered by the O.S.C. . That report states: "*the only reliable indication of gold [was] the assay.*"

Farquharson agreed that "*normally speaking drill results trump geochemical puzzles.*"

Transcript: April 4, 2005, page 45

Farquharson also agreed that if Freeport had had results that were comparable to Bre-X then Strathcona would never have become involved. In other words, if there had been no tampering, then even if all of the facts that Strathcona alleges existed to form the basis of the red flag allegations in fact existed there would be no allegation of red flags. Without the tampering these same facts would not have been viewed with 20/20 hindsight as red flags.

When a property is prospective and the drill hole results are consistent with the geology of the core, as was the case in Busang, then the "*puzzles*", the "*poorly understood*" and "*often contradictory*" exploration results are resolved by the drill hole results and are never seen as red flags.

This is so whether or not the results were or were not tampered with but once the tampering is discovered those once resolved "*puzzles*" again become unresolved and then turn into red flags as happened in this case.

"*Once there are drill hole results available, all other data assume less importance.*" "*The drill hole results are the final test of the many (often contradictory) exploration surface results.*" Kilborn and Felderhof and everyone else accepted drill hole results that were plausible in this prospective property.

COMPARISON WITH THE KELIAN GOLD MINE

Dr. Hellman

Dr. Hellman's opinion with respect to Strathcona's allegation that Busang is not similar to Kelian is set out at pages 20-21 of Exhibit 1202:

The Strathcona allegation that Kelian is not similar to Busang

> The style of gold mineralization found at Busang was compared by Bre-X geologists to the Kelian gold mine (about 150 km to the southwest of Busang, see Figure 56 in Appendix 4E). Strathcona concluded that this was an invalid comparison, stressing that that the two deposits sites have few similarities. In contrast, numerous independent consulting groups emphasized the similarity of Busang with Kelian. Consultants assisting Bre-X such as Mr. J. Borner (petrologist), MRDI, Normet and Kilborn were all very familiar with Kelian.

Within the body of their 2000 report, Strathcona states several allegations that appear to undermine the comparison of Busang to the Kelian gold mine. Strathcona's [37] allegations can be summarised in the following way:

- There is an absence of free or liberated gold at Kelian.
- This is consistent with no gravity plant at Kelian.
- Any comparison of Kelian with Busang on the basis of the presence of coarse gold is invalid because of Strathcona's belief that there was no evidence in the logs for coarse gold at Busang or at Kelian.
- The rarity of visible gold at Kelian and its lack at Busang should not have been used to suggest that the analogy of Busang with Kelian was valid. This is because much of Kelian's gold was described as refractory and submicroscopic whereas there was coarse gold identified in the Busang samples by mineralogical studies.
- Gold from the Kelian deposit is of an entirely different nature than that found in the tampered samples from Busang and reported on to Bre-X management including Mr. Felderhof.

Strathcona's understanding of Kelian is flawed. In actuality:

- the gravity plant (retro-fitted several years after production started) at Kelian is well known and large;
- the gold mineralization is characterized by coarse gold grains;
- the gold is not predominantly refractory; and
- mineralogical consultants who had studied Kelian reported to Bre-X that the samples from Busang were similar to Kelian.

Strathcona appears to have made no effort to discover that Kelian has a large gravity plant, which means that coarse gold occurs in the primary mineralization. The true situation at Kelian was, at the time of reporting of Strathcona's allegations, readily available from public sources. It was known that visible gold was rarely identified in drill core at Kelian even at grades over 25 g/t.

Van Leeuwen, et al. (1990) [8] provide the following comment which was written before production commenced:

> "Free gold [*at Kelian*] is rarely visible megascopically in either outcrop or drill core, and is also rarely detectable on the microscopic scale, even in samples assaying over 25 g/t Au."

Van Leeuwen's description of the apparent absence of visible gold is paradoxical in the light of Kelian's large gravity plant that produces significant amount of coarse gold. Kelian demonstrates that, although coarse gold may be significant in a deposit, it may be difficult to identify coarse gold in drill core and it may be grossly underestimated at the exploration stage.

With Kelian being used as a legitimate model for the Busang mineralization, it was natural and reasonable for Mr. Felderhof to place little importance on the levels of visible gold in the Busang mineralization compared with the obvious amount of visible gold observable in the gravity concentrates.

Strathcona's criticisms of the Busang-Kelian comparison are based on an out-dated and pre-production understanding of Kelian that is quite different from what is now known. It is often the case that the geological understanding significantly improves after mines commence and as greater complexity is revealed.

Exhibit 1202: pages 20-21

Leach

Leach's opinion is at pages 74-78, Exhibit 1328A and 127-139 Exhibit 1328B. Leach states in part in Exhibit 1328A:

> **C. SIMILARITIES BETWEEN BUSANG AND KELIAN GOLD MINE**
> **a) Introduction**
>
> ...
>
> It is my opinion that the many similarities between Kelian and Busang would have been a significant 'green flag' that would have given the Bre-X personnel confidence in the validity of the project.
>
> ...

The following is an outline of a comparison of the geological, geochemical, alteration, mineralization, and metallurgical features between Kelian and Busang.

...

b) Geological Comparisons

- The tectonic and regional structural settings of the two projects are very similar.

...

- The physiography of Kelian and Busang are similar and reflect comparable host rocks and alteration styles.

c) Surface Geochemistry

- Alluvial workings by local miners are recorded at both Busang and Kelian

- Exposure in the Prampus region at Kelian was poor and the high grade Northeast Zones were not exposed at the surface. Surface exposure in the Central Zone at Busang was poor. In the South East Zone, there was very poor exposure in the creeks and most leached surface rocks were covered by a veneer of mud and swamp debris.

- The results of assays from rock chip samples were comparable at both projects.

d) Resources

- Very similar average grades of 2.5-3 g/t Au.

...

e) Alteration and Mineralization

- The style of alteration and mineralization at Kelian and Busang are similar, and also closely comparable to carbonate-base metal gold systems throughout the Southwest Pacific region. The Prampus and Central zones are more comparable to those systems that are more base metal-rich (sphalerite-galena-tennantite-pyrite), whereas the North East Kelian and South East Zone at Busang are of the more carbonate-rich types.

- Two main stages of hydrothermal activity have been recognized at Kelian...

...

- Although four main stages have been documented at Busang (Felderhof et al., 1995 [2]; Leach, 1997 [17]), they can be condensed into three main events...

...

These three stages at Busang are closely comparable to the main events at Kelian.

f) Gold Mineralisation

Visible gold was extremely rare in the core from both Kelian and Busang...

...

The gold observed under the microscope in the Kelian polished thin sections is very similar to that observed in sections from the Central Zone...

...

g) Metallurgical Characteristics

The metallurgical characteristics of the Kelian and Busang ore are very similar:

- At Kelian, a gravity circuit was installed 3 years after the start-up and recovered approximately 50% of the gold. The gold from the gravity circuit is flattened, elongated and commonly agglomerate, and up to 5-7mm in diameter.

- At Busang, approximately 49% of the overall gold was recovered as gravity gold in a pilot plant test by Normet (7/12/91996) [sic]. The vast majority of the gold recovered had shapes and sizes comparable to that described above for Kelian.

At page 127 (Exhibit 1328B) Leach states:

A. SUMMARY

The Kelian gold mine is operated by Rio Tinto Indonesia (RTI) and is located approximately 150 km southwest of Busang in East Kalimantan on the island of Borneo. Many geologists who have worked on Busang have noted numerous close similarities to the Kelian gold deposit. Felderhof et al. (1995) [2] also

> recognized the close similarities between Busang and Kelian. Although only two publications have been made public on Kelian during the exploration and development of Busang in the mid-1990's (van Leeuwen et al., 1990 [8]; Corbett and Leach, 1998 [25], information was readily shared between RTI and Bre-X geologists (van Leeuwen per som). Therefore, many of the procedures, as well as many of data interpretations made at Busang were made based on the understanding of the Kelian deposit.

Farquharson

Farquharson agreed it was "*important to understand the geology of the Kelian deposit in order to understand the red flags.*"

Transcript: April 4, 2005, page 9

Farquharson was in error about many important aspects of Kelian. In Exhibit 681, page 13 Strathcona states:

> The Busang alteration and mineralization is characterized as carbonate-base metal style, similar to the Kelian gold deposit, situated 100 kilometres to the southwest of Busang. Kelian has been successfully exploited and although it has gold grades similar to that reported for Busang it does not have coarse free gold as implied for Busang.

Exhibit 681: page 13

Farquharson did not know there were gravity concentrators at Kelian when he wrote his report Exhibit 681 and Strathcona was wrong when it stated Kelian did not have coarse free gold.

Transcript: March 29, 2005, pages 91-98

Farquharson did not know that Kelian had distinct zones similar to the Central Zone and the Southeast Zone.

Farquharson did not know that contrary to his statement in Exhibit 681, page 14, that Kelian had very pronounced gold anomalies at surface, the North East Zone at Kelian was a blind deposit without surface expression similar to the Southeast Zone.

Transcript: March 29, 2005, page 94
Transcript: December 12, 2005, pages 134-140

Farquharson stated on page 14 of Exhibit 681 that Kelian had gold at surface with roughly coinciding silver and gold anomalies. But on cross-examination, he gave the following evidence:

> MR. GROIA: You will recall, Mr. Farquharson, I took you through the results of the work that was done at Kelian and I showed you the fact that there was no consistent correlation between gold values and other base metals such as copper, lead and zinc and arsenic. Do you recall that?
>
> MR. FARQUHARSON: Yes, based upon the numbers in table 6.

Transcript: April 4, 2005, page 27
Transcript: March 29, 2005, page 99-103

Farquharson had little, if any experience in a tropical geological setting (Exhibit 676 and 677) while Dr. Hellman and Leach had extensive experience in the Pacific Rim and tropical geological settings and specifically Indonesia and both had familiarity with the Kelian deposit. (Dr. Hellman Exhibit 1202, pages 5-11, Leach Exhibit 1328 A, pages 12-16).

Farquharson testified he would defer to the knowledge and experience of Leach and Corbett in their description of the type of deposit such as Busang.

Transcript: April 4, 2005, page 11

Dr. Hellman and Leach's experience in the Pacific Rim, Indonesia, tropical geological settings and their greater familiarity with Kelian adds weight to their opinions about the comparison between Kelian and Busang. Farquharson's opinion suffers from his lack of experience.

Like Dr. Hellman and Leach, Felderhof had extensive experience in the Pacific Rim and tropical geological settings and specifically Indonesia, and Felderhof also had familiarity with Kelian.

THE CHANGING BRIGHTEST RED FLAGS

In Exhibit 681 at page 4, Strathcona repeats what Farquharson states in his letter of October 20, 1997 to David Walsh:

> Some of the red flags are more significant and more obvious than others. Some of them, individually, on their own, might not create any doubt or questions to the casual observer but, collectively, they all point in the same direction.

At page 5 of Exhibit 681(reproduced on pages 123 of these reasons) Strathcona lists the three most striking areas of red flags.

When asked about the most striking areas of red flags in re-examination (reproduced on pages 123-124 of these reasons), Farquharson then lists four and not three striking areas of red flags.

Transcript: April 7, 2005, pages 4-7

The O.S.C. sometimes refers to the red flags listed in the re-examination as bright red flags.

In cross-examination Farquharson states:

> MR. FARQUHARSON: Oh, I compliment you on doing some excellent research on a few points there that would modify a few of the words that we have used in some of the statements. But the flags are all still there. I don't think we would pull down any of the flags that we raised. And as we have mentioned before, there are perhaps two or three of the flags that would, on their own, be very serious flags such as the lack of an expression of gold over the top of this huge deposit. But many of the others require putting together two, or three, or four flags which all tend to point in the same direction and suggest that somebody look into why these concerns or flags are there.

Transcript: April 6, 2005, pages 121-122

Between the opinion and cross-examination and re-examination, the number of "*striking*" or "*big*" serious red flags varies from a low of two to a high of four.

That is an important difference and inconsistency because according to Farquharson the most serious red flags can stand on their own and cause a geologist to do further work but Farquharson testified that with respect to "*[t]he other flags, one on its own, you might sort of shrug your shoulders and say well maybe there is a reason for that*" and "*many of the others require putting together two, or three, or four flags which all tend to point in the same directions and suggest that somebody look into why these concerns or flags are there.*"

Transcript: April 7, 2005, pages 6-7
Transcript: April 6, 2005, page 122

The inconsistency is not limited to how many very serious red flags there are but also what in fact are the alleged very serious red flags or most striking areas of red flags.

The lack of gold at surface in the Southeast Zone, which is the first of the three most striking areas of red flags in Exhibit 681, is similar to the first "*big*" flag in re-examination except that in Exhibit 681 Strathcona adds the absence of gold in sediments in streams draining the Southeast Zone, which is not something that is referred to in the October 1997 letter. There is no satisfactory explanation why the absence of gold in sediments is not listed per se in the 20 Red Flags in the October 1997 letter but is then added to the first most striking area of red flags in Exhibit 681.

This first most striking area in fact incorporates two red flags, 1 and 2, found in the October 1997 letter.

The third most striking area in Exhibit 681, the absence of visible gold in the core, is similar to the second big red flag listed in re-examination. This is similar to Red Flag 7 in the October 1997 letter.

The second most striking area in Exhibit 681 is similar to Red Flags 9 and 16 in the October 1997 letter.

The third most striking red flag in re-examination though does not correspond to Red Flags 9 and 16 but to a totally different allegation in Red Flag 8 in the October 1997 letter. Red Flag 8 is not only not a striking red flag in Exhibit 681, it is not included in the

body of Exhibit 681 (it is found only in Appendix VII which is a copy of the October 1997 letter).

A fourth major flag is added in re-examination which corresponds to Red Flag 12 in the October 1997 letter. Red Flag 12 is not listed as one of the most striking red flags in Exhibit 681 nor is it found in the body of the opinion but like Red Flag 8, Red Flag 12 is found only in Appendix VII.

As noted above it is significant that in Exhibit 681 there are three most striking areas and four in re-examination. It is significant that even if the fourth red flag (Red Flag 12) in re-examination is removed, the remaining three in the re-examination and the three in Exhibit 681 are not all the same.

If the opening of the sample bags (Red Flag 12) is not most striking in Exhibit 681 in 2000 how does it become so in re-examination on April 7, 2005. Similarly, Red Flag 8 is not most striking in 2000 but is in 2005. Conversely Red Flags 9 and 16 are most striking in 2000 but are not in 2005.

I have concerns with respect to this evidence and as to which red flags are allegedly "*most striking*" or "*big*" or "*major*" or "*very serious*" and which are not and "*you...sort of shrug your shoulders and say well maybe there is a reason for that*" and which are like Red Flag 20 with respect to which Farquharson testified "*was not a flag that I would particularly condemn Mr. Felderhof for not seeing.*"

Transcript: March 30, 2005, page 108

No Examination-in-Chief On Some Red Flags

The O.S.C. did not examine Farquharson in-chief on some of the 20 Red Flags; for example 3, 4 and 20. Although the O.S.C. did not abandon these as red flags, the O.S.C. stated at page 74, March 30, 2005:

> ...but it isn't a question of anybody having abandoned anything. It's just that we put the evidence forward in the way we thought was the most understandable. And, I guess, if we didn't ask about a particular red flag and my friend doesn't cross-examine on it, it will be hard for us to go back to you and tell you how important it was since we didn't ask any questions about it in-chief anyway.

And at page 76:

> If there are items in there to which we never took the witness, it's debatable whether we are really going to make much of them in the end.

Transcript: March 30, 2005, pages 69-81

October 1997 Red Flags Not Included In Strathcona's Opinion, Exhibit 681

At pages 136-137, April 6, 2005 the O.S.C. states:

> MR. MARROCCO: Your Honour, of course we have been listening to this for a while so I don't intend to try to repeat it. I think he really says two things. I think he says some of them are quite striking on their own and I think he says others are perhaps less striking, unusual, whatever word you want to use, and that if you take those and you lump them together with the others they all point in the same direction. So I think he actually has really taken, he has taken the position that some of them are more significant than others and I think in his report he gets you to the ones that he wants to get to.

In his report, Exhibit 681, Farquharson does not "*get to*" October 1997 Red Flags 3, 4, 6, 8, 10, 11, 12, 13, 19, 20. They are listed in Appendix VII and some are discussed in Exhibit 208, the Strathcona report of May 8, 1997 referred to on page 4 of Exhibit 681, but they are not found in the body of Strathcona's 2000 opinion, Exhibit 681.

Red Flags To Be Related To Allegations

Felderhof is not on trial for not following the best possible practice in every aspect of developing Busang.

What is relevant for Counts 5 to 8 are red flags that would have led Felderhof to question the reliability of the resource calculations in the press releases. Some of the red flags listed by Strathcona (for example, Red Flags 3, 4, 5, 6, 10 and 11 and the Duplicate Sample Numbers) have more to do with best practices, with respect to which there may be a difference of opinion, than with the reliability of the resource calculations.

Recommendations and Red Flags

The O.S.C. relies on recommendations made by third parties to Bre-X to change some practices as support for the red flag allegations; for example, Kilborn and M.R.D.I. with respect to Red Flag 5: Drill Core Not Split. The recommendations are not irrelevant to the issue but there is a substantial difference between recommending a change to improve a practice and alleging that the original practice is a red flag.

PROFESSIONALS AND EXPERTS INVOLVED WITH BUSANG

Dr. Hellman

Dr. Hellman's opinion is found at page 2 of Exhibit 1202:

> Mr. John Felderhof, as well as the many professionals who worked on the Busang project, either as employees or consultants, did not fail to recognize or ignore the alleged warning signs of Strathcona. These professionals included specialists in mineralogy, metallurgy, mining engineering, petrology, resource estimation,

sampling and assaying. The reason why Strathcona's red flags were not recognized is because they did not exist.

Dr. Hellman's detailed opinion is found at pages 65-68, 287-295, 305-317 of Exhibit 1202.

Farquharson

Farquharson criticized Bre-X management, the Bre-X board, Kilborn, mining analysts and the regulatory authorities for surveillance failures:

> MR. GROIA: You were, in fact, chosen to be the C.I.M. distinguished lecturer for, I think, 1998?
>
> MR. FARQUHARSON: I have forgotten what year it was, but yes, for one year.
>
> MR. GROIA: And you were chosen to be the distinguished lecturer because of primarily your role at Busang.?
>
> MR. FARQUHARSON: Yes.
>
> MR. GROIA: And you were invited on several occasions to give presentations or talks to a number of interested audiences?
>
> MR. FARQUHARSON: C.I.M. audiences, yes.
>
> MR. GROIA: Were there 80 or 100 lectures you gave? Do you recall how many?
>
> MR. FARQUHARSON: It certainly wasn't that many. It would be in the order of 20 to 25.
>
> MR. GROIA: And you recall, towards the end of each of those talks, reaching a part of your lecture where you talked about surveillance failures, right?
>
> MR. FARQUHARSON: Yes.
>
> MR. GROIA: And after you went through management and the board of the company, the third group you criticized for surveillance failures were independent consultants such as Kilborn, right?
>
> MR. FARQUHARSON: Yes.

MR. GROIA: Do you recall why you criticized them?

MR. FARQUHARSON: Because they did not recognize these red flags that they were working with when they were doing their assignments on Busang.

MR. GROIA: And according to you they should have recognized them, right?

MR. FARQUHARSON: Yes.

MR. GROIA: And then you criticized the mining analysts for their surveillance failures, right?

MR. FARQUHARSON: Yes.

MR. GROIA: Do you recall what you said about the mining analysts?

MR. FARQUHARSON: Well basically that they had accepted all of this data, these reports from Bre-X; that they had been to the property, a number of them; that they did not see any visible gold in core samples from the Southeast Zone. And despite the fact that several of them had told me that they took away samples from their visit, assayed it for gold, did not get any gold, but still went on believing in Busang.

MR. GROIA: And then you criticized the regulatory authorities, did you not?

MR. FARQUHARSON: Yes.

MR. GROIA: And do you recall what you said about the surveillance failures of the regulatory authorities?

MR. FARQUHARSON: That a project of this magnitude and with a company with the market value of Bre-X, based upon falsified data was allowed to achieve the status that it did on the Toronto Stock Exchange.

Transcript: March 29, 2005, pages 53-55

In Dr. Hellman's opinion noted above the defence for those criticized by Farquharson for not seeing Strathcona's red flags is that there were no red flags. They did not have the hindsight that Farquharson had. They were not working under the new regulations. They

were not looking for unprecedented tampering at an obviously prospective property. The assay results were plausible. They were in a similar position to Felderhof.

Chart, Exhibit S4, Appendix B

Appendix B to Exhibit S4 was a chart filled out by Mr. Groia in court as he cross-examined Farquharson. A check mark means the particular red flag would have been apparent to the named person. An "X" means the red flag would not have been apparent. A question mark means Farquharson did not know. A question mark with a check mark means that if that named person knew of the alleged fact then they should have recognized it as a red flag. The date column shows the date the red flag would have become apparent to Felderhof. Farquharson testified that for each of the red flags noted not only Felderhof but others would have been aware of the red flag. Yet except for Freeport who drilled and found no gold (and see Barrick in the next paragraph), no one else before Strathcona did in fact raise a red flag.

Transcript: April 4, 2005, pages 49-50
Transcript: April 5, 2005
Transcript: April 6, 2005
Exhibit S4: Appendix B

No One Saw Red Flags

Excluding the Barrick sampling of December 1996, Farquharson agreed he was "*not aware of any one else in three years of results raising a red flag*" at Busang before Freeport and Strathcona's negative results.

In January 1997, after getting and assaying further samples, Barrick continued to pursue Busang convinced of its value as a gold property.

Transcript: March 29, 2005, pages 44-45

Dr. Kavanagh

Dr. Kavanagh did not raise any red flags. Farquharson testified he was "*not suggesting Dr. Kavanagh had any knowledge of these red flags or at least didn't see them as red flags.*" But then Farquharson changed his evidence. He testified Dr. Kavanagh "*should have known about Red Flag 20.*" And with respect to Red Flag 9, Farquharson did not know that Dr. Kavanagh called Anne Thompson who had done the study discussed in Red Flag 9 and that Dr. Kavanagh had satisfied himself with respect to her results and that this was not a red flag, but assuming that Dr. Kavanagh had done so, Farquharson testified Strathcona would still not agree with Dr. Kavanagh.

Transcript: March 30, 2005, pages 107-110

Dr. Kavanagh testified he had in fact called Thompson and satisfied himself there was no red flag. Thompson told Dr. Kavanagh that in her opinion the gold was so erratic in nature or so unevenly distributed in the core that it could have been missing in the samples she examined so she did not consider the fact that she did not find gold in her study to be a concern.

Transcript: March 8, 2005, pages 44-45, 63-69

Dr. Kavanagh got drill results directly from Indonesia and did his own plotting. He saw no red flags, no warning signs. Dr. Kavanagh's independent plotting is some evidence of due diligence by Bre-X. Dr. Kavanagh did not detect the unprecedented and sophisticated

tampering. The results lined up from hole to hole and down the holes as would be expected in a bona fide deposit.

Transcript: March 2, 2005, pages 28-29

Dr. Kavanagh agreed "*that scissors and twin holes were being drilled at the request of Kilborn.*" Dr. Kavanagh also agreed that *"[t]hat would be another green flag, the fact that those results lined-up with the original holes.*"

Transcript: March 14, 2005, pages 56-57

Analysts

The analysts who visited Busang, for example Egizio Bianchini from Nesbitt Burns and Bruno Kaiser from CIBC Wood Gundy, did not raise any red flags. Other analysts also recommended investors buy Bre-X shares, for example, Michael Fowler from Levesque Beaubien.

Transcript: March 14, 2005, page 52

Suitors

In the trial companies interested in investing in and developing Busang with Bre-X have been individually and collectively referred to as 'suitors'. Barrick, Placer Dome, Tech Corp., Newmont Mining, and Freeport-McMoRan who are among the largest gold companies in the world wanted to joint venture with Bre-X. They would not have continued to show any interest if they had had any suspicion about the Busang results.

Transcript: March 14, 2005, page 52

Financial Advisers

Dr. Kavanagh agreed that *"[t]he financial advisors that Bre-X chose, J.P. Morgan and Republic National Bank...[were]...both very senior, very reputable financial advisors."*

Dr. Kavanagh also agreed that *"the fact that they did their own due diligence before they took on the engagement and still were willing to work for Bre-X would have been a green flag."*

Transcript: March 14, 2005, page 57

Peter Munk was more subdued about the significance of J.P. Morgan's due diligence although there he was referring to title issues. See page 383 of these reasons.

Transcript: December 8, 1995, page 16

Experts Retained by Bre-X

Kilborn, Normet, Hazen, Oretest, Mintek, Petrascience, Paul Semple, R. Pooley, Roger Townend, John Borner, Anne Thompson, Martha Schwartz, Sophie Ashby, M.R.D.I., John Irvin, Indo Assay Laboratories, John Irvin, J.P. Morgan, Republic National Bank were well recognized, reputable professionals retained by Bre-X. Not one of them raised a red flag.

John Borner

Although Farquharson, who is not a petrologist, saw Red Flag 9 in John Borner's petrological work, John Borner who is a petrologist saw no red flag.

Exhibit 600
Exhibit 657

Exhibit 658
Transcript: April 5, 2005, pages 60-63, 104

Anne Thompson

Similarly, Farquharson saw Red Flag 9 in Anne Thompson's work, although Anne Thompson who is a petrologist saw no red flag.

Transcript: April 6, 2005, pages 113-114
Transcript: March 8, 2005, pages 44-45, 63-69

Hazen Report, Exhibit 494

Hazen, the expert consultant retained by Bre-X did not see a red flag in their report Exhibit 494. Farquharson saw Red Flag 15.

Normet Report, Exhibit 660

Farquharson, who is not a metallurgist, found the Normet Report (Red Flag 17) alarming while the metallurgists who prepared the report did not.

Transcript: March 31, 2005, pages 61-63

Townend, Normet, Schwartz, Hazen

These expert consultants retained by Bre-X did not see Red Flag 16. Farquharson who is neither a petrologist, nor a mineralogist, nor a metallurgist saw Red Flag 16.

Kilborn, Normet, Hazen, Oretest

These metallurgical groups retained by Bre-X for their expertise did not see Red Flags 17 and 18. Farquharson who is not a metallurgist did.

Hazen, Kilborn, M.R.D.I.

Farquharson also testified that the people at Hazen and Kilborn should have been shocked and M.R.D.I. should have been shocked if M.R.D.I. had looked at the feasibility study.

Transcript: April 6, 2005, pages 62-63

Hazen, Kilborn, M.R.D.I. were not alarmed, not shocked.

Kilborn

Kilborn was one of the world's leading engineering companies responsible for the resource calculations which are the subject matter of Counts 5 to 8. Sophie Ashby at Kilborn was using a Data Mine model which did not detect the unprecedented tampering. She saw no red flag.

Transcript: January 23, 2006

Kilborn did a preliminary and then an intermediate feasibility study and saw no red flags.

Transcript: January 26, 2006, page 3

Kilborn was interested in becoming a partner with Bre-X to invest and develop Busang. If Kilborn suspected red flags, it is trite to say they would not have been interested in investing in a fraud. Even after the negative results from Freeport's drilling program

Semple believed a more plausible explanation was the Freeport assays were wrong rather then accept that tampering had occurred.

Transcript: January 25, 2006, pages 6-62

The metallurgical test work was above industry standard. Semple testified Kilborn reviewed the metallurgical test work. Kilborn reviewed the test work done by Oretest for Normet and saw nothing that caused concerns.

Kilborn reviewed the gravity test work and saw nothing unusual. It was consistent with gold deposits that react well to gravity. Semple saw nothing that caused concern that there had been salting. Kilborn looked at the amalgamation tests. The results of the amalgamation tests were inconsistent with samples being salted.

Transcript: January 23, 2006, pages 85-99

Farquharson testified the amalgamation test results were a mystery to him.

Transcript: March 22, 2005, pages 26-27

Mineral Resources Development, Inc. (M.R.D.I.)

Dr. Hellman's opinion about M.R.D.I and their work at Busang is found at pages 1-2

Exhibit 1202:

> An independent, extensive and detailed review by one of North America's best known and respected minerals auditing groups, MRDI Inc., was commissioned by Bre-X in October 1996 specifically to assess its work at Busang. That review stated:
> "*Our principal conclusion is that the exploration work is being done to a high standard.*"

It is difficult to reconcile this and the many other positive comments about Bre-X with the numerous criticisms made by Strathcona...

The MRDI review did not identify any of the 20 red flags that Strathcona alleges should have been obvious to an observer "*familiar with the exploration and evaluation of gold projects.*" The MRDI review was authored by four highly qualified and experienced people who specialized in the geology of mineral deposits, coarse gold sampling, resource estimation, technical audits and reviews, analytical chemistry. Quality Control issues and even fatal flaw audits. As such, all were well familiar with the exploration and evaluation of gold projects.

The MRDI review does not have the characteristics of a "rubber-stamping" exercise. It includes a number of useful and constructive recommendations and suggested improvements. It strongly contrasts in both tone and content with the reports of Strathcona.

Exhibit 1202: pages 1-2

Farquharson testified about M.R.D.I:

MR. FARQUHARSON: I have never worked personally with M.R.D.I., but Mr. Thalenhorst of our firm has done a few assignments with M.R.D.I.

MR. GROIA: And I take it you know that Mr. Thalenhorst speaks very highly of M.R.D.I.?

MR. FARQUHARSON: Yes.

MR. GROIA: In fact, he speaks so highly of them, M.R.D.I., that in this memo that you have produced late he indicates that one of the things that fairly describes M.R.D.I. is that,

> "They are the well known and well respected consulting firm specializing in mineral reserve and fatal flaw audits".

You knew that's how he described them?

MR. FARQUHARSON: Yes.

MR. GROIA: And then he comments on the point that Mr. Helman made about M.R.D.I. where he says,

> "One of the more serious points in favour of John Felderhof that Helman raised is that the well known and well respected consulting firm Mineral Resources Inc. specializing in mineral reserve and fatal flaw audits did not

> catch on to the salting process at Busang, so why should Felderhof have been suspicious?"

You know that that was Mr. Thalenhorst's sentiment?

MR. FARQUHARSON: That was a statement that he wrote, yes.

MR. GROIA: And then he goes on and says this,

> "M.R.D.I. is indeed a well respected company with whom we have worked together on several projects."

And that's true?

MR. FARQUHARSON: Yes. Mr. Thalenhorst does work with them, yes.

MR. GROIA: And then after making the comment that you don't have the scope of the work, he makes the following statement,

> "Most of the points raised in the M.R.D.I. report address short-comings as is normally the case where exploration geologists are guiding a project that is heading for a feasibility study. The point made by Hellman that such a company would not notice the many red flags that others have seen remains a powerful argument in my opinion which can only be partly de-clawed by pointing to the very technical scope of work that concentrated on making the project documentation bankable and did not include the review of the barren surface trench samples."

Do you agree with that statement?

MR. FARQUHARSON: Yes.

MR. GROIA: And so how did you plan to de-claw the argument that Mr. Felderhof ought to be entitled to rely on M.R.D.I. and de-claw the argument, the powerful argument that if they didn't detect this salting scam he should have? What is your de-clawing plan, Mr. Farquharson?

MR. FARQUHARSON: Just a couple of observations there. First of all, we don't know how long M.R.D.I had, how much time they had to do their assignment. I looked at their report and it doesn't indicate whether they were there for a day, or a week, or what.

The second point was I am not sure –we don't know how much data they were given. Whether or not, for example, they were also given the results of the surface sampling as was given to us when we were at Busang. Whether or not they were given that same data, I don't know. But we are not going to try and defend

M.R.D.I. They will have to defend themselves as to why they did not spot the red flags that we say were there.

We would point out that when Freeport did their due diligence and the paper that they published following that program, that they indicated within one or two days of being on site there were a number of red flags that became apparent to them and I believe that paper is an exhibit that's been tabled.

MR. GROIA: Well I just have a couple of things I would like to pursue because I was a little bit puzzled by some evidence you gave to Mr. Marocco. I am right, am I not, that in the 1997 report which you did for the directors of Bre-X, you quote quite extensively from M.R.D.I.'s work, do you not?

MR. FARQUHARSON: We may have. I'm sorry, I can't remember the specific quotes.

MR. GROIA: Well if I ask you to get out your report.

THE COURT: What exhibit again please?

MR. GROIA: It's exhibit 208, Your Honour. And it's page 28 in the top right corner and page 23 in the bottom right corner.

MR. GROIA: And if you start under the heading "Sample Preparation and Assaying for Bre-X", you quote from the M.R.D.I. report of 1996. Then over the page, near the bottom of the next page, you comment on M.R.D.I.'s recommendations. And again at the next page you say you would have endorsed M.R.D.I.'s recommendations. So there is a fair amount, or at least some discussion in this report that you rely on the work of M.R.D.I. in writing this report, right?

MR. FARQUHARSON: We endorsed the recommendations that M.R.D.I. had for various items related to sample preparation, et cetera, and assaying.

MR. GROIA: And if I then take you to your report for the Securities Commission, exhibit 681, and I look at the list of studies or work that you say you relied upon in your schedule, do I find the M.R.D.I. work there or not?

MR. FARQUHARSON: I don't believe so.

MR. GROIA: And did Mr. Marocco not ask you about the M.R.D.I. report and whether that was something that you considered or relied upon in your March, 2000 report and did you not say to him that you considered it but you didn't rely upon it?

MR. FARQUHARSON: For our 2000 report?

MR. GROIA: Yes.

MR. FARQUHARSON: Yes.

MR. GROIA: So between 1997 where you are quoting the recommendations to Bre-X and 2000 when you are working for the Securities Commission, would I be right to suggest to you that M.R.D.I. goes from quotable status to let's forget about it status?

MR. FARQUHARSON: No, because in 1997, in our 1997 report we are commenting upon the recommendations made by M.R.D.I. to some of the basic sampling and assaying procedures which we were in agreement with. But that was not something that we were asked to comment upon in 2000.

MR. GROIA: But by 2002 Strathcona clearly knew that one of the powerful arguments that was going to be raised by Mr. Felderhof was reliance on M.R.D.I., right?

MR. FARQUHARSON: Well I think even before that. We were aware of the M.R.D.I. report back in 1997.

MR. GROIA: And rather than, as you could have, stepping back and saying, you know, that's a good argument, we really ought to think a bit more carefully about these red flags, maybe there is something in the position that Mr. Felderhof is putting forward, Strathcona instead set about to try and find ways to "de-claw" that argument, right?

MR. FARQUHARSON: I'm sorry. You are losing me there. When you use the word "de-claw" coming from Mr. Thalenhorst's memo of 2002 or whenever he wrote it, what does that have to do with our 2000 report?

MR. GROIA: Well it's got this to do. First of all, will you agree with my statement that the expression "de-claw" is an offensive term when used in the context of this case?

MR. FARQUHARSON: "Offensive" meaning?

MR. GROIA: Inappropriate. Not the sort of thing one would expect from an expert witness hired by the Commission to give testimony for the Court to consider?

MR. FARQUHARSON: It's not my word and this was a memo that he wrote on his own volition, using his words not, of course, ever expecting to see this document in a court room.

MR. GROIA: But I am asking ---

MR. FARQUHARSON: But I don't get particularly upset by the word "de-claw" for reading something into it.

MR. GROIA: Well let me then take it one step further. By 2002, because of the Phil Helman talks and papers, it was clear to Strathcona that it was going to have to deal with the argument that would be made by Mr. Felderhof that how could he know if M.R.D.I. didn't. You knew that, right?

MR. FARQUHARSON: Correct.

MR. GROIA: And I am going to suggest that rather than doing what any fair independent expert would do, which is to carefully consider those arguments, instead Strathcona set about to do one thing and one thing only and that was to find some way to de-claw that argument?

MR. FARQUHARSON: But we haven't done anything since 2002. We haven't written any reports since 2002. So how does one suggest that we are trying to de-claw if that's meant to be an unacceptable term? We haven't done anything since 2002.

MR. GROIA: Didn't you give testimony last week in your examination-in-chief?

MR. FARQUHARSON: Yes.

MR. GROIA: And unless I overlooked it, did you say anything about the powerful argument that M.R.D.I. presented to your case?

MR. FARQUHARSON: No.

MR. GROIA: And did you say to the Court, you know, I think these are red flags, but in fairness to Mr. Felderhof who I am trying to assist the prosecution in prosecuting, I should tell you that we think there is a powerful argument to be made that if M.R.D.I. didn't spot these results it's not reasonable to think Mr. Felderhof would have. Did you think about saying that to the Court?

MR. FARQUHARSON: No.

MR. GROIA: And if we hadn't dragged this memo out of you as a result of the request that you provide us with everything else, as you say, it never would have seen the light of day, right?

MR. FARQUHARSON: That was a memo that, as I mentioned, even I had not reviewed before it came out. But we are not trying to deny that M.R.D.I. is a reputable firm capable of doing good work and they did not recognize the red flags at their time at Busang. Whether it was because they were not there long enough; they were not given all of the data, we don't know. But we do acknowledge that it is a point in favour of Mr. Felderhof that a firm like that did not recognize the red flags that we say were there.

MR. GROIA: And would you then concede, Sir, that this memo gives us some insight into the Strathcona approach to these issues? You only concede those things you have to and only then if you can't de-claw them?

MR. FARQUHARSON: No. We have focused on what we considered to be red flags that we think people familiar with this project should have spotted. The fact that M.R.D.I. did not spot them; the fact that Kilborn did not spot some of them in their area of expertise, they will have to answer for themselves as to why they did not spot them.

Transcript: March 30, 2005, pages 113- 120

Farquharson concedes that the fact that M.R.D.I. did not see any red flags is an argument in favour of Felderhof. M.R.D.I. and Farquharson's evidence with respect to M.R.D.I. is also discussed later at pages 215-216 of these reasons.

In paragraphs 397 to 420 of Exhibit S5 Volume II the O.S.C. makes submissions as to the alleged limitations of M.R.D.I.'s work. In reviewing those submissions, it must be kept in mind that M.R.D.I. is "*one of North America's best known and respected mineral auditing groups.*"

Exhibit 1202: page 1
Exhibit S5 Volume II: paragraphs 397-420

And it must be kept in mind that M.R.D.I. reported:

> The work Bre-X has done at Busang... is of a high industry standard.

Exhibit 505: page 7

The O.S.C. submits at paragraph 400, Exhibit S5 Volume II:

> There is no evidence that MRDI reviewed the Kilborn Intermediate Feasibility Study that was issued on November 15, 1996 three days after MRDI's site visit which alerted Strathcona to many of the red flags. MRDI did not refer to the Kilborn Intermediate Feasibility Study in its report.

As noted by the Defence, the final M.R.D.I. report was drafted December 2, 1996 after the issue of the Intermediate Feasibility Study. Also, many of the reports and studies included and relied upon in the Intermediate Feasibility Study had been released earlier in 1996. It would have been difficult for M.R.D.I. to have reviewed and commented on the items listed as its scope of work and review without having reviewed the various reports and studies available.

Exhibit S5 Volume II: paragraph 400
Exhibit 505: page 5
Exhibit 1202: page 154

The O.S.C. submits "*MRDI did not have the opportunity to observe the four bright flags identified by Strathcona because they were beyond the scope of their work.*".

Exhibit S5 Volume II: paragraph 407

The scope of work is set out on page 5 of Exhibit 505. A simple review of what is included there indicates that most of the red flags were within the scope of work or would be touched on by that work.

The O.S.C. submits *"[t]here is no evidence MRDI reviewed the maps that would identify whether there was a surface geochemical anomaly over the SEZ".*

Exhibit S5 Volume II: paragraph 408

But M.R.D.I.'s scope of work included "*geological mapping*" and "*adequacy of exploration data*". And M.R.D.I. comments that Bre-X's work "*both in terms of discovery and ongoing exploration development...is of a high industry standard.*" M.R.D.I. goes on to say "*[t]he regional and local geological setting, ore occurrence model, and interpretations are well founded on detailed geological investigation, sampling and research, and provide a solid frame work for the ultimate development of a world-class project.*" M.R.D.I.'s review of "*discovery and ongoing exploration development*" would include the review of surface geochemical anomaly among other matters.

Exhibit 505

The O.S.C. submits there is no evidence M.R.D.I. considered whether Bre-X identified visible gold.

Exhibit S5 Volume II: paragraph 409

That would be part of the scope of work "*Ore and gangue mineralogy.*"

Exhibit 505: page 5

The O.S.C. submits M.R.D.I. did not review the skeleton core.

Exhibit S5 Volume II: paragraph 410

But without reviewing the skeleton core how could M.R.D.I. conclude *"[t]he core logging procedures at Busang are excellent, providing highly detailed and informative geological and geotechnical logs of all drill core."*

Dr. Kavanagh did not receive the M.R.D.I. report until March or April 1997.

Transcript: March 15, 2005, page 51

Dr. Kavanagh testified M.R.D.I.'s scope of work was extensive. When asked if anything would have made the review more comprehensive, he answered conducting its own drilling or taking core samples which was the less expensive.

Transcript: March 10, 2005, pages 65-66

There is no indication that M.R.D.I. thought it was necessary to drill or take core samples which would be some indication that M.R.D.I. saw no need to do so to test the work done by Bre-X at Busang because M.R.D.I. did not suspect that there were any red flags.

M.R.D.I. made recommendations to Bre-X for improvements as was their function and *"as is normally the case"*.

Transcript: March 30, 2005, page 114

Summary of M.R.D.I. Conclusions

M.R.D.I. concluded in Exhibit 505:

> The work Bre-X has done at Busang both in terms of discovery and on-going exploration development of the Busang Hardrock Gold Project is of a high industry standard. The regional and local geological setting, ore occurrence model, and interpretation are well founded on detailed geological investigation, sampling and research, and provide a solid framework for the ultimate development of a world-class project.

...

The core recovery at Busang is invariably better than 97 percent, and an average of 98.7 percent is very good and provides high confidence that the core is fully representative of the rock intervals being sampled.

...

As mentioned, exploration development of the Busang Gold Project is being carried out at a high industry standard. Cross sections based on drilling and assaying results show a high level of detail and provide an adequate geological and ore occurrence interpretation upon which to base resource/reserve estimation and mine planning.

...

The core logging procedures at Busang are excellent, providing highly detailed and informative geological and geotechnical logs of all drill core.

...

Bre-X has developed a good understanding of the alteration, ore and gangue mineralogy, ore controls and their inter-relationships.

...

There is significant potential to add to reserves at Busang with the currently defined mineralizing system being open along a strike both to the northwest and southeast, and also at depth below 400 m.

Exhibit 505: pages 7, 8, 12, 13, and 14

M.R.D.I. did not see any red flags but saw the opposite: that the work Bre-X did at Busang was "*of a high industry standard*".

BARRICK GOLD WAS CONFIDENT THERE WAS GOLD IN BUSANG

Peter Munk is the Chairman of Barrick Gold Corporation.

The only time Barrick came to the conclusion that the results at Busang were not accurate was after Freeport's negative drill results became publicly known. Peter Munk's reaction was "*[d]isbelief and horror*". When asked why, Munk replied:

> MR. MUNK: Because ever since I heard the name Bre-X and I followed the case quite closely, it never occurred to me once that a fraud of this magnitude could be possibly happening in a country as developed in the mining industry as Canada.

Transcript: December 7, 2005, page 65

At the time of Munk's testimony, Barrick was the world's third largest gold company by production with annual resources as of 2004 of 89 million ounces of proven and probable gold. At the time of Munk's testimony, Barrick was in the middle of a bid to acquire Placer Dome for nine billion dollars (U.S.) which would make Barrick the world's largest gold company.

Transcript: December 7, 2005, pages 4-5

Barrick's motto was "*to be the best gold mining company in the world*" and Munk felt "*that being the biggest is certainly a plus.*" If Busang had the gold Barrick believed it had and Barrick had formed a partnership or acquired Bre-X, then Barrick "*would have become the number one gold producer in the world.*"

Transcript: December 7, 2005, page 19

Barrick first became interested in Bre-X in 1995. Dr. Kavanagh, then Senior Vice-President of Exploration at Barrick and another geologist at Barrick, Larry Kornze, visited Busang in October 1993 and wrote memo Exhibit 541 recommending Barrick

invest in Bre-X. They wrote "*Bre-X has an excellent, motivated exploration team, very experienced in Indonesia, with a successful past record there.*" They concluded "*we consider that this excellent Indonesia opportunity is most appropriate...*"

Exhibit 541

Barrick made an offer to Bre-X which was not accepted but Barrick continued to actively pursue control of Busang for years to follow.

Exhibit 387

On that first visit Dr. Kavanagh and Kornze took some surface, or near surface, samples and obtained low results. "*Although these results were low, Kavanagh testified that he continued to be interested in the Busang property because the outcrops looked attractive and Felderhof had told him that the low assay results were due to depletion.*"

Exhibit S5 Volume II: Para. 484
Transcript: March 8, 2005, pages 97-99

Depletion at surface is Felderhof's geological explanation of Red Flags 1 and 2 based on his experience at other gold properties, Mirah and others.

With respect to Barrick's business, legal and geological personnel Munk testified:

> MR. GROIA: And can you comment on the quality of Barrick's business and legal team that worked on the Busang project and perhaps even compare them to the geological team?
>
> MR. MUNK: I think I – I think Barrick has a got a very outstanding group of people. With all due modesty I would say that we had the A-team in the world, otherwise we couldn't have done what we have done as a Canadian company with a small capital base, where we have gotten in 10 or 15 years.

Our legal team I would put against any other legal team again in the world, whether I would call number 1 and number 2, I would be too modest to say.

MR. GROIA: And you are giving all the credit for this team being built to Mr. Smith, I understand?

MR. MUNK: Absolutely. Smith was an outstanding businessman, an outstanding engineer, and I personally have the utmost respect for Bob Smith.

Transcript: December 7, 2005, pages 17-18

Munk testified about his role in pursuing Busang:

MR. GROIA: Can you tell us in general terms, Mr. Munk, what your role was in the leadership of the team that Barrick put together to look at the Busang property? What did you do as opposed to Mr. Smith, for example?

MR. MUNK: I think we done what we had done traditionally in our business. Bob, of course, had all the operational mining geological people report to him because that was his total expertise – it certainly was not mine – while I was more involved in the business aspects.

MR. FARQUHARSON: And would the team meet on a regular basis?

MR. MUNK: Bob and I would be talking, yes, several times a day, so we were on regular communications, not just on that subject, but generally on the subject of how to run Barrick on a day by day basis.

Transcript: December 7, 2005, pages 19-20

And:

MR. GROIA: So who was leading the team on behalf of Barrick and looking at Busang?

MR. MUNK: Mr. Groia, this was an evolution over a 2 or 3 year period and, therefore, as the issue became more serious it became more overriding business issue of prime importance as, again, one of the many investments we make in the junior company. So at the end I personally became involved in supervising the

various phases together with Bob. But I must say that I felt I was becoming more and more responsible for the whole matter.

MR. GROIA: You have been quoted, Sir, as saying that your biggest regret about Barrick's pursuit of Busang was the fact it took about a year of your professional life. Is that a fair statement?

MR. MUNK: That probably would be a very fair statement from my personal point of view. From the company's point of view, I think we lost many many millions of dollars and opportunities, but c'est la vie.

Transcript: December 7, 2005, page 18

Munk described the kind of work Barrick did in looking at a property:

MR. GROIA: Now when Barrick got interested in a junior property, or a potential acquisition, can you describe for the Court in general terms what kind of work the Barrick team would do looking at a property?

MR. MUNK: I think we start off with a geological evaluation. We have in our files, in our records, a global satellite metallurgical geological matrix that indicates those regions the likelihood of gold to be found. Then if a junior comes up with a programme that is in the proper or credible geological area, then our people can evaluate public information. That information then gets correlated to the information which we have because we have our own exploration team and if it makes sense then they clearly take it a step further. Our people then would make contact with the promoters or the geologists who found it and see if we can take the matter further to be an investor, or to be a shareholder, or to be a joint venture partner, or whatever.

Transcript: December 7, 2005, pages 37-38

Exhibit 1284 is a memo from Allan Hill a senior mining executive at Barrick, to Munk dated February 22, 1996 setting out that Kilborn's estimate was 15.7 million ounces of gold in Busang but Barrick's was 20 million while the market was at about 40 million. Munk testified this would have been the work of "*[p]eople reporting to Mr. Hill's*

technical group" and that it was "*quite common*" for Barrick to have its own estimates "*[t]o make sure that the information they got valid with the information which makes sense to them.*"

Transcript: December 7, 2005, pages 42-43
Exhibit 1284

Munk testified there were many discussions about Barrick's view of the size of the Busang deposit which "*was a continuously moving target*".

Transcript: December 7, 2005, page 55

Exhibit 1603 is an internal Barrick memo dated November 20, 1995, from Alex Davidson, Senior Vice-President of Exploration to Hill, about rumours that Busang "*is all a scam*". But Munk who had "*the maximum amount of information*" "*never... once*" thought it was a fraud and Barrick continued to pursue Busang.

Exhibit 1603

Munk testified Barrick became "*totally pre-absorbed by the Bre-X issue*":

> MR. MUNK: We have employed, as I have mentioned to you, Sir, earlier, we have become interested in Indonesia. We opened up an office, I think, in '94 or '95. I think I was told last night by one of my people that at the end of '94 or '95 we, in fact, became the single largest owners of Indonesian exploration land. We have a lot under our budget there. And, of course, as Bre-X became by far the most exciting discovery in modern times in gold mining in that country and we were large land owners around it, we became totally pre-absorbed by the Bre-X issue. And, as you know from my earlier testimony, we employed a large number of legal, contract, financial and other local people to be able to get the maximum amount of information. So what I say to you now from my impression that came from all of the sources we used including our own people who continuously had a presence in that country during those critical months.

Transcript: December 8, 1995, pages 53-54

Further discussion of Barrick's contacts and ability to get information ("the maximum amount of information") is found at pages 561-571 of these reasons.

Munk testified he could not recall ever having seen Exhibit 1609, a confidential fax to Hill dated January 23, 1996 with attached "*Terms of Reference*" for obtaining information about Busang in Indonesia. The Terms of Reference states "*The objective of the review is to ascertain the current status of the Busang project, particularly of the geology, exploration and ore potential of the area.*"

Munk was asked:

> MR. GROIA: But was that your understanding, Mr. Munk?
>
> MR. MUNK: That would be all part of the overall due diligence, not just one part of it, Sir.

Transcript: December 7, 2005, pages 81-87

Munk testified that in terms of geological due diligence Barrick had "*done absolutely everything they could think of*" but the critical part was to get on the property and drill. It was Bre-X "*policy not to allow anyone on the property except on conducted tours.*" It was understood with Bre-X that any deal would be subject to Barrick going to Busang and drilling.

Transcript: December 7, 2005, page 60

Although in this next passage Munk is being asked about Bre-X's title issues it indicates the scrutiny generally directed at Bre-X and Busang:

MR. MUNK: What we have found in Bre-X – and to be fair, Sir, I am not saying that other properties would not have had equal amount of problems, but other properties would not have received the kind of thorough examination that this one did. Other properties do not have value increases that have never been rivalled [sic] in the history of Canadian mining. So clearly the scrutiny and the exploration and the examination by us and by everybody else was much more thorough. The more thorough your examinations are, clearly you are able to discover more flaws.

Transcript: December 8, 2005, page 15

But Barrick did not see any red flags.

Munk testified he had not seen Exhibit 292, a letter dated December 6, 1996 from John Cannington, Chief Operating Officer at Barrick to Felderhof thanking him for his help during Barrick's trip to Busang:

> On behalf of Alan Hill, Larry Kornze and myself, I would like to thank you for your hospitality and help during our trip to Busang last weekend. Your arrangements and assistance certainly made it much more enjoyable for us.
>
> As I told you and have written to Mike, Busang is a great deposit and you have done a very professional job in bringing it to its current status. Congratulations!
>
> Once again, John, thank you for a great visit.

Exhibit 292

Munk was read the letter and asked:

> MR. GROIA: ...Does that help your recollection, Sir, as to whether a visit took place by Barrick people to Busang?
>
> MR. MUNK: Yes. I am afraid I still cannot help you. If I am correct we at that stage were given the ability to obtain samples, core samples from the Busang office and I think that was what this memo refers to. But I don't think that we were allowed to enter the property which is understood to be the gold deposit itself. But again, to – just to my memory.

Transcript: December 7, 2005, page 58
Exhibit 292

Barrick was given core samples from Busang in December of 1996 around the time of Exhibit 392 above. The assay results were very disappointing.

Transcript: December 7, 2005, pages 59-61

Barrick continued to pursue Busang because Barrick was assured by Felderhof that there was a mistake in the shipment of core samples and Barrick was told that they would be given permission to drill their own core.

Transcript: December 7, 2005, pages 60-63

Exhibit 286 letter dated January 7, 1997 from Cannington to Felderhof also refers to thanking Felderhof for his assistance "*with the visit Alan and I made.*"

As with Exhibit 292, Munk's "*recollection is that the visit to Busang as a village was not the same as the visit to visit the site and look at the drill holes.*"

Transcript: December 7, 2005, page 89

The letter refers to "*results we have so far on the second lot of samples are corroborating the Bre-X numbers quite well.*"

Munk confirmed Barrick received a second set of Busang samples that "*did indicate a similarity to Bre-X's announced results.*"

Transcript: December 7, 2005, page 90
Exhibit 286

The first samples Barrick received were unsalted core samples while the second samples were from the salted crusher rejects.

Munk made the following comments in the context of Bre-X's title issues but there is no issue that they are not equally applicable to geological issues:

> MR. MUNK: ...But, you know, we could not risk our investors and our shareholders' money to the tune of $2 billion here, or $3 billion based on what J.P. Morgan said. We had to rely on our own due diligence. This was much more thorough, much more detailed, and had started and went much further than J.P. Morgan whose involvement was only two weeks old at that time.

Transcript: December 8, 2005, page 16

SUMMARY

Munk is an inductee in the Canadian Mining Hall of Fame. In 1993 he shared the Northern Miner's Mining Man of the Year award with his partner Bob Smith. He is an officer of the Order of Canada. At the time he, with Bob Smith, ran one of the world's largest gold mining companies (now the largest) Barrick Gold.

Peter Munk received a degree in electrical engineering. He is not a geologist by training. The weight given his evidence does not come from his training but from his position as Chairman of Barrick Gold at the pinnacle of "*the A-team in the world*" of business, legal and geological personnel. Barrick had an "*outstanding*" group of experts and professionals and sources of information and applied that expertise and information to investigate and pursue Busang.

Barrick's interest in Busang started in 1993. Barrick had a geological evaluation system and processes to evaluate junior mining companies. Barrick did their own estimates of gold reserves. Except for getting on the property and drilling, Barrick had "*done absolutely everything they could think of*" with respect to geological due diligence. Even after receiving disappointing results from core samples in December 1996, Barrick continued pursuing Busang after receiving corroborating numbers from the second set of samples in January of 1997.

As Barrick became "*totally pre-absorbed*" with Bre-X, Munk became "*more and more responsible for the whole matter*". Barrick's pursuit of Busang took a year of Munk's professional life and cost Barrick "*many many millions of dollars and opportunities*". When Munk heard on the BBC news "*that the big Bre-X deposit was given to Freeport/McMoran*", he testified "*I cried*". When he learned of Freeport's negative results his reaction was "*[d]isbelief and horror*".

Peter Munk's and Barrick Gold's expertise in gold mining is at least equal to that of Graham Farquharson and Strathcona Mineral Services. Peter Munk believed there was gold in Busang until Freeport's negative results. Barrick did not see any red flags. Barrick, like everyone else, saw gold.

Strathcona had hindsight. Strathcona had negative drill hole results and those negative drill hole results trumped other results. Strathcona saw red flags.

All of the other professionals involved with Busang and Felderhof and Barrick did not have Strathcona's hindsight. They had tampered positive drill hole results which looked plausible. They saw no red flags.

WHAT FARQUHARSON KNEW OF JOHN FELDERHOF'S EXPERIENCE

In chief, Farquharson testified the red flags would have been apparent to a geologist with Felderhof's experience. Farquharson's evidence with respect to Strathcona's knowledge of Felderhof's experience is found at pages 101-103 of the March 30, 2005 transcript:

> MR. GROIA: Mr. Farquharson, am I right that Strathcona made no independent effort to try and determine what the background knowledge of Mr. Felderhof was?
>
> MR. FARQUHARSON: That's correct. We were aware of his background in Indonesia in general, but we did not carry out any detailed investigations into his past career history.
>
> MR. GROIA: So when you answered Mr. Marrocco's question when he asked you whether a particular red flag – and he used pretty much the same question for all of the Red Flags he asked you about – when you were asked the question would it have been apparent to someone, or a geologist of Mr. Felderhof's experience and you said "yes", I take it you did that based upon not having conducted any independent investigation into that experience?
>
> MR. FARQUHARSON: Well Mr. Felderhof certainly made it clear to us when we were meeting with him in Busang his experience in Indonesia and other projects that we knew about and so on. But, no, we didn't carry on any other inquiries as to his background and experience.
>
> MR. GROIA: And what about inquiries as to his qualifications?
>
> MR. FARQUHARSON: You mean as to whether he was, if he had a degree in geology?
>
> MR. GROIA: And where he got it from and when?
>
> MR. FARQUHARSON: No.

MR. GROIA: So you answered "yes" to the question based on qualifications without really knowing what those qualifications are in any detail?

MR. FARQUHARSON: Well we understood that Mr. Felderhof had a degree in geology, I believe from Dalhousie University, but I could be corrected there. But we knew he was a graduate geologist. But beyond that we didn't make any inquiries.

MR. GROIA: And when you were asked by Mr. Marrocco about whether a red flag would be apparent to someone with Mr. Felderhof's knowledge, what work had you done to determine what Mr. Felderhof's knowledge might have been?

MR. FARQUHARSON: Nothing, other than we were aware that he had worked for many years in Indonesia and before that in other parts of the world.

MR. GROIA: And when you were asked by Mr. Marrocco questions about Mr. Felderhof's background, what work had Strathcona done to try and determine what his background might have been?

MR. FARQUHARSON: As I indicated, we did not do any specific work on researching Mr. Felderhof's background or education.

Transcript: March 30, 2005, pages 101 -103

Farquharson testified in chief that in his evidence he relied on Exhibit 686 which included "*a map showing the relationship of Busang to various other gold properties*". When cross-examined with respect to these various other properties (found on the map on page 3 of Exhibit 686) Farquharson admitted he had no knowledge of the deposits at Munyup, Gunung Mas and Mirah. He had heard of Mount Muro but did not know any of the details.

When asked what Felderhof knew about those deposits Farquharson answered "*All we knew was that Mr. Felderhof had worked in Indonesia and perhaps he was familiar with those deposits.*" Farquharson did not know that Felderhof had worked on the Mirah and

Mount Muro properties. Farquharson did know Felderhof was credited as the co-discoverer of the OK Tedi deposit. Farquharson did not recall whether the was told that Felderhof "*had visited the Kelian property on at least two occasions.*"

Farquharson agreed "*that the experience of a geologist and the work he does on other deposits will influence or help direct the work he does on the new deposits.*" Farquharson knew little of Felderhof's experience yet testified what should be apparent to a geologist purportedly with Felderhof's experience.

Transcript: March 21, 2005, pages 42-44

Kilborn

Farquharson agreed that before testifying about what "*John Felderhof or somebody with his experience should have noticed, it would have been important to know what Kilborn's background may have been working on the same property.*" Sophie Ashby prepared the resource calculations at Kilborn which are the subject matter of Counts 5 to 8.

Farquharson agreed he "*knew absolutely nothing about Sophie Ashby's background or experience.*" Farquharson agreed he did not know "*very much*" about the background and experience of Paul Semple and John Robertson, also from Kilborn.

Farquharson testified that at first Kilborn refused to meet with Strathcona without their client's authorization but later Strathcona did meet with Paul Semple and John Robertson and there were other avenues open to investigate the qualifications, background and experience of Kilborn personnel.

Transcript: March 30, 2005, pages 110-113

Farquharson was qualified to testify in two areas. The first area was red flags at Busang. The second area was whether such red flags should have been apparent to an experienced geologist such as John Felderhof. Strathcona did a minimal amount of work to obtain the information necessary to give an opinion on the second area.

Transcript: March 17, 2005, page 12
R. v. Felderhof [2005] O.J. No. 6002

FELDERHOF'S EXTENSIVE EXPERIENCE IN THE PACIFIC RIM

Felderhof had extensive experience in the Pacific Rim of Fire, Indonesia in particular and tropical environments in general and their affect on gold and gold deposits. This kind of experience assists and influences a geologist's interpretation of gold and other deposits. Dr. Hellman and Leach also had extensive experience in the Southwest Pacific.

Exhibit 1202
Exhibit 1328 A
Exhibit 1328 B
Transcript: March 21, 2005, pages 42-44

FARQUHARSON'S LACK OF EXPERIENCE IN THE PACIFIC RIM

Farquharson had virtually no experience in the Southwest Pacific and so did not have the benefit of such experience in interpreting Busang or in comparing Busang to Kelian or any other property in the Pacific Rim of Fire or in Indonesia.

Exhibit 676
Exhibit 677

RED FLAGS FOR FELDERHOF BUT NOT FOR STRATHCONA'S CLIENTS

Some matters which Farquharson says are red flags for Felderhof are not red flags for companies associated with Strathcona or Farquharson. Dr. Hellman's opinion is found at page 24 of Exhibit 1202:

> **Red flags for Felderhof but not for Strathcona's clients**
>
> Many of Strathcona's alleged red flags for Mr. Felderhof occur in reports for Strathcona's clients but are only described using benign terms. These include: relationship of grind size to recovery; liberation of gold at a coarse crush size; whole core crushing, poor precision of repeat assays; lack of correlation of closely situated drill holes; and the visual identification of mineralization. It is clear that different standards and criteria for red flag allegations are used by Strathcona for Mr. Felderhof compared with Strathcona's clients.

Dr. Hellman's detailed analysis is at pages 268-273.

Examples of alleged red flags for Felderhof that are not red flags for Farquharson's or Strathcona's associated companies are found later in these reasons in the discussion of Red Flags 5 (at page 280), 6 (at page 286), 8 (at page 305), 18 (at page 357), 20 (at page 360) and the alleged red flag with respect to "*duplicate sample numbers*" (at page 223) which was not one of the original 20 Red Flags.

The Golden Spike

Another example is the gold spike in hole BSSE 204. Although Farquharson pointed out the gold spike from Southeast Zone, hole BSSE 204, which had a grade of 196 grams per tonne, he saw nothing unusual in a much larger spike reported by a company with which he was associated.

With respect to the gold spike in hole BSSE 204, Farquharson agreed it would be a "*bonanza*" and testified it "*must be a spectacular sample because with that amount of gold one would expect to see gold almost dripping from the rock.*"

Transcript: March 16, 2005, pages 90-92

Farquharson is on the board of Cambior. In a 43-101 Report, Cambior reported a hole at the Ponderosa Mine that was a little over ten times greater than the gold spike in hole BSSE 204. In contrast to his description of the Busang hole, Farquharson testified he did not "*see anything unusual*" about the spike reported by Cambior.

Transcript: March 23, 2005, pages 98-101
Exhibit 744

STRATHCONA'S RETAINER AND IMPARTIALITY

In McWilliam's *Canadian Criminal Evidence, Fourth Edition*, Canada Law Book, at pages 12-57 to 12-59 the authors state:

> The importance of impartial expert opinion testimony cannot be overemphasized. The expert's evidence is permitted in the limited circumstances of a necessary exception to an exclusionary rule. Partial or biased evidence amounts to an abuse of the exceptional indulgence or opportunity to provide opinion testimony. This is so having especial regard to the limited effectiveness of cross-examination of an expert witness and, as discussed below, the contours of the hearsay exception relating to an expert's reliance in formulating an opinion on facts, data or material not otherwise proven by admissible evidence at trial.
>
> Historically, the court called an expert witness to give evidence not as a witness for one side or the other and neutrality was assumed. With entrenchment of the adversary system, the professional witness emerged called by one party or the other and "frequently" the courts have seen an unfortunate move away from the impartiality generally associated with professional to the posture of an advocate.
>
> Expert evidence prepared independently of a party is more capable of belief. An expert witness is not called as an advocate. Lack of independence, professional objectivity, and impartiality, even in the absence of dishonest bias, can contribute

> to miscarriages of justice. Unprincipled predisposition to a conclusion, partiality, and lack of independence threaten objectivity. A touchstone of reliability is impartiality.
>
> The trier of fact is expected within the fact-finding function to arrive at an independent assessment of the facts. But there is a contextual limitation when expert opinion evidence is called. The ready-made inference or conclusion delivered by the expert witness with special knowledge can be accepted, rejected or ignored by the trier but rarely is the trier able to critically evaluate the situation with the expertise of the witness. After all, the trier does not become an expert. In reality, something is inevitably given away to the expert witness in the sense of taking on faith aspects of the expert's testimony – this underlies the necessity criterion itself while heightening the essentiality of impartiality in this exception to the exclusionary rule against opinion testimony. Ordinarily, with any witness, cross-examination exposes bias or favouritism or lack of independence. However, expert opinion testimony can be highly resistant to effective cross-examination. Cross-examination may or may not be equal to the task of exposing that the expert is not disinterested. As well, presented with the prospective evidence of a presumptively objective expert, the other side may not appreciate that it should call an opposing expert or, in the case of the defence, be unable to afford the cost of doing so.
> An expert witness may have a vested interest in the outcome of proceedings for reasons of economic gain, personal association with a party or lawyer or the police, or otherwise due to an effort to advance at all costs a particular point of view.
> Although an expert witness is not technically an officer of the court, his or her role is closely akin to that status –the court has a say in defining the ethical limits of the adversary system in admitting expert opinion evidence. The primary duty of an expert testifying in court is to the court itself.

Strathcona and Farquharson did comment "*on the features why Busang was perspective for gold mineralization*" and pointed out "*that one of the reasons why this unprecedented salting scandal could occur is that the Busang site was a wonderful geological opportunity for that to take place*", which are factors that assist the Defence. But otherwise Farquharson agreed that "*Strathcona only did what the Commission asked it to do and the Commission asked it to focus on certain red flags*" and that "*[a]t no time was Strathcona asked to prepare a report that would have set out all of the factors that might*

have led someone to believe the assay results." Strathcona was not asked by the O.S.C. to look for green flags.

Farquharson testified "*we never saw ourselves as an arm of the Commission*" but he agreed that it was "*fair*" to say that "*Strathcona saw its job was to provide assistance to the Commission in its efforts to prosecute Mr. Felderhof.*"

Transcript: March 23, 2005, pages 38-42
Transcript: March 29, 2005, pages 51-52

It is of some concern that an expert sees his or her role as assisting the prosecutor to prosecute. "*The primary duty of an expert...is to the court itself.*"

M.R.D.I.

Earlier in these reasons, at pages 187-197, I discuss M.R.D.I. . Farquharson's cross-examination is reproduced at pages 188-193 of these reasons and is found in the transcript of March 30, 2005, pages 113-120.

Farquharson was cross-examined on an internal Strathcona memo which concedes that the well respected consulting firm M.R.D.I. reviewed Bre-X's work at Busang and addressed normal short-comings in its report but did not suspect salting nor see any red flags. M.R.D.I. concluded Bre-X's work was "*of a high industry standard.*" The Strathcona memo concedes that the M.R.D.I. report was a "*powerful arguement*" for Felderhof. The memo then talks about how that powerful argument can be "*de-clawed*" conceding it can only be "*partly*" de-clawed. Farquharson also testified with respect to this memo that Strathcona did "*not of course ever [expect] to see this document in a court room.*"

This memo is of concern and in line with Farquharson's evidence that "*Strathcona saw it's job was to provide assistance to the Commission in its efforts to prosecute Mr. Felderhof*" as evidenced by Strathcona's efforts to "*declaw*" a "*powerful argument*" that would impede that prosecution. As noted above the primary duty of an expert is to the court and not to the prosecutor.

There are concerns when an expert testifies that it was never expected that the court see an internal memo which is very helpful to the Defendant while at the same time putting before the court their expert opinion (Exhibit 681 dated March 21 2000) which does not include in its list of "*References*" to that opinion the report (Exhibit 505) which is the subject matter of the internal memo. Strathcona had a copy of Exhibit 505 as is evidenced by Strathcona's reference to it in Exhibit 208 (dated May 3, 1997).

Lakefield

Later in these reasons at page 343-345, I discuss the evidence that Farquharson preferred Strathcona's own incriminating opinion identifying alluvial gold (Red Flag 16) over the contrary opinion of experts (Lakefield) retained by Strathcona itself.

On March 30, 2005, Farquharson testified at page 50:

> MR. GROIA: So in other words, Strathcona's opinion, as far as you are concerned, takes precedence over the work that you asked Lakefield to do to try and confirm that opinion?
>
> MR. FARQUHARSON: We are very much of the opinion that that is alluvial gold.

MR. GROIA: And nothing Lakefield or anyone else can say will persuade you that you might be mistaken?

MR. FARQUHARSON: Correct.

At page 57:

MR. GROIA: And nothing Lakefield could say would possibly put doubt in Strathcona's mind, I take it.

MR. FARQUHARSON: Correct.

And at page 121:

MR. GROIA: So as you said just before the lunch break, just as though there is nothing Strathcona could have said or done – I'm sorry – there is nothing that Lakefield could have said or done to get you to change your opinion about alluvial gold, there is nothing that anyone can say or do that will get you to change your opinion about these red flags. Isn't that right, Mr. Farquharson?

MR. FARQUHARSON: Yes.

Farquharson did not refer to Lakefield's statement which contradicts Farquharson's opinion in the body of Strathcona's opinion Exhibit 681 as would be expected from an expert in possession of a contradictory opinion from someone retained by the expert himself or herself.

The October 1997 letter is Appendix VII to Exhibit 681 and it sets out the red flags. Red Flag 16 makes references to Lakefield. There is no indication there of Lakefield's contradictory statement. In fact it indicates Lakefield's work was confirmatory:

Freeport made the same observations and we confirmed the nature of the gold with our work at Lakefield.

Kelian

At pages 166-173, 248-251, 265-266, 275, 296-298, 315-316, 354-355, of these reasons I discuss the Kelian gold property and Farquharson's general misinformation about Kelian. Farquharson testified new information would not change his opinion.

On March 31, 2005 at page 120:

> MR. GROIA: Well I know you are already on record, Mr. Farquharson, as saying there is nothing anybody can do to change your opinion about these red flags. But hypothetically, if I could show you that at Kelian there are two nearby deposits that are quite different with quite different surface expression and similar characteristics in some respects to Busang, would that change your opinion?
>
> MR. FARQUHARSON: No.

An expert must be open to re-assessing and re-evaluating his or her opinion particularly upon receipt of new information or realization of errors or omissions.

When Farquharson was asked whether after extensive cross-examination and after conceding errors, omissions, and corrections to his evidence whether he would concede that the red flags had "*been in any way tarnished or made less bright*" he answered that Strathcona "*would modify a few of the words that we have used in some of the statements. But the flags are all still there.*" This is difficult to reconcile with the errors and corrections in his evidence and the inconsistencies in what were the brightest red flags between the Strathcona opinion Exhibit 681 in 2000 and Farquharson's re-examination in 2005. The brightest red flags are discussed at pages 173-178 of these reasons.

Transcript: April 6, 2005, pages 121-122

OTHER ISSUES WITH GRAHAM FARQUHARSON'S EVIDENCE

In considering the weight to give to Farquharson's evidence, I take into consideration the issues, errors, omissions, concessions and corrections raised in the following pages: 138, 145-149, 161, 166, 171-193, 208-228, 247-252, 257-268, 270, 275, 280-281, 285-286, 292-299, 305-307, 310-316, 329, 334-339, 342-357, 360 and 378 of these reasons. Following are three other areas of Farquharson's evidence which, although not directly relevant to the charges, also raise some concerns about reliability.

The Origin Of The Salted Gold

I heard evidence and submissions on the issue of when the salting began. It is not an issue I need to determine in this judgement.

Transcript: August 28, 2006, page 67

For purposes of this judgement it is sufficient that I find that there was substantial salting before and during the time periods which encompass the four press releases in Counts 5 to 8, June 20, 1996 to February 17, 1997. The salting resulted in the announcements of "*measured, indicated and inferred resources*" in each of the press releases being "*misleading or untrue*".

Farquharson contradicted himself with respect to what statement he had made about the connection between the salted gold and the gold from the warung (Indonesian word for small shop) bought by Forensic Investigation Associates Inc. (F.I.A.):

> MR. FARQUHARSON: ...But we did not make a statement where we said that gold that F.I.A. bought is the gold that was used for the salting.

MR. GROIA: You have never said that anywhere at any time in any report, or lecture, or article?

MR. FARQUHARSON: Well I probably have. I probably have said that the gold that was found in those samples was probably purchased from the local gold seller.

MR. GROIA: Well, in fact, I'm glad you agree. It saves me the trouble of showing you that you have...

Transcript: March 22, 2005, page 59
Exhibit 1202: pages 14, 36

Farquharson did not fingerprint the gold found in the tampered samples nor the gold purchased by F.I.A. from the local warung yet Strathcona made the statement that the gold purchased by F.I.A. was probably the gold used for salting.

Farquharson agreed fingerprinting would have given a definitive answer. Farquharson based his opinion not on fingerprinting but on the basis that the similarities in the gold examined was "*very striking*" and that "*they look awfully similar.*"

Transcript: March 22, 2005, pages 58-59

Dr. Hellman had the gold fingerprinted and determined that the warung was not the source of the gold used for salting. Strathcona was wrong and gave an opinion without conducting a definitive test.

Exhibit 1202: pages 15, 38-39

Trading in Bre-X's Stock Suspended On March 26, 1997

Farquharson testified trading in Bre-X stock was halted for several weeks after his March 26, 1997 telephone call and letter to Bre-X stating "*there appears to be a strong*

possibility that the potential gold resources on the Busang property have been overstated". Farquharson testified this resulted in the issuance of a press release by Bre-X and the suspension of trading by the Toronto Stock Exchange. Farquharson confirmed this evidence several times. After being shown the Toronto Stock Exchange records that showed the suspension was for one day only, Farquharson testified that was not his recollection but that "*I stand to be corrected.*"

This is an example of the witness being wrong on a not insignificant matter and continuing in the error even after being challenged several times until it is proven otherwise by independent evidence.

Transcript: April 6, 2005, pages 122-133
Exhibit 208: Appendix I

Strathcona Sample Mix-Up

Farquharson testified Strathcona took "*extraordinary precautions to the best of Strathcona's ability to ensure that [their auditing] program was handled in a competent manner.*" Yet four boxes of Strathcona samples intended "*under the strictest of security*" to be sent to Canada were sent to Indonesia and four boxes intended for Indonesia went to Canada. Strathcona did not accept this as their mistake in the sample process but a mistake with the courier. Farquharson's evidence was once they relied on a competent firm, Strathcona was no longer responsible. This was not the standard applied to Felderhof in his reliance on Kilborn, Hazen, Normet, M.R.D.I. and the many other professionals retained by Bre-X. Strathcona did not acknowledge, nor explain, the sample mix-up in Strathcona's opinion, Exhibit 681.

Transcript: March 23, 2005, pages 21-24
Exhibit 732

Dr. Hellman's and Terry Leach's evidence are also not free of issues and concerns.

ISSUES WITH DR. HELLMAN'S EVIDENCE

In considering the weight to give to Dr. Hellman's evidence there are some matters that need to be considered. Foremost was his change of position with respect to Red Flags 1 and 2 discussed at pages 234-247 of these reasons. Other issues of concern are discussed at pages 258-259, 281-282, 320-321, 342, 350, 356-357 of these reasons.

ISSUES WITH TERRY LEACH'S EVIDENCE

In considering the weight to give to Leach's evidence there are issues that need consideration. There, are, for example issues with respect to Leach's evidence about Red Flag 8 (at pages 299-305 of these reasons) and a concern that he inferentially conceded that he would have been involved in post dating a report at pages 300-301.
Other issues of concern are discussed at pages 254-256, 261, 266-269, 273-274, 314 and 322-323.

Other Criticism About Defence and O.S.C. Experts

There are other criticisms made by the O.S.C. about the evidence of Dr. Hellman and Terry Leach that I have not listed because they were more minor and/or resolved by a careful review of the O.S.C. and Defence submissions in Exhibit S5 Volume II.
The same is true of other criticisms by the Defence about Farquharson's evidence in Exhibit S4 and Exhibit S13.

Not Listed As Red Flags

Before I address the red flags, I will deal with two issues that arose during the trial but are not listed as red flags in the October 1997 letter nor in Strathcona's opinion Exhibit 681. Nor did the O.S.C. include them in their written submissions about red flags.

Exhibit S10
Exhibit S5 Volume II

Duplicate Sample Numbers

The Defence position and O.S.C. comments are set out in paragraphs 220-221 of Exhibit S3 and S13.

Dr. Hellman set out why in his opinion this was not a red flag at Exhibit 1202, pages 49-50, 158-159.

About 4,000 Bre-X samples had duplicate sample numbers. In chief, Farquharson described this as a "*troubling occurrence*". But in another Strathcona report with respect to another property, Angostura, Strathcona stated that all procedures were followed although Angostura also had a problem with duplicate sample numbers. See page 212 of these reasons.

Farquharson did not know that Kilborn was aware of the problem early on and of the explanation for the problem and that the samples could be properly identified by their job number.

In any event, Farquharson testified "*I don't believe that we made a lot of noise about this in our opinion report.*"

Exhibit 767
Transcript: April 6, 2005, pages 99-103

This is an alleged red flag that has more to do with best practices, with respect to which there may be different opinions, than with questioning the reliability of the resource calculations in the press releases which is what is relevant to Counts 5 to 8.

See 178 of these reasons.

Strathcona Cross-Section –Central Zone 4850 E, Exhibit 679, Exhibit 721

The Defence position and O.S.C. comments are set out in paragraphs 83-92 of Exhibit S3 and S13.

The Defence sets out the purpose of this cross-section prepared by Strathcona in paragraph 83:

> Para. 83. In an attempt to demonstrate that Bre-X's drilling results from the Central Zone were tainted compared with the previous drilling of Westralian, Strathcona prepared a cross section from the Central Zone of section 4850E. It shows four Westralian holes and one Bre-X hole. The cross section was prepared to assist Mr. Farquharson's evidence concerning the supposed conflict between the Bre-X drilling gold results and the earlier results of Westralian. As Mr. Farquharson testified "the intent of that section was to show the results from the four holes drilled by Westralian versus the one very good hole drilled by Bre-X [BRH-99]."

The O.S.C. comments on that paragraph state in part:

> The purpose of section 4850E is not to show all the holes drilled in the area, but to demonstrate how the very different gold grades in Budpholes [sic], particularly BUD 18 and hole BRH-99 should have been a concern for someone in Felderhof's position.

Exhibit S13: paragraph 83

The section included four Westralian holes and one Bre-X hole. Farquharson testified the section "*should illustrate to whoever is looking at the results, how can we have such a fantastic hole in the middle of all of these other not so good holes.*"

In cross-examination, Farquharson acknowledged that Strathcona had left off five other Bre-X holes drilled inside the section while including the one Bre-X hole (BSSE 99) drilled 30 meters outside the section.

Farquharson testified at page 12, March 22, 2005:

> MR. GROIA: So you had to go 30 metres outside the section to come up with hole 99, right?
>
> MR. FARQUHARSON: Yes.
>
> MR. GROIA: So you leave out five holes that were drilled by Bre-X inside the section and you go 30 metres outside the section to show one hole?
>
> MR. FARQUHARSON: Yes.
>
> MR. GROIA: Now would you agree with me, Sir, that all of the holes that were drilled inside your section that you chose to leave off of your map show results that are much more comparable to the holes that were drilled by Montague?
>
> MR. FARQUHARSON: They are not as strong as the results as Bre-X had in hole 99, yes.
>
> MR. GROIA: They are more typical?
>
> MR. FARQUHARSON: Well if the BUD holes are all like the four holes that are shown on there. These assays here have some pretty good kicks in them, as we would say.
>
> MR. GROIA: Well if we look at Bre-X hole 81, for example, and compare it to BUD hole 1 ---

MR. FARQUHARSON: Yes.

MR. GROIA: ---that hole is not nearly as good as the Montague hole, is it?

MR. FARQUHARSON: It's okay.

THE COURT: Sorry. 81 is not as good as BUD-1, is that the question?

MR. GROIA: That's correct.

MR. GROIA: You would agree with that?

MR. FARQUHARSON: Yes.

MR. GROIA: And you chose to leave hole 81 off your map?

MR. FARQUHARSON: Yes.

MR. GROIA: And if we looked at Westralian hole BUD-2 and compare it to Bre-X hole 70, BUD-2 shows some kicks near the bottom of the hole and the Bre-X hole shows some kicks a quarter of the way down and three-quarters of the way down; is that fair?

MR. FARQUHARSON: Yes.

MR. GROIA: Would you agree with me that hole 70 which you chose to omit from your map is much more typical of the BUD-2 hole than hole 99?

MR. FARQUHARSON: Yes.

MR. GROIA: Is there any Bre-X hole that you left off your map that's anywhere close to hole 99?

MR. FARQUHARSON: No. It was the best one.

MR. GROIA: Well it was so good you had to go outside the section in order to find it, didn't you?

MR. FARQUHARSON: I don't think 30 metres off the section is really going outside the section.

MR. GROIA: And you don't think leaving out five closer holes could be perhaps seen as a bit misleading?

MR. FARQUHARSON: For completeness we should have shown the other holes. We were trying to illustrate here the comparison between this hole and the four holes that were drilled by Westralian.

And at page 15:

MR. GROIA: And you are not concerned about the fact you chose to leave all those other holes off your map?

MR. FARQUHARSON: No, because we think that this hole should illustrate to whoever is looking at the results, how can we have such a fantastic hole in the middle of all of these other not so good holes.

MR. GROIA: That's right. And to understand that you would have to understand the geology of that particular part of the Central Zone, correct?

MR. FARQUHARSON: Yes.

MR. GROIA: So what do you know about the geology of line 4850E?

MR. FARQUHARSON: I don't recall anything specific about that section.

MR. GROIA: Do you know where the Vassel Dykes are located?

MR. FARQUHARSON: Not off hand, no.

MR. GROIA: So in order for anyone to have some understanding about the relationship between 99 and the eight holes that we are now discussing, they would have to do a fairly close review of the geology of the area, would they not?

MR. FARQUHARSON: Yes.

MR. GROIA: And you haven't done that I take it?

MR. FARQUHARSON: No.

Transcript: March 22, 2005, pages 12-15

The five Bre-X holes left off the section are more typical of the Westralian holes than the one Bre-X hole included. When asked whether "*leaving out five closer holes could be perhaps seen as a bit misleading?*" Farquharson answered that "*For completeness we should have shown the other holes.*" Farquharson agrees that to understand Strathcona's cross-section and to understand the relationship between BSSE 99 and the other holes would require "*a fairly close review of the geology of the area*" which Strathcona did not do but yet purported to express an opinion.

Transcript: March 22, 2005, pages 7-17

Exhibit 679
Exhibit 721
Exhibit 722

THE RED FLAGS: 1 TO 20

Red Flags 1 and 2: Absence of Gold Surface Anomalies In the Southeast Zone

The O.S.C. position is set out in paragraphs 316-559 of Exhibit S5 Volume II and S10.

The Defence position is set out in paragraphs 112-190 of Exhibit S3 and S13.

Farquharson

In the October 1997 letter Farquharson states:

1. No gold geochemical anomaly over the Southeast Zone

We asked the question of whether or not there was a geochemical expression on surface of the major deposit that was said to be located in the Southeast Zone,

having been aware that there was a geochemical expression for the gold mineralization that had been identified in the Central Zone by the Australian group that carried out exploration at Busang prior to Bre-X. There really was no satisfactory explanation given as to why there was no geochemical anomaly over the Southeast Zone.

2. No gold in outcrop samples –"it had been leached"

We also asked why there was no gold in samples of outcrop over the Southeast Zone as indicated by an outcrop map in the office at Busang, particularly given that the orebody as projected by Kilborn, and based on the drill core assays, extended right through to surface. The answer came back that the gold on surface had been leached and probably was concentrated a few metres below surface which, of course, was not the case.

Exhibit 681: Appendix VII (The complete letter is found at pages 115-121 of these reasons).

Farquharson's detailed opinion with respect to Red Flag 1 and 2 is set out at pages 13 to 16 of Exhibit 681:

Absence of Gold in Surface Samples from the Southeast Zone

...

Confronted with this recorded evidence of lack of gold in the Southeast Zone at surface by Strathcona, John Felderhof stated that the gold had been leached out of the surface layer, which, from his experience was not unusual for gold deposits in this area. The literature on gold deposits from Indonesia confirms quite to the contrary (van Leeuwen, 1994), that gold is not removed from the surface layer during weathering, but remains there, and might even become enriched near surface (supergene enrichment as explained previously on page 8).

The Busang alteration and mineralization is characterized as carbonate-base metal style, similar to the Kelian gold deposit, situated 100 kilometres to the southwest of Busang. Kelian has been successfully exploited and although it has gold grades similar to that reported for Busang it does not have coarse free gold as implied for Busang. The weathered layer of such a deposit may contain lead, zinc, copper, silver, arsenic and other metals besides gold. Different from base metals, which mostly occur as sulfides and are mobile during weathering, gold in its native form, or as a gold-silver alloy, is chemically inert and cannot be easily leached.

The presence of base metals in soil or weathered bedrock in the absence of gold, is a strong indication that gold is not present in the unweathered rock. The following facts corroborate this:

- van Leeuwen, in his 1994 paper on 25 years of mineral exploration and discovery in Indonesia states that: "*Erosion and weathering contributed to significant supergene enrichment at a number of prospects. This constituted an important gold source for local miners, but often led to disappointing results for the exploration companies when the underlying primary zone was tested by drilling.*"

This indicates that gold became enriched over these occurrences during weathering, and not depleted as indicated by Felderhof.

...

- The Central and Southeast Zones are situated on a hill which rises above the lower land surrounding it and is subject to strong erosion under the prevailing climatic conditions. Rapid erosion is documented by the rather shallow layer of only several metres of oxidized rock intersected in drill holes at Busang. This rapid erosion would have counteracted the leaching of metals from surface materials –which requires time – and is therefore inconsistent with any suggestion of leaching of gold near surface in the Southeast Zone.

- Surface depletion of gold would have been highly inconsistent with the fact that good gold values started at the top of many Bre-X drill holes...

...

The presence of base metals in surface samples over the Southeast Zone and the lack of gold in those samples disprove the claim that gold had been leached or depleted at surface. The geochemistry of the Southeast Zone from surface sampling rather confirms that it is very unlikely there is gold in the underlying rocks. In contrast the Central Zone had a surface expression of gold as would be expected given the underlying in-situ gold content. [Emphasis in Original]

Exhibit 681: pages 13 to 16

Farquharson testified at pages 25 to 27, March 17, 2005:

MR. FARQUHARSON: Mr. Felderhof offered the view that the gold from the surface had been leached. In other words, put into solution and carried away.

MR. MARROCCO: Can you comment on that?

MR. FARQUHARSON: And we found that difficult to accept because the drill holes that Bre-X had going through the surface oxidized material showed gold right from the surface through the oxide zone. And if the gold had been depleted then there would not be any gold values in the drill holes as reported by Bre-X.

Secondly, there was no what we would call a super gene concentration of gold in the oxide zone.

...

MR. FARQUHARSON: No super gene, s-u-p-e-r-g-e-n-e. And that term means that if the gold had been leached, put into solution from the tops of this deposit there should be a corresponding concentration lower down in the deposit. And from our review of all of the assay values from the drill holes we found no evidence for any super gene concentration.

The third factor that made it difficult to accept this theory of surface depletion of the gold was that the base metal values remained strong in the surface sampling and in the drill core sampling. And because gold, being the most noble of metals and, therefore, the last to be put into solution, if there is a leaching process, then the base metal values should be negligible and should have disappeared long before the gold disappeared. But there were base metal values in the surface samples, in the drill hole samples near surface, but there was a marked absence of gold.

Leach

Leach's opinion is that these allegations are not a red flag. (Exhibit 1328A, pages 41-49,

Exhibit 1328B, pages 42-80)

At page 43 of Exhibit 1328B Leach states:

A. SUMMARY OF ALLEGATIONS AND REBUTTALS

Two of the three main processes for mobilization of metals during weathering support Felderhof's model of surface gold depletion which is without base metal or silver depletion. Strathcona (2000) [37] described the other main processes of

weathering, which does not reflect the surface geochemical expressions at Busang. In addition, Strathcona omitted from their report reference to surface samples from the South East Zone that did contain significant gold. Furthermore, they overstated the 'absence' or 'lack' of gold and the 'presence' of base metals in Bre-X surfaces trenches. Strathcona also omitted evidence of other surface geological expressions that indicate gold should occur below the surface.

Surface gold depletion in Indonesia deposits has been described by van Leeuwen (1994) [608] in Indonesian [sic], and there is evidence of gold depletion at Busang, both of which were not referred to by Strathcona (2000) [37]. Gold depletion is also documented in papers on other major Southwest Pacific gold deposits. Experienced geologists who visited Busang knew of, and did not disagree with, Felderhof's explanation of surface gold depletion in the South East Zone.

Strathcona (2000) [37] failed to understand that the geology in the high grade Northeast Zone at Kelian, where there is no pronounced surface gold geochemistry, is comparable to the South East Zone at Busang. On the other hand, the Prampus Zone at Kelian, which has surface gold and base metal expressions, exhibits some similarities to the Central Zone at Busang. Furthermore, their misconstrued comparisons of the Central and South East Zone at Busang are also based on the misconception that surface geochemical expressions should be uniform throughout a mineral deposit.

Contrary to the allegations by Strathcona (2000) [37], gold is depleted in the top of the South East Zone drill holes and this depletion was observed from the very first holes drilled in the South East Zone. Many of the holes along the section lines twinned by Strathcona showed depletion at their tops, and where this was not the case, there was gold in surface samples in the immediate vicinity of the drillhole, or there was no surface data available for comparison. In addition, there were many wrong assumptions made by Strathcona concerning comparisons between surface samples and assays at the top of the drill holes.

Allegations on apparent inconsistencies between the rates of erosion and gold depletion by Strathcona (2000) [37] are based on incorrect comments or omissions concerning the relative topography, rock types, alteration and vein types between the Central and South East Zones. Furthermore, gold depletion is recorded in similar deposits that have comparable, or even more rapid, erosion rates than at Busang.

Contrary to the allegations by Strathcona (2000) [37], it is common in Pacific Rim mineral deposits for large ore-bodies to be either concealed at the surface or some or most of the deposit to be concealed. On the other hand, there are significant geological indications that there would be a large ore body below the surface in the South East Zone.

Leach did not agree with Strathcona that there was no gold in samples over the Southeast Zone.

Exhibit 1328B: pages 43, 48-50

Leach did not agree with Strathcona's opinion that if there was a geochemical expression on the surface of the Central Zone then there should be a geochemical expression at the Southeast Zone. Leach's rebuttal is at page 76 of Exhibit 1328B:

i) It is very common in the Circum Pacific Region (Pacific Rim) for large ore-bodies to be either totally concealed at the surface (blind deposits), or for some or most of the deposit to be concealed.

ii) Contrary to the statements by Strathcona, the South East Zone at Busang does have a strong geochemical expression, as well as a strong geological expression at the surface, which indicate that there should be a large ore body below the surface.

Leach did not agree with Strathcona's allegation "*that the presence of a pronounced surface gold expression in the Central Zone where there was gold in the underlying rocks, indicated that there was no gold in the underlying rocks in the South East Zone.*"

Leach's rebuttal is at page 62:

i) Strathcona failed to distinguish between the Prampus ore zones at Kelian, which do have a pronounced surface gold expression, and the high grade Northeast Kelian ore zone, which are shown to extend to the surface but in fact do not have significant surface geochemical signatures.

ii) Comparisons made by Strathcona between Busang and the Kelian gold deposits are based on a lack of understanding of the geology of both deposits. Although some features of the Prampus zones at Kelian which have surface geochemical expression and are similar to those in the Central Zone at Busang, the characteristics of the South East Zone at Busang are much more comparable to those of the Northeast Zone at Kelian where there is no pronounced surface expression.

iii) The assertions made by Strathcona are based on the misconception that the surface geochemical expressions should be uniform throughout a deposit. They assert that the surface expressions in the South East Zone should be the same as those in the Central Zone, or that the surface expressions in the Prampus Zone at Kelian are representative of the rest of the deposit. This is clearly not the case.

Dr. Hellman

Dr. Hellman's opinion is also that these allegations are not a red flag. (Exhibit 1202, page 15-18, 21-22, 39-42, 46-47, 100-130, 252-260)

At pages 15-18 Dr. Hellman states:

> In my report, I made several statements that I considered to be reasonable at the time, but subsequently they were proven to be incorrect because they were based on incomplete information. These statements were:
>
> - the absence of gold in trenches compared to gold occurring in adjacent drill holes is not logical (p5)
> - enrichment rather than depletion of gold values should occur
> - virtually no gold occurs in the trenches from the SEZ
> - anomalous Ag-Pb (silver-lead) in surface samples from the SEZ should result in anomalous gold at surface
>
> These and other similar statements made to the RCMP and SEC were made without the benefit of three important pieces of data:
>
> - The drill hole database was eventually provided after numerous requests in April 2000.
> - The assay results of several thousand surface samples were received in April 2000.
> - The 10 December 1994 map of geochemical results was subsequently provided.
>
> My chief conclusion concerning the tampering, however, was correct mainly on the basis that I could not understand how Freeport's drilling results could be wrong. I came to the same conclusion as Strathcona over a similar amount of time.

Unlike Strathcona, however, I have never claimed that there were red flags ignored by those associated with the project because I do not believe that to be true.

Once I received the additional information, I was able to confirm the following:

- Mr. Felderhof's belief that surface depletion of gold was supported by the drill hole and surface geochemical data.
- Depletion of gold at the surface had been documented at many locations and was consistent with Mr. Felderhof's immediate past experience.
- There was anomalous gold in surface samples from the South East Zone.
- Concentrations of Ag and Pb are not diagnostic of gold.

Strathcona's Summary of Red Flags

Strathcona (2000, p 2) divided the red flags into two major groups. The first group deals with the absence of gold surface anomalies over the SEZ. The second group concerns the physical nature of the gold. Appendix 3 provides more details on Strathcona's red flags.

"Absence of gold anomalies in the SEZ"

The ***first assertion*** by Strathcona is that sediments from streams draining the SEZ contain no gold.

Gold, however, is known to be present in the streams draining the SEZ. To my knowledge, no data to the contrary have been presented by Strathcona.

The owner of the small shop or "warung" near the main Busang camp informed me that the streams draining the SEZ have pannable gold. The gold from the local streams that I purchased has an isotopic signature similar to that from surface mineralization over the SEZ.

The ***second assertion*** by Strathcona is that the presence of base metals in the surface samples over the SEZ and the lack of gold in those samples disprove Mr. Felderhof's view that gold had been leached.

This is incorrect for several reasons. There is no law of geochemistry which requires gold to be associated with base metals. In fact, it commonly has a weak association with base metals.

Strathcona's view on the mobility of gold is "*gold...is not dissolved in an oxidizing environment*". This view has been known to be incorrect since the 1930's and does not reflect mainstream science. It is not consistent with my experience and I have not found support for this view during an extensive literature search that I conducted. On the contrary, there is extensive geochemical literature that documents numerous examples of the mobility of gold in oxidizing environments.

The ***third assertion*** by Strathcona is that the CZ does have a typical surface expression in soils and surface outcrops. The gold-in-soil expression over the CZ is similar to that over many gold prospects. The CZ, however, has important geological differences from the SEZ which have not been addressed by Strathcona.

Gold deposits that have a subdued geochemical expression, like that of the SEZ, have been documented. Modern exploration in countries like Indonesia has been limited and directed at deposits with obvious geochemical characteristics. It is unknown how many other gold deposits exist that have more subtle geochemical expressions.

At pages 100-101 Dr. Hellman states:

***A. Red Flag Number 1 – "No gold geochemical anomaly over the Southeast Zone"* (Strathcona, 2000, [37], Appendix 7, pp 1& 2)**

Summary of Allegation

Strathcona alleges that:

- *The literature (eg. van Leeuwen, 1994) [8b] on gold deposits from Indonesia confirms that gold remains at the surface and may even be enriched, which is contrary to Felderhof's statements regarding the depletion at Busang. (p 13)*
- *"Gold in its native form, or as a gold-silver alloy, is chemically inert and cannot be easily leached." (p 13)*
- *"The presence of base metals in surface samples over the Southeast Zone and the lack of gold in those samples disproves any claim that gold had been leached or depleted at surface." (p 2)*

- *"Surface depletion of gold would have been highly inconsistent with the fact that good gold values started at the top of many Bre-X drill holes." (p 14)*
- *"Different from the Southeast Zone at Busang, the Kelian deposit had very pronounced gold anomalies at surface." (p 14)*

Summary of Opinion

Although Strathcona refers to Mr. van Leeuwen's paper on mineral exploration and mineral discoveries in Indonesia, they omit a clear reference in that paper to the surface gold depletion at the Mirah deposit, Central Kalimantan. Strathcona does not refer in any way to this deposit despite knowing that Mr. Felderhof had been involved in the exploration success at Mirah.

The weak gold response over the SEZ at Busang was consistent with Mr. Felderhof's experience at Mirah. The Mirah example demonstrates that, although enrichment of gold in soils and the supergene zone may be common in the tropical environment, exceptions do occur. It was with one of these exceptions that Mr. Felderhof had considerable immediate experience, which caused him to see an analogy with Busang.

It is difficult to find any support for Strathcona's statement regarding the inertness of gold from all the modern (in the last 50 years) literature on the geochemistry of gold. This likely reflects their limited experience in geochemical exploration and tropical or oxidized environments. There is an extensive and accessible literature and also international research programs directed at the documentation of gold's mobility.

In contrast to Strathcona's assertions, a study of the relationship between base metals such as lead (Pb) and silver (Ag) and gold at both Busang and other prospects in Indonesia indicates that there is no strong correlation between the base metals and gold. High gold may occur with low concentrations of Pb or Ag and vice versa. Low concentrations of gold may also occur with high values of Ag and Pb.

The lack of correlation between Au and other metals is the norm, particularly when moderately coarse gold is present. It is exacerbated by nugget effects in sampling which can obscure the relationship of gold to other metals. The lack of correlation means little or nothing while a strong correlation is, in my experience, rare.

A study of the variation of gold from the surface to the depth in the Central and South East Zones confirms Mr. Felderhof's views concerning the existence of depletion towards the surface in the South East Zone. The variation in gold grades with depth in the South East Zone is fundamentally different from the Central Zone and is consistent with the geology of the two areas.

It is true that there are examples of elevated surface gold values in the drill holes of the South East Zone. These appear to occur close to the largely negative surface channel samples only in a minority (less than 5%) of cases. These discrepancies, however, become less obvious when the topographic differences between the surface trenches (close to surface) and drill hole collars (may be up to 5-10 metres below surface) are taken into account.

And at pages 252-253 Dr. Hellman states:

The Mobility of Gold

Summary of Allegation

Strathcona alleges (2000, p 8, para 2) that:

> "gold is not dissolved in an oxidizing environment due to its chemical inertness and thus its designation as the most noble of all metals. Gold is mainly moved mechanically as particulate gold."

Summary of Opinion

The ability of gold to dissolve in oxidizing environments is well known and has been documented in numerous studies dating back to early last century. The statement made above by Strathcona concerning the insolubility of gold runs counter to the extensive published literature on gold and conflicts with the prevailing experience of the exploration community.

There has been considerable industry-based and academic research into the way gold dissolves in the oxidizing environment and concerning the mobility of gold. The results of this research are frequently published in accessible and reputable journals (eg. Journal of Geochemical Exploration, papers from which are cited by Strathcona). [37]

> In my view, Strathcona's allegations are implausible and reflect a profoundly limited experience with gold exploration. Their views conflict with the clearly expressed views of the authors in references that they cite.

At pages 110-113 Dr. Hellman sets out the "*Evidence of Depletion Towards the Surface at Busang.*" He concludes an observer "*would understandably find support for gold depletion at the surface.*"

Dr. Hellman's Change of Opinion

Originally, in 1997, Dr. Hellman reached the same conclusion as Strathcona when in Exhibit 774 he stated: "*[t]here are distinct contourable areas of anomalous gold... over the Central Zone deposit*" but "*[t]here is, however virtually no anomalous gold in the trench samples...from the South-East Zone mineralization despite the trenches recording anomalous Ag and Pb.*"

Dr. Hellman continued on page 5 of Exhibit 774:

> "It is the authors experience, that in the Busang environment, near surface mineralization such as that indicated by the assays of South-East drill core should result in anomalous gold in surface samples. Enrichment, rather than depletion as advocated by de Guzman (Alo, pers comm), will occur. The absence of gold in trenches at similar depths to gold enriched drill core is not logical. Its absence suggests there is negligible gold at the South-East Zone (-99% of the trench samples have less than 0.05 ppm Au)."

Exhibit 774: page 5

Dr. Hellman made similar statements in interviews with the R.C.M.P. (July 15, 1997) and S.E.C. (March 12, 1998).

Transcript: November 14, 2005, pages 70-75, pages 6-10

As noted above, Dr. Hellman now disagrees with Strathcona and in his opinion (Exhibit 1202) these allegations are not a red flag. The O.S.C. submits Dr. Hellman's "*credibility is questionable in light of the fact that he changed his story.*"

Exhibit S5 Volume II: paragraph 358

In his expert opinion Exhibit 1202 pages 39-42, Dr. Hellman discusses the statements he made originally which upon receiving further information he states have proven to be incorrect.

Issues Relating to Statements Made in May 1997 Report

In my observations on the soil and trench results in my May 1997 report (Appendix 2) I made several statements that were reasonable at the time, but have subsequently proven to be incorrect. I regarded the absence of gold in the trenches at similar depths to gold enriched drill core as not being logical (p5).

The results that I saw on the six 1:2500 sheets whilst at site, however, were not trench samples but mainly "outcrop channels" consisting of samples along drainages, a lesser number of samples along road cuts and a small number of actual trench samples. The drill hole locations were not plotted on the maps so it was not possible to determine whether the drill hole samples were in close proximity to the surface samples that had low grades. The results are plotted, in most cases, a long way from their actual sampling positions which gives the impression that the samples cover a wide area. In fact, they largely follow streams and roads.

Subsequently, in late 1999, I received a set of the six 1:2500 maps. On closer inspection, I was able to determine that very few of the surface samples were taken close to the drill holes. When I received the assay results of the surface samples in April 2000, it became clear that my statement concerning "*negligible gold at the South East Zone (-99% of the trench samples have less than 0.05 ppm Au)*" (p 5) was incorrect. This also became clear when I subsequently received the December 10, 1994 map [20] of the surface results from the SEZ.

I had also stated (p 5) in my May 1997 report that, in my experience, enrichment rather than depletion of gold values should occur in the surface samples. This, however, was different from Mr. Felderhof's experience which related to the very

large copper and gold deposit at Ok Tedi (PNG) and the gold deposit at Mirah (Kalimantan, Indonesia).

I was able to subsequently confirm that depletion of gold had been documented at both Ok Tedi and the Mirah deposit. From Mr. Felderhof's experience and perspective, it was no surprise that the geochemical expression of gold over the SEZ was subdued.

This became very clear when I received, in April 2000, the digital database of the drill hole assays. As I have detailed in my discussion of Strathcona's red flags 1 & 2 (below, and also in Appendix 3A & B), the gold assays in the drill core from the SEZ show an overall depletion towards the surface. I was able to confirm that Mr. Felderhof's experience and interpretation were consistent with the actual assay results.

I have shown in Appendix 3A that there is a broad relationship of Ag and Pb with the gold in the surface samples from the SEZ. I was able to determine this after I received the detailed assays of the surface samples in October 1999. My comments in my report (1997, p 5, section 6.1) relating to my view that anomalous Ag-Pb in the surface samples from the SEZ should result in anomalous gold were, therefore, unsubstantiated by a detailed and subsequent analysis of the data.

Kilborn did not provide the digital database despite requests at the original Sheraton meeting in mid-April 1997. It was three years before I received the data in April 2000. I was supplied the folder containing the surface results in October 1999. These results were subsequently computerized by me in April 2000 and form the basis of my analysis of surface depletion in the South East Zone that is discussed in the section on red flags (and also Appendix 3 A & B).

At the time of my visit to Busang in May 1997, I had no digital drill hole data or surface geochemical data and had not seen all the available surface maps. I was unaware of the evidence for surface gold depletion at the surface from the drill hole assays from the South East Zone. I was also unaware of the different style of surface expression in the Central Zone compared to the South East Zone. I was also not in a position to analyse the surface data collected from the South East Zone because it had not been provided in a digital format.

My conclusions on the absence of surface expression were based on a limited amount of data. These conclusions were never intended to be interpreted as red flags, but rather as inconsistencies with my experience.

The RCMP and SEC Interviews
The RCMP Interview, July 15, 1997

When the negative results of Freeport had been confirmed by Strathcona, I voluntarily contacted the Canadian consulate in Sydney and advised that I may be in possession of information of interest to Canadian investigative authorities. As a result, I was contacted by the RCMP and on July 15, 1997, I met with Cst. Mark van de Graf and Cpl. Tom Anderson in my Sydney home. I spent the morning with them, answered questions and showed them the slides of my work at Busang. I was not reimbursed for the time spent and did not expect any reimbursement. The record of interview [535] was provided to me about two years after it took place.

I reiterated my concerns about the absence of gold in the outcrop samples that were near the gold-bearing drill core. I also stated that the amount of gold panned by Mr. S. Imperial from the surface samples from SEZ was insufficient if a large gold deposit was underneath. I referred to this as "an obvious warning flag" (p 46), but forgot to say that Mr. Imperial's work was unknown to Mr. Felderhof and, to my knowledge, had never been reported. The location of Mr. Imperial's samples is unknown and I am not aware of any maps that show their location. I do not know how their locations relate to mineralized drill holes.

Mr. Imperial's work, therefore, could not be a warning flag when it was unknown. Mr. Imperial's explanation for the amount of gold panned was that it was due to leaching.

The SEC Interview, March 12, 1998

I volunteered to provide an explanation of my work for the Sheraton project to the SEC. This took place on March 12, 1998 in Dallas, Texas. Mr. M. Hubley of the OSC and Ms. D. McCombe of Watts, Griffis and McOuat were present in addition to two investigators from the U.S. SEC and various lawyers representing Mr. Felderhof. Hubley and McCombe left before the interview was finished. I was not reimbursed for the day and did not expect any reimbursement. The record of interview [522] was provided to me about two years after it took place.

The form of the meeting was completely different from that for which I understood I had volunteered. Rather than an explanation of my work, the meeting consisted mostly of a demanding cross-examination which commenced at 9 am and finished at 6:30 pm. Neither the SEC nor the OSC had indicated to me, via Mr. Felderhof's lawyers, that the meeting would be a detailed and exhaustive cross-examination.

As with the RCMP interview, I mentioned my issue with the depletion of gold over the SEZ (p 170).

In testimony Dr. Hellman stated:

MR. HELLMAN: There were two sets of information which profoundly affected me. I had, at the time at the Sheraton meeting, requested the digital database that Kilborn had, and I believe it was in April 2000, about three years later, that I was actually provided with the database of all the drill hole assays.

...

MR. HELLMAN: ...Earlier I had received a complete set of the surface samples, the actual assay results of the surface samples. I mentioned there were two sets of information, there was a third. There was a map dated the 10th of December 1994, that I believe was authored by Cesar Puspos which was a map of surface results as well. So in other words, there were two sets of surface results, two sets of maps, there was the 10th of December 1994 map, and there was a set of six, one to 2,500 maps, that was provided to me subsequently. And you will recall that I had only seen those 2,500 scale maps on site very briefly.

...

MR. HELLMAN: Okay. So we're talking about the different sets of information that I received. And at this time I was still disturbed by the apparent discrepancy between these surface results and the drill holes. The problem in my mind was that if you have a sample alongside a drill hole and the sample had negligible gold, and the drill hole sample had gold, then that is an apparent conflict which I needed to explain in my own mind.

So what I did to test Mr. Felderhof's view that there was depletion at the surface, and that was his very firm view at the time which he enunciated at the Sheraton meeting. He was completely open about that and since that meeting I've discovered that it was mentioned in the documents, and people like Barrick personnel had that explained to them and they readily accepted it. His view was that there was depletion at the surface in the drill holes and therefore that explained the subdued nature of the gold at the surface.

...

MR. HELLMAN: Yes. Well, I completed this work about three years later after I had written that report and obviously I could not have undertaken this analysis at the time because I did not have the data to do so. And it's very clear to me that my conclusions that I made at the time are incorrect on the basis of information that I subsequently received.

...

MR. GROIA: ...perhaps you could, if you would, just very briefly sum up your conclusions about what you consider to be the red flag allegation of Strathcona that there was no gold geochemical anomaly over the Southeast Zone.

MR. HELLMAN: In broad terms, all of that work of digitizing and creating the digital database was basically directed at a comparison of the surface drill hole grades with neighbouring surface samples. And I was able to demonstrate that there was only a minority of drill holes that actually had elevated grades at the surface, and that was the first conclusion. The second conclusion was that there was a very small number, I believe about less than five percent, of surface samples that had negligible gold that were closely situated with surface mineralized samples from drill core.

Now, I started this discussion by saying that this type of study is something that I have never personally seen undertaken by exploration and mining companies and it is certainly something that would have been impossible for Mr. Felderhof to have undertaken. The people who perhaps might have been able to plot the information that shows the juxtaposition of drill hole grades and surface samples would have been Kilborn. As far as I'm aware, Kilborn never digitized any surface information and I have never seen any sections with drill hole grades plotted in juxtaposition with the surface samples.

And in addition to that, we never quite know exactly where a drill hole collar has been located in terms of reference to the surface profile, because as I'd explained before, they can be at various depths below the surface because of the topographic relief.

MR. GROIA: But in broad terms, Doctor Hellman, do you agree with the Strathcona statement that there was no surface geochemistry in the Southeast Zone?

MR. HELLMAN: No, I don't.

MR. GROIA: Do you agree, at least, that the gold geochemical anomaly in the Southeast Zone was different than the Central Zone?

MR. HELLMAN: Yes, I do.

MR. GROIA: And do you agree that those differences, at least to you, seem to be generally consistent with the geological model that had been developed?

MR. HELLMAN: Yes, I do.

Transcript: November 3, 2005, pages 14-20, pages 76-77

And in cross-examination:

MS. COLE: And I put it to you, Doctor Hellman, that receiving the Kilborn digital database didn't make any difference to your opinion at all.

MR. HELLMAN: It made a huge difference, Ms. Cole.

MS. COLE: And Doctor Hellman –

MR. HELLMAN: It completely amazed me that when I undertook this study, it supported Mr. Felderhof's opinion.

...

MS. COLE: And when did you first realize that what you said in your Sheraton report and the R.C.M.P. interviews and the S.E.C. interviews was incomplete, or different?

MR. HELLMAN: There was, I think an evolution with – as I obtained more and more information and that culminated, as I mentioned this morning, in the receipt of the digital database. That had a major impact on my understanding of Mr. Felderhof's view of depletion and the reasons for that in the Southeast Zone.

...

MS. COLE: So I took from that that the fact you hadn't seen the available surface maps was something that was important in your changing your opinion.

MR. HELLMAN: Well, the changing of my opinion was over a period of time and gradually getting the grips with the accumulated data and evidence that came before me. And that 10th of December map was certainly part of that, and also a part of that was digitizing all the surface geochemical data, and what I referred to here as the digital hole data which is the Kilborn database. So it was an evolution of thought. And the area of depletion was one which had perplexed me and even disturbed me. And it was important for me to obtain verifiable and independently gathered data to assist Mr. Felderhof's view and how reasonable it was to have that view in terms of the data that I could actually establish for myself.

THE COURT: Sorry, could you just remind me how that data, the Kilborn data, led you to the conclusion that Felderhof's view about depletion was appropriate for the Southeast Zone?

MR. HELLMAN: Yes. Yes, Your Honour. I had been frustrated for, I think, three years because I had not had access to the digital assay information. And I think one has to keep in mind that let's say we're talking about 60,000 records of drill hole assays, each one of those records has a hole name, a sample number, an interval start, an interval two, and you can have up to eight to 10 assays. So to help me to [sic] my mathematics, if the average hole is 200 metres, and we're

dealing with say 10 fields of information, we're now up to 2,000 individual pieces of data, and you multiply that by 200, and it's a very substantial number. And that's why I thought it was foolish to embark on just trying to enter all of that information from possibly incomplete records, when I knew that there was a digital database out there which would do all that work for me. It would just have been a waste of time for me to try and have a student put all that in. And even if I'd done that, there would be no guarantee that that was accurate. And that was the same thing that Kilborn had used.

So it was in March or April 2000 when finally the digital database came my way – I was able to store it in my computer. And for the first time I was able to construct maps, cross sections, and actually look at the data that Kilborn had.

And one of the areas that was of great interest to me was whether I could test Mr. Felderhof's view that there was actual independent evidence for depletion in the Southeast Zone. So what I did was I looked at the variation of gold grades in the Central Zone and the Southeast Zone as you go from depth to surface. And astoundingly I found in the Southeast Zone, on average, that there is a very pronounced depletion of gold as you go from depth towards the surface. There was a slight similar effect in the Central Zone, but not nearly as pronounced. And then it was at that moment that I realized that not only had the perpetrators of the fraud succeeded in creating an apparently real deposit that was consistent in terms of geology and across a large area, but also somehow they had taken advantage of Mr. Felderhof's immediate past experience which had been at Mirah, where there was a documented account of this depletion. And I guess in a sense I had a new respect for the perpetrators of the fraud and, in my mind, I had established, using independently provided data, that Mr. Felderhof's view, based on that information, was reasonable.

Transcript: November 14, 2005, pages 34, 78, 81-84

Dr. Hellman has given a not unreasonable explanation for his change of position.

Gold Geochemical Anomalies Over The Central Zone And The Southeast Zone

The Defence agrees with Farquharson and the O.S.C. that there is a gold geochemical anomaly over the Central Zone.

Exhibit S5 Volume II: paragraph 344

The Defence disagrees with Strathcona's statement in Red Flag 1 that "*there was no geochemical anomaly over the Southeast Zone.*"

Strathcona prepared a map, "*Busang General Location Map*", showing the gold geochemical anomaly in the Central Zone and the absence of a gold anomaly in the Southeast Zone. Farquharson conceded in cross-examination that in preparing Strathcona's map, Strathcona left off anomalous samples from the Southeast Zone shown on the Bre-X December 10, 1994 map, Exhibit 712, and marked approved by Felderhof.
Transcript: March 22, 2005, pages 39-54

Farquharson is not correct when he categorically states "*there was no geochemical anomaly over the Southeast Zone.*"

Exhibit 761

In Exhibit 761 Strathcona failed to put six Strathcona holes on their map prepared to illustrate surface sampling.
Farquharson first testified Strathcona used all the drill hole results but then conceded the omission of the Strathcona holes. He testified it is just a coincidence that Strathcona included the fourteen holes that Strathcona was skeptical about but omitted the six holes that supported Felderhof's surface depletion theory.
Transcript: April 6, 2005, pages 26-27

Kelian

Leach's opinion at pages 62-63 Exhibit 1328 B sets out Strathcona's failures in understanding Kelian:

> ***i) Absence of surface gold expressions in some zones at Kelian***
>
> Strathcona failed to distinguish between the Prampus ore zones at Kelian, which do have a pronounced surface gold expression, and the high grade North Kelian ore zones that do not have significant surface geochemical signatures.
>
> ...
>
> However, Strathcona failed to show in their figure 2 (March 2000) [37] that the East Prampus Pit was extended to the Northeast to take in the high grade K393 and K394 ore bodies (TL 088; TL 090) and the intervening low-grade mineralisation. The Northeast Zone contains the most extensive and highest-grade mineralisation at Kelian (e.g. K466 –300m@ 5.5 g/t including 232m @ 7.18 g/t Au; Leach 2000) [29].
>
> Strathcona also failed to mention that, although the high grade K394 ore body is shown to extend to the surface, this ore body had virtually no significant expression at the surface.
>
> Therefore, the following conclusions can be made:
>
> - The surface geochemistry outlined the mineralisation in the Prampus Zone at Kelian, but did not define the high-grade ore zones that extended to the surface in the Northeast Zone.
> - The surface expressions in the Prampus Zones at Kelian are very similar to those in the Central Zone at Busang, which also has significant gold, silver and base metal in the surface material that coincides with gold in the underlying rocks.
> - The weak surface geochemical expressions in the Northeast Kelian Zone are comparable to those in the South East Zone at Busang, which also have very low silver and base metal surface expressions and appears to contain gold in the underlying rocks as evidenced by the drilling results.

When Farquharson was asked "*And what does Strathcona know about the North Prampus Zone?*" he replied "*not very much*".

Transcript: March 29, 2005, page 94

With respect to Northeast Zone or North Pampus Zone in Kelian Leach testified:

> MR. GROIA: And what was the surface expression, if any, for the 255 zone?
>
> MR. LEACH: It is blind. There was no surface expression at all.
>
> MR. GROIA: In both soil and in trench?
>
> MR. LEACH: Yeah, that's right. There was quite a lot of depths, so there wasn't – it was below the surface.
>
> MR. GROIA: Well how can you have a high grade zone and no surface expression?
>
> MR. LEACH: Well in this instant with the deposit actually, it didn't come to the surface. The actual mineralization didn't extend to the surface.
>
> MR. GROIA: And is that common or uncommon in the Pacific Rim?
>
> MR. LEACH: That's very common. I mean, yeah, it's very common. It's very common for a deposit to be blind. In fact, now most people look for blind deposits because we are looking at areas where there is no surface expression and most deposits which have a surface expression have already been mined.
>
> MR. GROIA: So if there was a suggestion that there being no surface expression was a red flag and indicative of tampered results or samples, what are these people doing looking for blind deposits?
>
> MR. LEACH: Well because I mean most people look for blind deposits because most of the ones that have an obvious surface expression has been mined. So what we are looking for now is more subtle indications of deposits that are not exposed at the surface.
>
> MR. GROIA: So when you are doing work as a consultant now, Mr. Leach, how much of your time do you spend looking at field prospects that are without surface expression?

MR. LEACH: Most of the work that I do is in that way. A lot of the work that I do is to look at known deposits and then see what the signatures are around them, about them on the side, so I can get some indication of even though there may not be significant surface geochemistry there is indications that there is an ore body depth even though there may not be a surface expression.

...

MR. GROIA: And do you consider the Southeast Zone at Busang to be a blind area?

MR. LEACH: Yeah, it's blind in that there is no surface expression, although you would expect there to be mineralization at depth.

...

MR. GROIA: And is there any comparison between the Southeast Zone at Busang and any of the zones at Kelian, in your opinion?

MR. LEACH: The Northeast Zone with its very high content of manganese carbonate is very very similar to what we saw in the Southeast Zone and there is a very low amount of sulphides associated with it. So I mean what I would do is – I mean there is a good comparison between the Northeast Zone at Kelian and the Southeast Zone at Busang.

MR. GROIA: And do you have any idea of how much gold was mined in the Northeast Zone at Kelian?

MR. LEACH: That extended the resource by 50%, so there was about another geological resource of 5 million ounces. It doubled the resource by doing that.

Transcript: December 12, 2005, pages 133-142

Literature And Other Gold Deposits

On page 13 of Exhibit 681 Strathcona states:

> Confronted with this recorded evidence of lack of gold in the Southeast Zone at surface by Strathcona, John Felderhof stated that the gold had been leached out of the surface layer, which, from his experience was not unusual for gold deposits in this area. The literature on gold deposits from Indonesia confirms quite to the contrary (van Leeuwen, 1994), that gold is not removed from the surface layer

during weathering, but remains there, and might even become enriched near surface (supergene enrichment as explained previously on page 8).

Dr. Hellman and Leach reviewed the van Leeuwen paper to which Strathcona referred and their evidence was that contrary to what Strathcona states in Exhibit 681 the van Leeuwen paper refers to surface gold depletion at the Mirah deposit.

Exhibit 1202: pages 101-103
Exhibit 1328 B: page 55

That is significant because Felderhof was relying on his experience in Mirah to support his theory of surface depletion.

At paragraphs 103-109 Exhibit 1202 Dr. Hellman lists other deposits with surface depletion. As does Leach at paragraphs 55-58 of Exhibit 1328B. Both Dr. Hellman and Leach refer to OK Tedi. Felderhof was co-discoverer of OK Tedi.

In his opinion Exhibit 1202 Dr. Hellman cites a paper reminding mineral explorers of prospects "*where Au [gold] at the surface is strongly leached and no longer reflects the Au at depth.*"

Exhibit 1202: pages 109-110

Farquharson could not agree or disagree that there are other gold deposits in Indonesia with limited or no surface expression because Strathcona did not look at other deposits in Indonesia other than what they read about Kelian.

Transcript: March 31, 2005, page 74

Barrick

When Dr. Kavanagh and Larry Kornze visited Busang in 1993 on behalf of Barrick, they took some surface or near surface samples and obtained "*low, not blank, but low*" results. Felderhof had cautioned Dr. Kavanagh that the grade would be less than in the original rock because of depletion. Dr. Kavanagh accepted depletion as a reasonable geological or weathering theory. Barrick continued to be interested in Busang. Dr. Kavanagh's evaluation of Busang was based on the appearance of the outcrops, his personal observations, the prior drilling work and Felderhof's explanation of depletion at Busang.

Transcript: March 8, 2005, pages 97-99
Exhibit S5 Volume II: paragraphs 483-485

STRATHCONA ALLEGES THE BRE-X DRILL HOLE RESULTS SHOWED GOLD RIGHT THROUGH THE OXIDE ZONE TO SURFACE

The O.S.C. submits that "*[s]urface depletion of gold would have been highly inconsistent with the fact that good gold values started at the top of many Bre-X holes.*"

Exhibit S5 Volume II: paragraph 430

Dr. Hellman

Dr. Hellman's opinion does not agree with this submission. At page 101 of Exhibit 1202

Dr. Hellman states:

> It is true there are examples of elevated surface gold values in the drill holes of the South East Zone. These appear to occur close to the largely negative surface channel samples only in a minority (less than 5%) of cases. These discrepancies, however, become less obvious when the topographic differences between the surface trenches (close to surface) and drill hole collars (may be up to 5-10 metres below surface) are taken into account.

And at page 119:

> My analysis in 2000 indicated that there are 1195 drill hole intervals (two metre composites) between 0 and 10 metres from the surface trench data south of 3500N (the heart of the South East Zone). These represent 239 drill holes. Of these, 132 or 55% have no assay from the interval 0 to 2 metres. The interval from 0 to 2 metres, as explained above, does not correspond to the surface of the ground because of the need to cut a drill pad into the sloping ground in order to have a horizontal platform from which to drill.
>
> Of the remaining 107 holes (ie. 45%), 29 holes have assays from the top two metres that are less than 0.1 g/t. Another 26 holes have surface grades between 0.1 and 1.0 g/t. Thus, a total of 78% of the holes in the main part of the South East Zone have either no assays or assays less than 1 g/t. 71% of the surface intervals have either no assays or assays less than 0.5 g/t.

And at pages 120-121:

> This detailed study reveals that some higher grades in the drill samples are in close proximity to the surface samples with lower grades. The number of these locations, however, only constitutes 1.1% of the locations for 0 to 10 metres and 4.4% of the locations if 0 to 20 metre distances are used. Such an exercise assumes that the surface locations have been accurately surveyed. It takes no account of the fact that many of the surface samples would have been taken from nearer the surface than the drill samples from the 0 to 2 metre intervals.

Leach

At pages 73-74 of Exhibit 1328B at iii) Leach states:

> **iii)** ***Gold grades at the top of the Bre-X drill holes, which were twinned by Strathcona, are consistent with surface geochemical data***
>
> ...
>
> c) **Section Line 49** (TL 178)
>
> Strathcona hole BSSE 63S was drilled on section line SEZ 49 to twin the Bre-X hole 63. This hole was drilled within a very large zone (650m wide) of intense argillic alteration and correlates with an area of significant gold assays from the surface material.
>
> A 2.08 g/t outcrop sampled (J15) was collected by Westralian (1989) from a stream that drains the area of BSSE 63. In addition, five trenches were sampled between holes BSSE 61 and BSSE 64, and the maximum in all trenches returned anomalous gold grades (up to 3.7 g/t Au, and the maximum average was 0.79 g/t Au).
>
> The top 8 meters of holes BSSE 61, BSSE 62, BSSE 63 and BSSE 64 returned average grades of 1.89 g/t Au, 0.78 g/t Au, 1.04 g/t Au and 0.88 g/t Au. The average grade over the top 8 meters of these drill holes is 1.15 g/t which correlates well with the average of the maximum value in the trenches at the surface. Good grades up to 3.70 g/t Au were collected from a trench immediately adjacent to the hole BSSE 61, in which ore grades (up to 2.5 g/t Au) extended to the top of the hole.
>
> The press release by Bre-X, which was quote by Strathcona (1997) [37], stated that:
>
> > "*Bre-X reported in a news release of Oct 17, 1995, that holes 61 and 64, drilled 150 meters apart on line SEZ 49, firmly indicate by themselves a 240 meter open-pittable thickness of +4 g/t starting literally at the surface.*"
>
> This statement is valid, especially since the cut-off grade that was
>
> proposed for the mine was 0.47 g/t Au.

At paragraphs 438-462 of Exhibit S5 Volume II, the O.S.C. is critical of Leach's opinion set out at above with respect to his conclusions about Strathcona's hole BSSE 63S which twinned Bre-X hole 63 and about holes BSSE-61 and 62 and 64 and the five trench samples between holes 61 and 64.

The O.S.C.'s criticism includes: that Leach referred to 3.70 g/t Au when sample number RDK 01415 had three assay results of 3.70, 0.57 and 1.34 which averaged 1.87 g/t gold and the average of all samples taken in trench 2A n37 was 0.21 g/t gold and the averages of the other four trenches were 0.05 g/t gold, 0.03, 0.02, and 0.02; that Leach referred to "*the maximum average [of] 0.79 g/t gold*" which was calculated by taking the maximum value from each of the trenches and averaging them; that if 1.87 from RDK 01415 above was used rather than 3.70 the "*maximum average*" would be 0.54 g/t.

Leach's explanations given in cross-examination should have been set out more clearly in his opinion Exhibit 1328A and Exhibit 1328B.

It is not clear on the evidence why maximum values were used by Leach.

In evidence, Leach conceded "*that the average grade over the top 8 meters of the drill holes, ...1.15 grams per ton, does not correlate well with the average of the value in the trenches at surface.*"

Transcript: December 14, 2005, pages 99-100

Leach was "*not sure*" why trenches were dug and samples assayed after drilling had already begun in the area.

Transcript: December 14, 2005, pages 102-103
Exhibit S5 Volume II: Paragraphs 463-466

Leach did not agree with Strathcona that surface depletion in the Southeast Zone was highly inconsistent with good gold values starting at the top of Bre-X holes. Leach found that *"[m]ost of the drill holes along the same section as the drill holes quoted by Strathcona do in fact show depletion of gold at the top of the drill holes."*

Exhibit 1328A: page 47

Contrary to Strathcona's allegations, Leach concluded that *"plots of gold assays and depth of drill holes in the South East Zone show that gold is significantly depleted in the top 10 meters, whereas this is not the case in the drill holes from the Central Zone."*

Exhibit 1328B: page 71

Exhibit 717 –Map Section SEZ 66.5

With respect to at least one section, Section Southeast Zone –66.5, Exhibit 717, Farquharson conceded that only 2 out of 13 holes supported his theory that the Bre-X drill hole results showed gold through to surface.

Transcript: March 21, 2005, page 76

Further in preparing this section line for SEZ-66.5, Strathcona left off three holes (211, 212 and 213). When asked why, Farquharson answered *"I don't have a good answer for you."*

Transcript: March 21, 2005, pages 67-69

Strathcona Analysis of Surface Depletion –Scattergraph Exhibit 747

Strathcona did their own analysis in response to a paper by Dr. Hellman that indicated that there appeared to be a pattern developed by those involved in the tampering to create the impression of surface depletion.

Farquharson testified that the pattern was that in 2/3 of the drill holes there is a lower grade in the oxide zone than there is in the fresh rock; that is, 2/3 of the data conforms to the depletion theory. Farquharson testified this was not statistically significant. It is not clear what number is "*statistically significant*". Farquharson's evidence was not specific: "*Some very high number. Whether it's 80%, or 90%*" But in Farquharson's opinion 2/3 was not sufficient to assist the Defence.

Farquharson's "*statistically significant*" number appeared to be more of a subjective than a statistically objective number.

Transcript: March 29, 2005, pages 2-20

Drill Hole Collars

Dr. Hellman

In paragraphs 435-436 of Exhibit S5 Volume II, the O.S.C. submits:

> Para. 435. On cross-examination, Hellman was shown the assay results for the intervals starting at zero for holes BSSE-60, BSSE-61, BSSE-75, BSSE-86 and BSSE-90. He agreed that there was some gold that came to surface in these holes.
>
> Para. 436. He stated that those holes were not necessarily at surface but admitted under cross-examination that he had only visited one drill pad that was cut below surface.

Dr. Hellman's testimony was as follows:

MR. HELLMAN: Yes. They're at – not necessarily at surface, Mr. Cole, but they're at the start of the drill hole.

Transcript: November 14, 2005, page 39

And Dr. Hellman testified:

MR. GROIA: Can I just ask you one question about the first part, the digital database information? Can you tell us whether or not that information allows you to tell how far below the contour of the surface the drill collar would be located?

MR. HELLMAN: No, not at all. The actual elevation, of course, is the elevation of the drill rig, that is the point at which the drill enters the ground. And of course you can imagine in hilly terrain, or even boggy terrain, you have to cut in to establish a level surface, because drill rigs can't drill on incline surfaces, so you can imagine the side of a hill, and you have to put a sizable cut into the side of the hill to establish a firm base for your drilling. So typically, a drill hole collar, or a drill hole pad as it's sometimes called, can be up to five to 10 metres below the actual natural surface of the ground. And the depth below the actual natural surface, in my experience, is rarely recorded by companies, so it's often quite unknown as to how far below the natural surface one's dealing with.

...

MR. GROIA: Thank you. And while you were at the Busang property, did you go and visit any drill holes?

MR. HELLMAN: Yes. I visited one location that was currently drilling at the time I was there, and that was as I described it, it was on a steep side of a hill and it was cut at some depth below the surface.

Transcript: November 3, 2005, page 16

Dr. Hellman discusses cutting level drill pads into the ground at pages 110-113 of Exhibit 1202.

Farquharson

Farquharson agreed that drill hole collars could be 8 meters below surface. Farquharson agreed he did not consider the impact of the collar location on his evidence.

Farquharson agreed that when Strathcona said the hole twinned at 202S showed gold at zero mark that meant showing gold at perhaps eight meters below the surface.

In cross-examination Farquharson testified that when he said in chief that "*the drill hole results showed gold right through to the surface*" that meant right through to the collar of the hole and not the original surface of the land. Farquharson also testified "*when we use the terminology drill results through to surface it is understood in the mining industry that you mean to the top of the drill holes, where you start to take your samples.*"

The explanation of the use of terminology though does not resolve issues raised with respect to Strathcona's opinion.

Strathcona's opinion is that the theory of surface depletion of gold is not valid because assay results show that there was gold at surface, for example, gold values from 0 to 1.0 meters, Strathcona's opinion is substantially weakened if the assay results relied upon for the opinion were in fact with respect to gold found 8 meters below the surface and not at surface where by definition surface depletion would occur.

Transcript: March 22, 2005, pages 32-34
Exhibit 1202: pages 47, 111-112

STRATHCONA ALLEGES THAT BASED ON STRATHCONA'S REVIEW OF ALL THE ASSAY VALUES FROM THE DRILL HOLES THERE WAS NO EVIDENCE OF ANY SUPERGENE CONCENTRATION OF GOLD IN THE OXIDE ZONE

O.S.C. Position

The O.S.C. states at paragraphs 475, 476, 480 and 489 of Exhibit S5 Volume II:

> Para. 475. Supergene enrichment occurs where gold has been leached and put into solution at the top of a deposit and there is a corresponding increased concentration of gold lower down in the deposit.
>
> Para. 476. Felderhof told Farquharson that in his view the gold from the surface had been leached. Farquharson testified if the gold had been leached and put into solution from the top of this deposit, there should be a corresponding increased concentration lower down in the deposit. If the gold had been depleted, there would not be any gold values in the drill holes as reported by Bre-X. In addition, there was no supergene concentration of gold in the oxide zone.
>
> ...
>
> Para. 480. Farquharson opined that gold became enriched over these occurrences during weathering and was not depleted as indicated by Felderhof.
>
> Para. 489. The Defence experts were also unable to answer that puzzling question even though they were asked on several occasions, in-chief, on cross-examination and by this Court.

In paragraphs 490-496, Exhibit S5 Volume II, the O.S.C. submits that Leach gave several examples of depletion in Southwest Pacific gold deposits but did not include references to corresponding zones of enrichment.

Those examples are found at pages 51-58 of Exhibit 1328B. There are in fact some references to enrichment but also this discussion in Leach's opinion is in rebuttal to Strathcona's opinion that gold is not depleted at surface and might even become enriched near surface and not a discussion about a zone of enrichment per se.

Defence Position

The Defence theory of depletion and enrichment is different than what Strathcona was commenting on and expecting to find but did not.

Dr. Hellman's evidence is found at pages 77-78 of the November 3, 2005 transcript:

THE COURT: If the gold gets leeched, does it go someplace? Did I hear evidence earlier in the trial that there would be some sort of a – I think it was referred to as a supergene zone or –

MR. GROIA: Doctor Hellman, could you comment on that?

MR. HELLMAN: Yes, I had, Your Honour, discussions with Mr. Felderhof about that, and his view was that the surface depletion in the Southeast zone had manifested itself basically in the mineralization in the Southeast Zone. So he saw the Southeast Zone mineralization as basically imprinted by gold that had been removed from the surface; so he saw the Southeast Zone mineralization as basically a combination of primary in-situ mineralization, with an imprint of supergene mineralization that had developed by leeching.

MR. GROIA: And are you able to comment on the reasonableness of that view?

MR. HELLMAN: I think in general it's a reasonable view. As I found when I did the very detailed work of actually doing a computer analysis of which high-grade samples from drill holes might be near other surface samples, in detail it would break down, but in general it would be found.

THE COURT: My impression was that when you got the leeching, you got a supergene zone that would sort of be concentrated. You have an area that gets leeched and then you get a layer of a lot of gold.

MR. HELLMAN: Like sort of a mushroom type thing.

THE COURT: Yes.

MR. HELLMAN: Yes. Yes. There was no evidence for that. Mr. Felderhof's view was that there was a large upper portion of the Southeast Zone had been affected by the downward percolation of the gold.

The Defence theory was not that there would be depletion and a supergene zone or layer, which as Strathcona states does not exist, but percolation of gold throughout the deposit evidence of which Dr. Hellman states does exist.

STRATHCONA ALLEGES THE ABSENCE OF GOLD IN THE STREAMS AND RIVERS DRAINING THE SOUTHEAST ZONE INDICATED THERE WAS VERY LITTLE GOLD THERE

Farquharson

Strathcona's detailed position is found at pages 11-12 of Exhibit 681.

The O.S.C. states in paragraph 319 of Exhibit S5 Volume II:

> Farquharson testified that there was virtually no gold in the streams and rivers draining the SEZ. This indicated that the rock eroded by those streams contained very little gold. Farquharson opined that this was a very definite and strong red flag that a competent geologist with Felderhof's experience acting reasonably would have appreciated.

The Defence agrees this was Farquharson's evidence but submits the evidence has no factual basis.

This alleged red flag of absence of gold in Southeast Zone streams is found in Farquharson's evidence and Exhibits 208 and 681 but it is not specifically referred to in the October 1997 letter listing the 20 Red Flags, as would be expected of a very definite and strong red flag.

This factor is a strong red flag for Farquharson based on hearsay evidence of lack of local alluvial mining activity.

Transcript: March 17, 2005, page 23

Farquharson testified his conclusions were based upon the Levings and Ogierman Report (1989), photographs by de Guzman (1992) and statements by Freeport and Corbett and Leach. The Leving's Report and de Guzman photographs demonstrate alluvial mining in the Central Zone and not that there was no alluvial mining in Southeast Zone.

Exhibit 681: page 12

The evidence of Dr. Hellman was that he concluded that there was in fact a reference in the Leving's Report to samples from the streams draining the Southeast Zone with anomalous gold values.

Exhibit 1202: pages 257-258

Farquharson relied on statements by Freeport and Corbett and Leach that they did not observe any artisinal mining in the Southeast Zone. Farquharson does not recall asking Freeport what, if any, investigations they had done.

Strathcona did not conduct an independent investigation into artisinal mining either in the Southeast Zone or Central Zone. They did not have discussions with on-site geologists at Busang nor make their own observations of streams draining the Southeast Zone.

Transcript: March 22, 2005, pages 54-56

Farquharson testified it is not ordinarily Strathcona's professional practice to draw conclusions based on hearsay statements.

Transcript: March 22, 2005, pages 55-56

Farquharson prepared a map to illustrate "*the principle directions of the drainage pattern*" in Busang but he agreed "*there is a great deal of the drainage pattern for the Central and Southeast Zone that is not on [the] map.*"

Transcript: March 21, 2005, pages 29-30.

Strathcona could not reconcile why in their opinion there was no artisinal mining in the Luun Besar River given anomalous gold results in the Yati Creek area.

Transcript: March 22, 2005, page 54

Dr. Hellman

Dr. Hellman's evidence is the opposite and states that there was hearsay evidence of local alluvial mining and that the absence of gold in streams does not necessarily indicate the absence of gold in a deposit.

Exhibit 1202: pages 257-259

Dr. Hellman spoke to Mr. Imperial, a geologist at Busang, who showed him gold grains that he had panned from streams in the Southeast Zone. Dr. Hellman had some samples of that gold fingerprinted which matched the gold from the Southeast Zone bought from the warung.

Exhibit 1202: pages 36-37
Transcript: November 3, 2005, page 9
Transcript: November 11, 2005, pages 56-57

Dr. Hellman spoke to the owner of the warung who told him that gold was panned from streams draining the Central Zone and the Southeast Zone.

Dr. Hellman purchased two types of gold from the warung that came from the Central Zone (white gold) and the Southeast Zone (red gold).

The owner helped Dr. Hellman draw a sketch map of streams where gold was found. Dr. Hellman's evidence was that this sketch map included streams draining the Southeast Zone and was consistent with maps he later inspected .

Exhibit 1202: pages 14, 17, 36-39, 258
Transcript: November 3, 2005, pages 60-63

Leach

Leach's expert report included references to alluvial mining in streams draining the Southeast Zone.

Exhibit 1328A: page 72
Exhibit 1328B: pages 130-131

Kelian

In paragraph 329 of Exhibit S5 Volume II, the O.S.C. notes the Defence position that Felderhof believed that Busang was analogous to Kelian and the Defence agrees that Felderhof believed that Busang shared many similarities with Kelian. The Defence also agrees with the O.S.C. submission at paragraph 335 that Dr. Hellman's opinion was that Kelian was analogous in several ways including "*the presence of local alluvial mining*" though the Defence points out the evidence of Dr. Hellman was that at Kelian the local mining was downstream from the deposit.

Exhibit S5 Volume II: paragraphs 335, 340

The O.S.C. submits though that the alluvial mining was different at Kelian than at Busang relying on the Theo M. Van Leeuwen article describing the large scale of alluvial mining at Kelian. Though at paragraph 336 the O.S.C. also agrees that Dr. Hellman testified that with every deposit there is no area where everything is exactly the same.

The Defence concedes the larger scale of alluvial mining at Kelian but relies on the comparisons made by Dr. Hellman above and by Leach at Exhibit 1328B, paragraphs 130-131.

Exhibit S5 Volume II: paragraph 341
Transcript: November 9, 2005, page 33

Finding

Although Dr. Hellman also relied on hearsay, as did Farquharson, given that Dr. Hellman did more investigation into artisinal mining activities in the Southeast Zone than Strathcona and given his experience in Pacific Rim tropical geological settings and tropical environments, I prefer his evidence to that of Strathcona.

STRATHCONA ALLEGES THE CENTRAL ZONE AND SOUTHEAST ZONE ARE SITUATED ON A HILL THAT IS SUBJECT TO STRONG EROSION WHICH WOULD HAVE COUNTERACTED THE LEACHING OF METALS FROM SURFACE MATERIAL

At paragraphs 423 to 428 the O.S.C. submits and the Defence comments as follows:

> Para. 423. Strathcona opined that the CZ and SEZ are situated on a hill that is subject to strong erosion. This rapid erosion is evidenced by the shallow layer of oxidation in the Bre-X drill holes. Strathcona opined that this rapid erosion would have counteracted leaching of metals from surface materials. Therefore, Felderhof's leaching theory does not make sense.
>
> > The Central and Southeast Zones are situated on a hill which rises above the lower land surrounding it and is subject to strong erosion under the prevailing climatic conditions. Rapid erosion is documented by the rather shallow layer of the only several metres of oxidized rock intersected in drill holes in Busang. This rapid erosion would have counteracted the leaching of metals from surface materials – which requires time – and is therefore inconsistent with any suggestion of leaching of gold near surface in the Southeast Zone.
>
> **The Defence agrees that this was Mr. Farquharson's opinion.**
>
> Para. 424. Leach's report attempts to contradict Strathcona's evidence that the CZ and SEZ are situated on a hill that would be subject to rapid erosion. However, a closer look at the cross-section that Leach relied on shows that it actually supports Strathcona's conclusion.

i) *Topographic differences between the Central and South East Zones*

Contrary to the statement by Strathcona (2000) [37], the Central and South East Zones are not situated on a (single) hill. Rather, the Central Zone is located within a series of prominent hills that are located on the northern portion of the Busang I project area (TL 202). The northernmost hill of the Central Zone is a recent basalt plug, and the South East Zone is located in an area of lower undulating relief in the southern portion of the project area.
The difference in topography is illustrated in a NW-SW cross section through the Busang Project area (TL 203). It is obvious that the two Zones have different topographies. The Central Zone is located on a hill that has steep topography and is significantly less eroded than the lower lying terrain in the South East Zone. This indicates that the rates of erosion in the two zones were significantly different, which contradicts the inference made by Strathcona that the erosion rates were the same.

The Defence agrees that this is an accurate quote from Mr. Leach's Report.

Para. 425. During cross-examination it was clearly shown that Leach's cross-section referred to in the passage above is misleading. Leach admitted that he deliberately exaggerated the height of the hill in the CZ by using a different scale for the horizontal axis of his cross-section than the scale he used for the vertical axis. The ratio of the horizontal scale to the vertical scale is 4:1.

The Defence disagrees. There is absolutely no evidence to support the suggestion by the OSC that Mr. Leach "deliberately exaggerated" the height of the hill in the CZ.

By attacking, in an unfair fashion, Mr. Leach's evidence with respect to the topography of the CZ, the OSC is attempting to deflect attention from the fact that Strathcona completely misapprehended the topography of the Busang area. The basis of Strathcona's opinion is that there was one hill upon which both the CZ and SEZ were located. Therefore, Strathcona's opinion that the two zones at Busang would be subject to the same erosion rates as they shared a common topography. This is completely erroneous and based upon a completely incorrect understanding of the very basic facts.

Further, the suggestion that Mr. Leach in some fashion was attempting to mislead this Court with respect to the topography of the Busang area is unfair. The scale is clearly shown on his topographic representation of the CZ and SEZ. The use of vertical exaggeration in topographic depictions is an industry accepted technique. As Mr. Leach testified "[I]t's quite common to have vertical and horizontal scales

[that are not equal]" (Evidence of Mr. Leach, December 14, 2005, Vol. 150, page 111) If a vertical exaggeration is not used, the result would itself be misleading. For example, a topographic map of Canada not using a vertical exaggeration, would render a depiction of Canada as having an almost flat and homogenous topography. The Rockies and the Prairies would be virtually indistinct.

Para. 426. As a result, Leach's cross-section showing the topography of the CZ and SEZ is extremely exaggerated. By exaggerating the scale, Leach made it appear that there was one hill in the CZ that was much higher than a second hill in the SEZ. If the vertical exaggeration is removed by using the same horizontal scale and vertical scale, it is evident that there is one hill over the CZ and SEZ with about the same height and topographical relief consistent with Strathcona's view.

The Defence disagrees and notes that this is even contradicted by Strathcona's own evidence. Exhibit 1236, mostly consisting of material prepared by Strathcona, put to Dr. Hellman in cross-examination (Evidence of Dr. Hellman, November 11, 2005, Vol. 139, page 71) shows the Central Zone to be on a hill at an elevation of 270 metres (886 feet). Exhibit 717 prepared by Strathcona is a cross-section of the Southeast Zone ("SEZ-66.5"). This section shows the average elevation to be at approximately 160 metres (525 feet). This is a difference of 110 metres (361 feet). This is completely consistent with Mr. Leach's Expert Report. (See Exhibit 1328A, Mr. Leach's Report, Vol. 1, page 46). Such a difference in height cannot be reconciled with the stated view of Strathcona.

Para. 427. When shown the same cross-section with no vertical exaggeration, Leach responded, "well I am not saying that the vertical scale is the same as the horizontal scale".

The Defence agrees that this was Mr. Leach's evidence.

Para. 428. Leach conceded that these hills look very different when you remove the vertical exaggeration.

> Q. ...you will agree with me that these hills look very different when you remove the vertical exaggeration...
>
> A. Well of course they do because they are different scales.

The Defence agrees that the quote is accurate.

Exhibit S5 Volume II: paragraphs 423-428

It would have been preferable if Leach had specifically pointed out on the diagram itself (Exhibit 1363) or in the body of his report that the horizontal and vertical scales are not equal or if he had also provided a second diagram, as the O.S.C. did (Exhibit 1397) showing equal horizontal and vertical scales for purposes of comparison.

But the horizontal and vertical scales are set out on Leach's diagram and they are quite obviously different. And more importantly both diagrams (Exhibit 1363 and Exhibit 1397) show that the Central Zone and Southeast Zone are not situated on a single hill as stated by Farquharson and both show that the Central Zone hill is taller (as both diagrams have the same vertical scale) and that the Central Zone hill is steeper.

Exhibit 1363: (Also found at Exhibit S11 Tab 7)
Exhibit 1397: (Also found at Exhibit S11 Tab 8)

Leach's detailed opinion contrasting the Central Zone and the Southeast Zone is found at pages 68-70 of Exhibit 1328B. At pages 68-69 Leach states:

i) In their map of the geology of the Busang project area, Strathcona (2000) [37] failed to include the presence of maar sediments that immediately overlie mineralization in the Central Zone. These sediments are relatively resistive to erosion and could therefore, inhibit weathering of metals from the underlying dacite. On the other hand, the South East Zone was not protected from erosion by these sediments.

ii) The Central and South East Zones are not situated on a (single) hill as implied by Strathcona (2000) [37]. The topography of the Central and South East Zones is different, which reflects different rates of erosion, and not the same 'rapid' rates as alleged by Strathcona.

iii) The dacite in the Central Zone has undergone intense quartz-sericite-pyrite alteration which is moderately resistive to erosion, whereas the same quartz-sericite-pyrite alteration in the South East Zone has been overprinted by widespread, intense clay alteration that renders the rock prone to extensive erosion.

iv) The carbonate in the veins in the South East Zone is prone to rapid dissolution removal of gold, whereas in the Central Zone, the gold occurs in sulphide minerals, which are more resistive to weathering.

v) Leaching of gold from the surface material is documented in deposits, which would have similar, if not more rapid, rates of erosion than at Busang.

Farquharson testified he would defer to Leach and Corbett's knowledge and experience in their description of a deposit of the type such as Busang. Farquharson agreed Leach described two distinctive styles of mineralization in the Central Zone and Southeast Zone.

Transcript: April 4, 2005, pages 11, 15

Leach concluded at page 70 of Exhibit 1328B:

> The leaching of metals in an environment of rapid erosion would, therefore, have been expected in the South East Zone at Busang and was not a 'red flag' as alleged by Strathcona.

STRATHCONA ALLEGES THAT GOLD WAS NOT MOBILIZED BY HUMIC ACID

Felderhof

In paragraphs 512-517 of Exhibit S5 Volume II the O.S.C. makes the following submissions and the Defence the following comments:

> Para. 512. Felderhof believed that the gold had been depleted at surface in the SEZ. One of the Defence theories appears to be that depletion may have been caused by gold being mobilized by humic acid and transported away.
>
> **The Defence agrees.**
>
> Para. 513. Leach opined that it was reasonable for Felderhof to believe that the gold in the SEZ was removed from the surface by organic acids.
>
> **The Defence agrees.**
>
> Para. 514. The Defence has not proven the underlying fact to Leach's opinion. There is no direct evidence that Felderhof believed this explanation for the absence of gold at surface in the SEZ. Felderhof does not mention the phrase "humic acid" in any of his correspondence or in his papers.

The Defence disagrees. While we have not reviewed all of Mr. Felderhof's correspondence and papers as the OSC seems to suggest it has done, it is clear that Mr. Felderhof held the belief that the surface gold had been depleted by reason of a mechanism such as humic acid. In paragraphs 483 and 484 of this Submission, the OSC refers to a discussion that Dr. Kavanagh had with Mr. Felderhof in 1993 when Dr. Kavanagh worked for Barrick, where Mr. Felderhof explained the low sample results were due to depletion in a rainforest environment.

"Q. And without wanting to go through each and every sample, can you provide the Court with a general conclusion or observation about the results of all those samples?
A. They were low, not blank, but low.
Q. But nevertheless, you continued to have an interest in the property?
A. Yes.
Q. Why was that?
A. Are you talking about the four from Busang?
Q. Yes.
A. Because John Felderhof had mentioned that different from what occurs in the arid countries of Central America and western South America, where there's what we call residual enrichment of the gold, in a rainforest there's an opposite effect that the heavy rains will take gold away from its original source. And these samples were low and they were, in my opinion, at least part of the lowness was a result of that phenomenon." (Evidence of Dr. Kavanagh, March 8, 2005, Vol. 78, pages 97-98)

As discussed previously, in that same passage of his evidence, Dr, Kavanagh agreed that he believed that is was a "reasonable geological theory", "a reasonable weathering theory".

In Freeport's Site Visit report (Exhibit 755), in the paragraph previously quoted, they report that they were advised of the humic acid theory by Mr. de Guzman.

In paragraph 476 of this Submission, the OSC repeats Mr. Farquarhson's testimony that Mr. Felderhof told him that the gold from the surface had been leached and put into solution "and carried away" from the top of the deposit. (Evidence of Mr. Farquarhson, March 17, 2005, Vol. 84, pages 25-26).

It is clear that, while perhaps the words "humic acid" were not used in correspondence or on paper, Mr. Felderhof held the view that the surface gold had been leached in a rainforest setting such as Busang by the mechanism described by Mr. Leach in his Report.

Para. 515. There is no direct evidence that Felderhof held any belief, reasonable or otherwise, about the cause of the surface depletion in the SEZ.

The Defence disagrees.

Para. 516. Kavanagh testified that Felderhof told him that Felderhof believed that the gold was depleted at surface. There is no evidence, however, that Felderhof

told Kavanagh or any one else that he believed that gold had been depleted through humic acid.

> Q. Did you understand there to be any suggestion that in the Southeast Zone there had been gold depletion at surface, and that the gold had been carried through humic acids, or other processes, further down into the deposit?
>
> A No.

The Defence agrees that this is an accurate quote from this section of Dr. Kavanagh's evidence.

Para. 517. The Defence cannot rely on what the Defence expert team including Hellman and Leach testified that Felderhof told them, as proof of the truth of what Felderhof said. Such evidence runs afoul of the rule against hearsay.

The Defence disagrees that this is always the case in law.

Exhibit S5 Volume II: paragraphs 512-517

In addition to the indirect evidence set out by the Defence above, Leach also points out in Exhibit 1328B, pages 55-57, Felderhof's connections to and familiarity with OK Tedi and Ampalit gold deposits and the interpretations of those deposits that the gold was dissolved or depleted by humic acid.

In paragraph 512 above the O.S.C. concedes that "*Felderhof believed that the gold had been depleted at surface in the Southeast Zone*" but then in paragraph 515 the O.S.C. states "*[t]here is no direct evidence that Felderhof held any belief, reasonable or otherwise, about the cause of surface depletion in the Southeast Zone*".

Leach

The O.S.C. points out that Leach had never encountered gold mobilization due to humic acid in the field and refers to Exhibit 1328B page 20 and Leach's cross-examination.

Exhibit S5 Volume II: paragraph 522

On page 20 of Exhibit 1328B Leach states:

> Felderhof explained that the weathered bedrock graded <0.1 –0.3 g/t Au, 1-4 g/t Ag and <500 Zn + Pb. He explained to us that he interpreted the surface depletion of gold as being due to the mobilization by humic acid. Neither Corbett nor myself had encountered this in the field. Corbett asked me if it sounded reasonably geochemical. I thought that such a process could be possible since organic complexes are one of the ways to mobilise gold. I put this explanation 'on the shelf' until later, but did not see it as being of any concern.

In cross-examination Leach testified at page 6, December 15, 2005:

> MR. LEACH: No, there is none of those that I would have encountered the possibility of depletion by gold through humic acid.
>
> MS. COLE: So you still have no direct experience of gold depletion by humic acid?
>
> MR. LEACH: That's right.

With respect to page 20 of Exhibit 1328 B, Leach testified also on page 6:

> MS. COLE: And you also say at page 20, you said although this process was outside of our experience at that time it sounded it [sic] reasonable. And does it continue to be outside of your experience to today?
>
> MR. LEACH: Well, no, because as I said, it was outside my experience and, therefore, I did some research into it and found out that, in fact, there had been other areas where that had occurred. But that had been outside my experience at that time.

At pages 55-57 of Exhibit 1328B Leach discusses his research into Ampalit and Ok Tedi and the mobilization there of gold by humic acid.

Finding

I find there is indirect evidence, as noted above, that Felderhof believed the cause of surface depletion in the Southeast Zone was humic acid.

STRATHCONA ALLEGES THERE WAS NO GOLD AT THE SURFACE BUT THERE WERE BASE METALS PRESENT WHICH SHOULD HAVE BEEN LEACHED FIRST

Farquharson

Strathcona's opinion Exhibit 681 states at page 2:

> • The presence of base metals in surface samples over the Southeast Zone and the lack of gold in those samples disproves any claim that gold had been leached or depleted at surface, as gold, if present and being the most noble of all metals, would be the last to be leached or put into solution and transported elsewhere.

And at page 13:

> The weathered layer of such a deposit may contain lead, zinc, copper, silver, arsenic and other metals besides gold. Different from base metals, which mostly occur as sulfides and are mobile during weathering, gold in its native form, or as a gold-silver alloy, is chemically inert and cannot be easily leached. The presence of base metals in soil or weathered bedrock in the absence of gold, is a strong indication that gold is not present in the unweathered rock.

Kelian

In Exhibit 681, page 14, Strathcona's opinion states that "*the Kelian deposit had very pronounced gold anomalies at surface..., with roughly coinciding silver and lead anomalies.*"

But in cross-examination Farquharson testified he had no reason to disagree with Van Leeuwen (Exhibit 688, dated 1990) that at Kelian "*there was no consistent correlation between gold values and other base metals such as copper, lead, and zinc and arsenic.*"

Transcript: April 4, 2005, pages 28-29

Dr. Hellman

Dr. Hellman's opinion that this allegation is not a red flag is found at pages 252-256 of Exhibit 1202 where Dr. Hellman states:

> ***Summary of Allegation***
>
> Strathcona alleges (2000, p.8, para 2) that:
>
> > "gold is not dissolved in an oxidizing environment due to its chemical inertness and thus its designation as the most noble of all metals. Gold is mainly moved mechanically as particulate gold."
>
> ***Summary of Opinion***
>
> The ability of gold to dissolve in oxidizing environments is well known and has been documented in numerous studies dating back to early last century. The statement made above by Strathcona concerning the insolubility of gold runs counter to the extensive published literature on gold and conflicts with the prevailing experience of the exploration community.
>
> There has been considerable industry-based and academic research into the way gold dissolves in the oxidizing environment and concerning the mobility of gold. The results of this research are frequently published in accessible and reputable journals (e.g. Journal of Geochemical Exploration, papers from which are cited by Strathcona). [37]
>
> In my view, Strathcona's allegations are implausible and reflect a profoundly limited experience with gold exploration. Their views conflict with the clearly expressed views of the authors in references that they cite.

Leach

Leach's opinion that this is not a red flag is found at page 43 of Exhibit 1328A and pages 44-51 of Exhibit 1328B.

FINDINGS

Dr. Hellman in his report stated that "*once drill results have been received, all other data assume less importance*" and that the "*[t]he drill hole results are the final test of the many (often contradictory) exploration surface results*" (Exhibit 1202, pages 126-127). Farquharson agreed that "*normally speaking drill results trump geochemical puzzles.*" This has some application to Red Flags 1 and 2.

The property was prospective. There was tens of thousands of meters of drilling done over several years. The results lined up on the Data Mine model. The results were consistent and plausible. The results matched the core that looked mineralized or unmineralized. The tampering was unprecedented.

There were other gold properties with no surface anomaly. There were other gold properties with surface depletion. There was the general comparison to Kelian. There was gold at surface in the Southeast Zone.

Not one of the many professionals and experts involved with Busang raised this or any other red flag. Felderhof's experience at OK Tedi and Mirah was consistent with the development of and results at Busang.

I prefer the evidence, with its shortcomings, of Dr. Hellman and Leach over the evidence of Farquharson with its errors, omissions, corrections and concessions.

Red Flag 3: Location Of New Drill Holes Was Never Influenced By Results Of Previous Drilling

In the October 1997 letter to Bre-X Farquharson states:

3. **Location of new drill holes was never influenced by results of previous drilling**

   We noted on our arrival at Busang that the spotting of new drill holes was simply done by the surveyor according to a predesigned grid without any consideration by the geologists as to whether or not the hole locations might change because of drilling results from surrounding holes.

Exhibit 681: Appendix XII

The O.S.C. position is set out in paragraphs 662-669 of Exhibit S5 Volume II and S10.

The Defence position is set out in paragraphs 222-223 of Exhibit S3 and S13.

This is one of those red flags with respect to which Farquharson was not examined in-chief. The O.S.C. position with respect to those flags not examined in chief is found at page 177 of these reasons. This red flag is not included in the body of Strathcona's opinion, Exhibit 681. The O.S.C. position with respect to red flags not found in Farquharson's opinion is found at page 177.

This is also one of those alleged red flags that has more to do with best practices, with respect to which there may be different opinions, than with questioning the reliability of the resource calculations in the press releases which is what is relevant to Counts 5 to 8. See page 178.

Dr. Hellman

Dr. Hellman's opinion that allegation 3 is not a red flag is found in Exhibit 1202 at pages 3, 50-51, 160-161. Dr. Hellman concluded "*that geological considerations played a vital role in the drilling program.*" (page 51) In his opinion "*the drill-out of resources often follows a predesigned grid.*" (page 160)

Dr. Kavanagh

Dr. Kavanagh testified:

> MR. GROIA: Would you agree that the Bre-X drilling program was influenced by prior data or prior drilling results? In other words, Bre-X was analyzing the data they were getting from drill holes and using that data to decide where to do future drilling.
>
> MR. KAVANAGH: Yes.
>
> MR. GROIA: And if my recollection serves me, Doctor Kavanagh, on occasion you, in fact, made some suggestions about where future holes might be drilled based on your analysis.
>
> MR. KAVANAGH: Yes. More frequently in the early stage when the drilling was confined to the Central Zone, very rarely with respect to the Southeast Zone drilling.
>
> MR. GROIA: And of course when Bre-X moved into the in-fill drilling program, it's less important at that stage because you have a sense about the size of the deposit.
>
> MR. KAVANAGH: Yes.

Transcript: March 14, 2005, page 57

Red Flag 4: Busang Geologists Never Went To Drill Sites

In the October 1997 letter Farquharson states:

> **4. Busang geologists never went to drill sites**
>
> When we were working with the drilling company in spotting our audit holes the remark was made that they never saw a geologist from Bre-X at any of the drill sites, despite six drills being in operation at the time. It became apparent that the Busang geologists were not really interested in watching what came out of the hole as the core was stored for many weeks after drilling prior to going through the logging, sampling process etc.

The O.S.C. position is set out in paragraphs 670-671 of Exhibits S5 Volume II and S10.

The Defence position is set out in paragraphs 224-225 of Exhibits S3 and S13.

This is another red flag with respect to which Farquharson was not examined in-chief and a red flag that is not mentioned in the body of Strathcona's opinion Exhibit 681. The O.S.C. position with respect to red flags in those categories is found at page 177 of these reasons respectively. This is also a red flag that has more to do with best practices than questioning the reliability of resource calculations. See page 178 of these reasons.

Dr. Hellman's opinion is found in Exhibit 1202 at pages 22 and 51. In Dr. Hellman's opinion the Bre-X geologists showed their interest in the geology of the core in the accuracy of their observations recorded in the drill logs. Farquharson agreed the logging at Busang was "*[r]easonably well done.*" (Transcript: April 5, 2005, p.36). M.R.D.I. reported "*[t]he core logging procedures at Busang are excellent*".

Exhibit 505: page 13

Red Flag 5: Drill Core Not Split-All 14 Kilograms of Core From Each Two-Meter Sample "Required For Accurate Assays"

In the October 1997 letter Farquharson states:

> **5. Drill core not split –all 14 kilograms of core from each two-metre sample "required for accurate assays"**
>
> Many observers have commented on this particular red flag and with good reason. A sample weighing 14 kilograms, and representing but two metres is a very large sample and most people with any experience in the gold industry would have recognized that a seven-kilogram sample would have been just as representative of that two-metre interval.

The O.S.C. position is set out in paragraphs 672-684 of Exhibit S5 Volume II and S10.

The Defence position is set out in paragraphs 226-230 of Exhibit S3 and S13.

Not Red Flag For Strathcona's Clients (See Pages 212 Of These Reasons)

Strathcona recommended whole core sampling in the Angostura project, a client of Strathcona, while at Busang this is an alleged red flag. Farquharson testified that the difference was that "*in Angostura they had already been through a very extensive sampling program of 52,000 meters of core where they had retained one-half of the core in case anyone wanted to go back and do more assaying, or review the core, whereas that record did not exist at Busang.*"

But Bre-X retained skeleton core which could and was used, for example by Barrick, "*to go back and do more assaying, or review.*"

Transcript: March 29, 2005, page 76
Exhibit 766

Farquharson was a director of Placer Dome which had majority ownership of Placer Pacific. In Exhibit 1202 at pages 163 and 164, Dr. Hellman discusses the use of whole core crushing by Placer Dome and Placer Pacific in various of their deposits.

Freeport reported "*[t]he use of whole core for assay is an unusual practice (not unheard of, just unusual).*"

Exhibit 755: pages 199-200

Dr. Hellman

In Dr. Hellman's opinion allegation 5 is not a red flag.

Exhibit 1202: pages 5, 52-53,162-164

Dr. Hellman testified:

> MS. COLE: And I take it if one were to split the core, the rationale behind splitting the core is to provide them a means for someone to audit the sampling?
>
> MR. HELLMAN: No, not really. There is a debate in geological circles as to whether one should split the core or whole crush the core when whole crushing is indicated. Generally speaking, at that time the necessity of auditing, tampering, security, all that sort of thing was basically not even thought about. The issue was whether the Busang core would be useful for on-going geological studies. For instance, for somebody to come back and look at structure or something like that. There was a debate. You know, it was not unanimous either way.
>
> MS. COLE: Okay. I'm sorry, I perhaps misphrased my question. When I said "audit" I was referring to people like, for example, potential joint partners ---
>
> MR. HELLMAN: Right.
>
> MS. COLE: --or people who were going to invest in the project. Those sorts of people ---
>
> MR. HELLMAN: Yes.
>
> MS. COLE: --would be interested in seeing half a core so that they could use it to do their own auditing?
>
> MR. HELLMAN: Yes, they would certainly look at either the split core, or any skeleton core, or even in the case of most gold projects in Australia there would be just bags of chips from reverse circulation.

Transcript: December 5, 2005, pages 15-16

In Exhibit 1202, Dr. Hellman refers to Francis Pitard, one of the world's leading sampling experts who is a proponent of whole core sampling:

> Bre-X's practice followed the advice of Mr. Francis Pitard who is one of the world's leading sampling experts in the minerals industry. He is well known as a proponent of whole core sampling and had previously advised CRA to undertake whole core sampling for the drill-core from Kelian to ensure that the sample was representative. The distribution of gold at Kelian, like that thought to be at

> Busang, was patchy or "spotty", coarse and irregularly distributed. The sampling protocol at Busang was very similar to that recommended by Mr. Pitard for Kelian which had a significantly understated resource gold grade compared with that achieved in production.

The O.S.C. submits that "*Hellman's report is misleading because it suggests that Francis Pitard, another one of the three leading experts in the world on sampling, recommended whole core crushing and assaying at Busang.*" I do not read the report in the way suggested by the O.S.C. . Hellman is not saying Pitard had in fact advised Bre-X but that Bre-X was following a practice generally recommended by this world expert. Hellman testified over some eight days and this accusation was never put to him although he was certainly examined and cross- examined about Pitard and whole core assaying. Exhibit S5 Volume II: paragraph 683

Recommendations

There was a debate in geological circles about whether to split the core or sample the whole core. Skeleton core, as kept by Bre-X, was sufficient for auditing purposes.

In his report, Exhibit 1328B, pages 24-25, Leach states the skeleton core sampling and storing at Busang "*was well above the industry standards.*" Leach and Corbett suggested assaying half the drill core. At page 141 of Exhibit 1328B Leach's opinion was that "*[t]he assaying of the whole core at Busang is an acceptable industry practice.*"

Semple agreed that "*MRDI had recommended some of the same things that Kilborn recommended...and one... was that Bre-X split the core.*"

Transcript: January 25, 2006, pages 113-119

M.R.D.I. commented "[w]e have seen other projects where the whole core was sent for assay: Colonac, N.W.T., Fort Knox, A.K., and the Alaska Juneau (A.K.) come to mind." The M.R.D.I. report states "[r]etaining some split core is also useful" but the report also states "[a]ny decision to change the protocol (from whole to half core as suggested by Dr. Francois Bongarcon) should be based on a thorough sampling study." M.R.D.I. recognized other projects with whole core assaying. M.R.D.I.'s recommendation is conditional on further study. A conditional recommendation is far from being a red flag. See page 178 of these reasons.

Exhibit 505: page 2

No One Else Saw Red Flags

In the Defence chart, Appendix "B", Exhibit S4, described at page 179 of these reasons Farquharson testified this red flag should have been apparent to all the persons listed including M.R.D.I. and Kilborn, with a single question mark only for the regulators. No one said this was a red flag There were recommendations made by M.R.D.I. and Kilborn but neither saw this as a red flag. There is a substantial difference between a recommendation to consider change and a red flag.

This is another alleged Red Flag that has more to do with best practices, with respect to which there may be different opinions, than with questioning the reliability of the

resource calculations in the press releases which is what is relevant to Counts 5 to 8. See page 178 of these reasons.

Red Flag 6: Selected Intervals Designated Visually As "Mineralized" And Received Different Sample Treatment

In the October 1997 letter Farquharson states:

> 6. **Selected intervals designated visually as "mineralized" and received different sample treatment.**
>
> We were amazed that the geologist logging the core could designate which areas were likely to contain gold mineralization and which would be barren, simply based upon visual observations. The geology of the Southeast Zone is such that the only way one can tell if there is gold present is to sample the interval. There are some obvious areas that are unlikely to have any gold mineralization but based upon the geological theory for the existence of gold at Busang any of the host andesite rock, or dacite as the Busang geologists preferred to call it, was prospective for gold, with the degree of alteration having an impact on the degree of prospectiveness.
>
> The other common description that the Busang geologists used in logging core was a frequent reference to silicification which our geologists could not identify and any competent observer could have readily refuted this description by applying the penknife scratch test for silica.

The O.S.C. position is set out in paragraphs 685-691 of Exhibit S5 Volume II and S10.

The Defence position is set out in paragraphs 231-239 of Exhibit S3 and S13.

This is another red flag not found in the body of Strathcona's opinion Exhibit 681.

The O.S.C. position with respect to those red flags is found at page 177 of these reasons.

This is another red flag that has more to do with best practices then questioning the reliability of resource calculations. See page 178

Farquharson

In Exhibit 208, page 19 Strathcona states:

> The observed rock types and alteration assemblage confirm the classification of Busang as a "porphyry-related, low sulfidation carbonate-base metal –(gold) system" (Corbett and Leach, 1997). The two major alteration styles –propylitic and carbonate-sericite-clay-pyrite- are easy to recognize in drill core and have been used by the Bre-X geologists during core logging to separate un-mineralized ("dacite") from mineralized ("mineralized zone") sections. This classification is correct, as long as "mineralization" refers to pyrite, marcasite, and base metals, and logging by Bre-X and Strathcona (or any other geologists familiar with the rocks), would, and has produced very similar results, as far as identification of these units is concerned. At Busang, "mineralized zone" core was bagged and shipped via Samarinda to Indo Assay Lab in Balikpapan, and generally returned good gold values. Propylitic "dacite" core was considered waste, and was shipped to Indo Assay Laboratories for assaying at a later date, with assay preparation done at Busang.

Farquharson agreed with the suggestion that in this paragraph Strathcona is saying that separating the core into mineralized and unmineralized sections was "*easy to do*". This contradicts Red Flag 6.

Transcript: April 5, 2005, pages 33-34

Also in a telephone discussion on April 17, 1997 between Farquharson and the O.S.C. and T.S.E., Farquharson was asked "*Are the core logging...procedures up to the standards of major mining corporations?*" He answered "*...the core logging has been fairly well done. We have some difference with them on their terminology.*" This also contradicts Red Flag 6.

Transcript: April 5, 2005, pages 38-40

<u>Not Red Flag For Strathcona's Clients (See Page 212 Of These Reasons)</u>

Farquharson's evidence was "*that normally all samples go through the same process and treatment and that it's a red flag if they don't.*" Yet with respect to the Angostura

property, a company associated with Strathcona, Strathcona found it appropriate for Angostura to separate mineralized from non-mineralized core and to follow two separate assay processes.

Farquharson attempted to distinguish Angostura and Busang by saying it was easy to separate the mineralized from the unmineralized core in Angostura but not in Busang. But in his evidence noted above Farquharson conceded Strathcona had said it was in fact also "*easy to do*" at Busang.

Transcript: March 29, 2005, pages 81-82
Exhibit 766

Leach

Leach's opinion was that allegation 6 is not a red flag.

Exhibit 1328A: pages 6, 49-52

At page 6 Leach states:

- The geological model of late "post-mineral' dikes, and the identification of such dikes by site geologists looking at the core, makes it possible to determine unmineralised intervals during drilling. Red flag #6 was therefore not a 'red flag'.

At page 51:

- It is not uncommon during exploration programs for site geologists to designate core as mineralised and unmineralised based on visual observations and for the core to be treated for analyses in separate ways. This designation is typically done during the early stages of exploration drilling and continues throughout the remaining exploration program.

He concludes "*This 'red flag' of Strathcona indicates a lack of understanding of the geology of Busang.*"

Dr. Hellman

Dr. Hellman's opinion was also that this is not a red flag.

Exhibit 1202: pages 6, 53,165-166

Dr. Hellman states at page 53:

> Strathcona states "*that the only way that one can tell if there is gold present is to sample the interval.*" (p 2) The highly altered intervals at Busang were clearly evident and contrasted with the less altered darker green intervals (see photograph in Appendix 3F). It is common sense to give priority to those intervals identified as mineralised and to sample those first with the less altered intervals sampled later, if at all. Bre-X did not solely rely on visual logging as implied by Strathcona but processed the lower grade, less-altered material later than intervals with obvious mineralisation. This is common practice.

Figure 37 at page 163 of Exhibit 1202 shows the difference between mineralized and non-mineralized core.

Kilborn

The Kilborn Intermediate Feasibility Study (Exhibit 610, page 0008) states: "*The mineralized and non-mineralized Zones can be distinguished visually (the barren zones are significantly darker than the mineralized zones).*"

Dr. Kavanagh

Dr. Kavanagh testified:

> Q. Now, let me ask you about that, something I'm quite interested in. We've seen, on a number of occasions, references to geologists, trained geologists eyeballing core and picking out mineralized from unmineralized sections, right?
>
> A. Yes.

Q. And you'd agree with me that that's a fairly standard exploration technique?

A. A very—

Q. –standard exploration technique.

A. Yes.

Q. And although it may be difficult for a layman, an experienced geologist can, generally speaking, tell the difference between mineralized core and non-mineralized core.

A. In any particular prospect, and after gaining some acquaintance of the rocks in that prospect. It's not an immediate – you cannot go into a property and the first hole, start to eyeball it.

Q. Right.

A. You have to have the experience of trying an eyeballing, and then seeing what the core is assaying.

Transcript: March 2, 2005, pages 84-87

No One Else Saw Red Flags

Farquharson testified Kilborn, Dr. Kavanagh and M.R.D.I. would have known about

Red Flag 6. They did not raise any objection.

Exhibit S4: Appendix "B"

Red Flag 7: In Over 60,000 Meters Of Core Logging No Reports of Visible Gold

In the October 1997 letter Farquharson states:

7. In over 60 000 metres of core logging no reports of visible gold

The nature of the gold found at Busang Southeast zone had generally been reported to be coarse in nature and, therefore, one would have thought that in

over 60 000 metres of drill core some evidence of visible gold would have been reported in the drill logs but when we asked the question we were told that there were no reports of visible gold. This conflicts with the statement "gold dominantly occurs in free native form" in the technical paper presented in early 1996 (?) entitled Busang Gold Deposit by Felderhof, de Guzman, Puspos and Nassey.

Also, it would be normal practice for the person responsible for a major project such as Busang to have requested thin-sections be prepared from the core in some of the higher grade areas to be able to visually confirm the presence of the gold and its association. This was not done and we are not aware if others asked if this procedure had been done.

The O.S.C. position is set out in paragraphs 526-559 of Exhibit S5 Volume II and S10.

The Defence position is set out in paragraphs 240-264 of Exhibit S3 and S13.

Farquharson

Strathcona's detailed opinion is found at pages 20 and 21 of Exhibit 681:

Absence of visible gold in core samples

Gold grains in crusher reject samples from Central and Southeast Zone core samples were described in mineralogical studies by Roger Townend and Associates on behalf of Normet (October 1996), and by Hazen Research (October 1996) in the Intermediate Feasibility Study by Kilborn. In both cases, the gold particles were found to be liberated, rounded with beaded outlines or nearly spherical in shape, and relatively coarse, ranging in size from 60 to 400 microns, yet visible gold was never reported by Bre-X from the logging of core from approximately 400 [Farquharson corrected this in testimony to be 300]drill holes or from surface samples.

The May 1997 report by Strathcona commented on the Townend study and the absence of visible gold in Busang core samples as follows (page 46):

With the very coarse liberated gold of up to 400 microns reported in this study, one would have expected to see visible gold somewhere in the many thousands of metres of drill core from Busang. However, there is no mention of visible gold in any of the documentation that we have seen with the Kilborn feasibility study or resource estimate, or in the drill logs prepared by Bre-X geologists, other than in the mineralogical studies done on the obviously

foreign gold in the metallurgical concentrate samples derived from the core samples sent by Bre-X for assaying.

In gold exploration projects geologists logging drill core always carefully mark locations on the drill core where visible gold has been observed. It is one way of providing assurance to visitors and management that there really is gold on that property. That was never done or possible at Busang despite the reported coarse liberated nature of the gold, which should have made observations of visible gold in drill core a frequent occurrence. The geologists responsible for the Busang exploration program should have and must have wondered how such a non-visible result could occur that would be completely opposite to what their experience, and that of the exploration community, would expect.

Visible gold was found in the core of two holes drilled in the Central Zone by Westralian in 1988 (June 1989 report): Hold BUD-2: *One speck of visible gold at 23.8 metres* [the assay for the interval 23-24 m was 2.49 g/t Au]. Hole BUD-3: *One speck visible gold at 63.20 metres; 10 cm pyrite + galena + sphalerite vein, with two specks of visible gold at lower contact* [64.3 m], [the assay for the interval 62-65 m was 1.72 g/t Au].

Felderhof, in his press statement of July 25, 1997 refers to Kelian to defend the lack of visible gold in Busang core samples, by quoting van Leeuwen et al.: "Free gold [at Kelian] is very rarely visible megascopically in either outcrop or drill core, and is also rarely detectable on the microscopic scale, even in samples assaying over 25 g/t Au." However, Felderhof does not mention that Kelian has much refractory gold, tied up in pyrite or arsenopyrite, and it does not have the coarse, liberated, rounded and beaded gold that is exclusively found in Busang samples sent for assaying. Gold from the Kelian deposit is of an entirely different nature than that found in the tampered samples from Busang and reported on to Bre-X management including Felderhof.

No visible gold was ever observed in the core drilled by Bre-X on the Busang property. Considering the coarse gold found in the samples sent for assaying and subsequently for metallurgical tests, and the amount of core drilled in the Southeast Zone (over 130 kilometres) and in the Central Zone (over 18 kilometres), visible gold should have been found in many of the core samples, had it been part of the in-situ rock, and not added later.

Dr. Hellman

Dr. Hellman's opinion is that this is not a red flag. Exhibit 1202, pages 18, 22, 54, 167-177.

Dr. Hellman states at page 54:

> There are numerous references in the Central Zone and South East Zone drill logs to visible gold, and these commence with BRH 03 which has six references to visible gold including "gold veinlets".
>
> The references to visible gold in the drill logs are clear and unambiguous. Strathcona's numerous other red flag allegations and complaints are dependent upon there being no visible gold recorded from the Busang core.

And page 173:

> Numerous people identified gold in the core and rocks from Busang.

Bre-X Logging

Farquharson agrees that there was a high degree of similarity for the main features in the logging done by Strathcona and the Bre-X geologists. Farquharson agreed the logging at Busang was *"[r]easonably well done"* despite the inability to recognize there was very little silicate in the samples. But Farquharson would not extend that to Bre-X reporting of visible gold. Strathcona ignored references to gold in the Bre-X logs which they did not accept as "*industry standard*" references such as the plus/minus references.

Transcript: March 29, 2005, pages 88-91
Transcript: April 5, 2005, pages 31-37, 41-43.

M.R.D.I. reported *"[t]he are logging procedures at Busang are excellent"*.

Exhibit 505: page 13

"No Visible Gold"

In the October 1997 letter Strathcona states: "*In over 60,000 meters of core logging no reports of visible gold.*"

On page 2 in the Exhibit 681 summary Strathcona states "*No visible gold was observed in all the core drilled by Bre-X.*" On page 5 in Exhibit 681 in describing the third most striking Red Flag Strathcona states:

> The total absence of any visible gold in more than one hundred kilometers of drill core...

In cross-examination Farquharson conceded that in fact there were several references to visible gold and not "*no*" references nor a "*total absence*" of references.

Transcript: March 23, 2005, pages 73-82

Farquharson conceded Strathcona reported the "*total absence of any visible gold*" although he was "*aware of a number of instances where somebody saw gold in the core logs.*"

Transcript: March 23, 2005, page 77

Strathcona had not looked at any of the Central Zone drill logs nor at all of the Southeast Zone drill logs before making the statements above.

Transcript: March 29, 2005, pages 88-91
Transcript: April 5, 2005, pages 36-37, 41-43

Strathcona applied its faulty observations of some holes to all of the holes including holes they did not look at.

Transcript: April 5, 2005, pages 41-43

As noted above, Strathcona's opinion Exhibit 681, page 2 states that *"[n]o visible gold was observed in all the core drilled by Bre-X"* including both the Southeast Zone and Central Zone. In cross-examination Farquharson agreed it would have been helpful if he had pointed out to the court that in his testimony unlike in Exhibit 681 he was making a distinction between the Central Zone and the Southeast Zone.

Transcript: March 23, 2005, page 85

Farquharson conceded there were references to visible gold in the core logs and therefore portions of Exhibit 681 needed to be rewritten.

Transcript: March 23, 2005, pages 78-82

Having conceded that there were some references to visible gold in the logs, Farquharson then took the position the references were statistically not significant. He suggested a statistically significant number "*would be 50, 100, perhaps not 1000 but a lot more than the few that were there, much more*". He testified there was no "*scientific basis*" for the cut off point just "*what one would anticipate*"

Transcript: March 23, 2005, pages 88-90

Farquharson agreed that his statement that there is no gold in the Southeast Zone in fact means no economic gold in the Southeast Zone.

At one point Farquharson suggested it was a red flag for the core logging geologists not to see the salted gold but the salted gold was obviously not added to the solid core and added after the logging.

Transcript: March 23, 2005, pages 76-77

Exhibit 579

Farquharson testified the lack of trophies of visible gold at Busang was a very powerful red flag that would have been apparent to Felderhof.

Transcript: March 17, 2005, pages 40-41

Exhibit 579 is a piece of solid drill core in a plastic bag marked 68, 51-52.55 meters with the visible gold circled in blue. Dr. Kavanagh testified the drill core was sent to him from Indonesia and that it was from the Central Zone BRH-68. Dr. Kavanagh showed this drill core to potential investors and at the Prospectors and Developers Association Conference (P.D.A.C.). Dr. Kavanagh testified he did not see any other pieces of Busang drill core with visible gold.

Transcript: March 2, 2005, pages 13-17

The O.S.C. submits there is no evidence that this drill core was from Busang.

Dr. Hellman testified he went to Dr. Kavanagh's lawyer's office to look at Exhibit 579. He then reviewed the drill log for BRH-68 @ 52.00-52.55 which described "*minor visible*

Au." This is some evidence Exhibit 579 was from Busang. Dr. Hellman also noted in Exhibit 1202, page 175, that "*it would equally be appropriate to describe the gold as 'significant'...*"

Transcript: November 7, 2005, pages 42-43
Exhibit 1202: page 175

Plus/Minus References

Farquharson testified he ignored the plus/minus references to gold in the logs because those references were not the normal practice and not industry standard references.

Transcript: April 5, 2005, pages 31-37, 41-43
Transcript: March 29, 2005, pages 88-91

Dr. Hellman testified the use of plus/minus is not unusual in Australia, the Philippines and Indonesia. He testified "*It would cause no concern to anybody familiar with exploration in that area.*"

Transcript: November 3, 2005, page 10

In Exhibit 1202, page 171 Dr. Hellman states that Bre-X geologists used plus/minus "*in the geological logs to describe the position of various minerals... and base metals, as well as gold in the sense of 'approximately' or 'with or without'.*"

M.R.D.I. uses "$\pm$" in its report, for example, at page 14 of Exhibit 505: "*quartz + calcite $\pm$ dolomite $\pm$ manganocalcite, and sulphides of pyrite + arsenapyrite $\pm$ marcasite $\pm$ pyrrhotite*".

Another example of using "+/-" is found throughout Exhibit 685, a Summary Report On Exploration Activities Busang Project by Levings and Ogierman which was entered into evidence by the O.S.C.

Levings was an Australian geologist working for WRPL. In 1989 Levings logged gold in BUD-2, Exhibit 1254 and BUD-3, Exhibit 1255. Farquharson described these logs as good examples of the industry accepted way of recording observations of visible gold. But Levings used plus/minus in Exhibit 1254; for example, interval 5.6 to 15. 4 meters: "*calcite + - quartz + - pyrite*".

Transcript: April 5, 2005, page 2

Kelian

The O.S.C. submits "*Busang is not analogous to Kelian because the absence of visible gold at Kelian was due to the fact that the gold at Kelian was refractory.*"

Exhibit S5 Volume II: page 188

Strathcona relied on Van Leeuwen and Leach's paper (Exhibit 688) in reaching its opinion that the gold at Kelian was of an entirely different nature than that at Busang, that Kelian had refractory gold and not the coarse liberated gold found at Busang.

Exhibit 688 was received by the journal of Geochemical Exploration on September 6, 1988; revised and accepted June 15, 1989 and published in 1990.

Exhibit 681: page 21

Strathcona was not aware that Kelian had later installed a gravity circuit because Kelian had a coarse gold problem although the information was publicly available in 1994 and Strathcona's opinion Exhibit 681 is dated 2000. See pages 354-355 of these reasons. Transcript: March 29, 2005, pages 58-62

When Strathcona stated in Exhibit 681 that one of the three most striking red flags was the total absence of any visible gold (which is incorrect), Strathcona based this in part on their mistaken understanding Kelian did not have coarse gold and a gravity circuit. When Farquharson was testifying in chief he knew he had been mistaken and that Kelian did have coarse gold and a gravity circuit but did not correct this evidence or Exhibit 681 although while testifying in chief he had been asked about corrections and had specifically made other corrections to Exhibit 681.

In Exhibit 1202, Dr. Hellman states at page 20:

> Strathcona's understanding of Kelian is flawed. In actuality:
>
> - the gravity plant (retro-fitted several years after production started) at Kelian is well known and large;
> - the gold mineralization is characterized by coarse gold grains;
> - the gold is not predominantly refractory; and
> - mineralogical consultants who had studied Kelian reported to Bre-X that the samples from Busang were similar to Kelian.

Leach testified that at Kelian "*gold was virtually not seen in any of the core.*" Leach testified in carbonate base metal systems such as Busang and Kelian "*very rarely do you ever see any visible gold in those types of system.*" Leach testified that "*the amount of visible gold that was seen at Busang both in the Central Zone and that was recorded in*

the Southeast Zone, it was very similar to what... was recorded at Kelian and Hidden Valley and Mount Kare and a large amount of other similar types of deposits, so it's very comparable."

Transcript: December 13, 2005, pages 5-7

Farquharson gave the following testimony:

> MR. GROIA: Do you know what the visible gold experience was at any deposit in Indonesia?
> MR. FARQUHARSON: No.

Transcript: March 23, 2005, page 90

In Exhibit 1202 at pages 175-177 Dr. Hellman sets out "*examples in [the] literature of gold mineralization with a significant coarse gold component that have rare visible gold.*"

Farquharson Re-Examination

In re-examination Farquharson contradicted Red Flag 7:

> MR. FARQUHARSON: When a geologist is logging core and he has the pleasant experience of encountering visible gold when he is logging core from an exploration program for gold, that is a significant event because it doesn't happen very often with many deposits.

Transcript: April 7, 2005, pages 26-27

No One Else Saw Red Flags

Farquharson testified that if Dr. Kavanagh and Kilborn were getting copies of the logs then Dr. Kavanagh and Kilborn should have seen that there was no visible gold in the

logs. M.R.D.I. would have looked at the logs because they commented on the logging procedure.

Transcript: April 5, 2005, pages 44-45

Neither Dr. Kavanagh nor Kilborn nor M.R.D.I. saw a red flag.

M.R.D.I. concluded: "*The core logging procedures at Busang are excellent, providing highly detailed and informative geological and geotechnical logs of all drill core.*"

Exhibit 505: page 13

Red Flag 8: The Geology Of The 10-Centimeter "Skeletons" From Reported High-Grade Intervals Did Not Appear To Support Such Assays

In the October 1997 letter Farquharson states:

> **8. The geology of the 10-centimetre "skeletons" from reported high-grade intervals did not appear to support such assays.**
>
> We looked at some of the skeletons remaining from those intersections that had grades of 20 grams per tonne or more fully expecting to see geology typical of high-grade epithermal deposits but the high-grade areas looked no different and were just as tight and solid as those areas reported as being very low grade or barren.

The O.S.C. position is set out in paragraphs 560-605 of Exhibit S5 Volume II and S10.

The Defence position is set out in paragraphs 265 and 266 of Exhibit S3 and S13.

Red Flag 8 is the O.S.C.'s Bright Red Flag 3. Farquharson listed Red Flag 8 in his re-examination as one of the most striking areas of red flags.

It is a significant inconsistency that Red Flag 8 is not listed as one of the most striking areas of red flags in Strathcona's opinion, Exhibit 681, page 5.

It is also significant that except for its inclusion in the October 1997 letter as an appendix to Exhibit 681, this O.S.C. bright red flag (Red Flag 8) is not only not listed as one of the most striking areas of red flags in Exhibit 681it is not even found in the body of Strathcona's opinion Exhibit 681. The O.S.C.'s position with respect to red flags not listed in Exhibit 681 is found at page 177 of these reasons. See pages 173-178.

Corbett

With some additional comment, the Defence agrees with paragraphs 574-584 of the O.S.C. submissions, Exhibit S5 Volume II. Those submissions make some references to Corbett. Corbett's position in refusing to be involved in Felderhof's defence is noteworthy but it is hearsay. He did not testify and could not be cross-examined on the issue.

Leach could not recall if he and Corbett postdated their Reconciliation of Assay Data report, Exhibit 773, as Corbett appears to have told the RCMP. Corbett's statements to the RCMP are hearsay and Leach did not recall if they had in fact post-dated the report but it is of some concern that Leach inferentially concedes that he could have been involved in post dating a report.

Leach

In Leach's opinion allegation 8 is not a red flag.

Exhibit 1328A: pages 23-24, 33-35, 53-55.

BSSE 198

The O.S.C. submits "*Corbett and Leach could not reconcile the geology of BSSE-198 high-grade intervals skeletons with the assay results.*"

Exhibit S5 Volume II: page 202

In Exhibit 773, a memo from Leach and Corbett to Felderhof dated April 14, 1997, Leach and Corbett state:

> In conclusion it is difficult to understand the high grades in drill hole BSSE 198.

This statement supports the O.S.C. position and supports Red Flag 8.

In his 2005 expert opinion Leach states at page 34 of Exhibit 1328A:

> It was only after the detailed analyses by Corbett and myself of the skeleton core, drill logs and assay data from Hole 198 (drilled July/August 1996; assayed late 1996) that it became difficult to reconcile the very high assays.

The O.S.C. submits that in 2005 (Exhibit 1328A) Leach "*resiled*" from his 1997 (Exhibit 773) position, when in 2005 he states "*that it was only difficult for him to reconcile the very high assays after detailed analysis.*" The O.S.C. objects to Leach adding that it was difficult to reconcile the very high assays "*only after the detailed analyses.*"

Exhibit 773
Exhibit 1328A: pages 33-34
Exhibit S5 Volume II: paragraphs 589-594

The Defence disagrees that Leach resiled from his position in the Defence comments to paragraph 591 of Exhibit S5 Volume II:

> **The Defence disagrees that Mr. Leach resiled from his position in his Report (Exhibit 1328A and B). Mr. Leach's evidence has always been that he and Dr.**

Corbett performed a preliminary inspection of BSSE 198 on April 5, 1997 where the core exhibited a "very strong alteration and contained abundant disseminated pyrite, with local sulphide-rich shear zones. We did, however, consider that there should be more fracturing in the skeleton core to justify the very high grades" (page 22). While visiting Busang on April 9, 1997 Dr. Corbett and Mr. Leach started a much more detailed look at the skeleton core from BSSE 198. It was this detailed analysis which Mr. Leach is referring to in Volume 1 of his report cited by the OSC in support of its position. In other words, Mr. Leach never changed his position. It was only after the detailed analyses conducted by Dr. Cobett himself of the skeleton core, drill logs and assay data from hole BSSA 198 that it became difficult to reconcile the very high assays from that hole.

In Exhibit 1328A at pages 23-24 Leach states:

ii. BSSE 198

Drill hole BSSE 198 was drilled in late 1996 and returned the highest and most consistent grades at Busang (400m @ >12 g/t). This was unusual for carbonate base metal gold systems. However, comparable consistent high grades were also recorded in hole K466 in the Northeast Zone at Kelian. In this hole, a 300m interval assayed 5.5 g/t, including 232m @7.18 g/t Au.

- Corbett and I carried out a preliminary evaluation of skeleton core from BSEE 198 on the third day and observed the following:
    - The core exhibited intense alteration with local sulphide-rich shear zones.
    - That there should be more extensive vein development in the skeleton core to justify the high grades.
    - There was abundant pyrite in BSSE 198 skeleton core which was disseminated throughout the rock and this pyrite had a strong reddish tinge to it. We postulated at that time that the pyrite may be mercury-, antimony-or arsenic-rich and that it could therefore also contain high percentages of gold.

- Upon a more detailed examination of the skeleton core from BSSE 198 four days later, we compared what we saw with the Bre-X assays and the geological logs and made the following observations:
    - Although most of the core had undergone intense sericite-quartz-pyrite and clay alteration, there was a paucity of fracturing and vein development in both the skeleton core and the logs that did not justify the very high gold grades.
    - De Guzman and Puspos had informed Felderhof, at his request, that the high grade was caused by shear zones, and Felderhof relied on that explanation. However, when we plotted the shear zones

from the logs and the assays together, many of the very high grade (>30 g/t Au) intervals did not correspond to the shear zones marked on the log sheet. Felderhof was visibly shocked by the results of this work.

- Therefore, only upon a very detailed analysis was it apparent that there were inconsistencies between the Bre-X assays and the geology in core from BSSE 198.
- Such an analysis would not have been industry practice and not customary unless one was looking for a problem. In addition, this type of analysis would have been beyond the scope of a general manager of exploration, such as Felderhof, who correctly questioned and relied on the information supplied to him by the exploration manager (de Guzman) and project geologist (Cesar Puspos).

In Exhibit 1328B at Tab 4 entitled "*Site Visit April 1997*" Leach sets out the "*Preliminary Inspection of BSSE-198*" on April 5, 1997 at page 22 and the detailed analysis of BSSE-198 on April 9, 1997 at pages 28-30.

It does not appear that Leach "*resiled from his position*" as submitted by the O.S.C. but simply that he came to his position that "*it was difficult to reconcile the higher grade Busang gold assays with the skeleton and drill core logs in the very-high grade intervals in hole BSSE 198*" not after the preliminary evaluation on April 5, 1997 but after the very detailed analysis on April 9, 1997.

The very detailed analysis was "*not...industry practice and customary unless one was looking for a problem...*" and "*...this type of analysis [was] beyond the scope of a general manager of exploration, such as Felderhof, who correctly questioned and relied on the information supplied to him by the exploration manager (de Guzman) and project geologist (Cesar Puspos).*"

In Leach's opinion Strathcona did not carry out the necessary "*analysis on which to base their 'red flag #8'*" allegation:

- It is considered that Strathcona personnel were not sufficiently familiar with the features of the high grade skeleton core from the South East Zone to be able to adequately assess correlations between the geology and grades in these core because:

    - As stated in Strathcona's Interim Report (1997) [6]:

"*Geological observation made by Strathcona at Busang were restricted to those made during logging of core from six holes drilled in the South East Zone I South, and to exposures of weathered rock near the drill sites.*" (Pg 16)

    - Significant intersections that had grades of more than 20 g/t Au were only recorded in hole BSSE-198. When Corbett and I carried out a brief inspection of the skeleton core from BSSE 198, Strathcona geologists accompanied us. However, they were not familiar with the skeleton core from that hole at that time, and we did not see them carry out any further inspection, even though we were in the area of the core samples for most of the rest of Strathcona's time at Busang.

...

- There is no evidence that Strathcona carried out such an analysis on which to base their 'red flag #8'. It would certainly not have been within the scope of Felderhof, as the general manager of exploration, to carry out such a detailed analysis.

This allegation indicates that Strathcona is not really familiar with the characteristics of gold deposits in the Pacific Rim region.

Exhibit 1328A: pages 53-55

BSSE 96

In paragraphs 602-604 of Exhibit S5 Volume II the O.S.C. submits that Leach's 2005 opinion Exhibit 1328A and B that BSSE 96 was "*well mineralized*" contradicts his 1997 report Exhibit 773 that "*does not describe a hole that was well mineralized*". When

Leach examined the skeleton core from BSSE 96 he did so "*as an example of a drill hole twinned by Freeport which contained no significant gold or silver assays*", that is, he knew before he started his examination of the skeleton core that it did not contain gold. In Exhibit 1328B, page 30, Leach did not say that BSSE 96 is well mineralized, he knew it had no gold, but simply reported that "*on an initial inspection, the hole appeared to be well mineralized and in accordance with the Bre-X assay data.*" Leach then continued that, as was the case with BSSE 198, when BSSE 96 was inspected in detail "*we found poor correlation between the Bre-X assays and ...[what] was documented in the logs.*" In Exhibit 773, page 3 Leach had made that same comparison between holes 96 and 198: "*and so the same conclusions must be drawn from this hole [96] as for BSSE 198.*"

Exhibit 1328A and B
Exhibit 773
Transcript: December 14, 2005 page 21

Not Red Flag For Strathcona's Clients (See Page 212 Of These Reasons)

Farquharson had said that hole 198 was the best he had ever seen. He was shown hole 86 in Cortez, a Nevada property in which Placer Dome has an interest. Farquharson was on the Board of Directors of Placer. In cross-examination Farquharson testified:

> MR. GROIA: And we are showing a whole series of intervals which I hope you will agree, Mr. Farquharson, exceed by two, or three, or four times the best intervals from Busang 198?
>
> MR. FARQUHARSON: In that hole 86?
>
> MR. GROIA: Correct.
>
> MR. FARQUHARSON: Yes.
>
> MR. GROIA: So coming back to your evidence about hole 198, would you agree with me that Placer Dome has an interest in a property that, if 198 was

like winning the lottery ticket, Cortez hole 86 must be like winning the lottery ticket three times in a row?

MR. FARQUHARSON: Well they are exceptional holes. I don't know whether they win the lottery three times in a row or not, but –

MR. GROIA: Twice in a row?

MR. FARQUHARSON: -- those are spectacular results.

MR. GROIA: So do you want to take back what you said about Bre-X hole 198, that it's the best you have ever seen?

MR. FARQUHARSON: Yes. We have now seen a better one.

...

MR. GROIA: And you made no effort, I take it, to do a study of the literature to see what kind of high grade holes were out there?

MR. FARQUHARSON: No.

MR. GROIA: You didn't even know about holes that were being reported from a public company of which you are a director, right?

MR. FARQUHARSON: Correct.

MR. GROIA: So would it be unreasonable for me to suggest that your experience on this issue isn't very meaningful?

MR. FARQUHARSON: No, I wouldn't say that. We have looked at an awful lot of drill properties over the years and I had never seen a drill hole like that.

MR. GROIA: Until today?

MR. FARQUHARSON: Yes.

Transcript: March 23, 2005, pages 97-98, 104
Exhibit 743

M.R.D.I.

As noted earlier M.R.D.I. concluded:

"The core logging procedures at Busang are excellent, providing highly detailed and informative geological and geotechnical logs of all drill core."

Exhibit 505: page 13

Red Flag 9: No Gold Identified In 103 Petrographic Samples Selected To Represent The Deposit

In the October 1997 letter Farquharson states:

> **9. No gold identified in 103 petrographic samples selected to represent the deposit**
>
> Anne Thompson of PetraScience Consultants in Vancouver was given 103 samples on which to do different petrographic studies, in other words to identify the component minerals and mineral associations in the Southeast Zone with the samples being selected by the Busang geologists to be representative of the Southeast Zone. Somewhere in that minute detailed work that she did there should have been some evidence of gold if it was present but she commented in her report that she was unable to find any gold in those samples.

The O.S.C. position is set out in paragraphs 692-712 of Exhibits S5 Volume II and S10.

The Defence position is set out in paragraphs 267-284 of Exhibits S3 and S13.

The Defence agrees with the O.S.C. that Farquharson's opinion, Exhibit 681 (pages 3, 5, 21-25) expanded on Red Flag 9 by adding earlier petrological work done by John Borner a petrologist at Mintek. This expanded red flag is part of the second of the three most striking areas of red flags on page 5 of Exhibit 681:

- the discrepancy that existed between the very few specks of find gold detected under the microscope in rock samples from only the Central Zone with none at all being detected by Bre-X in samples from the Southeast Zone, and the coarse liberated alluvial gold found and reported in all crusher core samples from the Central and Southeast Zones used for metallurgical tests and mineralogical studies.

It is of significant that this most striking red flag though is not one of the four most striking red flags listed by Farquharson in his re-examination. See pages 173-178 of these reasons.

Transcript: April 7, 2005, pages 4-7

Dr. Hellman

In Dr. Hellman's opinion this is not a red flag.

Exhibit 1202: pages 18-19, 22-23, 55-56, 178-188

At page 55 Dr. Hellman states:

> There are no negative comments in Ms. Thompson's report and the samples are described in terms that are consistent with legitimate gold mineralization. The purpose of her work is briefly described as:
>
> > "for study of the characteristics of alteration and mineralization" (10/09/1996) [15]
>
> Ms. Thompson reiterates this in a letter to Mr. Farquharson (21/04/97) [52]:
>
> > "The primary objective of the study was to tie the alteration characteristics to the mineralization, based on the samples provided by the on-site geologists."
>
> The most qualified person to raise a red flag regarding this work was Ms. Thompson who summarized her findings by comparing both the mineralization in the Central Zone and South East Zone to the characteristics of well documented mineral deposits found throughout the world.

Anne Thompson did not raise a red flag.

And at page 178 Dr. Hellman:

> **Summary of Opinion**
>
> The mainstream industry experience, as reflected in scientific publications, indicates that it is difficult to locate gold grains in microscope studies. This difficulty increases with the increasing size of the gold grains due to the

decreasing statistical probability of intersecting the rare and irregularly distributed gold grains. Ms. Thompson, a petrologist who had visited Busang, specifically advised Mr. Farquharson that the primary purpose of her study was to "tie the alteration characteristics to the mineralization, based on the samples provided by the on-site geologist". The purpose was not to locate gold grains.

The petrological studies made constant reference to either Kelian (and other gold deposits) or legitimate styles and models of mineralization. No warnings were made or irregularities reported by several experienced independent petrologists and mineralogists.

Gold had been identified by Mr. Borner, and the chance of intersecting a coarse gold grain in a thin section is very low. Both Ms. Thompson's and Mr. Borner's work were not directed at identifying gold grains. Strathcona does not appear to be familiar with the nature or purpose of microscope studies of rocks, ores and minerals (termed "petrography").

John Borner also did not raise any red flags.

Leach

Leach's opinion is that this is not a red flag.

Exhibit 1328A: pages 55-60
Exhibit 1328B: pages 81-99

Leach is experienced in petrographic and mineragraphic work.

Exhibit 1328A: pages 12-16

Farquharson's Lack of Expertise

Leach and Dr. Hellman found the allegations by Strathcona are invalid and indicate a basic lack of understanding of microscopic studies.

Exhibit 1328A: page 57
Exhibit 1202: page 178

Farquharson testified he did not have a great deal of background or knowledge in petrological examinations in contrast to the expertise of Leach noted above and in contrast to Borner and Thompson who carried out the petrological examinations. Farquharson testified:

> MR. GROIA: If you are doing a study of alteration you would normally use transmitted light and not refracted light, correct?
>
> MR. FARQUHARSON: I can't answer that question.
>
> MR. GROIA: Do you know the difference between a mineragraphic petrological examination and some other kind of petrological examination?
>
> MR. FARQUHARSON: Not unless you expand upon that term.
>
> MR. GROIA: Well how much background or knowledge do you have in petrological examinations, Mr. Farquharson?
>
> MR. FARQUHARSON: I don't have a great deal, but my colleagues who would have co-authored this report do.
>
> MR. GROIA: And so if I was to suggest to you that Mr. Borner saw gold in his mineralographic examinations but no gold in his transmitted light examinations and Anne Thompson saw no gold in the transmitted light examinations, we would have a consistency between Mr. Borner and Ms. Thompson, would we not?
>
> MR. FARQUHARSON: Yes.

Transcript: April 5, 2005, pages 58-59

Borner Report

In the summary at page 3 of Exhibit 681 Strathcona points out that Borner found gold in only 4 samples out of 75 examined. In cross-examination Farquharson concedes that Strathcona was wrong to include those studies using transmitted light because gold cannot be observed using transmitted light but only by using reflected light. Farquharson

conceded Strathcona should only have made references to those studies using reflected light.

The reference should have been to seeing gold in 4 of 40 samples and not in 4 of 75.

Transcript: April 5, 2005, pages 78-79

In cross-examination Farquharson was taken to authority that indicated that statistically gold would be found in 1 out of 100 samples. Farquharson did not challenge that study but in his opinion it was a red flag to find gold is only 1 out of 10 samples at Busang. Farquharson could not point to any study other than Strathcona's opinion that this was a red flag.

Transcript: April 5, 2005, pages 91-92

There is no evidence of any concerns being raised by Borner. Yet Strathcona states that *"[t]his lack of gold must have caused Borner considerable concern and resulted in descriptions of what he did not see under the microscope, i.e. gold in any shape or form, and in suggestions where the gold that should be there, given the assays, may be hiding..."*

Exhibit 681: page 22

In Leach's opinion in Exhibit 1328B, pages 84-85.

> i. Contrary to the statement by Strathcona, fine gold is orders of magnitude more likely to be seen under the microscope than coarse gold. This fact was understood by both Borner and Thompson. Therefore, unlike Strathcona, the scarcity of gold in the samples analysed by Borner and Thompson obviously did not concern them.

ii. The abundance of gold observed by Borner is in fact totally consistent with the Bre-X assay data.

...

iv. The abundance of gold observed by Borner is in agreement with what would have been expected by one experienced in the petrological analyses of similar styles of gold deposits.

...

vii. It is common practice for petrologists to indicate where gold may occur, especially when no gold is observed in a sample. This information is intended to assist metallurgical test work and is not an indication of concern as speculated by Strathcona.

Leach testified he saw nothing in the work done by Borner that he would have considered a red flag. Leach testified the amount of gold that Borner saw was similar to the ratio that Leach saw in the work that he did.

Transcript: December 12, 2005, pages 96-100

Exhibit 657 is a fax dated January 19, 1996 from de Guzman to John Robertson, Phil Hearse and John Borner with copies to Felderhof among others marked critical. The first two paragraphs read:

> Mr. John Borner confirmed the occurrence of free gold from drill core specimen, of which photographs are available at our office. These supplement our known visual experience of identifying the same occurrences; likewise as manifested in assay results.
>
> Our concern refers to the mineragraphy study conducted by Mr. John Borner from the Normet composite specimen, which did not register any gold occurrence; contrary to Normet gravity test results.

Exhibit 658 is a response to Exhibit 657 dated January 23, 1996, from Normet to de Guzman attaching a note from Borner with copies to Kilborn and Mintek answering de

Guzman's concern that "*the mineragraphy study...did not register any gold occurrence, contrary to Normet gravity test results*". The response referred to Kelian and compared Busang to Kelian.

Farquharson's evidence was that this was a "*very inadequate response.*" Farquharson is then asked:

> MR. GROIA: So as I see it, Mr. Farquharson, on the one side we have Mintek, Normet, Kilborn, all looking at this and not seeing anything except the comparison to Kelian, supported by Mr. Henley and the literature and on the other side we have Mr. Farquharson supported by nothing. Is that about the way it shapes up?
>
> MR. FARQUHARSON: No. Our support is not based on nothing. It's just based on common sense.
>
> MR. GROIA: So these are all men lacking in common sense?
>
> MR. FARQUHARSON: These are all men that were apparently carried away by the excitement of being part of the Busang story and did not recognize something as simple and as evident as this, that if you produce a gravity concentrate where you have got coarse free liberated gold why the hell can't you see it.

Transcript: April 5, 2005, page 104

Neither Farquharson nor Felderhof have the expertise in petrology as do Mintek, Petroscience, Normet, Kilborn, Borner, and Thompson.

Thompson Report

With respect to Thompson, Leach states at Exhibit 1328B page 85:

> viii. Thompson's study was aimed at understanding the distribution in alteration and not mineralization. Therefore, the samples she analysed were not representative of the core in which gold would have been expected as alleged by Strathcona, nor was her study comparable to that carried out by Borner.

ix. Contrary to the allegation by Strathcona, it would have been reasonable not to see gold in these samples since the samples Thompson analysed were not selected in order to find gold, nor were they of high enough grade in which gold would have been expected to be seen.

In cross-examination Leach was shown a fax (Exhibit 1253) from de Guzman to Thompson with a copy to Felderhof and Puspos dated April 26, 1996. Leach agreed that in fact Thompson was asked to also check for gold in all of the samples she looked at. It is of note that Thompson herself, as was the case with Leach, had no concerns with her findings.

Transcript: December 15, 2005, pages 30, 36
Transcript: April 6, 2005, pages 113-114

Red Flag 9 states there was no gold identified in 103 petrographic samples. Red Flag 9 states that these 103 samples were from the Southeast Zone. But in fact 53 are from the Central Zone and only 50 are from the Southeast Zone. Farquharson agrees there is gold in the Central Zone. Yet Thompson found no gold in the 53 samples from the Central Zone.

Farquharson was asked:

> And yet for the 53 samples from the Central Zone, a deposit which is known to contain gold, she find's no gold there either. If you are right, Sir, in that you always would find gold in petrographic samples from deposits that contain gold, can you explain to us why there was no gold in any of the Central Zone samples?

Farquharson answered:

> No, I can't. That's a good point Mr. Groia.

Transcript: April 6, 2005, pages 10-11

Farquharson testified anyone who read the Thompson Report and did not agree with Strathcona's views must have been negligent.

Yet Farquharson agreed Thompson had no concerns about her work.

Transcript: April 5, 2005, page 115
Transcript: April 6, 2005, pages 113-114

Dr. Kavanagh spoke to Thompson and satisfied himself that the gold was so erratically distributed that it might not be seen in the particular samples examined.

Transcript: March 8, 2005, pages 44-45, 63-69

Kelian

Kelian was a successful gold mine. Mr. Borner reported that the Busang samples that he examined matched "*the Kilean samples I have in my collection very closely in all ways.*" Farquharson conceded this evidence in cross-examination. Strathcona did not have a copy of this report before preparing their opinion but Farquharson testified it would not have changed Strathcona's view.

Transcript: April 5, 2005, pages 60-63

In Exhibit 600 Borner reports on "*Sample No. BRH-12 96.00-97.00*" where he states (at p.110825):

> Particles of visible gold are not exposed...Mineralization is almost identical to that seen at the Kelian deposit, also located at Kalimantan.

Although Borner who had more experience with Kelian then Farquharson makes a favourable comparison between Busang and Kelian, Farquharson does not.

No One Else Saw Red Flags

Felderhof was not a petrologist. Bre-X retained reputable experts in that area and relied on their work. Farquharson is not a petrologist but he purports to see red flags in the work of petrologists when they themselves do not.

Red Flag 10: The Excellent Sample Preparation Facility At Busang Was Under-utilized Despite Large Backlog of Core Waiting To Be Sampled

In the October 1997 letter Farquharson states:

> **10. An excellent sample preparation facility at Busang was under-utilized despite large backlog of core waiting to be sampled**
>
> We were impressed with the excellent sample preparation facility that had been erected at Busang but during the two weeks that we were there were equally impressed by the fact that the crew had nothing to do during our period of residence at Busang and no samples were given to them to process despite a very large backlog of drill core waiting to be sampled.

The O.S.C. position is set out in paragraphs 713-721 of Exhibit S5 Volume II and S10.

The Defence position is set out in paragraphs 285-286 of Exhibit S3 and S13.

This Red Flag is not found in the body of Strathcona's opinion Exhibit 681.

The O.S.C. position with respect to red flags not in Strathcona's opinion is found at page 177 of these reasons.

This is another alleged red flag that has more to do with best practices, with respect to which there may be different opinions, than with questioning the reliability of the reserve

calculations in the press releases which is what is relevant to Counts 5 to 8. See page 178 of these reasons.

Dr. Hellman

In Dr. Hellman's opinion this is not a red flag.

Exhibit 1202: pages 23, 56-57, 189

Dr. Hellman agreed with T. Showell of Normet. Dr. Hellman's opinion was that "*Segregation of gold during transportation is well known. The reason for having the samples prepared at IAL in Balikpapan was sound.*"

Exhibit 1202: page 57
Exhibit 748

No One Else Saw Red Flags

According to Farquharson this should have been a red flag for Kilborn and M.R.D.I. among others. It was not.

Exhibit S4: Appendix "B"

Red Flag 11: Only "In-Fill Samples" Designated as "Non-Mineralized" Could Be Prepared At Busang

In the October 1997 letter Farquharson states:

> **11. Only "in-fill samples" designated as "non-mineralized" could be prepared at Busang.**
>
> We queried why only "non-mineralized" samples were allowed to be crushed and prepared for assaying at Busang and the response was that they wanted to be sure there was no opportunity for "sample contamination" of the areas

considered likely to have potential for gold and that samples from those areas would only be treated by an independent laboratory.

The O.S.C. position is set out in paragraphs 722-724 of Exhibit S5 Volume II and S10.

The Defence position is set out in paragraph 287 of Exhibit S3 and S13.

This Red Flag is also not found in the body of Strathcona's opinion Exhibit 681. The O.S.C. position with respect to red flags not in Strathcona's opinion is found at page 177 of these reasons. This is also another red flag that has more to do with best practices then with questioning the reliability of resource calculations. See page 178 of these reasons.

Dr. Hellman

Dr. Hellman disagrees that this is a red flag at pages 23 and 57 of Exhibit 1202. In Dr. Hellman's opinion "*Strathcona provides no reason why this practice is a red flag. Streaming of mineralized and non-mineralized samples is a common practice in the laboratories to avoid cross-contamination. Impartial observers would commend this practice.*"

No One Else Saw Red Flags

According to Farquharson this should have been a red flag for Kilborn and M.R.D.I. among others. It was not.

Exhibit S4: Appendix "B"

Red Flag 12: All Sample Bags Delivered To Samarinda Had To Be Opened To "Check For Bag Breakage" and "Confirm Core Logging Description"

In the October 1997 letter Farquharson states:

> **12. All sample bags delivered to Samarinda had to be opened to "check for bag breakage" and "confirm core logging description"**
>
> We were astonished to hear on two or three occasions at Busang when the sample treatment process was being described that it was readily acknowledged that the sample bags were opened at Samarinda in order to check that there had not been any deterioration in the fiberglass bags during the few weeks that it took to get the samples from Busang to Samarinda and to allow Cesar Puspos, as the chief geologist, to have a final check on whether or not the core logs properly described the sample interval. It is, or course, standard practice in the industry that once a sample bag has been closed it should never be opened again until in the assay laboratory.

The O.S.C. position is set out in paragraphs 606-660 of Exhibit S5 Volume II and S10.

The Defence position is set out in paragraphs 207-219 of Exhibit S3 and S13.

Farquharson

Farquharson testified he was told in separate conversations with Alo and Ramirez, employees of Bre-X, that the sample bags were opened so a senior geologist could compare the core to the bags and to check for broken bags during the voyage down river.

Transcript: March 17, 2005, page 72

Farquharson testified it "*is absolutely contrary to normal practice in the mining industry*" to open sample bags.

Transcript: March 17, 2005, page 72

Dr. Kavanagh

Dr. Kavanagh also testified "*that normally sample bags going from a drilling prospect to a laboratory would be unopened.*"

Transcript: March 14, 2005, page 50

Dr. Kavanagh did not know the sample bags were being opened until after the fact in 1997.

Transcript: March 14, 2005, page 51

Dr. Hellman

Dr. Hellman's opinion is found at Exhibit 1202, pages 23, 49, 285. At page 49 Dr. Hellman states:

> **Strathcona Allegation**
>
> Strathcona alleges that, contrary to industry practice, the sample bags containing drill core were opened at Samarinda.
>
> **Opinion**
>
> There is no industry standard practice concerning opening of sample bags. There is no rule against opening sample bags in the JORC Code or in CIM Best Practices Guidelines. I have opened many sample bags to check that the number on the sample bag corresponds with that inside.
>
> Spot checking of sample numbers on the outside and inside of the bags would normally be regarded as an indicator of diligent and professional work. It is a green flag. From my experience, this part of the exploration effort requires checking and may be subject to transcription errors, sample mix-ups, obliteration of sample numbers and rupturing of bags.
>
> It would, however, be a matter of concern if it was known that every sample bag or even large numbers of bags containing core were being opened. An explanation would be mandatory. I am unaware of the evidence for Strathcona's allegation that "all sample bags opened". I was advised by Mr. Felderhof that he was unaware of this practice.

Dr. Hellman agrees with Farquharson that opening all or even a large number of sample bags is a matter of concern.

At paragraphs 611 and 612 of Exhibit S5 Volume II the O.S.C. states:

Para. 611. It is misleading for Hellman to offer this Court an expert opinion in 2005 under oath that spot checking is a green flag in light of evidence that he knew in April 1997 that all of the sample bags were opened.

Para. 612. Corbett and Leach told the participants at the April 11, 1997 Sheraton project meeting that the sample bags were sent to Samarinda where they were all opened and checked. Hellman's notes of that meeting state:

> Site → plastic bags (5cm lengths) 2m heavy duty plastic bags. A, B. (2m). Four bags into rice sack → Samarinda. Samarinda stored, open check (numbers erased sometimes), all opened checked re-numbered, truck to Samarinda...

The O.S.C. submission that Dr. Hellman knew in April 1997 that all sample bags were opened is based on Dr. Hellman's note above of what Corbett reported at the Sheraton project meeting.

There appears to be some inconsistency in Dr. Hellman's position but it is unclear from Dr. Hellman's note whether Corbett was talking about the outside and inside bags, which would be a concern, or just the outside bag which would not be a concern.

Leach

At paragraph 615 the O.S.C. states:

Para. 615. Leach contradicted Hellman by testifying that it would be a positive thing to have a policy or procedure that all the sample bags be opened. He also testified that such a policy would be established by Felderhof and de Guzman.

The Defence disagrees with the characterization of Mr. Leach's testimony by the OSC in this paragraph. This passage of evidence clearly establishes that Mr. Leach could not remember when he was told that all of the bags were opened at Samarinda. The Defence does not agree that it has been established that all of the bags were opened at Samarinda at all times. Mr. Leach's evidence was that opening the sample bags would be a reasonable thing to do if the bags suffered from condensation because of the humidity of the climate at Busang. Mr. Leach testified:

"A. ...but I mean I would think in that kind of environment that, I would think it would be quite a good policy to instruct, you know, the people knowing that that's the case, that the samples get, the labels get degraded because of the condensation. I would think it would quite reasonable to put into practice that that's what was done, you know, as a routine practice. To me it seems quite a reasonable thing to suggest".

Q. So you think it would be reasonable to have a policy of procedure that all the sample bags be opened?

A. Yeah. I think it would be quite a positive thing to do. And if you wanted to ensure that everything was in order before you sent it be assayed, then..." (Evidence of Mr. Leach, December 15, 2005, Volume 151 at pages 54-55)

Mr. Leach did testify that if such a policy was set up he thought it would have been Mr. De Guzman and Mr. Felderhof who would have established such a policy.

Leach's evidence appears to contradict Dr. Hellman, Dr. Kavanagh and Farquharson.

Leach testified he could not recall whether he was told that the sample bags were opened while he was at Busang although he agreed that it was evident from his report that in fact he was.

Transcript: December 15, 2005, at pages 48-49

Mihailovich testified he told Corbett and Leach at Busang that the sample bags were opened.

Transcript: May 12, 2005, page 43

Leach testified he did not recall any discussion at the Sheraton Project about open sample bags but agreed he would have been in the room and would have heard it.

Transcript: December 15, 2005, pages 47-48

Mihailovich

Alexander Mihailovich graduated as a mining engineer in 1996 and started to work for Bre-X in Samarinda in the middle of October 1996. He was in Samarinda for his first rotation which ended approximately on December 11 or 12, 1996. When he came back after Christmas he was transferred to Busang at the end of January or beginning of February 1997.

Transcript: May 12, 2005, pages 1-5, 56

Mihailovich's evidence was that after the fiberglass bags were taken off the truck, they were undone and the smaller clear plastic sample bags were taken out and they were lined up on the floor in the poolroom to match the sequence that they were taken out of the ground. If the photograph Exhibit 991 D is not clear, Mihailovich's evidence is quite clear that the inner sample bags, over which he would walk over to get to the dining room or bathroom, were open. The open inner sample bags were in plain view. Mihailovich described what the saw when he looked inside the clear plastic bags "*toward the top it was sort of a muddy uncongealed mess*" ... "*further down it was solid core of rock.*" He testified he saw the sample bags being removed from Samarinda. The open clear plastic bags were "*rolled back up, sealed, and placed inside the larger fiberglass bags and then...put back on the truck.*"

Transcript: May 12, 2005, pages 25-38

Finding

Contrary to the Defence submissions on August 28, 2006, pages108-128 there is direct evidence referred to above from Mihailovich that the inner sample bags were opened. I find that Mihailovich saw open inner sample bags.

Felderhof's Knowledge Of The Open Sample Bags

The O.S.C. states at paragraphs 629, 630, 631, and 649 of Exhibit S5 Volume II:

> Para. 629. Felderhof visited the Bre-X Samarinda office and either saw the open sample bags at Samarinda, knew they were being opened or ought to have known that they were being opened.
>
> Para. 630. Felderhof was in charge of Bre-X's Indonesian exploration program. He had an obligation to know the sampling procedure from the time the core came out of the drill until it reached the assay lab, and to ensure that it was in accordance with industry standards.
>
> Para. 631. Farquharson opined that as the person with the overall responsibility for the exploration programme, Felderhof should have looked at the sampling protocol at a very early stage and made sure that it was being carried out in accordance with generally accepted procedures for handling samples.
>
> ...
>
> Para. 649. It was common knowledge among Felderhof's staff that the sample bags were being opened at the Samarinda office. Everyone seemed to know except allegedly Felderhof.

At paragraph 643 the O.S.C. submission and Defence response are:

> Para. 643. Felderhof's own handwritten faxes prove that he was at Busang eight times after they stopped preparing samples at the Busang sample preparation lab and started sending the core sample bags to Samarinda. If Felderhof was at the Busang site, he had to have been aware that the core was only being broken up, placed in bags and closed with wire at Busang. Yet after the fraud was discovered, Felderhof told the public that he was only occasionally at Busang and not at all from August 1996 to February 1997. His own handwriting established that he was at Busang four times between August 1996 and February 1997.

My role in Bre-X's Indonesian operations

> As Bre-X's chief administrative officer in Indonesia (I was not "chief geologist"), **I was rarely in our Samarinda office and only occasionally on site at Busang.** I worked from Bre-X's Jakarta office, over 1000 miles away, where I was also responsible for overseeing 3 other Be-X projects. I never visited the warehouse at Loa Duri because it was my understanding that our warehouse was used only to store crusher rejects. **From August 1996 until February 1997,** I was primarily engaged in negotiations with the Indonesian government and potential suitors for the Company. **During this entire 6 month period, I did not have an occasion to visit Busang.** [emphasis added]

Our review of the evidence found that Mr. Felderhof visited Busang only once during the time period referenced by the OSC in this paragraph; he was there from February 7 to February 9, 1997 after the fire. In August 1996, there is a discussion of a trip in October 1996, but no evidence as to whether the trip was made. When read in full, it is clear that there is no misrepresentation in Mr. Felderhof's press statement. Mr. Felderhof was simply demonstrating that there were long gaps between his visits to Busang. In no way did he mislead the public about his visits to Busang in 1997 (Exhibit 90E, fax from Mr. Felderhof to Mr. Walsh, August 13, 1996, Exhibit 90E, fax from Mr. Felderhof to Mr. De Guzman, September 20, 1996, Exhibit 90F, fax from Mr. Felderhof to Mr. Tobing, February 6, 1997).

At pages 51 to 53 of Exhibit S4 the Defence states:

> An example of the OSC misconstruing the evidence is found in paragraph 643PR where they cite a press statement made by Mr. Felderhof on July 25, 1997 in relation to the issue of the opening of the sample bags. The OSC paraphrases the press statement, arguing that Mr. Felderhof "told the public that he was only occasionally at Busang and not at all from August 1996 to February 1997". They then imply that this statement is false as, according to them, Mr. Felderhof's handwritten notes establish that he was at Busang four times during that time period that the core sample bags were sent to Samarinda.

OSC Volume II, paragraph 643 PR

As the OSC provided no particular exhibit references, our review of the evidence found that Mr. Felderhof visited Busang only once during the time period referenced by the OSC; he was there from February 7 to February 9, 1997 after the fire. In August 1996, there is a discussion of a trip in October 1996, but no evidence as to whether the trip was made. When read in full it is clear that there is no misrepresentation in Mr. Felderhof's press statement, it reads as follows:

> *From August 1996* ***until*** *February 1997, I was primarily engaged in negotiations with the Indonesian government and potential suitors for the Company. During this* ***entire 6 month period****, I did not have an occasion to visit Busang.*

Exhibit 90E, Fax from Mr. Felderhof to Mr. Walsh, August 13, 1996
Exhibit 90E, Fax from Mr. Felderhof to Mr. de Guzman, September 20, 1996
Exhibit 90F, Fax from Mr. Felderhof to Mr. Tobing, February 6, 1997
Exhibit 709, Mr. Felderhof's Press Statement, July 25, 1997, page 3

The use of the words "until February 1997" coupled with the "6 month period" suggests that Mr. Felderhof was discussing the period August 1996 to January 1997. It also is clear that Mr. Felderhof was simply demonstrating to the public that there were long gaps between his visits to Busang. In no way did Mr. Felderhof mislead the public about his visit to Busang in February 1997 as the OSC is now striving to colour and interpret this evidence.

Exhibit 709, Mr. Felderhof's Press Statement, July 25, 1997, page 3

There is no direct evidence or persuasive indirect evidence that Felderhof was in Busang from August 96 until February 1997.

With respect to the knowledge of Felderhof and of the Bre-X board that the sample bags were opened the O.S.C. refers to Exhibit 198 (at paragraph 655-657), Exhibit 200 (at paragraph 658), Exhibit 202 at (paragraph 659) and Exhibit 709 at (paragraph 627-628).

Exhibit 198 are the minutes of the Bre-X board meeting dated March 29, 1997:

> Mr. Francisco enquired to Mr. Felderhof as to the possibility that sample bags were being opened in Samarinda. Mr. Felderhof was not aware of such, however he mentioned that he would follow up the matter.

Exhibit 198: page 55

Exhibit 200 is a memo to Francisco, dated April 13,1997 from MacDonald reporting on his investigation of sample handling in which he stated that he had not told Felderhof that he was told that sample bags were opened and that Cesar Puspos had lied to Felderhof when he told Felderhof sample bags were not opened except when they were broken.

Exhibit 200: pages 315-317

Exhibit 202 are the minutes of the Bre-X board meeting dated April 14, 1997 where Felderhof stated the bags were opened for the following reasons:

- During transportation, number written on the bag was erased, therefore to rewrite number on the bag (similar to tag inside) for control purposes;

- 10% of the bags were broken in transit

> Suggestions were also made that bags were opened to remove waste or to ensure that only mineralized core was sent for assaying. A discussion ensued as to Cesar Puspos' previous comments regarding this matter. Mr. Felderhof also questioned as to what the geologists were relating to and that it was impossible to "salt" all the samples.
>
> ***Mr. Felderhof also advised the participants that a copy of the sample preparation procedure from "cradle to grave" was forwarded to Calgary in April 1997.***

Exhibit 202: page 70

Exhibit 709 is the Felderhof press statement dated July 25, 1997:

> It was not until early April 1997 that I first learned that bags were being opened in Samarinda. Even then, I was told that only a small percentage of bags had been opened before delivery to the lab because they were damaged, or needed to be checked for legitimate reasons.

With respect to Red Flag 12 and 13, Farquharson agreed he could not give "*any evidence as to any date when this would have been evident to Mr. Felderhof*" but "*it's something he should have been on top of.*"

Transcript: April 6, 2005, pages 97-98, 103

Finding

The evidence reviewed above supports the position that Felderhof did not have knowledge that the sample bags were opened.

No One Else Saw Red Flags

Farquharson, testified Kilborn and M.R.D.I. among others should also have been on top of it "*if they had the same information as Strathcona received.*"

Transcript: April 6, 2005, page 103

M.R.D.I.'s scope of work included "*sample collection and preparation procedures*" and "*ore controls*".

Exhibit 505: page 5

Kilborn and M.R.D.I. did not raise this alleged red flag.

Red Flag 12 And Salting

Farquharson testified this red flag started sometime in 1995 when samples started to be sent to Samarinda rather then directly to Balikpapan from Busang. Strathcona's theory is that the salting occurred in Samarinda where the sample bags were opened before the

samples were sent to be assayed. It is not clear what Strathcona's theory is with respect to how the salting occurred before the sample bags were sent to Samarinda.

Transcript: April 6, 2005, pages 104-105

Brightest Red Flags

This O.S.C. bright red flag is listed by Farquharson as one of the four most striking areas of red flags in his re-examination. Yet it is not found in the body of Farquharson's opinion Exhibit 681. It is found only in an appendix (Appendix VII, the October 1997 letter). It is inconsistent and contradictory that this most striking red flag in testimony is not included in the body of the written opinion: it is not listed as one of the most striking areas of red flags (page 5), it is not found in the summary (pages 1-3), it is not found in the detailed discussion (pages 4-32). The O.S.C position with respect to red flags not included in Strathcona's opinion is found at page 177 of these reasons. See pages 173-178 of these reasons.

Red Flag 13: Despite A Large Accumulation of Samples At Samarinda No Samples Were Shipped Unless De Guzman or Puspos Released Them

In the October 1997 letter Farquharson states:

> **13. Despite a large accumulation of samples at Samarinda and assaying capacity available at Indo Assay, no samples were shipped unless Michael de Guzman or Cesar Puspos released the samples**
>
> This particular red flag was one that we became aware of at a later date but we did hear from John Irvin at Indo Assay Laboratories that frequently he had capacity and was waiting for samples and knew that there was a large accumulation of samples at Samarinda but they would not be released until they had been through the "final inspection".

The O.S.C. position is set out in paragraphs 725-728 of Exhibit S5 Volume II and S10.

The Defence position is set out in paragraph 288 of Exhibit S3 and S13.

This red flag is not found in the body of Strathcona's opinion, Exhibit 681. The O.S.C. position with respect to red flags not included in Strathcona's opinion is found at page 177 of these reasons.

Dr. Hellman

Dr. Hellman disagrees this is a red flag at pages 23 and 57-58 of Exhibit 1202. Dr. Hellman's opinion at page 58 states:

> It is standard industry practice for senior staff to authorize the dispatch of samples. This is not a red flag and would normally be commended as a demonstration of management control.
>
> Strathcona also did not like IAL having capacity for sample preparation whilst Samarinda had a large accumulation of samples. This may not have been ideal, but these situations happen in the context of a large drilling program. It is hardly a red flag. I have worked on projects where a large backlog of samples occurred.

Exhibit 1202: pages 23, 57-58

Red Flag 14: Poor Reproducibility Of Assays

In the October 1997 letter Farquharson states:

> **14. Poor reproducibility of assays**
>
> All of the laboratories that have done test work for the metallurgical investigations and the check assays that have been done for Barrick, Placer Dome etc, have indicated problems in reproducing assays from the same

sample and while coarse gold always does present some problem in attaining acceptable reproducibility the variations at Busang were extreme.

The O.S.C. position is set out in paragraphs 729-755 of Exhibit S5 Volume II and S10.

The Defence position is set out in paragraphs 289-295 of Exhibit S3 and S13.

Strathcona's retailed analysis is found in Exhibit 681, pages 30-32.

Dr. Hellman

Dr. Hellman's opinion is that this is not a red flag.

Exhibit 1202: pages 19-20, 23, 58, 190-207

At pages 206-207 of Exhibit 1202, Dr. Hellman concludes:

> The repeatability of the Busang assays was a simple outcome of the presence of coarse gold. Although analyses and reviews of the repeat assays had been made by a number of experts such as Mr. Irvin of IAL, Mr. Seidel and Colombo of Hazen, comments from these people were that the results were **typical** (Colombo) [107], Hazen, 3/12/1996) [95], **expected** (Seidel) [108], (Hazen, 10/06/1996) [109] and **similar to other mineralization** (Irvin, IAL, 10/6/1994) [99].
>
> Mr. Hearse of Normet stated:
>
> "It should be noted that it is consistent with the difficulties a nearby gold project experienced with head assays where, despite great efforts to estimate the head grade accurately, the head grade of the orebody was significantly underestimated. The mineralogy of the Busang orebody has much in common with that orebody." (11/11/1995) [110]
>
> The nearby orebody referred to by Mr. Hearse was Kelian. Thus, Mr. Felderhof had received confirmation from numerous experts that the problems of obtaining good agreement between the duplicate assays were typical and similar to Kelian. None expressed the views of Strathcona or issued any warnings.
>
> Late in the project, two well-known Canadian laboratories, Chemex and Acme, undertook approximately 580 screened assays of samples from the South East Zone (Kilborn, 31 March, 1997) [104]. Neither they, nor Kilborn who reviewed

and reported on the data, expressed any concerns or advised that the results were in any way irregular or suspicious.

In early 1997 (18 February, 1997, pp 395-400) [112], the results of the Barrick check assay program were reported by Mr. E. M. Puspos. The mean value based on 214 pulp residues for Lakefield by screen fire assay is 3.09 g/t and by IAL using cyanide is 3.02 g/. The scatter plot provided shows good agreement. A similar good agreement was achieved using crusher rejects. Overall, Lakefield reported grades higher than IAL by 4.29%.

The analysis of these types of studies is typically done by specialists such as Kilborn. It is appropriate for a person in the position of Mr. Felderhof to defer to such specialists.

Kilborn did not see a red flag.

Indo Assay Laboratories

In Exhibit 692, 696, and 701, I.A.L. raised issues about assay results but then continued in each exhibit to analyze the situation and to resolve it.

Cyanide Leach Method

In Exhibit 1427, dated August 9, 1994 in discussing reproducibility, I.A.L. recommended a larger sample size "*either by cyanide leach...or by screened assay.*" Felderhof responded on October 3, 1994 (Exhibit 1037, Tab 453) and directed I.A.L. to switch from the fire assay method to the cyanide leach method of assay. In Exhibit 1202, page 190, Dr. Hellman states "*Felderhof used a cyanide leach technique on a large sample size. In doing so, he was following one the world's best known sampling experts Mr. Francis Pitard...*"

M.R.D.I.

In Exhibit 505, page 7, dated December 2, 1996, M.R.D.I. wrote that the "*cyanide leach method to estimate gold is not industry standard*" and recommended "*a comprehensive random check program...by metallic screen fire assay...to validate the cyanide leach results.*" M.R.D.I. made a recommendation but was not alleging a red flag. See page 178 of those reasons.

At page 6, M.R.D.I. noted "*a relatively wide dispersion of results*" between cyanide leach assays and fire assays. M.R.D.I. noted this but does not say this is a red flag.

M.R.D.I. also concluded the Bre-X work at Busang was "*of a high industry standard.*"

Check Assay Program

In Exhibit 1202, page 200, Dr. Hellman sets out the comprehensive check assay program undertaken by Kilborn in early 1997. Dr. Hellman reported Kilborn's conclusion: "*The standard deviation and variance observed in the analysis of the database is consistent with previous test work done on Busang samples and is typical to other gold ores where coarse free gold is known to occur.*"

Exhibit 1202: Figure 44

At page 201 of Exhibit 1202 Dr. Hellman states:

> 332 reject samples obtained from Loa Duri in December 1996 by Barrick were check assayed at Lakefield by screen fire assaying. The Lakefield assays were commissioned by Barrick as part of their evaluation of Busang. The scatter plot is provided in Figure 44. The correlation coefficient is high at 0.92 which indicates a significant correlation as is reflected in the scatter plot.

Farquharson would not agree that a 92% correlation between the Barrick results with respect to the crusher rejects and the Bre-X results was "*a very high correlation*".

Farquharson could not answer whether he was *"aware of any deposit where there is a correlation in excess of 95%."*

Farquharson was not "*aware of any literature that suggests that a 92% correlation is statistically out of control.*" Farquharson was not "*aware of what the threshold would be for the repeatability to be statistically out of control.*"

Transcript: April 5, 2005, pages 48-49

Exhibit 756 was marked for identification during Farquharson's cross-examination.

Exhibit 756 is Figure 44 in Exhibit 1202 marked as an exhibit in Dr. Hellman's evidence.

No One Else Saw Red Flags

Bre-X retained experts and relied on their expertise I.A.L., John Irvin, Hazen, Normet, Kilborn and M.R.D.I. did not see red flags.

Barrick And Placer Dome

Red Flag 14 refers to check assays done for Barrick and Placer Dome as examples of this red flag.

Farquharson testified:

> And when one has coarse gold as Busang was reported to have, there can be a problem in getting good reproducibility of assays from the same sample interval. But we had never seen the extremes in the variation between the first and second sample as reported by Barrick and Placer Dome working on the material that they had been given by Bre-X.

Transcript: March 17, 2005, page 60

Farquharson, with hindsight, saw this as a red flag. Barrick and Placer Dome did not. They continued to pursue Bre-X and Busang. My very definite impression from Peter Munk's evidence, given Barrick's expertise and knowledge of Busang, was that Barrick did not need Mr. Farquharson's assistance (with respect to this Red Flag 14 and the next Red Flag 15) in looking after what was in Barrick Gold's best interests. I have more confidence in Barrick than in Strathcona. See pages 197-208 and 339 of these reasons.

Red Flag 15: Screen Analyses of Sample Rejects Indicate Almost All Gold in Plus 106 Microns (150 Mesh) Fractions

In the October 1997 letter Farquharson states:

> **15. Screen analyses of sample rejects indicate almost all gold in plus 106 microns (150 mesh) fraction**
>
> One of the first items of documentation that we received before leaving Toronto was some assay results of samples taken by Barrick. We had never seen such a distribution of gold before because all of the gold was located in a particular coarse fraction and for a primary deposit, such as Busang was reported to be, the gold should have been distributed throughout all size fractions.

The O.S.C. position is set out in paragraphs 756-758 of Exhibit S5 Volume II and S10.

The Defence position is set out in paragraphs 296-305 of Exhibit S3 and S13.

Exhibit 748

In Exhibit 748 dated December 4 1996 Ken Thomas of Barrick reported in an internal memo that:

> The four metallurgical composites were assayed by Hazen on the 2 Dec. 1996 at the request of Barrick. The results, which are attached, are surprising; note the gold is concentrated in the +150 mesh even after extensive crushing and pulverizing. The results are even more surprising when people remark they have not seen free gold (note duplicate tests for each zone, pages 5 to 12, giving significantly different results).

Exhibit 748

Barrick continued to pursue Bre-X and Busang after this report and Munk never suspected the gold estimates at Busang.

Exhibit 494

Farquharson was cross-examined on the Hazen Report (Exhibit 494) on which the Barrick report (Exhibit 748) is based.

Farquharson testified that in Exhibit 494 Hazen reported to Barrick among other things that the "*assays also show considerable variation in plus and minus 150 mesh gold content and indicate a fairly broad range of gold particle size.*"

Farquharson conceded that Hazen indicated there was a fairly broad range of gold particle size. Hazen did not say it was "*an a-typical range or a range to be worried about.*" Farquharson agreed "*that exhibit 494 contains no indication that Hazen saw a red flag in the plus/minus results.*"

Transcript: March 31, 2005, pages 63-64

Farquharson conceded that 7 of 8 Hazen samples are opposite to Red Flag 15 and only 1 of 8 supports Red Flag 15.

Transcript: March 30, 2005, pages 9-10

Exhibit 408

To reconcile Hazen's test results with Red Flag 15 Strathcona relied upon the Lakefield results attached to Exhibit 408. Farquharson conceded Strathcona "*didn't do any statistical analysis*" of the Lakefield results and Farquharson agreed "*all Strathcona did was flip through these charts and eyeball them.*"

"All of the Gold"

Farquharson could not say what percentage of the samples in Exhibit 408, "*50% or 60% or 90%*" support Red Flag 15 because Strathcona had not done the analysis, but Red Flag 15 states "*all of the gold was located in a particular coarse fraction.*" Farquharson also conceded that if the percentage "*is much lower than say 80 or 90%*" than Strathcona's statement "*would not be correct.*"

Transcript: March 30, 2005, pages 9-11, 20, 28-31

On March 30, 2005, page 29 Farquharson conceded that 80% is "*a little bit short*" of the statement in Red Flag 15 referring to "*all of the gold.*" Although on April 4, 2005, pages 8 and 9, Farquharson defended 75% for some of the drill holes as "*still a substantial majority of the gold.*" But in any event the reference in Red Flag 15 is "*all of the gold*" and not 80% nor 75% nor a "*substantial majority of the gold.*"

Farquharson testified that in reviewing Exhibit 408 he was looking at "*the high grades in the +150 mesh material versus the very low grades in the –150 mesh material*"

Farquharson then conceded:

MR. GROIA: But your red flag number 15, Mr. Farquharson, to be fair, you will have to agree, has nothing to do with grades and has everything to do with weights of the total gold, right?

MR. FARQUHARSON: Yes.

MR. GROIA: And also to be fair, you will have to agree that when you made the statement that almost all the gold, or all the gold could be found in the +150, you had no basis because Strathcona hadn't done the work to be able to make that statement?

MR. FARQUHARSON: It was a statement made upon the visual observation of these assay results.

Transcript: March 30, 2005, pages 29-30
Transcript: April 4, 2005, pages 8-9

Dr. Hellman

In Dr. Hellman's opinion this is not a red flag.

Exhibit 1202: pages 23, 58-59, 202-207

Dr. Hellman's opinion at page 205 Exhibit 1202 states that Hazen's "*assay results demonstrate that the majority of the gold was in the fine fraction and not in the coarse fraction.*" At page 59 Dr. Hellman states:

> The role of consulting groups such as Hazen, Kilborn and Normet is to interpret the screen fire results because they aid in the metallurgical understanding of their clients' ores. None of these groups, as well as IAL, expressed any concern with the results from Busang.

Exhibit 1202: pages 205, 59

No One Else Saw Red Flags

Neither Kilborn, Hazen, Normet, nor I.A.L. saw a red flag. Bre-X retained experts and relied on their expertise.

Barrick

As with Red Flag 14, Farquharson refers to Barrick's test results in Red Flag 15. Farquharson saw red flags in those results while Barrick did not. Barrick continued to pursue Bre-X and Busang. Peter Munk "*cried*" when he heard that Bre-X was given to Freeport. Peter Munk did not suspect the gold estimates at Busang until Freeport's negative results in March of 1997. His reaction was "*disbelief and horror*". As noted above in the discussion of Red Flag 14 I have more confidence in the expertise of Munk and Barrick than in the expertise of Farquharson and Strathcona. See pages 197-208 and 335 of these reasons.

Transcript: December 7, 2005, page 65
Transcript: December 8, 2005, page 129

Red Flag 16: Mineralogical Studies Identified Gold In Metallurgical Samples As Being "Coarse, Rounded And With Gold-Rich Rims"

In the October 1997 letter Farquharson states:

> **16. Mineralogical studies identified gold in metallurgical samples as being "coarse, rounded and with gold-rich rims"**
>
> This particular red flag had received much attention in the press and we were certainly not the first to point it out. In fact, we were the fourth group to have commented on this. Included in the feasibility studies assembled by Kilborn were mineralogical studies carried out by Hazen Research in Colorado and Roger Townend working for Normet in Perth, Australia and both identified the nature of the gold which an observer with a gold industry background should recognize as being placer gold in origin. Freeport made the same observations and we confirmed the nature of the gold with our work at Lakefield.

The O.S.C. position is set out in paragraphs 759-799 of Exhibits S5 and S10.

The Defence position is set out in paragraphs 191-206 and 306-324.

Strathcona's detailed analysis is found at pages 17-20 of Exhibit 681.

Dr. Hellman

Dr. Hellman's opinion is that allegation 16 is not a red flag.

Exhibit 1202: pages 18, 23, 47-49, 130-157, 208-216

Dr. Hellman states at pages 47-48:

> Ms. Martha Schwartz (Hazen), Dr. Roger Townend (Townend) and Mr. John Borner (Mintek) all studied gold grains from Busang. The mineralogical studies at Busang exceeded industry norms.
>
> The shape and texture ("morphology") of gold particles from Busang is presented in this allegation as being alluvial in character. Gold obtained from gravity concentrates is alleged to be "mostly rounded with beaded outlines". This conjures up an image of marbles or beads of gold similar to river-rounded cobbles. The quote purports to summarise the work of Dr. R. Townend, a consulting mineralogist, who produced a 22-page report in June 1996 on metallurgical samples from the CZ and the SEZ. The description quoted above, however, was never used by Dr. Townend who, out of 10 grains, identified only one grain as "beaded" and another grain as "rounded".
>
> Dr. Townend described only two grains from the SEZ. Both have a morphology that would not normally be considered characteristic of alluvial grains, even using over-simplified criteria. For example, the grains from the SEZ are small (50 by 15 microns and 70 by 20 to 5 microns) in comparison to others from the CZ. They also have somewhat delicately preserved features and are described as silver-rich.
>
> The use of the term "beaded" appears to be unprecedented in the geological literature and has a meaning that can only be gleaned by reference to the actual microphotograph of the grain. The grain appears nearly identical to gold found in outcropping hard-rock carbonate base-metal veins from the Wau district of Papua New Guinea. The beaded gold grain was described as silver rich. This, together with its shape and small size, suggests that an alluvial origin is unlikely.
>
> None of the mineralogical specialists described the gold grains as "alluvial" and none issued a warning that the microscopic appearance of the grains was incompatible with a primary hardrock origin of the Busang mineralization.

There is a large overlap of gold grain morphologies in primary and alluvial environments. Gold grain morphology is largely undiagnostic of the origin of the gold. Many of the same descriptions are used for both primary and alluvial grains.

Gold rich rims are not only present in alluvial gold grains, but also in gold grains from supergene (in-situ) environments and have been documented in a diverse range of environments including those found in Papua New Guinea, Ghana, Gabon, Brazil, Mali, USA and Australia. Gold rich rims are not diagnostic of alluvial gold.

All the gold grains studied by Dr. Townend and Ms. Schwartz came from the samples that had been pulverized in grinding circuits. Modification of gold grains due to grinding is well known to result in the substantial modification of the original shapes. Such modified shapes include folding and rounding.

Even after the doubts about Busang had surfaced and after studying the mineralogy of numerous gold grains from Busang, Lakefield, which is one of Canada's best known mineral analytical laboratories stated (July 28, 1997):

> "Gold grain morphology in the Crusher Rejects can not be used solely as an adequate measure to determine "origin" or prove that the gold was placer and surreptitiously added to the sample, especially if the sample had undergone any form of comminution." (p 5)

The fact that the most qualified persons in terms of being "*observers with a gold industry background*" and having petrological and mineralogical expertise did not recognize the gold as being of "*placer origin*" should demonstrate that the mineralogical characteristics of the gold did not constitute a red flag.

Exhibit 1202: Page 211, Table 2

In paragraphs 796-799 of Exhibit S5, Volume II, the O.S.C. submits Dr. Hellman changed his evidence about Table 2 entitled "*Example of Deep Oxidation from Bre-X Geological Logs.*" After being cross-examined on the actual wording in the logs, which differed from the wording in Table 2, Dr. Hellman testified that his chart did not have "*an exact transcription of the drill logs*" although he added that was "*of no consequence.*" He testified "*I don't think I took that to be an exact transcription of that interval. I was*

focusing on the examples of deep oxidation and the comments are there." The chart and text of the opinion should have been clearer.

Transcript: November 14, 2005, pages 43-57
Exhibit 1202: pages 210-211

Thalenhorst

Farquharson had to be asked twice before he agreed with Henrik Thalenhorst's view that "*[t]he occurrence of spherical gold per se does not constitute a red flag.*" Thalenhorst was one of the authors of Strathcona's Busang Technical Audit, Exhibit 208.

Transcript: March 31, 2005, pages 15-16

With respect to gold with beaded outline Farquharson conceded the following:

> MR. GROIA: So the evidence you just gave me a moment ago about why the beaded outline was significant is exactly the reference that Mr. Thalenhorst said was not a red flag, right?
>
> MR. FARQUHARSON: Correct.
>
> MR. GROIA: So now you are disagreeing with Mr. Thalenhorst in attempting to come up with another somewhat red flag, I guess I will call it?
>
> MR. FARQUHARSON: No. I will bow to Mr. Thalenhorst's opinion here.

Transcript: March 31, 2005, page 39

Farquharson

Farquharson agreed "*that placer gold can sometimes look very different than spherical rounded grains.*"

Transcript: March 31, 2005, page 18

Oxidation could result in gold rich rims. On cross-examination Farquharson agreed that Townend's report had reference to oxides although in his view "*the oxidation process has not been very thorough and gone on for a long period of time.*"

Transcript: March 31, 2005, pages 23-28

Lakefield

Although Lakefield was retained by Strathcona to do a mineralogical examination and although Farquharson refers to Lakefield in Red Flag 16, Farquharson disagreed with Lakefield when they stated:

> Gold grain morphology in the Crusher Rejects cannot be used solely as an adequate measure to determine "origin" or prove that the gold was placer and surreptitiously added to the sample, especially if the sample had undergone any form of comminution.

Exhibit 749: page 5

On March 30, 2005, page 47, when cross-examined with respect to this disagreement with Lakefield, Farquharson testified:

> MR. GROIA: In other words, you cannot tell if this was Placer gold that was salted based on these test results, right?
>
> MR. FARQUHARSON: That's what that sentence says there.
>
> MR. GROIA: Pretty loud and clear it says that, right?
>
> MR. FARQUHARSON: Yes.
>
> MR. GROIA: Loud and clear enough to be a red flag to Strathcona in its attempting to determine if these gold samples were Placer samples that had been used to be salted?
>
> MR. FARQUHARSON: We don't agree with this particular statement.

MR. GROIA: Strathcona disagrees with Lakefield?

MR. FARQUHARSON: Yes, on that statement.

At pages 50, 57 and 121, Farquharson agrees with the statement that "*nothing Lakefield or anyone else can say will persuade you that you might be mistaken.*" Farquharson disagrees with Lakefield although he agrees at pages 36 - 37 that "*Lakefield is a very well known and well respected laboratory.*"

As stated earlier at pages 216-217 of these reasons Farquharson did not refer to Lakefield's statement which contradicts Farquharson's opinion in the body of Strathcona's opinion Exhibit 681 as would be expected from an expert in possession of a contradictory opinion from someone retained by the expert himself.

The October 1997 letter is Appendix VII to Exhibit 681 and it set out the red flags. Red Flag 16 makes reference to Lakefield. There is no indication there of Lakefield's contradictory statement. In fact it indicates Lakefield's work was confirmatory:

> Freeport made the same observations and we confirmed the nature of the gold with our work at Lakefield.

Exhibit 681
Transcript: March 30, 2005, pages 36-37, 47, 50, 57, 121

Experts Retained By Bre-X

With respect to the mineralogical studies done for Bre-X, Farquharson testified:

> MR. GROIA: Can you agree with me that having four separate series of mineralogical studies was at or above industry standards for an exploration property?

MR. FARQUHARSON: It would be acceptable, in line with industry standards.

...

MR. GROIA: And so can you tell me, based on your experience, what would the norm be for a project such as this?

MR. FARQUHARSON: Normally one would do a petrological study on the drill core, on thin sections from the drill core which would be similar to what Borner and Thompson did. And then one would do mineralogical studies on the products recovered from the metallurgical test work which was what was done by Townend and by Schwartz.

Transcript: April 4, 2005, page 2

Farquharson also refers to Roger Townsend, Normet, Hazen and Kilborn in Red Flag 16 as if they were of the same view as Strathcona but they were not. They did not see a red flag. Farquharson testified with respect to what Townend, Normet, Schwartz and Hazen reported or, more to the point, did not report about this allegedly obvious red flag:

MR. GROIA. And so what you are saying is that to an experienced petrologist and metallurgist like Mr. Townend it would have been perfectly obvious to him that he was looking at alluvial gold. In other words, he was looking at a salted sample, right? A powerful red flag that would have been obvious to anybody having the experience of Mr. Geologist, right?

MR. FARQUHARSON: Yes.

MR. GROIA: And you know, of course, Mr. Townend said no such thing, right?

MR. FARQUHARSON: He described the gold that was in the samples that he was given to analyze and left it at that.

...

MR. GROIA: So you think that if Mr. Townend had found shavings of gold from jewellery he would have just said this is what I found, no need to worry about it?

MR. FARQUHARSON: He might well have.

MR.GROIA: You are actually suggesting to this Court that a respected petrologist or metallurgist who found gold shavings in a sample that was submitted to him from a hard rock deposit would say nothing about it to the people involved in the property. That's your evidence?

MR. FARQUHARSON: No.

MR. GROIA: Well you just said that, Mr. Farquharson.

MR. FARQUHARSON: Obviously if there is something as dramatic as shavings from jewellery then he would have done what the Lakefield people did which was described that as shavings from jewellery.

MR. GROIA: I am going to suggest to you, Sir, that any petrologist or metallurgist who was aware of a sample that even had the slightest hint of tampering or salting is going to make that known loud and clear to everyone who will listen to them. Isn't that the standard in the industry?

MR. FARQUHARSON: It should be.

MR. GROIA: Do you have any reason to doubt that Mr. Townend would have done that if he even suspected the possibility of salting?

MR. FARQUHARSON: No, I have no reason to doubt it.

...

MR. GROIA: Well I am suggesting to you, Sir, that your statement a few minutes ago that Mr. Townend would not scream loud and long if he suspected there was salting is simply incorrect, right?

MR. FARQUHARSON: If there was something in there that struck him as being very unusual such as jewellery shavings, I am sure he would have done exactly what Lakefield did and say I found shavings of jewellery in the core.

MR. GROIA: And if he thought the gold rich rim was a powerful red flag indicating a problem, he would have done the same thing, right?

MR. FARQUHARSON: Well that's not as dramatic as finding shavings from jewellery obviously.

...

MR. GROIA: So just as was the case with M.R.D.I., he will have to answer for his failure to point out this powerful red flag. Is that your evidence?

MR. FARQUHARSON: I don't think it is up to the petrographer or the mineralogist on something like this to start raising questions other than describing the gold that he has found in the samples. And I think Hazen did the same, without having looked at their report. They described the nature of the gold, but they didn't say that this can't be.

MR. GROIA: Well would you at least agree with this, that if Mr. Townend didn't report it and Martha Schwartz didn't report it, they are both, as far as you are concerned, negligent for not having observed the red flags, or grossly irresponsible for not having mentioned it?

MR. FARQUHARSON: No. I think they did their job. They described the gold. And it's up to those that are familiar with the deposit and the geology to determine whether or not that looks reasonable.

MR. GROIA: So your view continues to be that if Lakefield suspected salting in a deposit on samples that it was sent from somebody telling them these were legitimate samples, Lakefield would just describe what they saw and say no more. That's your evidence, right?

MR. FARQUHARSON: That they would describe the gold rich rims and they would leave it up to the reader to take it from there.

Transcript: March 31, 2005, pages 24, 29-33

It is difficult to accept that a petrologist or mineralogist or metallurgist working on what was thought to be potentially one of the world's largest gold deposits (Red Flag 20) would not comment on finding placer gold in a hard rock deposit. With respect to leaving it "*to those familiar with the deposit*," certainly Kilborn and also Hazen and Normet and most of those reading the reports were familiar with the deposit and raised no red flag. At one point above Farquharson testified that it should be the industry standard for "*any petrologist or metallurgist*" at "*the slightest hint of tampering or salting... to make that known loud and clear...*" and that he had "*no reason to doubt*" that Townend would have done that. Townend raised no red flag.

No One Else Saw Red Flags

As noted neither Townend, Normet, Schwartz, Hazen nor Kilborn raised any concerns. Quite the opposite was the case. Exhibit 768 is a fax from Normet to Felderhof, Walsh, and Bre-X dated April 6, 1997 which unequivocally states that Normet "*never had a question about the authenticity of the samples nor have we ever inferred the presence of alluvial gold in the samples.*"

Felderhof was neither a petrologist nor a mineralogist nor a metallurgist. Bre-X retained reputable experts in those areas and relied on their work. Farquharson is neither a petrologist nor a mineralogist nor a metallurgist but he purports to see red flags in the work of others who are the experts when they themselves do not.

Red Flag 17: Metallurgical Testwork Indicated More Than 90% Gold Recovery In Gravity Concentrates Of One Percent To Six Percent Of Feed

In the October 1997 letter Farquharson states:

> **17. Metallurgical testwork indicated more than 90 percent gold recovery in gravity concentrates of one percent to six percent of feed**
>
> When reviewing the Kilborn feasibility study in the hotel room in Jakarta on our first day there this particular item caught my attention and I initially thought that there must be a typographical error but both Hazen and Normet commented on the remarkable ease with which the gold could be recovered in a gravity concentrate. In the case of the Hazen report only one percent of the millfeed would be required to drop into a gravity trap to recover more than 90 percent of the gold and this was a characteristic that we had never seen nor has anyone else in a so called "primary deposit".

The O.S.C. position is set out in paragraphs 800-820 of Exhibit S5 Volume II and S10.

The Defence position is set out in paragraphs 325-337 of Exhibits S3 and S13.

Strathcona's analysis is found in Exhibit 681, pages 25-28.

Dr. Hellman

In Dr. Hellman's opinion this is not a red flag.

Exhibit 1202: pages 19, 23, 59-60, 217-251

Starting at page 59 Dr. Hellman states:

A. Allegation regarding gravity recoveries

Strathcona (3 May, 1997) [6] is quoted to the effect that no one has seen a gravity recovery of 90% that was achieved for Busang. Also (p 113, para 7), Strathcona asserts that Kelian, the mine that Mr. Felderhof used as an analog for Busang, did not even build a gravity circuit into their process plant.

Opinion

The definitive Pilot Plant trial based on a 27-tonne sample showed that only 49% of the gold was gravity recoverable. Furthermore, Strathcona is incorrect about Kelian. The mine had five Knelson concentrators with a gravity recovery (-40%) similar to that predicted from the Busang Pilot Plant Test and produced big slugs of coarse gold. The reason why the operators at Kelian did not build a gravity plant, at the start, was due to a mistake. Kilborn and Normet were well aware of this.

B. Allegation regarding metallurgical characteristics of the gold being incompatible with those from a "primary" deposit

It is alleged that metallurgical information available to Mr. Felderhof was inconsistent with what would be expected with gold from a primary gold deposit.

Opinion

This allegation disregards the testwork results that were consistent with Busang having hard-rock characteristics, such as the 49% gravity recovery from the 27-tonne pilot plant and the tests that showed increasing recovery with increased grinding.

If this was true, the metallurgical experts, whose companies had a combined experience that exceeded 500 man-years of experience, would have been the first to comment. Normet, Kilborn and Hazen, who were all well-known and respected

metallurgical groups, reported nothing suspicious about Busang's metallurgy. Is Mr. Felderhof expected to know more metallurgy than the metallurgical experts?

Dr. Hellman's statement that the Pilot Plant trial "*showed that only 49% of the gold was gravity recoverable*" relied on Kilborn's February 1997 monthly report. But as the O.S.C. points out Exhibit 651 the Pilot Plant Trial report states (page 0023) that the "*Overall Trial*" "*Total Gravity Gold %*" is 49% but the "*Grind Without Cyanide*" in 74% and the "*Grind With Cyanide*" is 32%. Kilborn continued to refer to the 49% "*recovered as gravity gold*" in several reports after the Pilot Plant Trial conducted by Normet and Dr. Hellman relied on Kilborn's statements.

Exhibit 660 Normet Report –90% Recovery

Farquharson agreed he found the Normet report Exhibit 660 alarming because of the remarkable 90% recovery. Farquharson also agreed no red flags were being raised by the authors of the report nor could Farquharson point to any one of all the people that saw that report that share Strathcona's view.

Farquharson agreed that he did not have as much metallurgical training as the metallurgists at Normet. Farquharson agreed that if a metallurgist saw something "*out of whack*" that he would expect them to say so. Farquharson would have expected Normet to say something to Kilborn or Bre-X if there was something "*out of whack.*"

Transcript: March 31, 2005, pages 61-63

Farquharson agreed that it was such a strong red flag that the metallurgists at Normet "*would have just about fallen off their chair when they got the results*", but "*they appeared to have been completely oblivious to what was going on*" and *"[i]t did not seem to register with them that they were getting such unusual results.*" The results were unusual for Farquharson but not for the experts that conducted the tests.

Farquharson testified the people at Hazen and at Kilborn should have been shocked and if M.R.D.I. looked at the feasibility study they also should have been shocked.

No one was shocked and no one saw red flags.

Transcript: April 6, 2005, pages 62-63

In Exhibit 681 Strathcona states that the 90% recovery "*was a characteristic that we had never seen nor has anyone else in a so called 'primary deposit'.*" On cross –examination Farquharson conceded that the statement "*nor has anyone else*" is a "*strong*" statement which Strathcona "*would like to take back*".

Transcript: April 6, 2005, pages 47-48

In Dr. Hellman's opinion under the sub-heading "*Predicted vs. Actual Gravity Recoveries*" he states "*that it is unreasonable to expect the testwork from Knelson concentrators in well-controlled laboratory conditions to be a good estimator of actual results from operations.*"

Exhibit 1202: page 249

Pilot Plant Study

Strathcona did not discuss the gravity test results from the pilot plant study in their expert opinion, Exhibit 681. Farquharson testified Strathcona focused on the 90% laboratory results that raised Red Flag 17.

Farquharson testified that if Strathcona had had the pilot plant results at the time of their opinion, Exhibit 681,that Strathcona "*would have had to explain why these results... are not comparable to the laboratory results.*"

It was then pointed out to Farquharson that in fact the Pilot Plant report was listed in the References to Exhibit 681(at page 35, Exhibit 651) and Farquharson agreed "*[t]herefore, we had it.*"

Transcript: March 29, 2005, pages 65-70

Amalgamation Tests

Amalgamation tests reported by Oretest in Exhibit 587 did not show the free gold that would be expected where salting occurs and gold is added to samples. Farquharson testified "*I don't have an answer for that*" and agreed it was a "*mystery.*"

Transcript: March 22, 2005, pages 26-27

The Oretest amalgamation test Exhibit 587 were not included in Strathcona's opinion Exhibit 681. Although Farquharson agreed "*the best and most reliable indicator of the amount of free gold is the amalgamation test.*"

Transcript: March 22, 2005, page 25

With respect to amalgamation test as reported in the Normet report Exhibit 659 Farquharson testified "*I don't have a good explanation for them.*" He agreed the reports presented a "*conundrum*" to Strathcona. He testified "*[w]hen I read that it was a puzzle.*" Farquharson did not feel Strathcona needed to do further work to get to the bottom of the puzzle because he did not think it had any relevance to Strathcona's various assignments. But one of Strathcona's assignments is set out in Exhibit 208, page 51. "*[w]e have spent some time considering how the tampering process could have occurred...*" and Strathcona's theory is that the tampering occurred by adding free gold and amalgamation tests are relevant to testing for free gold.

Transcript: March 31, 2005, pages 50-51

Coarse Gold

Farquharson agreed that two important tests for coarse gold, the amalgamation test and the pilot plant test were not included in Strathcona's reports.

Transcript: March 29, 2005, page 69

At page 19 of Exhibit 1202 Dr. Hellman states:

> The ***fourth Strathcona assertion*** is that the metallurgical gravity recoveries would be unachievable for, and incompatible with, a hardrock gold deposit.
>
> The most definitive studies that relate to the core of the red flag allegations were two metallurgical tests. These were a mercury amalgamation study of CZ gravity gold in 1995 and a 27-tonne pilot plant test on drill-core material from the SEZ in late 1996. To any impartial observer, the results from both of these studies are incompatible with the gold being alluvial.
>
> **Although the results from both of these studies unequivocally disprove a central part of the red flag allegations, neither result was mentioned by Strathcona.** Strathcona, however, refers to documents that detail the results of both these studies.

Kelian

Farquharson agreed that "*Felderhof regularly held up the Kelian model for a comparison to Busang*" and that it was "*extremely important... for Strathcona to understand as much as it possibly could about the Kelian property.*"

Transcript: March 29, 2005, page 58

With respect to Kelian, Strathcona reviewed an extract from a dated feasibility study, a report by Van Leeuwen on the geology and the Kelian web site. Strathcona was mistaken and did not know that Kelian had a gravity circuit and coarse gold.

On April 6, 2005 at page 61 Farquharson testified:

> MR. GROIA: But by '97, if we were comparing Kelian to Busang, everyone would have known that there had been gravity circuits there for a couple of years except Strathcona, right?
>
> MR. FARQUHARSON: Correct.

Farquharson did not testify about this mistake and did not correct Exhibit 681 until he was cross-examined on it.

Transcript: March 29, 2005, pages 58-62

At page 128 of Exhibit 1328B Leach states:

> The Kelian gold mine is operated by Rio Tinto Indonesia (RTI) and is located approximately 150 km southwest of Busang in East Kalimantan on the island of Borneo. Many geologists who have worked on Busang have noted numerous close similarities to the Kelian gold deposit. Felderhof et al. (1995) [2] also recognized the close similarities between Busang and Kelian. Although only two publications have been made public on Kelian during the exploration and development of Busang in the mid-1990s (van Leeuwen et al., 1990 [8]; Corbett and Leach, 1998 [25]), information was readily shared between RTI and Bre-X geologists (van Leeuwen per som). Therefore, many of the producers, as well as many of data interpretations made at Busang were made based on the understanding of the Kelian deposit.

No One Else Saw Red Flags

Felderhof is not a metallurgist. Bre-X retained reputable experts and relied on their work. Farquharson is not a metallurgist but he saw red flags in the work of metallurgists when they themselves do not. According to Red Flag 17 and Farquharson he saw this red flag on his first day in Jakarta while those who actually have the expertise and who worked on the Busang project for months if not years never saw this red flag. Kilborn, Normet, Hazen, Oretest did not see this red flag.

Red Flag 18: Metallurgical Recovery Was Independent Of Fineness Of Grind And The Gold Was Already Liberated

In the October 1997 letter Farquharson states:

> **18. Metallurgical recovery was independent of fineness of grind**
>
> Both the Hazen and Normet reports went on to comment on a remarkable lack of effect on gold recovery in changing the grind when processing the Busang material. Normally one would expect when treating a primary ore that the recovery would increase with a finer grind but in this case, apparently, no grinding was required at all as the gold was already liberated.

The O.S.C. position is set out in paragraphs 821-846 of Exhibit S5 Volume II and S10.

The Defence position is set out in paragraphs 338-343 of Exhibit S3 and S13.

Strathcona's analysis is found in Exhibit 681, pages 29-30.

Dr. Hellman

In Dr. Hellman's opinion this was not a red flag.

Exhibit 1202: pages 23-24, 60-61,230-237

Dr. Hellman refers to reports by Kilborn, Hazen, Normet and Oretest not referred to by Strathcona that indicated recovery was grind dependent. Dr. Hellman's opinion also states that on the other hand Strathcona did not refer to the statement in the Kelian report that "*increased grinding gives only marginal improvements in recovery*".

Exhibit 1202: pages 61, 230-237

Dr. Hellman in his opinion lists examples where gold recovery is not particularly dependent on grind.

Exhibit 1202: pages 236-237

In paragraph 841 of Exhibit S5 Volume II, the O.S.C. submits Dr. Hellman was "*evasive*" on cross-examination with respect to Oretest metallurgical test work discussed in Exhibit 587 "*[w]hen asked whether the results of the grind test for composite A appeared to be contradictory to the amalgamation results for composite A.*" Dr. Hellman's evidence was "*No...they're just different.*" Dr. Hellman did not give an explanation because he testified: "*...we're getting, from my perspective, into a domain that's very much the realm of specialized metallurgists and I feel that if I make comments on the possible reasons, then I'm not quite sure if I'm really informing the Court.*"

It is appropriate for an expert not to testify beyond his or her expertise.

At page 60 of Exhibit 1202 Dr. Hellman states:

> The relationship of fineness of grind to recovery is a subject that would involve few geologists because it is outside of their expertise and experience. The supervision of the metallurgical testwork by reputable metallurgical groups with considerable experience in the interpretation of gravity recoveries would normally

be regarded by someone in Mr. Felderhof's position as comforting. It would be highly unusual for a geologist to be involved in the detailed assessment of these types of metallurgical studies, especially if no items of concern had been raised.

No One Else Saw Red Flags

Felderhof was a geologist and not a metallurgist. Bre-X retained "*reputable metallurgical groups*", Hazen, Normet, Oretest who raised no items of concern. Kilborn did not raise a red flag. Farquharson who is not a metallurgist raised a red flag.

Not Red Flag For Strathcona's Clients (See Page 212 Of These Reasons)

In cross-examination Farquharson agreed that at Angostura the metallurgical results were not grind dependent. That was not a red flag at Angostura, a company associated with Strathcona although it is for Felderhof.

Transcript: March 29, 2005, page 84

Red Flag 19: Request For Drill Holes Exclusively For Metallurgical Test Work Was Denied

In the October 1997 letter Farquharson states:

> **19. Request for drill holes exclusively for metallurgical testwork was denied**
>
> We only became aware of this red flag when we arrived in Perth and the Normet metallurgist advised that their request for complete core from drill holes to carry out metallurgical test work was denied on the basis that all the drills had to be kept working to expand the ore reserves as that was what the investors and the market were looking for at the time.

The O.S.C. position is set out in paragraphs 847-850 of Exhibit S5 Volume II and S10.

The Defence position is set out in paragraphs 344-345 of Exhibit S3 and S13.

This red flag is not found in the body of Exhibit 681. The O.S.C's position with respect to red flags not included in Strathcona's opinion Exhibit 681 is found at page 177 of these reasons.

Exhibit 703

In Exhibit 703 (page 26), Normet recommended drilling a hole(s) for metallurgical testwork:

> To gain further confidence in the resource assays it is recommended that a larger pilot type trial be undertaken. The methodology for this trial would be:
>
> - Drill a parallel hole(s) directly adjacent to an existing drill hole
>
> ...

Except in the unattributed hearsay found in the allegation above setting out Red Flag 19, there is no evidence that there was a request that was denied, which is quite different than a recommendation. See page 178 of these reasons.

Dr. Kavanagh

Dr. Kavanagh testified that if "*Normet had requested permission...to drill a hole*" and was denied he would consider it a red flag. Dr. Kavanagh gave hearsay evidence that Farquharson told him it was denied by de Guzman not Felderhof. It is alleged that de Guzman was involved in the salting. There is no such allegation made about Felderhof. Transcript: March 15, 2005, page 59

Dr. Hellman

Dr. Hellman's opinion set out at pages 24, 61-62 of Exhibit 1202 is that allegation 19 is not a red flag. Dr. Hellman's opinion was that Bre-X was "*not shy of having their*

samples tested." "*Bre-X had already accepted and carried out Kilborn's recommendations for twin and scissor holes*" and "*also carried out a 27 –tonne pilot plant test whose samples had been independently supervised by Normet*".

Exhibit 1202: page 61

Red Flag 20: Could One Deposit Contain As Much As 8% of the Known Gold Resources In The World

In the October 1997 letter Farquharson states:

> **20. Could one deposit contain as much as eight percent of the known gold resources of the world**
>
> This of course is a red flag that is easy to point out in hindsight but with all the experienced observers that had been to Busang perhaps someone should have asked is it really possible, that considering there are thousands of gold deposits in the world, that one could be on such a larger scale than any of the others and why would nature be so generous as to endow Busang with such a large proportion of the world's gold resources.

The O.S.C. position is set out in paragraphs 851-852 of Exhibit S5 Volume II and S10.

The Defence position is set out in paragraphs 346-349 of Exhibit 3 and S13.

This red flag is not found in the body of Exhibit 681. The O.S.C. position with respect to Red Flags not included in Strathcona's opinion is found at page 177 of these reasons. Farquharson was not examined in chief with respect to Red Flag 20. The O.S.C. position with respect to such red flags is found at page 177 of these reasons.

The 8% was based on comments of Felderhof that he was not uncomfortable with 200 million ounces and not on what was stated in the press releases, which at the highest spoke of 70.95 million ounces in the February 17, 1997 press release.

Transcript: March 30, 2005, pages 57-59

Not Red Flag For Strathcona's Clients (See Page 212 Of These Reasons)

Farquharson was a director of Placer Dome. Farquharson testified he thought Placer Dome had 70 to 80 million ounces in their South Deep property. That was not a red flag for Placer Dome.

Farquharson was aware of the Muruntau deposit in Uzbekistan, which he thought was a 200 million ounce deposit which was substantially larger than the 70.95 million ounces noted above for Busang. (The Muruntau deposit unlike the South Deep property is not a Strathcona associated company but it was a deposit Farquharson knew about.)

Transcript: March 30, 2005, pages 61-64

Dr. Hellman states South Deep had 98 million ounces (Exhibit 1202, page 24) and that Muruntau had 170 million (page 62), both substantially larger than the Busang estimate. Dr. Hellman's opinion that allegation 20 is not a red flag is found at pages 24 and 62 of Exhibit 1202.

Dr. Kavanagh

Farquharson testified "*Yes*" when asked if Dr. Kavanagh should have known about Red Flag 20. Dr. Kavanagh did not raise a red flag.

Farquharson

Farquharson conceded this "*was not a flag that I would particularly condemn Mr. Felderhof for not seeing.*"

Transcript: March 30, 2005, pages 108-109

Different Opinions About Whether Red Flags Should Have Been Apparent To Felderhof

Farquharson

MR. GROIA: And I take it that even though – and let's just take Kilborn for sake of discussion— that even though for many of those red flags we are in agreement that they would have been apparent to anyone who saw them, nobody actually thought they were red flags other than Freeport at the end. I take it Strathcona's view is that that should not absolve the top technical officer of Bre-X of his duty to be vigilant and critical at the property, right?

MR. FARQUHARSON: Because he was on this project for 3 ½ years looking at all the data that was generated on the property, all the results, all the test work, was fully informed and he would be aware of how this project was unfolding whereas all the other participants were only involved in selected portions of it. But some of those portions in which they were involved we would say that it should have been apparent to them that there were problems. But Mr. Felderhof was the individual with exposure to all of the red flags that we have mentioned there and has seen all of the data.

...

MR. GROIA: Well how about the fact that there was unprecedented tampering with these results? Was Mr. Felderhof entitled to take the same view that Strathcona did initially that never before in the history of mining had anything like this gone on before?

MR. FARQUHARSON: But that's the point, that it went on for so long and how could it have gone on for so long if a competent geologist was looking at these results and looking at this drill core and not seeing any of the facts that one would expect, like gold in the surface over top of one of the largest gold discoveries in the world. No visible gold in the core. No gold in the skeleton samples that were in the library that any geologist would want to go and have a look at to see where these high grade assays were coming from. I just find it very difficult to absolve Mr. Felderhof from not having woken up to some of these obvious facts of why these things were not coming together to support this great story that was unfolding.

Transcript: April 6, 2005, pages 115-117

Dr. Hellman

MR. GROIA: So just for the sake of completeness, can you tell us whether on all of the red flags and sundry red flags you've looked at, whether you consider that any of those should have been apparent as a red flag to Mr. Felderhof, or someone with his experience?

MR. HELLMAN: Well, Mr. Groia, I think from my perspective, the answer to that is quite simple in that there were numerous people with Mr. Felderhof's background and experience who looked at the data in detail. The deposit was reviewed by MRDI in a very systematic and detailed way, and there are a lot of specialists who were responsible for aspects of the work which are right outside most geologists experience and training.

So I can confidently say that there were no red flags that I'm aware of, or that were brought to the attention of anybody at that time.

MR. GROIA: And the last question I have about red flags before I move on to green flags, is to ask you whether there is any difference to your answer if we combine the effect of the red flags; in other words, if your last answer was directed to the red flags looked at individually, are you able to comment on whether, if one takes all of the various flags and complaints and puts them all together, whether that would then, because of the combined effect, have been a red flag of some sort for a geologist such as Mr. Felderhof acting reasonably?

MR. HELLMAN: Well, if I include in this term "red flags" things like constructive comments, mild criticisms, suggestions, then the very worst I would come up with would be something like MRDI report, which is a very, very typical report that I have seen that our group undertakes, whereby we are commissioned to specifically look for problems, look for areas that might require improvement, and we express that in terms of suggestions and we provide reasons for it. These are not red flags, Mr. Groia. Some of them are constructive comments, helpful suggestions, pointing out possibly some mistakes. And as far as I'm aware, the MRDI report was quite typical and raised no red flag to suggest that there was a problem with the underlying data that they had studied.

...

MR. HELLMAN: But I would like to finish up in drawing your attention to a couple of matters in this overview. I guess I'm at a loss to understand why it is expected that Mr. Felderhof should have drawn conclusions that no other people, who were highly skilled, professional, independent, did not draw from the very material that he was assessing. I also do not understand why the express view of what without a doubt was North America's best known and respected minerals auditing group, MRDI that I refer to on that page there, the view which stated

"Our principle conclusion is that the exploration work is being done to a high standard," I fail to understand why that view is not more widely appreciated. And I guess to put my colleagues from Strathcona at rest who are with us today, I would wholeheartedly agree with them, that the Busang fraud, as I've expressed it on page 3 was achieved at a scale and over a period of time with the precision that, to our knowledge, is without precedent in the history of mining anywhere in the world.

Transcript: November 7, 2005, pages 60-61, 72

Leach

The evidence of Leach was:

MR. GROIA: And other than the negative results from Freeport and the negative results from Strathcona, are you able to say, Sir, whether you are aware of any red flag that would have suggested tampering to a geologist such as Mr. Felderhof?

MR. LEACH: I mean no. That's basically why I mean, you know, that I was more than happy to help him as a technical adviser because I mean I just totally felt that Mr. Felderhof had nothing that he could see at the time that he was doing the work that would tell him that it was tampering. I mean neither Greg nor myself could see it unless we did detailed work and that detailed work as way outside what would be expected of a general manager of a company. I mean general managers don't do that kind of work. And so, you know, I have been – I can't see anything that I could see that when Mr. Felderhof was working at Busang, given his position and also what was there, that he could have known. So I mean that's, I guess that's why I basically was happy to help him because I realized that there is nothing you could see. It was such a – the salting was done so well and the fact that it was done on a totally valid hydrothermal system with all the characteristics of mineralization, I can't see any way that he could have known.

Transcript: December, 13, 2005, pages 67-68

Dr. Kavanagh

Dr. Kavanagh testified:

MR. GROIA: Would you agree with me that over and over again, Busang was visited by independent people from Bre-X who had nothing but praise for the deposit?

MR. KAVANAGH: Independent people from Bre-X?

MR. GROIA: People who were not working for Bre-X.

MR. KAVANAGH: Visitors.

MR. GROIA: Visitors. And they all had praise for the deposit.

MR. KAVANAGH: Yes.

MR. GROIA: All of the experts who were hired by Bre-X to work on the deposit had nothing but praise for the deposit.

MR. KAVANAGH: Yes.

MR. GROIA: And I guess, to flip it around, not one of those experts, to your knowledge, ever raised anything approaching a red flag, suggesting the results had been tampered with.

MR. KAVANAGH: Right.

Transcript: March 14, 2005, page 42
Exhibit S13: paragraphs 366, 371-373

GREEN FLAGS

Dr. Hellman

Dr. Hellman describes green flags on page 25 of Exhibit 1202:

> As a result of my site visit and subsequently, whilst reviewing various documents and digital data, it became obvious that the Busang project was characterized by abundant information and positive data. I have collectively termed this information as "green flags". These green flags would normally impress impartial observers and would provide assurance to those involved in the Busang project that the gold mineralization was real.

On pages 25-28 Dr. Hellman summarizes his opinion of the green flags:

Description	Comment
Choice of senior staff	The senior Bre-X staff, M. de Guzman, J. Alo, Manny Puspos and Cesar Puspos, were all experienced in tropical geological

	environments, well-experienced in the industry and spoke Indonesian.
John Felderhof	He had extensive experience in Papua New Guinea and Indonesia and had a track record of exploration success.
Exploration Manager, M. de Guzman	De Guzman's various instructions reflect careful attention to detail (e.g. requesting to maintain the camp's sanitation and cleanliness) and order and give the impression of someone who is committed to efficient management.
Monthly reports	Comprehensive and well set-out.
Sample preparation methods	Clearly documented.
Choice of Kilborn	The choice of Kilborn to be the engineering group responsible for the project was logical given their immediate past experience with Kelian and Mt Muro.
Choice of metallurgical consultants	The choice of the independent metallurgical groups was logical given that Normet had extensive experience with the metallurgy of the Kelian gold mine and Oretest had extensive experience in gravity methods. Hazen had a world-class reputation.
Security	Above average security facilities at Busang and Samarinda.
Busang camp	The Busang camp was well set-up, was well run, and had good communications. Data were stored off-site in case of fire, and there was an on-site first aid post.
Whole core sampling	Whole core crushing and assaying of large samples was the best choice for "spotty" or "nuggety" gold and was recommended by Francis Pitard, one of the world's leading sampling experts.
Geology and assays	Gold assays were consistent with the

	geology such as the amount of alteration and fracturing.
Loa Duri sample storage	The Loa Duri sample storage area was secure, well set out, covered and managed by a competent store manager and well organised crew.
Checking of samples	The spot checking of sample numbers on the outside and inside of sample bags by senior staff before they are sent to a laboratory is a sign of diligent and professional work.
Gravity recovery from pilot plant	The predicted gravity response for the SEZ is not compatible with salting by alluvial gold. Kilborn predicted a gravity response of 49% of the total gold content based on a pilot plant study of 27 tonnes of Busang mineralization.
Amalgamation test on Central Zone	The only definitive test for free gold carried out during the entire project by the metallurgical consultants gave results that are inconsistent with salted or alluvial gold. The results are consistent with the CZ oxide and primary Busang ore types.
Metallurgical studies	Several of the world's best known metallurgical groups made no suggestion to Mr. Felderhof of irregular results. The metallurgical groups used by Bre-X were well-respected and included Kilborn, Hazen, Normet, Oretest, McPherson and Amdel.
Mineralogical studies	No concerns, contradictions or irregularities were reported despite detailed independent mineralogical assessments of the gold grains and examination of the

	mineralization by microscope.
Statistics of gold grades	The statistics of the gold grades from the drill holes were closely studied by two independent groups.
Geological and assay data	Two consulting groups, ECS and Kilborn, did not report unusual statistical grade distributions, geological interpretations or significant data errors.
Check assays at independent labs	Check assays of samples previously assayed by Indo Assay Laboratories ("IAL"), Balikpapan were completed at independent laboratories. These confirmed the assays performed by IAL.
Gold grains from pilot plant	Gold grains obtained from the 27 tonne pilot plant test were examined with a microscope. No comments were made to the effect that these results were characteristic of an alluvial source of gold.
Awareness of coarseness of gold	Dr. Harry Parker of MRDI was aware of the coarse nature of the gold from Busang and did not advise Bre-X that the size distribution of the gold was unusual or suggested a non-primary origin.
Pilot plant grade agreed with Bre-X	Normet commented that the good agreement between the estimated Bre-X grade (3.07 g/t) for the 27 tonne sample and the calculated metallurgical grade (2.87 g/t) from the 27 tonne pilot plant test gave additional confidence to the Bre-X assaying techniques.
Choice of Indo Assay Laboratory	Indo Assay Laboratory (IAL) was a well-respected laboratory which had extensive

	experience with screen-fire assays of Kelian mineralisation as well as other Indonesian gold deposits such as Minahasa, Mt Muro and Messel. It was commended by both Kilborn and Normet.
Audit of screen fire laboratory and checking of analytical solutions	Normet audited the laboratory undertaking screen fire assays, which formed a part of the metallurgical testwork and also requested re-assaying of solutions at an independent lab to ensure that no error had been made.
Audit of metallurgical sampling	Kilborn audited and documented the sample preparation for the metallurgical composite samples. A site visit was carried out by Sean Waller from Kilborn and Tony Showell from Normet on March 25 to April 3, 1996 to audit the sample preparation of metallurgical samples. The conduct of the work was described as: *"...smooth, orderly and on schedule to the satisfaction of the visiting consultants."*
On-site sample preparation	Normet commented on the use of the on-site sample preparation laboratory and was aware that the on-site sample preparation facility was used for exploration samples whereas the mineralised samples from drilling were sent to IAL for sample preparation and assay.
Environmental studies	Environmental studies and baseline monitoring had commenced and were managed by Kilborn.
Topographic survey	A comprehensive topographic survey was completed, standing water levels in drill holes had been recorded and the Bre-X surveyor was described as well-informed.

Surface depletion	Mr. Felderhof's belief in surface depletion was consistent with the drill hole data. A detailed examination of the gold grades in the drill core from the CZ and the SEZ demonstrated that there was a near-surface depletion of gold in the SEZ that was different from the behaviour of gold in the CZ.
Analogies with Kelian	Numerous commentators, including petrologists, over the life of the project, who were familiar with the Kelian gold mineralization, commented on the similarity of Busang with Kelian and other deposits.
Geological mapping	Bre-X had undertaken very detailed geological mapping that was well above industry standards.
Cross sections	Detailed cross-sections were above industry standards and were complimented by MRDI
Gold fineness	The gold and silver content ("fineness") reported for various gold grains was compatible with primary mineralisation.
Constrained resource estimates	The resource estimations for both the CZ and SEZ were based on geological constraints which is a good practice.
Spatial analysis by Kilborn and ECS	Spatial analysis ("variography") of the mineralization completed by Kilborn did not produce results that were unusual or aberrant. ECS described their results as "good".
Spatial analysis by myself	I performed a variographic analysis on the digital data supplied by Kilborn and confirmed that an experienced observer who examined the resultant variograms would not suspect that the underlying data were anything but real.

Geological logging	There was a good standard of geological logging by Bre-X geologists as confirmed by independent observers who checked the core logging at Busang, including MRDI and Strathcona.
Sample splitting	There was a high standard of sample splitting as evidenced by the use of a mechanised Rotary Splitter at Loa Duri and Busang. These devices are far superior to many other forms of sub-sampling equipment.
Skeleton core	There was a high standard of storage of skeleton core at Busang. Detailed listings of intervals and drill holes were displayed outside racks, and skeleton core was enclosed in strong plastic bags that were well labelled.
Assay logs	Assay logs that I requested were provided quickly and in good order.
Geotechnical logging	Reported to be excellent.
Core photography	Regarded as excellent.
Mr. Felderhof's insistence on good core recovery	Mr. Felderhof insisted on good core recovery and specifically warned against the assaying of samples that were characterised by poor core recoveries and counselled for close cooperation between drillers and geologists.
Actual core recoveries	Good core recoveries were achieved which gave confidence that sample representivity was being achieved.
Testimony of independent mining engineer	R. Pooley said he: *"...is of the opinion that the drilling, sampling and assaying has been*

	competently and honestly carried out".
Checking by Kilborn	Sophie Ashby of Kilborn had checked the drilling, sampling and logging methodologies and was satisfied.
Conclusion of MRDI	An independent, extensive and detailed review by one of North America's best known and respected minerals auditing groups, MRDI Inc., was commissioned by Bre-X in October 1996 specifically to assess its work at Busang. That review stated: *"Our principal conclusion is that the exploration work is being done to a high standard".*
Compliments	In addition to MRDI, Barrick, Teck and Kilborn complimented Bre-X on their work. R. Ward of Republic National Bank of New York was impressed with the work.
Petrological and mineralogical studies	The number of petrographic and petrological studies commissioned by Bre-X was well above that which is typical in the industry.
Project management	Kilborn and Normet both complimented Bre-X on project management.

Dr. Hellman sets out the green flags in more detail at pages 63-75 of his opinion and at pages 274-318 of Appendix 4 under the general headings of:

- Choice of Key Staff and Management Issues
- Sampling and Assaying
- Metallurgical Results
- Independent Metallurgical, Mineralogical and Other Studies
- Geology and Geochemistry
- Good Practices
- Independent Reviews and Comments

Leach

Leach describes green flags on page 68 of Exhibit 1328A:

> A 'green flag', on the other hand, is a feature of the Bre-X exploration program that did provide confidence that the Busang deposit was valid and that the exploration program was being carried out in an efficient and professional manner.

Leach divided the Green Flags into four main areas:

- The prospectivity of the Busang Project area
- The similarities between Busang and the Kelian Gold Mine
- The manner in which the exploration program was carried out by Bre-X geologists
- The Bre-X management structure

> Although there are numerous other 'green flags' related to Bre-X activities at Busang, the green flags discussed in this document are confined to those which lie within my core competency.

Some of his opinion found at pages 68-81 is set out below:

> **B. PROSPECTIVITY**
>
> **a) Introduction**
>
> The excellent prospectivity, or potential to discover a major deposit within the Busang Project area was widely accepted. As stated by Strathcona (1997) [6]: *"Busang has characteristics favourable for gold deposition. These include its location on a major tectonic belt... which also hosts the Kelian ...gold deposit... The proposed maar diatreme setting and the type and large size of the alteration system at Busang are also further positive indicators of gold mineralisation."*
>
> **b) The Regional Setting**
> The Busang Project is located within a major gold district that also hosts the world class Kelian Gold Mine.
>
> ...

c) Busang I: Central Zone
It is my opinion that there is still an excellent potential for the Central Zone to host significant gold mineralisation as is indicated by:

- Favourable surface geology

...

- Favourable surface geochemistry from Westralian exploration program

...

- Favourable surface geochemistry from the Bre-X exploration program

...

- Westralian drilling

...

- Bre-X drilling

...

d) Busang II - The South East Zone
It is also my opinion that there is still significant potential in the South East Zone for gold and base metal mineralisation. This is supported by:

- Surface Geology

...

- Surface Geochemistry

...

- Bre-X Drilling

...

C. SIMILARITIES BETWEEN BUSANG AND KELIAN GOLD MINE

a) Introduction

...

Many geologists who have worked on Busang (e.g. Leach and Corbett, 1997 [1]; Thompson, 1996 [15]; Borner, 1995 [16]; Leach, 1997 [17]) have noted numerous close similarities with the Kelian gold deposit.

...

It is my opinion that the many similarities between Kelian and Busang would have been a significant 'green flag' that would have given the Bre-X personnel confidence in the validity of the project.

...

The following is an outline of a comparison of the geological, geochemical, alteration, mineralisation, and metallurgical features between Kelian and Busang.

...

b) Geological Comparisons

- The tectonic and regional structural settings of the two projects are very similar

...

- The physiography of Kelian and Busang are similar and reflect comparable host rocks and alteration styles.

c) Surface Geochemistry

- Alluvial workings by local miners are recorded at both Busang and Kelian

- Exposure in the Prampus region at Kelian was poor and the high grade Northeast Zones were not exposed at the surface. Surface exposure in the Central Zone at Busang was poor. In the South East Zone, there was very poor exposure in the creeks and most leached surface rocks were covered by a veneer of mud and swamp debris.

- The results of assays from rock chip samples were comparable at both projects.

...

d) Resources

- Very similar average grades of 2.5-3 *g/t* Au.

...

e) Alteration and Mineralisation

- The style of alteration and mineralisation at Kelian and Busang are similar, and also closely comparable to carbonate-base metal gold systems throughout the Southwest Pacific region. The Prampus and Central zones are more comparable to those systems that are more base metal-rich (sphalerite-galena-tennantite-pyrite), whereas the North East Kelian and South East Zone at Busang are of the more carbonate-rich types.

- Two main stages of hydrothermal activity have been recognised at Kelian

...

- Although four main stages have been documented at Busang (Felderhof et al., 1995 [2];Leach,1997[17]),they can be condensed into three main events

...

These three stages at Busang are closely comparable to the main events at Kelian.

...

f) Gold Mineralisation

Visible gold was extremely rare in the core from both Kelian and Busang:

...

The gold observed under the microscope in the Kelian polished thin sections is very similar to that observed in sections from the Central Zone:

...

g) Metallurgical Characteristics

The metallurgical characteristics of the Kelian and Busang ore are very similar:

...

D. EXPLORATION AT BUSANG

There were many features of the exploration programme that indicated that the Bre-X personnel had carried out activities in a professional and efficient manner. These 'green flags' were evident during the site visit in April 1997 and during subsequent work on the Sheraton Project.

...

- Project Exploration:

  o Approach to exploration.
  The approach that Bre-X took in further developing the results of the early Westralian work that led to the 'discovery' of Busang in the Central Zone is very sound, systematic, and based on a good understanding of the controls on mineralisation in the Southwest Pacific gold systems.

  o Mapping
  The data on the geological and geochemical map sheets (Bre-X, 1995-1996) [21] are presented in a very clear and precise manner and are above the industry standard. This made it easy to verify the interpretations made from this data and to correlate this information with the drilling data.

  o Drilling
  The exploration drilling in the Central Zone had been undertaken in a well defined and methodical manner, and the philosophy to extend the drilling to the South East Zone along to section SEZ 24 was also based on sound geological interpretations.

  ...

  o Drill Sections
  The cross sections show that both the geology and mineralisation on the same sheets are well presented, comprehensive and well above the industry standard. I do not recall going to a project at a comparable stage of an exploration program and finding the drill data so well presented.

  ...

  o Drill Logs
  The core logging was very clear, precise, and easy to follow. However, it is considered that the tabulated or graphic log format, rather than the narrative one used at Busang, would have been more appropriate in the more advanced stages of exploration.

  o Whole Core
  The assaying of whole core is a common industry practice where coarse gold has resulted in poor reproducibility in assays.

  o Skeleton Core

The method of selecting and storing of the skeleton core at Busang was well above the industry standard and the best that I have seen.

...

E. BRE-X MANAGEMENT STRUCTURE

The management structure of Bre-X operations in Indonesia was comparable to most of the overseas companies that operated in Indonesia at that time (Tab 12, volume 2). In my opinion, Felderhof, as the general manager of exploration of Bre-X, exercised much more diligence in monitoring the activities at Busang than managers of other companies operating in Indonesia and elsewhere in the West Pacific region. This opinion is based on my observations while working with a large number of mining and exploration companies operating in the west Pacific region.
Unlike Felderhof, the general managers of exploration of companies like Rio Tinto, Newmont, Freeport and Newcrest, illustrated only minor in-depth technical knowledge of the geology or resources during late stages of exploration of major mineral deposits in this region. These managers are also not the authors of technical papers on these deposits, as John Felderhof has done.

Exhibit 1328A: pages 68-81

Green flags are also set out in detail in by Leach Exhibit 1328B Tabs 9-12, pages 116-157. Leach summarizes each of the tabs:

TAB 9: PROSPECTIVITY OF BUSANG
A. SUMMARY

The Busang project area is located within a major gold district and has the same optimum tectonic and structural settings as the Kelian and Indo Muro gold mines and other major gold prospects in Kalimantan. It is also situated along the Kalimantan magmatic arc that hosts Carlin-style gold deposits in Sarawak, porphyry copper deposits in Sabah prospects in Central Kalimantan, and epithermal gold and massive sulphide prospects in East Kalimantan.

The Busang project is located in an optimum geological setting for gold mineralization.

...

TAB 10: KELIAN –BUSANG COMPARISON
A. SUMMARY

The Kelian gold mine is operated by Rio Tinto Indonesia (RTI) and is located approximately 150 km southwest of Busang in East Kalimantan on the island of Borneo. Many geologists who have worked on Busang have noted numerous close similarities to the Kelian gold deposit. Felderhof et al. (1995) [2] also recognized the close similarities between Busang and Kelian. Although only two publications have been made public on Kelian during the exploration and development of Busang in the mid-1990's (van Leeuwen et al., 1990 [8]; Corbett and Leach, 1998 [25]), information was readily shared between RTI and Bre-X geologists (van Leeuwen per som). Therefore, many of the procedures, as well as many of data interpretations made at Busang were made based on the understanding of the Kelian deposit.

...

TAB 11: BRE-X EXPLORATION AT BUSANG
A. SUMMARY

1. Following the preliminary Westralian Atan Minerals exploration activities, the identification of Busang as a gold prospect and the subsequent approach to various stages of exploration and target delineation and definitions, were sound and systematic, and were clearly based on a good understanding of the various controls on gold mineralization in the Southwest Pacific region.

2. The data on the geological map sheets are presented in a very clear and precise manner and are above the industry standard. This would have made it easy to verify the interpretations that were made from this data and to correlate this information with the drilling data.

3. Core recovery is considered to have been excellent even in difficult terrain. The cross sections that show the geology and mineralization in the Southwest Zone were well presented, comprehensive and well above the industry standard.

4. The core logging was clear, precise, and easy to follow, although it is considered that the tabulated or graphic logs, rather than the narrative form used at Busang, would have been more appropriate in the more advanced stage of exploration activity.

5. The assaying of the whole core at Busang is an acceptable industry practice where coarse gold occurs and has reduced the poor reproducibility of assays.

...

TAB 12: BRE-X MANAGEMENT STRUCTURE
A. SUMMARY

Felderhof, who was the general manager of Bre-X at the time of the press releases on the resource calculations at Busang, exercised significantly more diligence than is evident for senior executives in a similar position in companies such as Rio Tinto, Newmont, Freeport, Newcrest and Barrick during comparable stages of exploration and development.

Exhibit 1328A: pages 68-81, 116-157
Exhibit 1328B: Tab 9-12, pages 116-157

O.S.C. Submissions

Dr. Hellman's and Leach's green flags are found in Defence paragraphs 350-372 of Exhibit S13. The O.S.C. submissions found in the O.S.C. commentary to those paragraphs are understandably similar to the O.S.C. submissions with respect to the red flags and my analysis is found in my discussion of the red flags.

Farquharson

With respect to green flags Farquharson testified:

> MR. GROIA: So in deciding that Mr. Felderhof should not be absolved, I take it in order to be fair Strathcona would have carefully considered all of the green flag factors that would have suggested to Mr. Felderhof that if results were, in fact, authentic you wouldn't want to just look at the red flags. You would have also wanted to carefully look at all the green flags, right?
>
> MR. FARQUHARSON: Mr. Groia, believe me, it's awfully different to find too many green flags when you are dealing with activities on the site of the largest gold fraud in the history of mining anywhere in the world and the fact that it went on for 3 ½ years. It's very difficult to come up with many green flags that would support allowing this process to have carried on for so long.
>
> MR. GROIA: Well didn't we agree on an earlier day that Strathcona thought this was a highly prospective site?
>
> MR. FARQUHARSON: Yes.

MR. GROIA: That's a green flag, isn't it?

MR. FARQUHARSON: Yes, it is.

MR. GROIA: And didn't we also agree that a number of people like M.R.D.I. and Barrick and Freeport went to the property and complimented Mr. Felderhof and his team's work and that's a green flag, isn't it?

MR. FARQUHARSON: And they made their remarks based upon short visits of a couple of days. I don't recall too many compliments coming from Freeport, but they were there for a short period of time. Mr. Felderhof was there for 3 ½ years.

MR. GROIA: So essentially what you are saying is that your focus has been to look at, because the Commission asked you to look at the red flags, and you have not really made any systematic review, or study, or analysis of the green flags? In other words, putting it simply, you did what the Commission asked you to do which was to focus on certain red flags and because no one asked you to write a report about green flags you never made any real effort to study those, right?

MR. FARQUHARSON: Well any references to green flags that one could think of are included in that report. And beyond the list of – the fact that the geology was prospective for gold, it's hard to think of many other green flags that would support Mr. Felderhof not being aware of what was going on over a period of 3 ½ years.

Transcript: April 6, 2005, pages 115-117

Farquharson also testified:

MR. GROIA: So again, Strathcona only did what the Commission asked it to do and the Commission asked it to focus on certain red flags, right?

MR. FARQUHARSON: Yes.

MR. GROIA: At no time was Strathcona asked to prepare a report that would have set out all of the factors that might have led someone to believe the assay results, were there?

MR. FARQUHARSON: No.

...

MR. GROIA: But you saw your job, Strathcona saw its job was to provide assistance to the Commission in its efforts to prosecute Mr. Felderhof for something; is that fair?

MR. FARQUHARSON: That's fair.

Transcript: March 23, 2005, pages 39, 41

Hindsight plays an important and perhaps unconscious role in Farquharson's opinion largely excluding the other factors set out in pages 136-222 of these reasons.

SUMMARY AND FINDINGS: DUE DILIGENCE DEFENCE

At page 113 of these reasons I set out the onus and the central issue that I need to determine with respect to the defence of due diligence:

> Do I prefer the Defence evidence over the O.S.C. evidence with respect to the red flags.
> If I prefer the O.S.C. evidence then of course the Defence would not have met its onus to prove due diligence on a balance of probabilities.
> If I find the O.S.C. and Defence evidence equally compelling then again the Defence would not have met its onus.

At paragraph 76 and 78 of Exhibit S4, the Defence states:

> Para. 76. The OSC places great stock on the testimony of Graham Farquharson; indeed to a great extent they have reposed their entire geological case in Strathcona. They repeatedly ask that his views be accepted over everyone else's; particularly those of Dr. Hellman and Mr. Leach.
>
> ...
>
> Para. 78. Without meaning any great disrespect to Strathcona, set out below are only a few of their errors, omissions, concessions and questionable judgements in this case that should be considered in deciding whether to prefer the evidence of Strathcona to that of Dr. Hellman, Mr. Leach, all the technical visitors to Busang, MRDI, Kilborn, Barrick, Dr. Kavanagh and others.

Exhibit S4: paragraphs 76, 78

On August 28, 2006, at pages 27-28 the Defence submitted:

> Now we deliberately and hopefully in a restrained way refrained from suggesting that Mr. Farquharson was trying to mislead the Court, although that suggestion was made repeatedly about Mr. Hellman, Mr. Leach and Dr. Hellman [sic]. And so I am not going to suggest to you that I think that Graham Farquharson set out deliberately to try and fudge his testimony in order to support his position. I am not going to attack his character. I am not going to attack his view of what he was asked to do. But I am going to say that over and over again it was demonstrated that he was simply and totally incorrect.

I largely agree with these Defence comments.

None of the experts was trying to mislead the court but it is my function to weigh their evidence and all of the evidence. As part of that function I must determine which evidence I prefer. (This case is not one where the opposing evidence is equally compelling).

On the O.S.C. side stand Strathcona and Farquharson largely alone with some support from Defence witnesses and the documentary evidence: for example Red Flag 12, where Dr. Hellman agrees that there would be cause for concern if Felderhof knew all of the inner samples bags were being opened or Red Flag 8 where Leach's evidence was that after detailed analysis he found inconsistencies between Bre-X assays and the geology of the core from BSSE 198. There are many other pieces of evidence as reviewed in these reasons that the O.S.C. submits support the O.S.C. position but in the main the O.S.C. position is dependent on the evidence of Farquharson.

On the other side are Dr. Hellman, Terry Leach, Paul Semple, Dr. Kavanagh, Peter Munk, Barrick Gold, M.R.D.I., Kilborn, Sophia Ashby, Normet, Hazen, Oretest, Mintek, Petrascience, Roger Townend, John Borner, Anne Thompson, Martha Schwartz, I.A.L, John Irvin, J.P. Morgan, Republic National Bank, analysts and suitors and others who did not see any red flags. Where everyone else saw gold, Strathcona with hindsight saw red flags.

Farquharson had an explanation why there were so many others who did not see any red flags. Farquharson was being asked about one particular red flag but I infer from the evidence that he would have applied his answer generally to all red flags. Farquharson testified that others "*were apparently carried away by the excitement of being part of the Busang story.*"

> MR. GROIA: So as I see it, Mr. Farquharson, on the one side we have Mintek, Normet, Kilborn, all looking at this and not seeing anything except the comparison to Kelian, supported by Mr. Henley and the literature and on the other side we have Mr. Farquharson supported by nothing. Is that about the way it shapes up?
>
> MR. FARQUHARSON: No. Our support is not based on nothing. It's just based on common sense.
>
> MR. GROIA: So these are all men lacking in common sense?
>
> MR. FARQUHARSON: These are all men that were apparently carried away by the excitement of being part of the Busang story and did not recognize something as simple and as evident as this, that if you produce a gravity concentrate where you have got coarse free liberated gold why the hell can't you see it.

Transcript: April 5, 2005, page 104

In a similar vein when Munk was asked about due diligence by J.P. Morgan (with respect to title issues but also applicable to geological issues) he testified:

> MR. MUNK: Listen! J.P. Morgan were my bankers. I know them very well. We all know bankers. They are respected in the full group. J.P. Morgan was at that time fighting in a very difficult environment for the mining industry to get that assignment. Every major investment banker was dreaming of becoming a banker for Bre-X. And J.P. Morgan jumped on the assignment.
>
> ...
>
> But, you know, we could not risk our investors and our shareholders' money to the tune of $2 billion here, or $3 billion based on what J.P. Morgan said. We had to rely on our own due diligence. This was much more thorough, much more detailed, and had started and went much further than J.P. Morgan whose involvement was only two weeks old at that time.

Transcript: December 8, 2005, page 16

On the evidence before me it would be speculative to find that others "*were apparently carried away by the excitement of being part of the Busang story and did not recognize something...simple and...evident...*". The O.S.C. did not call evidence in support of Farquharson's position. Farquharson's and Munk's evidence above was in response to questioning by the Defence and not the O.S.C. .

Those involved with Bre-X were well recognized, reputable professionals. Kilborn would not ignore evident concerns when it also wanted to invest in Busang and develop the property with Bre-X. Barrick's "*A team*" would not have missed any warning or concern with 2 to 3 billion dollars at stake. M.R.D.I. and the other independent professionals would not have missed the red flags if they had existed.

It is a valid submission but not a total answer simply to say that Felderhof was allegedly exposed to all of these red flags while others were only exposed to one or a few. Except for Red Flag 8, which was analyzed by Leach, Dr. Hellman considered and was exposed to all the red flag allegations and in his expert opinion there were no red flags. Leach was retained to consider Red Flags 1, 2, 6, 8, 9 although he was also obviously aware of the October 1997 letter with its 20 Red Flags as he refers to it in his expert opinion. In Leach's opinion there were no red flags.

M.R.D.I. and Kilborn and Barrick would have been exposed to many if not most red flags. Some such as Normet and Hazen would have been exposed to several. Some such as Thompson that may have only been exposed to one red flag had expertise beyond that expected of a geologist such as Felderhof. Felderhof was not required to go beyond or question her expertise nor that of Normet, Hazen, Kilborn and M.R.D.I. and the other professionals specifically retained because of their specialized training, knowledge, experience and expertise.

The significance of how many red flags Felderhof and others were exposed to, only comes into play if the alleged red flags are in fact red flags and not unproven allegations. Unproven because Strathcona was wrong, made errors about the facts or the significance of the facts or because the alleged red flags were benign or ambiguous or irrelevant. For example, Thompson's evidence is applicable to Red Flag 9. If on all of the evidence including her evidence I am satisfied on a balance of probabilities that this is not a red flag, as I am, it does not matter that she was only exposed to one alleged red flag while Felderhof was allegedly exposed to all the red flags because it is not a red flag and

Felderhof's alleged exposure to all of the other alleged red flags does not make it a red flag.

At pages 219-223 I set out the issues negatively affecting the weight to be given to the evidence of Dr. Hellman, Terry Leach and Graham Farquharson. I am left with many more concerns with respect to Graham Farquharson than with respect to Dr. Hellman or Terry Leach.

In weighing the evidence of due diligence and the red flags, I also consider the following issues discussed earlier in these reasons at pages 136-223 which I find have been established on a balance of probabilities.

Every professional and expert that went to Busang believed the property to be "*highly prospective*" for gold. The O.S.C. concedes Busang was prospective. Some reputable professionals, for example Dr. Kavanagh and Dr. Hellman still believe, even today, that at least the Central Zone is worth further investigation.

"*[T]he site selected for a tampering program had been well chosen.*" The tampering was "*without precedent in the history of mining anywhere in the world.*" The tampering was very sophisticated. "*[T]he Busang results were plausible, reasonable and something that would fit the geology.*" The assay results lined up with Kilborn's computer model used to estimate ore reserves for Busang. The assay results lined up within a hole and from hole to hole. Twenty-five thousand to 30,000 samples were tampered with over

three and one half years without any professional or expert involved with Busang raising a red flag.

The "*tampering...occurred for so long, on such a scale, and with such accuracy as to give the assay values and subsequent interpretation of those values the appearance of being plausible.*"

The brightest red flags vary between Farquharson's written opinion in 2000 and his evidence in 2005. How is it that two Red Flags, 9 and 16, combined in 2000 to be a most striking red flag are no longer so striking in 2005? How is it that Red Flags 8 and 12 are bright in 2005 when they were not found in the 2000 opinion? This inconsistency creates concerns that these alleged red flags are bright and concerns that they are even red.

It is important to understand Kelian to understand Busang and the red flags. Farquharson was mistaken about important aspects of Kelian. Dr. Hellman, Leach and Felderhof had a much superior understanding of Kelian. Farquharson did not know that Kelian had a gravity plant or coarse gold or a blind deposit.

A geologist's experience with similar deposits is important in his or her analysis of a new deposit. Dr. Hellman, Terry Leach and Felderhof had experience in the Southeast Pacific rim of fire, tropical jungle environments and Indonesia. Farquharson did not.

The professionals and experts retained by Bre-X were reputable and did their test work at a high industry standard and included: M.R.D.I., Kilborn, Normet, Hazen, Oretest,

Mintek, Petrascience, Sophia Ashby, Paul Semple, John Borner, Anne Thompson, Roger Townend, Martha Schwartz, I.A.L, John Irvin, J.P. Morgan, Republic National Bank. They raised no red flags.

Kilborn, one of the world's leading engineering companies, was responsible for the resource estimates, which are the subject matter of Counts 5 to 8. Kilborn did not see any red flags. In fact quite the opposite, Kilborn wanted to invest in Busang and join Bre-X in Busang's development.

M.R.D.I., one of North American's best known and respected mineral auditing groups found *"[t]he work Bre-X has done at Busang both in terms of discovery and ongoing exploration development of the Busang Hardrock Gold Project is of a high industry standard."* M.R.D.I. raised no red flags.

Dr. Kavanagh did not raise any red flags and was a true believer in Busang gold. Other experts and professionals involved with Busang did not raise any red flags: analysts, suitors.

Peter Munk of Barrick Gold, now the world's largest gold company, was at the pinnacle of an exceptional team of experts and professionals and sources of information that over years applied that expertise and spent millions of dollars investigating and pursuing Busang. When Peter Munk learned of the negative Freeport results his reaction was *"[d]isbelief and horror."*

To a large extent what separates Strathcona from all those others who did not see red flags and why Strathcona largely stands alone is hindsight or knowledge of the negative drilling results and the subsequent active search for red flags. Strathcona knew of Freeport's negative drilling results. Strathcona had its own negative drilling results. Strathcona "*went looking for trouble*".

Without hindsight there would be no red flags. Without the negative results of Freeport's drilling program there would be no red flags. The facts which form the basis for the alleged red flags would have remained the same but instead of being seen as red flags as Strathcona did they would have continued to be seen to be "*of a high industry standard*" as M.R.D.I. saw them. M.R.D.I. reported on what they saw. M.R.D.I. was not "*looking for trouble*" as was Strathcona. Strathcona *"saw its job was to provide assistance to the Commission in its efforts to prosecute Mr. Felderhof."* Strathcona did not see its job as providing assistance to the court by pointing out that the M.R.D.I. report was a green flag, a "*powerful arguement*" for Felderhof. Strathcona instead saw its role was to "*de-claw*" the M.R.D.I. report.

With hindsight and in response to the Bre-X fraud new rules have come into force to regulate the mining industry. Semple testified Kilborn was not looking for tampering. The tampering at Bre-X was unprecedented. It fooled Kilborn's computer model. The mining industry in general was not looking for unprecedented tampering and so the rules needed to be changed and were changed after the Bre-X fraud.

Drill hole results trump geological puzzles. Once gold is found by drilling then geological models and theories about whether there is gold in the deposit become less relevant and

are not red flags. Once gold is found, as everyone believed it was at Busang, then other data assumes less importance. Strathcona itself understands how to use drill hole results to trump other theories. Strathcona is using it's negative drill results to try to trump the views of the many independent experts and professionals and of Felderhof that reasonably believed Busang was a legitimate gold deposit.

There are many red flags that are red for Felderhof but not red for Strathcona's clients or associated companies. Why? Because with Felderhof, Farquharson was moving backward from known tampering and actively searching for red flags. There was no allegation of tampering with Strathcona's clients' deposits and without the search for red flags no red flags were found and similar or identical matters were seen to be and reported to be benign.

Transcript: August 30, 2006, page 87

The evidence with respect to each individual red flag and the merits of each red flag must not be overwhelmed by the general considerations noted above. But on the other hand each red flag cannot be looked at in isolation without regard to those general considerations which affect the weight to be given to the evidence. Balancing the evidence specific to individual alleged red flags discussed at pages 223-361 of these reasons and the more general considerations discussed above and balancing the short falls in the O.S.C. evidence against the short falls in the Defence evidence and considering the evidence of the green flags, I prefer the evidence that there were no red flags that were or should have been apparent to Felderhof.

This finding encompasses all of the alleged red flags although for a few in different ways. With respect to Red Flag 8; after a very detailed analysis, Leach found inconsistencies between the Bre-X assays and the geology of high grade intervals of some holes but in Leach's opinion such detailed "*analysis would not have been industry practice*" and "*would have been beyond the scope of a general manager of exploration, such as Felderhof, who correctly questioned and relied on the information supplied to him by the exploration manager...and project geologist ...*".

Red Flag 8 was not seen by M.R.D.I. nor Kilborn nor anyone else.

With respect to Red Flag 12, opening all or even a large number of samples bags was a matter of concern. There is direct evidence from Mihailovich that all of the sample bags in Samarinda were being opened while he was there between the middle of October and Christmas of 1996 but there is no evidence that Felderhof saw or should have seen open sample bags nor persuasive direct evidence that Felderhof was even in Busang from August 1996 until February 1997.

I am satisfied on a balance of probabilities that on all of the evidence the rest of the alleged red flags did not exist or that the Defence interpretation of the facts that they were not red flags is reasonable.

In addition there is the evidence of green flags reviewed above specifically at pages 364 to 380 and generally found throughout these reasons, for example, the M.R.D.I. report

and Bre-X's retainer of reputable professionals which are positive pieces of evidence that Felderhof took all reasonable care.

I find Felderhof has established due diligence on a balance of probabilities.

I find Felderhof not guilty of Counts 5 to 8.

COUNTS 1 TO 4: INSIDER TRADING

Felderhof is charged with four counts of insider trading "*contrary to s.s. 76(1) and 122(1)(c) of the Securities Act, R.S.O. 1990, c.S.5. as am.*". Counts 1 to 4 on the Information are set out at pages 1 to 2 of these reasons. The Particulars to the Information are at pages 3 to 4.

Securities Act

Section 76(1) states:

> **76.** (1) **Trading where undisclosed change.** –No person or company in a special relationship with a reporting issuer shall purchase or sell securities of the reporting issuer with the knowledge of a material fact or material change with respect to the reporting issuer that has not been generally disclosed.

Section 122(1)(c) states:

> **122.**(1) **Offences, general.** –Every person or company that,
>
> (c) contravenes Ontario securities law,
>
> is guilty of an offence and on conviction is liable to a fine of not more than $1,000,000 or to imprisonment for a term of not more than two years, or to both.

Section 76(1) refers to "*the knowledge of a material fact or material change.*" The allegations against Felderhof in Counts 1 to 4 are that he had knowledge of a "*material fact*" and not of a "*material change*". "*Material fact*" is defined in s.1(1) of the *Securities Act*:

> "material fact", where used in relation to securities issued or proposed to be issued, means a fact that significantly affects, or would reasonably be expected to have a significant effect on, the market price or value of such securities.

Exhibit 12: paragraph 4

Particulars

In the "*Particulars to the Information of Michael Hubley*" the O.S.C. particularizes the material facts alleged in Counts 1 to 4.

During the trial and in submissions the O.S.C. and Defence have somewhat reformatted and renumbered the particulars set out in the Particulars to the Information. I have adopted their approach. The correlation between the five particulars referred in the submissions of the O.S.C. and Defence and the particulars that form part of the information is as follows.

What is referred to Particular 1 in submissions is identical to 1.a) and 2.a) in the Particulars to the Information.

Particular 2 is identical to 1.b), 2.b), 3.a) and 4.a).

Particular 3 is identical to 1.c), 2.c), 3.b) and 4.b).

Particular 4 is identical to 2.d), 3.c) and 4.c).

Particular 5 is identical to 4.d).

The 5 particulars referred to in the submission and in these reasons are as follows:

PARTICULAR 1

That due to a failure to comply with contractual obligations owed to the Indonesian government and the shareholders of PT Westralian Atan Minerals ("PT WAM"), Bre-X had not secured its interest in the property known as Busang I; and/or

PARTICULAR 2

That Bre-X had misled the Indonesian government respecting the acquisition of an 80% interest in PT WAM; and/or

PARTICULAR 3

That Bre-X had unjustly excluded PT Krueng Gasui ("PT KG"), and/or PT Sungai Atan Perdana ("PT SAP"), and/or Jusuf Merukh, from obtaining an interest in the property known as Busang II.

PARTICULAR 4

That PT KG, and/or PT SAP, and/or Jusuf Merukh, had issued a complaint to the Indonesian government and Bre-X respecting their exclusion from obtaining an interest in the exploration of the property known as Busang II.

PARTICULAR 5

That the Indonesian government had cancelled the preliminary survey permit respecting the property known as Busang II.

The "material facts" referred to in each count are as follows:

- Count 1 –Particular 1 and/or 2 and/or 3
- Count 2 –Particular 1 and/or 2 and/or 3 and/or 4
- Count 3 –Particular 2 and/or 3 and/or 4
- Count 4 –Particular 2 and/or 3 and/or 4 and/or 5

The Defence agrees that it is sufficient if the O.S.C. proves any one particular with respect to each count.

Exhibit S5 Volume I: paragraph 131

Particular 4 is not consistent in counts 2, 3, and 4. Particular 4 set out above is as it is found in Counts 2 and 4. In count 3 the words "*the exploration of*" are omitted. The difference is not relevant.

R. v. Woods (sub nom. R. v. Plastic Engine Technology Corpor PETCO)

In Woods v. Ontario [1994] O.J. No. 651 (QL), the Ontario Court of Appeal refused leave to appeal from the judgement of Farley J. in R. v. Woods [1994] O.J. No. 392 (QL). The Ontario Court of Appeal confirmed section 75(1), now s.76(1), is a strict liability offence with a defence of due diligence available to the Defendant.

On page 9, Farley J. states:

> Para. 15. It should be observed that s. 75(1) S Act [sic] can be broken down into various constituent parts:
>
> (a) the defendant is in a special relationship with the public company;
> (b) and the defendant purchases or sells securities of that public company;
> (c) with that defendant having knowledge of material information about that public company;
> (d) which material information has not been generally disclosed.

Farley, J continues at paragraph 15:

> The offence then is in essence not a question of using insider information but of buying or selling securities of a company while possessed of insider information. It seems to me that the provisions of the insider trading prohibition are intricately linked with the timely disclosure requirements. The purpose of timely disclosure is to ensure that no one makes a trading decision (or fails to make one) while not having material information which would affect that decision. There is

recognition that the situation is a dual decision one - i.e. that of the buyer and that of the seller.

...

Para. 16. The insider trading provisions provide increased pressure on those who are required to ensure that a reporting issuer does make a timely disclosure does so in fact. The carrot and stick in this regard is that anyone in a special relationship who has insider information cannot buy or sell without incurring liability until the news has been disseminated.

Para. 17. The critical aspect is not of course that insider information is in fact used to make the trading decision but rather that a person with a special relationship with a reporting issuer cannot trade while possessed of insider information. The system is not perfect since it does not catch those situations where that person would have bought or sold but for possession of the insider information which changed the decision to a stand pat one.

At pages 24-25 Farley J. continues:

Para. 74. Woods submitted that upon removal of the "makes use of" defence the prohibition on insider trading contained in s. 75(2) became an absolutely [sic] liability offence. However it seems to me that this change had no impact on the classification of s. 75(1) as a strict liability offence. Although referred to as a defence, the "makes use of" defence helped to define the actus reus of the offence. Prior to the removal of this defence, the actus reus of the offence under s. 75(1) was in trading by an insider who made use of undisclosed material information. In order to commit the proscribed act the insider must not only have traded while in possession of undisclosed material information, but he would also have had to use that information in making the trade. Following the removal of the "makes use of" defence, the actus reus was broadened to include any trade made by an insider while in possession of material undisclosed information: see s. 75(1) and (2). One will appreciate the difficulty of finding evidence which would allow one to penetrate the brain of the insider to prove that the decision making process with respect to the trade in the securities made use of that insider information.

Para. 75. This change did not affect the degree of fault required to prove the offence; rather it changed the description of the proscribed act. Both before and after the removal of this defence, it was open to the accused to prove, on a balance of probabilities, that he used all reasonable care to ensure that he did not commit the proscribed act or that he acted under a reasonable mistake of fact. Further this "makes use of" defence was never a common law defence. All of the common law defences of due diligence and reasonable mistake of fact together with the statutory defence in s. 75(4) of the S Act and the defences created by the Regulations remain available.

Para. 76. In Sault Ste. Marie at pp. 1325-6, the Supreme Court of Canada made it clear that, once the Crown has proven the factual elements of the actus reus of a strict liability offence, there may be two components to the defence of due diligence at common law. The first requires proof of an honest and reasonable belief on the part of the accused which, if true, would have made the act committed by the accused lawful. The second requires proof by the accused that the prohibited act was committed despite the exercise by the accused of all reasonable care in the circumstances to prevent it. In the former case, the mistaken facts must be relevant to the offence, in the sense that the mistake operates to refute any knowledge on the part of the accused of one or more of the factual elements of the actus reus. Similarly, in the latter case, the care that must be exercised is care to prevent the occurrence or commission of the actus reus.

Para. 77. The factual elements of the actus reus of the offence under s. 75(1) have been listed in the discussion on Issue 1. There is room for these common law defences to operate with respect to each of these four factual elements of the offence. An accused may assert an honest and reasonable mistake as to any of the facts relevant to each of these factual elements. Further, this same defence with respect to the question of disclosure of the information to the public generally (fourth element) is expressly codified in s. 75(4). Moreover, an accused may assert that all due care was taken either to prevent the purchase or sale of the securities, for example where this occurs through an agent or broker (second element), or to determine whether the information had been publicly disclosed (fourth element).

Para. 78. The Supreme Court of Canada has rejected the position that a mens rea or fault element must be proven in connection with each and every factual element of the actus reus in order to comply with s. 7 of the Charter. As long as there is room for the defence of due diligence or a reasonable mistake of fact to operate with respect to one element of the actus reus in this case, there is no additional requirement that these defences extend to all other factual elements of the offence. See R. v. DeSousa, [1992] 2 S.C.R. 944, at pp. 963-6; R. v. Boyle, [1990] 2 S.C.R. 906, per McLachlin J., dissenting on the grounds, at pp. 939-40, and per Wilson J. for the majority at pp. 914, 917-8 and 925-6.

Para. 79. Thus where a person who stands in a special relationship with a reporting issuer acquires knowledge of material information about the issuer, it is neither unfair nor unreasonable to impose upon that person the duty to refrain from purchasing or selling securities of the issuer prior to public disclosure of the information. Moreover, where the prosecution proves beyond a reasonable doubt all of the factual elements which support the imposition and breach of that duty, it is neither unfair nor unreasonable to require that person to assume the burden of proving a common law defence of due diligence or reasonable mistake as to a material fact in order to escape liability.

As noted above in paragraph 15 of Woods Farley J. set out the various constituent parts of s.76(1) which are discussed below.

Element (A): The Defendant Is In A Special Relationship With The Public Company

The Defence agrees that Bre-X became a "*reporting issuer*" within the meaning of s.1(1) of the Securities Act on April 23, 1996 when it began trading on the T.S.E. . The Defence conceded that Felderhof was a person in a "*special relationship*" with Bre-X within the meaning of s.76(5). Felderhof was a director, officer and employee of Bre-X. On May 1, 1993, Bre-X hired Felderhof as its General Manager. On October 5, 1994 Felderhof was appointed Senior Vice-President of Exploration. On May 10, 1996 Felderhof joined the Bre-X Board of Directors as Vice-Chairman. See page 110 of these reasons.

Exhibit S5 Volume I: paragraphs 134-143
Exhibit S12: paragraphs 3, 9
Transcript: August 24, 2006, page 110

Element (B): The Defendant Purchases Or Sells Securities Of That Public Company

Felderhof allegedly had two trading accounts: the Nesbitt Burns trading account (Exhibit 778) conceded by the Defence (although it is not conceded that Felderhof gave the trading instructions) and the Deacon or Grays Inn J & I trading account (Exhibit 961) disputed by the Defence.

The O.S.C. called two witnesses, Sheila David and Michael Judge. With respect to David the O.S.C. states and the Defence agrees and comments as follows at paragraphs 165 and 166 of Exhibit S5 Volume I:

> Para. 165. Sheila David was the manager of trading, review and analysis at Market Regulation Services Inc. (RS), the independent regulation services provider for the Canadian equity markets, from March 2003 until her death in July 2005. David analyzed the trading in Bre-X shares by selected individuals, including Felderhof, from January 1, 1996 to April 30, 1997.
>
> **The Defence agrees with this paragraph with the addition that Ms. David analyzed the trading in a number of accounts and she concluded that certain accounts represented the trading of certain individuals. Ms. David confirmed, for example, that she had no knowledge as to whether Mr. Felderhof directed any trades in the Deacons account. (Evidence of Ms. David, April 12, 2005, Vol. 97, page 72) There is no evidence in this proceeding linking Mr. Felderhof, Mrs. Felderhof or anyone else outside of Barclays to the instructions to sell shares in the Deacons account.**
>
> Para. 166. David had extensive experience as an investigator for RS and the TSE. She received honours in the Canadian Securities Course and completed the Registered Representative's Examination, Canadian Futures Examination, Canadian Options Course and Traders Training Course. She received the Award of Excellence in the Branch Managers Course and Honours in the Canadian Operations Course.
>
> **The Defence agrees; however, Ms. David was not qualified as an expert. Her work involved taking data from account statements and putting it into a master spreadsheet.**

In oral submissions the Defence conceded:

> MR. GROIA: Seven seventy-six. You'll see that Sheila David's work, which I have to say there's very little dispute from us about the work Sheila David did.

Transcript: August 24, 2006, page 110

Michael Judge was a portfolio manager at Deacon Capital Corporation responsible for Barclays offshore banking centres including the Cayman Islands which was the address for the Grays Inn J& I account.

Exhibit S12: paragraph 11
Exhibit S5 Volume I: paragraph 158

THE NESBITT BURNS ACCOUNT

On July 20, 1995 Felderhof opened a personal account at Nesbitt Burns in his name. The broker or registered representative for that account was Barbara Horn.

Exhibit 778

In the new account application titled "*Client Account Agreement*", Ingrid Felderhof, the Defendant's wife at the time, is named as having "*trading authority in this account.*"

Exhibit 778

In their written submissions the O.S.C. sets out the shares allegedly sold by Felderhof in each of the charge periods.

The Defence agrees with the number of Bre-X shares sold from the accounts but submits the O.S.C. has not proven that Felderhof gave any of the instructions for the trades.

The O.S.C. refers to "*net profit*" in these paragraphs but by letter dated August 18, 2006 corrected this to read "*net proceeds*". Each paragraph must be read with that change in mind.

Following are those written submissions with the Defence comments.

- Count 1 –Paragraphs 145-146:

  Para. 145. Between April 24, 1996 and May 16, 1996, Felderhof sold 100,000 (pre-split) Bre-X shares from his personal Nesbitt Burns account 710-14707 for a net profit of $21,047,955.

  The Defence agrees that 100,000 shares of Bre-X were sold in the Nesbitt Burns account during this period for net proceeds of $21,047,955. The OSC has not proven that Mr. Felderhof gave any of the instructions for the fourteen different

trades that occurred during this period. The OSC appears to concede at paragraph 153 that Ingrid Felderhof gave the instructions for the sales on April 24 and 25, 1996. The OSC has cited no evidence to support its argument that Mr. Felderhof gave instructions to sell any of the shares in this period. The OSC bears the onus to prove that Mr. Felderhof gave instructions to sell the shares. The Defence submits that the OSC has failed to prove this.

Para. 146. From April 24, 1996 to May 16, 1996, Felderhof sold the following Bre-X shares:

Date	Number of Bre-X shares sold (pre-split)	Share price	Net profit
April 24, 1996	5,000	$188.76	$933,500.00
April 25, 1996	5,000	$185.88	$929,100.00
May 1, 1996	5,000	$205.028	$1,024,840.00
May 2, 1996	10,000	$213.165	$2,131,050.00
May 7, 1996	5,000	$199.24	$995,900.00
May 8, 1996	5,000	$197.76	$988,500.00
May 9, 1996	5,000	$200.649	$1,002,945.00
May 13, 1996	8,300	$212.6445	$1,764,452.00
May 14, 1996	7,400	$213.4324	$1,578,956.00
May 14, 1996	8,300	$213.8349	$1,774,332.00
May 15, 1996	14,000	$216.3428	$3,027,960.00
May 15, 1996	12,000	$219.9658	$2,638,870.00
May 15, 1996	5,400	$224.287	$1,210,826.00
May 16, 1996	4,600	$227.6086	$1,046,724.00
TOTAL	**100,000**		**$21,047,955.00**

The Defence agrees that these shares were sold. However, the OSC has not cited any evidence to support its argument or proven that Mr. Felderhof gave any of the instructions for these sales.

- Count 2 –Paragraphs 456-459:

Para. 456. From June 24, 1996 to July 26, 1996, Felderhof traded in both his personal Nesbitt Burns account 710-14707 and his Grays Inn J&I account J&I 34962A-3.

The Defence agrees that the shares of Bre-X were sold in the Nesbitt Burns account and the Grays Inn account during this period for net proceeds of $22,575,432.03. The OSC has not proven that Mr. Felderhof gave any of the instructions for the twenty-two different trades that occurred during this period. The OSC has cited no evidence to support its argument that Mr. Felderhof gave instructions to sell any of the shares in this period. The OSC bears the onus of proving that Mr. Felderhof

gave instructions to sell the shares. The Defence submits that the OSC has failed to prove this.

Para. 457. Between June 24, 1996 and July 26, 1996, the relevant period for Count 2, Felderhof sold 136,500 Bre-X shares from his personal Nesbitt Burns account 710-14707 for a net profit of $3,339,935.00.

Date	Number of Bre-X shares Sold	Share price	Net profit
July 17, 1996	70,000	$24.5214	$1,712,300.00
July 18, 1996	16,500	$24.4318	$402,135.00
July 19, 1996	50,000	$24.57	$1,225,500.00
TOTAL	**136,500**		**$3,339,935.00**

The Defence disagrees. See paragraph 456 above.

Para. 458. Between June 24, 1996 and July 26, 1996, Felderhof sold 855,300 Bre-X shares from his Grays Inn J&I account for a net profit of $19,235,497.0

Date	Number of Bre-X shares Sold	Share price	Net profit
June 24, 1996	50,000	$24.00	$1,196,250.00
June 25, 1996	5,000	$24.00	
June 25, 1996	45,000	$24.15	$1,203,000.00
June 26, 1996	22,300	$23.522	$522,877.02
July 4, 1996	35,500	$21.919	$773,493.31
July 5, 1996	133,000	$21.228	$2,813,415.50
July 8, 1996	50,000	$20.573	$1,024,930.00
July 8, 1996	31,500	$20.573	$645,705.90
July 9, 1996	50,000	$20.875	$1,040,000.00
July 10, 1996	50,000	$22.29	$1,110,750.00
July 10, 1996	50,000	$22.22	$1,107,250.00
July 12, 1996	50,000	$22.605	$1,126,505.00
July 15, 1996	50,000	$22.50	$1,121,250.00
July 16, 1996	50,000	$22.064	$1,099,450.00
July 17, 1996	50,000	$23.705	$1,181,500.00
July 18, 1996	50,000	$24.02	$1,197,250.00
July 19, 1996	15,000	$24.066	$359,875.50
July 25, 1996	63,000	$25.239	$1,585,369.80
July 26, 1996	5,000	$25.40	$126,625.00
TOTAL	**855,300**		**$19,235,497.03**

The Defence disagrees. See paragraph 456 above.

Para. 459. The Crown submits that it has proven beyond a reasonable doubt that between June 24, 1996 and July 26, 1996, Felderhof sold 991,800 Bre-X shares in

both his personal Nesbitt Burns and Grays Inn J&I account for a net profit of $22,575,432.03.

The Defence disagrees. See paragraph 456 above.

- Count 3 –Paragraphs 511-515:

Para. 511. From August 1, 1996 to August 16, 1996, Felderhof traded in both his personal Nesbitt Burns account 710-14707 and his Grays Inn J&I account 34962A-3.

The Defence agrees that the shares of Bre-X were sold in the Nesbitt Burns account and the Grays Inn account during this period for net proceeds of $17,323,961.75. The OSC has not proven that Mr. Felderhof gave any of the instructions for the thirteen different trades that occurred during this period. The OSC has cited no evidence to support its argument that Mr. Felderhof gave instructions to sell any of the shares in this period. The OSC bears the onus of proving that Mr. Felderhof gave instructions to sell the shares. The Defence submits that the OSC has failed to prove this.

Para. 512. Between August 1, 1996 and August 16, 1996, Felderhof sold 70,200 Bre-X shares from his personal Nesbitt Burns account for a net profit of $1,724,553.00.

Date	Number of Bre-X shares Sold	Share price	Net profit
August 7, 1996	20,200	$24.6019	$495,748.00
August 8, 1996	50,000	$24.6361	$1,228,805.00
TOTAL	**70,200**		**$1,724,553.00**

The Defence disagrees. See paragraph 511.

Para. 513. Between August 1, 1996 and August 16, 1996, Felderhof sold 644,700 Bre-X shares from his Grays Inn J&I account for a net profit of $15,599,408.75.

Date	Number of Bre-X shares Sold	Share price	Net profit
August 1, 1996	82,500	$24.99	$2,055,512.25
August 2, 1996	34,900	$24.989	$869,505.58
August 6, 1996	60,000	$24.695	$1,477,248.00
August 7, 1996	35,000	$24.457	$853,373.50
August 8, 1996	60,000	$24.562	$1,469,250.00
August 9, 1996	46,400	$24.001	$1,110,198.88
August 12, 1996	33,000	$23.995	$789,373.20
August 13, 1996	30,400	$24.017	$727,839.84

August 14, 1996	100,000	$23.804	$2,372,950.00
August 15, 1996	100,000	$24.043	$2,396,890.00
August 16, 1996	62,500	$23.711	$1,477,267.50
TOTAL	**644,700**		**$15,599,408.75**

The Defence disagrees. See paragraph 511.

Para. 514. Between August 1, 1996 and August 16, 1996, Felderhof sold 714,900 Bre-X shares in both his personal Nesbitt Burns and Grays Inn J&I account for a net profit of $17,323,961.75.

The Defence disagrees. See paragraph 511.

Para. 515. The Crown submits that it has proven beyond a reasonable doubt that Felderhof sold Bre-X shares.

The Defence disagrees. See paragraph 511.

- Count 4 –Paragraphs 523-525:

Para. 523. From August 26, 1996 to September 10, 1996, Felderhof only traded in his personal Nesbitt Burns account 710-14707.

The Defence agrees that the shares of Bre-X were sold in the Nesbitt Burns account during this period for net proceeds of $22,821,107.00. The OSC has not proven that Mr. Felderhof gave any of the instructions for the eleven different trades that occurred during this period. The OSC has cited no evidence to support its argument that Mr. Felderhof gave instructions to sell any of the shares in this period. The OSC bears the onus of proving that Mr. Felderhof gave instructions to sell the shares. The Defence submits that the OSC has failed to prove this.

Para. 524. Between August 26, 1996 and September 10, 1996, Felderhof sold 913,800 Bre-X shares from his personal Nesbitt account for a net profit of $22,821,107.00.

Date	Number of Bre-X shares Sold	Share price	Net profit
August 26, 1996	126,000	$25.0498	$3,148,720.00
August 26, 1996	124,000	$25.152	$3,111,410.00
August 27, 1996	86,300	$25.007	$2,152,927.00
August 27, 1996	7,000	$25.05	$174,930.00
August 28, 1996	121,000	$25.0461	$3,023,330.00
August 29, 1996	35,600	$25.0592	$889,914.00
August 30, 1996	208,500	$24.5303	$5,102,065.00
September 9, 1996	85,400	$25.6099	$2,181,966.00

September 10, 1996	10,000	$25.25	$251,900.00
September 10, 1996	10,000	$25.26	$252,000.00
September 10, 1996	100,000	$25.3794	$2,531,945.00
TOTAL	**918,300**		**$22,821,107.00**

The Defence disagrees. See paragraph 523.

Para. 526. The Crown submits that it has proven beyond a reasonable doubt that Felderhof sold Bre-X shares.

The Defence disagrees. See paragraph 523.

The total number of Bre-X shares sold above was corrected from 918, 300 to 913, 800.

Defence Position

Starting at paragraph 4 of Exhibit S3 Tab C the Defence submits:

Sale of Securities

Para. 4. In *R. v. Woods*, there is a lengthy discussion by Farley J. of section 75(1) (now s. 76(1)) of the *Securities Act* and the requirement to show that an accused either purchased or sold securities of a reporting issuer. In *Woods*, the accused argued that a purchase or sale had to be a beneficial purchase or sale of securities. The Court disagreed.
***R. v. Woods*, [1994] O.J. No. 392 (Ont. Ct. J. (Gen. Div.)) (QL) paras. 29-39**

Para. 5. In *Woods*, the accused gave the trading instructions for sales in accounts owned by others. The owners of the accounts were not charged.
***R. v. Woods, supra* at paras. 21-22 and 25**

Para. 6. It is submitted that the intent of s. 76 is to capture the person who had the undisclosed material information and prevent that person from giving any instructions to purchase or sell securities. To borrow from the words of Farley J. in *Woods*, there would be no sale without the person who provided the instructions to sell. It is the person who gives the instructions to sell who should be caught by s. 76, not someone who is only shown to be the owner of the shares.
***R. v. Woods, supra* at para. 32**

Para. 8. With respect to the Nesbitt Burns Account, the documentary record indicates that both Mr. Felderhof and Mrs. Felderhof gave instructions on the account. Mr. Felderhof was entitled to give instructions as the account holder. Mrs. Felderhof, on the other hand, was entitled to give instructions pursuant to her

trading authority, which, according to Ms. David, authorized Mrs. Felderhof "to trade in that account."

Para. 9. The defence submits that, for any given trade during the Charge Periods, the OSC has failed to establish whose instructions resulted in the sale of securities of Bre-X. Although there is a documentary record of trading instructions, that record is inconclusive with respect to specific trades. There is also no evidence with respect to oral instructions which may have been given by Mr. Felderhof or Mrs. Felderhof, either apart from, or in conjunction with, written instructions that are part of the documentary record.

In Exhibit S4 the Defence submits:

Sale of Shares

Para. 4. In paragraphs 149 through 153IT, the OSC acknowledges that Ingrid Felderhof had the authority to sell shares and in fact did direct the sale of certain shares of Bre-X in the Nesbitt Burns Account. The OSC alleges, without supporting evidence, that Mrs. Felderhof sold these shares "on behalf of" Mr. Felderhof. There is no evidence that Mr. Felderhof was aware of this sale by Mrs. Felderhof before the sale was made.
OSC Volume I, paragraph 149 – 153IT

Para. 5. The OSC appears to rely upon the fact that this trade was reported on Mr. Felderhof's insider report after the trade to conclude that "Mr. Felderhof knew he was responsible for the trading in [the Nesbitt Burns Account]". From this statement in paragraph 154IT and the subsequent 47 paragraphs in which the OSC argues that Mr. Felderhof was the beneficial owner of the Grays Inn Account, the OSC's position appears to be that if the OSC proves that Mr. Felderhof was the beneficial owner of the shares and that the shares were sold, then the OSC has proven that Mr. Felderhof sold the shares for the purposes of s. 76(1) of the *Securities Act*.
OSC Volume I, paragraph 154IT

Para. 6. The OSC provides no authority for its apparent position that it need not prove who directed the sale of the shares.

Para. 7. It is submitted that the OSC's position is and must be wrong. If the OSC's position were correct, then an insider of a company who had a managed account (an account managed by a professional portfolio manager who by the nature of a managed account exercised full trading authority over the account) could go to jail if the portfolio manager happened to buy or sell shares of the

insider's company at a time when the insider had material undisclosed information. The insider could go to jail despite the fact that the insider had no knowledge of or control over the decision to buy or sell the securities. The insider would only learn of the purchase or sale after the fact and would report it as required.

...

Para. 9. As Ms. David acknowledged on cross-examination, her tables and spreadsheets were simply a compilation of information from documents that she or the OSC had obtained. Ms. David had no firsthand knowledge regarding the Nesbitt Burns Account or the Grays Inn Account. Her tables and spreadsheets do not provide any evidence as to who directed the trading in either account.
Evidence of Ms. David, Volume 97, pages 15 - 16

In Exhibit S12 the Defence submissions and the O.S.C. comments are as follows:

Para. 14. Although the OSC advised this Court during its opening statement that Ms. Horn would be called as a witness, Ms. Horn did not testify at trial. The only witness called by the OSC who had any knowledge of the Nesbitt Burns Account was Ms. David, who had only reviewed certain account documents as part of her investigation. By her own admission, Ms. David had no firsthand knowledge of the Nesbitt Burns Account.
November 21, 2000, Volume 20, page 40
Evidence of Ms. David, Volume 97, page 15

The OSC did not call Horn. At the request of the Defence however, the OSC kept Horn under summons so that the Defence could consider whether they would call her. [Transcript, December 8, 2004, pp. 64-71].

The OSC admits that David relied on the documents contained in volumes 8, 9 & 10 to conduct her analysis of Felderhof's trading (David transcript, April 7, 2005 at 77; Exhibit SD788-780). These documents include new client application forms, monthly statements, trade tickets, receipt and delivery tickets, cheques, insider trading reports & share transfer ledgers, written instructions from Felderhof, Bre-X option exercise documentation, wire instructions from brokerage firms and business records of Nesbitt Burns, Deacon and Montreal Trust
[David transcript, April 7, 2005 p. 77].

...

Para. 16. The account opening documentation for the Nesbitt Burns Account indicates that Mr. Felderhof's wife, Ingrid Felderhof, had trading authority over the account. Ms. David testified that "[t]rading authority authorizes someone, other than the account holder, *to trade in that account*" [emphasis added]. Ms. David agreed that, with this trading authority, Mrs. Felderhof could initiate a sale of securities in the Nesbitt Burns Account on her own, and could place a trade on the account without discussing the trade with Mr. Felderhof.
Part of Exhibit 782, Nesbitt Burns Client Account Agreement, Tab 1
Evidence of Ms. David, Volume 97, pages 25-26

The OSC denies the first sentence of paragraph 16. The new client application form Exhibit SD782 states that: Ingrid Felderhof had trading authority **in** Felderhof's personal Nesbitt Burns account. Exhibit SD782 also states that Ingrid Felderhof did not guarantee the account or have a financial interest in it. See also OSC, Volume I, page 35, para 149-150.

The OSC admits that David testified that trading authority authorizes someone other than the account holder to trade in the account [David transcript, April 12, 2005 p. 25].

The OSC admits that David testified that Ingrid Felderhof could call Horn and place a trade on Felderhof's account. Horn did not have to ask whether Ingrid Felderhof had discussed it with Felderhof. [David transcript, April 12, 2005 p. 25]

David testified:

MR. GROIA: Okay. Now, can you explain to the Court what it means to have trading authority?

MS. DAVID: Trading authority authorizes someone, other than the account holder, to trade in that account.

MR. GROIA: Okay. So just to make it simple, it would allow Ingrid Felderhof to call Barbara Horn and place a trade on John Felderhof's account.

MS. DAVID: That's correct.

MR. GROIA: And Ingrid Felderhof could do that without discussing the trade with John Felderhof; in other words, if Ingrid Felderhof calls Barbara Horn, Barbara Horn doesn't have to inquire whether Ingrid has discussed it with the account holder, John Felderhof.

MS. DAVID: That's correct.

MR. GROIA: Barbara Horne could just put through the order on Ingrid's word.

MS. DAVID: That's correct.

Transcript: April 12, 2005, page 25

Continuing in Exhibit S12:

Para. 19. As Ms. Horn was not called as a witness by the OSC, there is no evidence as to what additional instructions she may have received from Mr. Felderhof or Mrs. Felderhof regarding sales of Bre-X shares in the Nesbitt Burns Account. In addition, there is no evidence as to who provided specific instructions for the majority of the sales in the Nesbitt Burns Account, the details of those instructions, when the instructions were given, whether the instructions were written or verbal, and whether written instructions were ever revised or countermanded by verbal instructions.

The OSC denies this paragraph. The OSC's position is that this Court may not draw an adverse inference from the OSC's decision not to call Horn. Where a witness is equally available to both parties, an adverse inference cannot be drawn from the party's decision not to call a particular witness. In other words, the Court cannot infer that Horn would have testified that Felderhof did not sell Bre-X shares. See *R v. Jolivet; King v. Merrill Lynch* and excerpt from Sopinka on Evidence provided to the Court during the oral submissions. [See discussion at Closing Submissions transcript, August 29, 2005 at 60-63.]

...

Para. 21. Mr. Felderhof filed Insider reports reflecting the sales of Bre-X shares in the Nesbitt Burns Account. With respect to Insider reports, Ms. David testified as follows:

Q. Okay. Would you agree with me that this report tells us nothing about who directed those particular sales of Bre-X shares?

A. That's correct.

Q. And so it doesn't indicate, for example, whether Mr. Felderhof knew in advance of those trades whether those trades were taking place.

A. No, it does not.

Q. And those trades could have been carried out without Mr. Felderhof's knowledge by the person who had trading authority on his account?

A. Yes.

Evidence of Ms. David, Volume 98, page 17

The OSC admits that Felderhof filed insider reports until May 30, 1996. [OSC Vol. I, page 42, paragraph 199] The OSC states that to the extent that Felderhof claimed his sales of Bre-X shares on his insider reports as required by section 107 of the Act, it can be inferred that Felderhof viewed these Bre-X shares as being under his control or direction and the sales of these Bre-X shares as a change in his direct or indirect beneficial ownership.

s. 107(1) Report
A person or company who becomes **an insider of a reporting issuer**, other than a mutual fund, shall, within 10 days from the day that he, she or it becomes an insider, or such shorter period as may be prescribed by the regulations, **file a report as of the day on which he, she or it became an insider disclosing any direct or indirect beneficial ownership of or control or direction over securities of the reporting issuer as may be required by the regulations**.

s. 107(2) Same
An insider who has filed or is required to file a report under this section or any predecessor section **and whose direct or indirect beneficial ownership of or control or direction over securities of the reporting issuer changes from that shown** or required to be shown in the report or in the latest report filed by the person or company under this section or any predecessor section **shall, within 10 days from the day on which the change takes place**, or such shorter period as may be prescribed by the regulations, **file a report of direct or indirect beneficial ownership of or control or direction over securities of the reporting issuer as of the day on which the change took place and the change or changes that occurred, giving any details of each transaction as may be required by the regulations.**

In oral submission the Defence stated:

> MR. RICHARD: And it appears from the OSC's factum that they are focusing more on, and have focused more on beneficial ownership of shares, or if I could

put it a different way, if we demonstrate that someone owned the shares and the shares were sold, then that's all that needs to be established under s. 76, and I submit that is an incorrect interpretation of the section.

...

So for that reason I come back to simply demonstrating beneficial ownership in shares is insufficient. I submit that what is necessary is the demonstration that the very person with the knowledge is also the person who gave the instructions for the purchase or the sale.

And Mr. Richter already referred to the somewhat the second connection I submit is necessary and that's really the temporal connection. If we look at the time the instruction was given – so if we taken an example of now we have just one person who may have knowledge and also gives the instruction, it's the timing of that instruction when we look at and analyze the person's knowledge to determine whether at that time they had knowledge of a material undisclosed fact.

...

MR. GROIA: And so the reason we've suggested that you start with determining which of the trades have been proven to be sales by Mr. Felderhof, is because if you decide that the OSC has not proven a reasonable doubt that he put in sale orders, that's the end of the inquiry, because the Statute says "a person, an insider who sells securities with knowledge."

Transcript: August 14, 2006, pages 86-87, pages 90-91, pages 111-112

O.S.C. Position

At paragraph 153 and 154 of Exhibit S5 Volume I the O.S.C. submits and Defence comments as follows:

Para. 153. Regardless of whether Ingrid Felderhof instructed Horn to sell 10,000 Bre-X shares on one occasion, Felderhof was the account holder and was fully responsible for the trading in his account.

The Defence agrees that it appears as though Mrs. Felderhof gave the instructions for the sale of shares that occurred on April 24 and 25, 1996. The Defence disagrees with any suggestion that an account holder can be guilty of insider trading just because he or she is the account holder. It is necessary for the OSC to prove that Mr. Felderhof gave instructions to sell in order to find a breach of s. 76(1). The OSC has failed to do so.

Para. 154. Felderhof knew he was responsible for the trading in his account and reported this sale in his May 4, 1996 insider report. Felderhof signed and submitted this insider report which is statutorily required.

The Defence agrees that Mr. Felderhof submitted his insider report in which the sales on April 24 and 25, 1996 were reported. The OSC does not state what it means by "knew he was responsible". As Ms. David confirmed in her evidence, an insider report does not give any indication that the person filing the report had any knowledge of the sale before the sale took place. (Evidence of Ms. David, April 13, 2005, Vol. 98, page 17) Where someone else has trading authority in an account, insider reports are of little to no assistance in proving what the OSC must prove: that Mr. Felderhof gave instructions to sell for every sale at issue.

In oral submissions the O.S.C. submits:

> MS. COLE: Element B is that the defendant purchased or sold shares of a public company. And Your Honour, it's our submission that a plain reading of s. 76 of the Securities Act requires the OSC to prove that the defendant purchased or sold shares, not that the defendant gave instructions to purchase or sell shares. The trading documents are proof of the sales and once those documents are admitted into evidence, the sales are proven.
>
> ...
>
> Your Honour, in every insider trading case that I'm aware of, except for Woods, the purchases or sales of securities have been proven in this way. To interpret the Act as requiring the OSC to prove who gave the instructions to trade in every case would make it unmanageable for the OSC to prosecute insider trading. It would be contrary to the purpose of the Act, which is to protect investors by preventing insiders from trading when they have material information that the trading public doesn't have.
>
> ...
>
> Your Honour, it's our submission that Woods was an extraordinary case and that it should not be interpreted as requiring the Crown in every case to prove who gave the trading instructions. This Court must interpret the Securities Act in a way that is workable, in a way that it fulfils the purposes of the Act.
>
> ...
>
> Well, it's almost this situation, but it's only the situation if you consider the fact that Mrs. Felderhof gave instructions in one instance as the sale. So my suggestion is you don't actually have to look at those instructions. The trade is Mr. Felderhof's trade, whether she gave the instructions or not, and it's not the same situation as the Woods case.

Transcript: August 29, 2006, pages 13, 14, 17, 18

There are two issues.

1. Is it sufficient to satisfy s.76(1) that the O.S.C. simply prove the sale of shares in the Defendant's account which as noted above the Defence admits (at least with respect to the Nesbitt Burns account because the Defence submits the O.S.C. has failed to prove the Grays Inn J & I account was Felderhof's)? Or does the O.S.C. have to prove each and every instruction given by the Defendant for each and every sale (as the Defence submits)?
2. If the O.S.C. has to prove that Felderhof gave instructions for each and every sale, does the evidence prove that beyond a reasonable doubt.

1. Proof of Selling Required Under S. 76(1)

The Canadian Oxford Dictionary defines purchase and sell, in part, as follows:

> **Purchase**: "*acquire by payment; buy*", "*obtain or achieve at some cost*",
>
> **Sell**: "*exchange (goods, services etc.) for money*"

I agree with the O.S.C. that s.76(1) states that the O.S.C. is required to prove that the Defendant purchased or sold shares and not that the Defendant gave instructions to purchase or sell shares. Can an insider purchase or sell shares within the meaning of s.76 (1) without giving instructions?

As noted above Farley J. in R. v. Woods, supra, at paragraph 77 states:

> Para. 77 The factual elements of the actus reus of the offence under s.75(1) have been listed in the discussion on Issue 1. There is room for these common law defences to operate with respect to each of these four factual elements of the offence...Moreover, an accused may assert that all due care was taken either to prevent the purchase or sale of the securities, for example where this occurs through an agent or broker (second element)...

These statements by Farley J. imply that where a purchase or sale occurs through an agent or broker and not through the insider that is sufficient to prove the actus reus and that then the defence of due diligence is available if the insider took all due care to prevent the purchase or sale.

That would support the O.S.C. position that they need not prove that the Defendant gave instructions to purchase or sell but can simply rely on the trading documents as proof of the sales in the Defendant's trading account.

With respect to the Nesbitt Burns account, applying the interpretation above of R. v. Woods and on the facts of this case, sales through Mrs. Felderhof would be sales within the meaning of s.76(1) with the onus then on John Felderhof to prove that all due care was taken to prevent the sale. Mrs. Felderhof is referred to as an agent on page 3 of the Client Account Agreement. Examples of Felderhof preventing sales by his broker are found in Exhibit 778, Tab Nesbitt, pages 93 and 106, which are respectively faxes dated July 20, 1996 and August 17, 1996 from Felderhof to Nesbitt Burns with respect to suspending his trading because of pending press releases by Bre-X.

The O.S.C. submits s.76(1) should be interpreted in a way that is consistent with and promotes the purposes and principles of the *Securities Act* found at:

> **1.1 Purposes.** –The purposes of this Act are,
>
> (a) to provide protection to investors from unfair, improper or fraudulent practices; and
> (b) to foster fair and efficient capital markets and confidence in capital markets.
>
> **2.1 Principles to consider.** –In pursuing the purposes of this Act, the Commission shall have regard to the following fundamental principles:
>
> 1. Balancing the importance to be given to each of the purposes of this Act may be required in specific cases.
>
> 2. The primary means for achieving the purposes of this Act are,
>
> i. requirements for timely, accurate and efficient disclosure of information
> ii. restrictions on fraudulent and unfair market practices and procedures, and
> iii. requirements for the maintenance of high standards of fitness and business conduct to ensure honest and responsible conduct by market participants.

Participation in the capital markets is a privilege and not a right. Section 76(1) and 122(1)(c) are regulatory and not criminal offences. The different sections of the *Securities Act* are part of a larger regulatory framework and are not to be analyzed in isolation but in a regulatory context.

Section 76(1) is a strict liability offence. In Woods, supra, Farley J stated:

> Para. 51. According to Stanley M. Beck ("Beck"), a former chairman of the OSC, the prohibition of insider trading is consistent with the objectives which underlay most securities regulations including the S Act. These are as follows – investor protection, the fair and efficient operation of capital markets and the fostering and maintenance of public confidence in these markets. See also Pacific Coast Coin Exchange v. OSC (1977), 80 D.L.R. (3d) 529 (S.C.C.) at p. 531 and 538. Beck and Michael R. Sprung ("Sprung"), a Canadian equities portfolio manager of the Ontario Teachers' Pension Plan Board, gave affidavit evidence to the effect that,

> without the protection of insider trading prohibitions, members of the public trade in securities at a disadvantage to those with knowledge of material insider information. If insider trading were permitted, insiders could make substantial profits at the expense of the public who trade in securities without access to material information known to the insider. It is not just a question of the house in a casino situation moving the odds in a card game or the dealer counting cards, it is akin to the dealer being able to play with marked cards. The result is a lack of fairness in the capital markets and the undermining of investor confidence in those markets. Beck and Sprung gave evidence that there is now a general consensus among the leading industrialized nations that insider trading is detrimental to the functioning of capital markets and that it should be controlled within strict limits as part of the overall regime of securities regulations...
>
> Para. 52. It would appear that insider trading provisions promote the broader objectives of the S Act in at least four ways:
>
> (a) they protect the investing public from trading at a disadvantage with those in possession of material information;
> (b) they encourage timely disclosure of material information, which in turn ensures that market prices reflect real values and promotes an appropriate allocation of capital in the marketplace;
> (c) they foster and protect special relationships; and
> (d) they promote compliance by market participants with an established standard of conduct.

Interpreting s. 76(1) in a way that promotes the purpose and principles of the *Securities Act* supports the O.S.C. position.

As noted above the Defence relies on Woods to argue that the O.S.C. is required to prove that Felderhof gave instructions for every sale. I agree with the O.S.C. submission that Woods was an extraordinary case where the insider sold share in another person's account. In Woods the owner of the account was not charged. In Woods the issue was quite different than the case at bar. In Woods the issue was whether someone who was an insider but not the owner of the account and who gave trading instructions on that account, could be charged and convicted for insider training in another's account.

2. Is There Proof That Felderhof Gave Instructions To Sell The Shares

The following discussion assumes the O.S.C. is required to prove Felderhof's trading instructions. There is no direct evidence Felderhof directed each sale. There is indirect or circumstantial evidence that Felderhof directed the sale of shares from the Nesbitt Burns account. Does it establish beyond a reasonable doubt that Felderhof directed each trade?

In paragraph 17 and 18 of Exhibit S12 the Defence sets out the correspondence from the Defendant and Mrs. Felderhof to Nesbitt Burns with respect to the Nesbit Burns account in or around the various charge periods.

> Para. 17. The documentary record indicates that Mrs. Felderhof sent the following correspondence to Nesbitt Burns with respect to the Nesbitt Burns Account (in or around the Charge Periods):

The OSC submissions about this issue are at OSC, Volume I, page 35, para 151-154:

151. At paragraph 10 of the Defence closing argument the Defence states that "the documentary record indicates that Mrs. Felderhof sent the following correspondence to Nesbitt Burns with respect to the Nesbitt Burns Account (in or around the Charge Periods)".

152. In nine of the letters sent by Ingrid Felderhof to Horn, Ingrid Felderhof instructed Horn to transfer money. In one of these letters, Ingrid Felderhof asked Horn to sell Bre-X shares on behalf of Felderhof.

153. Regardless of whether Ingrid Felderhof instructed Horn to sell 10,000 Bre-X shares on one occasion, Felderhof was the account holder and was fully responsible for the trading in his account.

154. Felderhof knew he was responsible for the trading in his account and reported this sale in his May 4, 1996 insider report. Felderhof signed and submitted this insider report which is statutorily required.

(a) In a fax dated April 10, 1996, Mrs. Felderhof provided Nesbitt Burns with instructions to transfer "funds from Bre-X shares sold" out of the Nesbitt Burns Account;

The OSC denies that this correspondence was sent in the charge period or that it was instructions to trade.

Part of Exhibit 778, Fax dated April 10, 1996, Tab Nesbitt, page 38

(b) In a fax dated April 17, 1996, Mrs. Felderhof instructed Nesbitt Burns to "give Bre-X Minerals Ltd. $1,278,750 to cover John Felderhof's options which he exercised on April 10, 1996";

The OSC denies that this correspondence was sent in the charge period or that it was instructions to trade

Part of Exhibit 778, Fax dated April 17, 1996, Tab Nesbitt, page 40

(c) In a fax dated April 18, 1996, Mrs. Felderhof provided Ms. Horn with Mrs. Felderhof's contact information;

The OSC denies that this correspondence was sent in the charge period or that it was instructions to trade

Part of Exhibit 778, Fax dated April 18, 1996, Tab Nesbitt, page 42

(d) In a fax dated April 18, 1996, Mrs. Felderhof instructed Nesbitt Burns to sell 15,000 shares of Bre-X over April 18 and 19, 1996. Those shares were sold on April 19, 1996, less than a week before the commencement of the First Charge Period on April 24, 1996;

The OSC denies that this correspondence was sent in the charge period.

Part of Exhibit 778, Fax dated April 18, 1996, Tab Nesbitt, page 43

(e) In a fax dated April 19, 1996, Mrs. Felderhof instructed Nesbitt Burns to "give Bre-X Minerals Ltd. $1,278,750 to cover John Felderhof's options which he exercised for the week of April 19, 1996";

The OSC denies that this correspondence was sent in the charge period or that it was instructions to trade

Part of Exhibit 778, Fax dated April 19, 1996, Tab Nesbitt, page 45

(f) In a fax dated Monday, April 22, 1996, Mrs. Felderhof instructed Nesbitt Burns to sell 5,000 shares of Bre-X over "Tuesday, Wednesday and Thursday, slowly for the best price that you feel you can achieve." Apparently acting on these instructions, Nesbitt Burns sold 5,000 shares on each of April 22, 24, and 25, 1996. The sales on April 24 and 25, 1996, fall within the First Charge Period;

Part of Exhibit 778, Fax dated April 22, 1996, Tab Nesbitt, page 47
Part of Exhibit 778, Nesbitt Burns Monthly Statement for the Month Ended April 30, 1996, Tab Nesbitt, pages 59-60

The OSC admits that on April 22, 1996 Ingrid Felderhof instructed Horn to sell 5,000 Bre-X shares on April 22, 24 and 25, 1996. "Please place 5,000 Bre-X Mineral shares on the market today, Tuesday [23], Wednesday [24], Thursday slowly for the best possible price you feel you can achieve."

These instructions appear to be a follow-up on some trading instructions given by Felderhof to sell 15,000 Bre-X shares per week for the next two months.

On April 18, 1996, Ingrid Felderhof told Horn that "**We** would like to put another 15,000 Bre-X shares on to be sold today through to tomorrow."... "**As you know we are looking to sell 15,000 per week every week for the next two months**."

The OSC admits that Horn sold 5,000 Bre-X shares on April 24, 1996 and 5,000 April 25, 1996. Exhibit SD778, tab Nesbitt Burns at 048. Felderhof reported these sales on his May 9, 1996 insider report. [Exhibit SD780 at 247-48].

(g) In a fax dated April 25, 1996, Mrs. Felderhof instructed Nesbitt Burns to "give Bre-X Minerals Ltd. $1,278,750 to cover John Felderhof's options which he exercised for the week of April 26, 1996";

Part of Exhibit 778, Fax dated April 25, 1996, Tab Nesbitt, page 49

The OSC admits that this correspondence was sent in the charge period but denies that it was instructions to trade.

(h) In a fax dated May 6, 1996, Mrs. Felderhof provided Nesbitt Burns with instructions to transfer funds out of the Nesbitt Burns Account;

Part of Exhibit 778, Fax dated May 6, 1996, Tab Nesbitt, page 65

The OSC admits that this correspondence was sent in the charge period but denies that it was instructions to trade.

(i) In a fax dated May 8, 1996, Mrs. Felderhof instructed Nesbitt Burns to "give Bre-X Minerals Ltd. $1,278,750 to cover John Felderhof's options which he exercised for the week of May 6, 1996"; and

Part of Exhibit 778, Fax dated May 8, 1996, Tab Nesbitt, page 67

The OSC admits that this correspondence was sent during the charge period but denies that it was instructions to trade.

(j) In a fax dated September 3, 1996, Mrs. Felderhof provided Nesbitt Burns with instructions to transfer funds out of the Nesbitt Burns Account.

Part of Exhibit 778, Fax dated September 3, 1996, Tab Nesbitt, page 116

The OSC admits that this correspondence was sent during the charge period but denies that it was instructions to trade.

Para. 18. The documentary record indicates that Mr. Felderhof sent the following correspondence to Nesbitt Burns with respect to the Nesbitt Burns Account (in or around the Charge Periods):

(a) In a fax dated April 29, 1996, Mr. Felderhof advised Nesbitt Burns to "[p]lease hold off of any sales until I have spoken to you."

Part of Exhibit 778, Fax dated April 29, 1996, Tab Nesbitt, page 56

The OSC admits this paragraph.

(b) In a letter dated May 2, 1996, Mr. Felderhof instructed Nesbitt Burns to "give Bre-X Minerals Ltd. $1,278,750 to cover John Felderhof's options which he exercised for the week of April 30, 1996." As indicated in the previous paragraph, Mrs. Felderhof gave similar instructions with respect to the exercise of options by Mr. Felderhof.

Part of Exhibit 778, Letter dated May 2, 1996, Tab Nesbitt, page 64

The OSC admits the first sentence of this paragraph.

(c) In a letter dated May 21, 1996, Mr. Felderhof instructed Nesbitt Burns to "give Bre-X Minerals Ltd. $852,500 to cover John Felderhof's options which he exercised on May 15 and May 16, 1996."

Part of Exhibit 778, Letter dated May 21, 1996, Tab Nesbitt, page 79

The OSC admits this paragraph.

(d) In a letter dated June 26, 1996, Mr. Felderhof authorized "my broker, Barbara Horn to exercise my options to sell 2,000,000 (two million) shares of Bre-X, paying Bre-X $8.525/share starting the month of July 1996. Please use proceeds to exercise further options at Bre-X and register the shares in my name in 50,000 denominations."

Part of Exhibit 778, Letter dated June 26, 1996, Tab Nesbitt, page 87

The OSC admits this paragraph.

(e) In a fax dated July 20, 1996, Mr. Felderhof advised that "[y]esterday, I phoned Natachia to suspend any trading until further notice as we will be issuing a press release Monday or Tuesday. I will notify when to resume."

Part of Exhibit 778, Fax dated July 20, 1996, Tab Nesbitt, page 93

The OSC admits this paragraph.

(f) In a fax dated August 6, 1996, Mr. Felderhof advised Nesbitt Burns to "proceed with original instructions with the exception that sales should be at minimum price of $24.50. Funds should be applied to exercise Bre-X shares as originally instructed."

Part of Exhibit 778, Fax dated August 6, 1996, Tab Nesbitt, page 100

The OSC admits that on August 6, 1996, Felderhof instructed Horn to *"Please proceed with original instructions with the exception that sales should be at minimum price of $24.50. Funds should be applied to exercise Bre-X shares as originally instructed."* and gave Horn his fax number until August 12, 1996. [emphasis in the original]

(g) In a fax dated August 7, 1996, Mr. Felderhof wrote, "Thank you for your fax advising me that I am responsible for filing my insider trading forms."

Part of Exhibit 778, Fax dated August 7, 1996, Tab Nesbitt, page 105

The OSC admits that on August 7, 1996, Horn wrote to Felderhof and asked him to *"Please confirm receipt of fax – that you must complete insider trading report yourself. Sorry, I just don't want trouble.* [Exhibit SD778, p 102 fax from Horn to Felderhof dated August 7, 1996].

The OSC admits that Felderhof wrote in response on August 7, 1996, *"Thank you for your fax advising me that I am responsible for filing my insider trading forms."*

(h) In a fax dated August 17, 1996, Mr. Felderhof wrote, "Do not sell until further notice. There will be a news release latest +/- 24 Aug."

Part of Exhibit 778, Fax dated August 17, 1996, Tab Nesbitt, page 106

The OSC admits that on August 17, 1996, Felderhof told Horn and Natashia *"Do not sell any shares until further notice. There will be a news release latest + - 24 August."*

(i) In a fax dated August 24, 1996, Mr. Felderhof instructed Nesbitt Burns to "proceed with sale of Bre-X. Proceeds thereof to be applied exercising of Bre-X options."

Part of Exhibit 778, Fax dated August 24, 1996, Tab Nesbitt, page 107

The OSC admits this paragraph and states that Felderhof also told Horn he would be leaving Holland that day and would provide her with new contact numbers in the US, which contact numbers are noted on the fax.

(j) In a fax dated September 2, 1996, Mr. Felderhof asked that Bre-X certificates be sent to him and that certain funds be transferred out of the account.

Part of Exhibit 778, Fax dated September 2, 1996, Tab Nesbitt, pages 114-115

The OSC admits this paragraph.

(k) In a fax dated September 9, 1996, Mr. Felderhof instructed Nesbitt Burns to "continue with sale of Bre-X for this week only commencing as of 9 Sept Monday."

Part of Exhibit 778, Fax dated September 9, 1996, Tab Nesbitt, page 121

The OSC admits that on September 9, 1996 Felderhof told Horn to *"Please continue the sale of Bre-X for this week only commencing as of 9 September Monday. I will phone you."*

(l) In a fax dated September 10, 1996, Mr. Felderhof asked that certain funds be transferred out of the account.

Part of Exhibit 778, Fax dated September 10, 1996, Tab Nesbitt, pages 123-124

The OSC admits that on September 10, 1996, Felderhof told Horn to transfer $100,000 Canadian *"to cover a placement as offered by Rianto Resources Ltd."*. He also asked Horn if any Bre-X shares certificates had been received. And if so, when they were

couriered to him?

In the faxes from Mrs. Felderhof only two give instructions with respect to selling shares. The April 18, 1996 fax refers to two sales before any of the charge periods start and the April 22, 1996 fax refers to one sale before the charge periods and to two sales in the very first days (April 24 and 25) of the first charge period. The charge periods start April 24 and end on September 10, 1996.

These two trades involved 10,000 shares out of 1,220,500 shares traded in the Nesbitt Burns account during the charge periods.

Of more significance is that the fax of April 18, 1996 states "*we would like to put another 15,000 Bre-X shares on to be sold today through to tomorrow...*" and "*[a]s you know we are looking to sell 15,000 per week every week for the next 2 months...*"

This is significant for several reasons. From the use of "*we*" it may be inferred that Mrs. Felderhof was not acting independently of Mr. Felderhof but that Mr. Felderhof was involved in these instructions. It also shows that there was a standing order " *to sell 15,000 per week every week*" that Horn was already aware of and which was from both Mr. and Mrs. Felderhof.

The sales set out in the April 22 fax, totaling 15,000, was a restatement of the standing order involving the Defendant.

Unlike Mrs. Felderhof's correspondence dealing with trades which was restricted to April of 1996, Mr. Felderhof correspondence dealing with trade instructions, although limited, covered the charging periods April to September 1996.

Exhibit 778
Exhibit S12: paragraphs 17, 18

In addition to the above correspondence from Mr. Felderhof and Mrs. Felderhof to Nesbitt Burns, there also faxes from Barbara Horn to the Defendant found in Exhibit 778 confirming orders to sell, confirming sales, setting out the current trading prices of Bre-X shares, confirming wire transfers or setting out insider trading information.
Felderhof also received the monthly statements from Nesbitt Burns setting out all the trades for the previous month.
In a fax to Tom Devlin, dated September 10, 1996, John Felderhof writes " *I have sold Bre-X to exercise my Bre-X option.*"
Exhibit 799: Tab 6

The April 18 and 22 faxes from Mrs. Felderhof as noted above established there were standing orders to sell shares which involved the Defendant. As well the faxes from Mr. Felderhof dated July 20, 1996 and August 17, 1996 suspending trading pending the issuance of press releases also indicate standing orders to sell. They also indicate Mr. Felderhof's direct involvement and direction of trades.
Exhibit 778

As noted above, Mrs. Felderhof was listed in the Client Account Agreement as having trading authority in the account. But the Agreement also states that she did not guarantee the account and did not have a financial interest in the account. Only John Felderhof had

a financial interest in the account. It was John Felderhof's personal account. Mrs. Felderhof was not a co-account holder. On page 3 she is referred to as an agent. The account was not a managed account. The Agreement states that no one at Nesbitt Burns has been authorized to use discretion in handling the account.

Exhibit 778

The share certificates were in John Felderhof's name. The stock options were John Felderhof's. Only he could exercise them.

John Felderhof filed and personally signed Insider Reports as required by S.107(1) and (2) of the *Securities Act* listing all of the trades in the Nesbitt Burns account. The Insider Reports do not prove John Felderhof gave instructions to sell but they are another piece of circumstantial evidence.

Exhibit 776
Exhibit 780
Exhibit 799

FINDING

I am satisfied beyond a reasonable doubt that the circumstantial evidence discussed above proves that within the meaning of s. 76(1) John Felderhof sold Bre-X securities through his Nesbitt Burns account as listed in paragraphs 146, 457, 512 and 524 of Exhibit S5 Volume I and reproduced above.

THE DEACON OR GRAYS INN J& I ACCOUNT

In oral submissions the O.S.C. stated:

MS. COLE: And you'll recall that Michael Judge testified that the Grey's Inn J and I account was Mr. Felderhof's account. You'll also recall the evidence that Mr. Judge testified that a Bre-X share certificate number C2020 for 384,000 Bre-X shares that was issued in Mr. Felderhof's name was deposited in that account in late February. And you remember, Your Honour, how I led him through that evidence that over the course of that Spring and Summer of 1996, Mr. Felderhof sold all of these shares and transferred the money out of the account.

...

Your Honour, Mr. Felderhof reported the sales from the Grey's Inn J and I account on his insider reports. And it's our submission, Your Honour, that the Securities Act must be interpreted in a manner that doesn't allow insiders to avoid liability for illegal insider trading by hiding the sales of shares in a beneficial account.

Transcript: August 29, 2006, pages 58, 59

In oral submissions the Defence stated:

MR. RICHARD: As I stated, Mr. Judge was the registered representative of the account, so he's the person who takes that instructions, he's the advisor. Currently his position would be referred to rather than a registered representative, an investment advisor. So Mr. Judge's evidence was that the instructions for the sales in Deacon account came from Barclays. He had stated it was from Alistair Carter or others at Barclays. Mr. Judge also stated that, in Deacon's view, Barclays was the account holder. You'll recall the account was Grey's Inn, I think (J) and (I).

And Mr. Judge confirmed that he had no knowledge of who gave instructions to Barclays. The OSC did not call anyone from Barclays. They did not call Mr. Carter. So, Your Honour, I'd submit this Court is left with no evidence to support the allegation that Mr. Felderhof sold any shares in a Deacon account. Mr. Judge confirmed he had never spoken to Mr. or Mrs. Felderhof. But as I raised before, we did hear from Mr. Judge who was the registered representative of the account. We did hear who the instructions came from and we heard that they came from Barclays.

Transcript: August 24, 2006, pages 94-95

In Exhibit S5 Volume I the O.S.C. submits and the Defence comments as follows:

Para. 156. Three months later, on February 13, 1996, Barclays Bank, Caymans opened a trading account called Grays Inn J&I account 34962A-3.

The Defence agrees that Barclays Bank PLC opened a trading account with Deacons called Grays Inn J&I on or about February 13, 1996.

Para. 157. Alistair Carter, a senior account executive with Barclays Bank in the Caymans, was responsible for the Grays Inn J&I account. The account holder was identified as an insider of Bre-X and a senior officer or director of a company whose shares were traded on an exchange.

The Defence agrees that Alistair Carter, among others, was responsible for the Grays Inn J&I account. Deacons account opening form, completed based on information from Barclays, indicates that the "client" is a senior officer or director of a company whose shares traded on an exchange and that company was indicated as Bre-X.

Para. 158. Michael Judge, a portfolio manager at Deacon Capital Corporation, was responsible for the Barclays offshore banking centres, including the Caymans. Carter gave Judge trading instructions for Grays Inn J&I account.

The Defence agrees that Mr. Judge and Mr. Cernik were responsible for Barclays' Caribbean offshore banking centres, including the Caymans. The Defence also agrees that Mr. Carter, and possibly others from Barclays, gave Mr. Judge trading instructions for this account. Mr. Judge did not know who provided Barclays with trading instructions. (Evidence of Mr. Judge, May 11, 2005, Vol. 114, page 52)

...

Para. 160. Judge was the registered representative on the Deacon Capital account.

The Defence agrees that Mr. Judge and Mr. Cernik were the registered representatives on this account.

Para. 161. Judge testified that Grays Inn was the nominee name for Barclays Cayman. A nominee name is used rather than the name of the beneficial owner to keep the identity of the beneficial owner confidential. Barclays Cayman denotes the nominee name with an alpha or numeric code associated with the beneficial owner.

The Defence agrees that Mr. Judge testified that Grays Inn was the nominee name for Barclays Cayman, that there was a legal reason for them using a nominee name, but he did not know what that was and that Barclays Cayman would "tag the nominee name with an alpha or numerical code to attach to the beneficial owner". (Evidence of Mr. Judge, May 11, 2005, Vol. 114, pages 6-7)

Para. 162. Judge testified that the beneficial owner of the Grays Inn J&I account was John Felderhof or John and Ingrid Felderhof as denoted by **J&I** on the account.

The Defence agrees that Mr. Judge testified as follows:
Q. Who was the beneficial owner of this account?
A. I believe it was Mr. Felderhof given the evidence, or Mr. Felderhof and his wife as denoted by the J & I on the account. **[Emphasis added] (Evidence of Mr. Judge, May 11, 2005, Vol. 114, pages 33 - 34)**

Mr. Judge also testified as follows:

Q. ***And am I correct, Sir, that you at no time had any contact with John or Ingrid Felderhof?***
A. ***That's correct.***
Q. ***In fact, you have never spoke [sic] to either John or Ingrid Felderhof?***
A. ***No.***
Q. ***Sir, am I correct that you have no firsthand knowledge of who provided any trading instructions to Barclays?***
A. ***That's correct.*** **(Evidence of Mr. Judge, May 11, 2005, Vol. 114, page 52)**

In any event, the beneficial ownership of shares or an account is not what the OSC must prove in an insider trading case. The OSC must prove who gave the instructions and they have failed to prove that Mr. Felderhof gave the instructions to sell the shares at issue.

Exhibit S5 Volume I: Paragraphs 156-158, 160-162

Judge also testified:

MS. COLE: Now about mid-way down the page on the right-hand side there is a box which says "Insider Information". Did you fill out the information on this form?

MR. JUDGE: Yes.

MS. COLE: And can you tell us who provided that information?

MR. JUDGE: Well Barclays would have provided that information.

MS. COLE: And can you just explain to us what this denotes here?

MR. JUDGE: Well what it denotes is that the beneficial owner of this account is an insider, but he or she does not have a control block of the underlying company

which in this case was Bre-X. We were very cognizant of asking our clients if the beneficial owners were insiders.

MS. COLE: And why is that?

MR. JUDGE: Because of the Ontario Securities Commission and the regulatory environment that we are in.

Transcript: May 11, 2005, page 9

Continuing in Exhibit S5 Volume I:

Para. 167. David testified that as a result of her analysis, she identified Felderhof as the beneficial owner of the Grays Inn J&I account.

The OSC did not cite any evidence. The Defence disagrees that Ms. David gave this evidence. In any event, beneficial ownership is not what the OSC must prove in this case.

David testified:

MR. MARROCCO: And sorry, so what is the conclusion that we draw from that?

MS. DAVID: The conclusion is that all of the shares that Mr. Felderhof owns as shown on his Insider Trading report dated the 30th of May, 1996, are held in the Grays Inn Limited account J & I.

Transcript: April 11, 2005, page 29

Para. 163. There is additional evidence that Felderhof was the beneficial owner of the Grays Inn J&I account 34962A-3:

(i) A Bre-X share certificate for 384,000 Bre-X shares registered in John Felderhof's name was deposited into the Grays Inn J&I account.

(ii) Felderhof reported sales of Bre-X shares from the Grays Inn J&I account on his insider reports.

The OSC cites no evidence in support of these arguments. The Defence does not agree that these arguments are "additional evidence that Mr. Felderhof was the beneficial owner of the Grays Inn J&I account".

Exhibit S5 Volume I: paragraph 163

The O.S.C. continues in Exhibit S5 Volume I with a detailed analysis of evidence supporting the O.S.C. submissions in paragraph 163 which evidence I find proves beyond a reasonable doubt that John Felderhof was the beneficial owner of the Deacon/Grays Inn J&I account.

With respect to the submission in paragraph 163 that *"(i) A Bre-X Share certificate for 384, 000 Bre-X shares registered in John Felderhof's name was deposited into the Grays Inn J&I account"* there is a substantial amount of evidence found at paragraphs 165-190 of Exhibit S5 Volume I briefly reviewed below.

In the "*New Account Application Form*" for the Deacon/Grays Inn J&I account the client is listed as an insider of Bre-X. In response to the question "*Is client a senior officer or director of a company whose shares are traded on an exchange or in the OTC markets*" the answer given is "*Yes*".

On the evidence it is proven that the client referred to is John Felderhof.

The following questions on the application as with most of the rest of the application are blank.

> "1. Will any other person(s):
> Have trading authorization in this account? _____
> Guarantee this account? _____
> Have a financial interest in this account? _____-
> ...
> 4. Is this account discretionary ____ or managed _____?"

Exhibit 779
Exhibit 782: Tab 9

Specifically with respect to paragraph 163(i) above Judge testified:

> MS. COLE: Now, Mr. Judge, I wonder if you could turn to the third tab in your binder which is marked "February". And the first document I am showing to you is what appears to be a monthly statement for Grays Inn Limited, account J & I, dated February 29, 1996 and the account number that you just described for us appears in the top left-hand corner?
>
> MR. JUDGE: Yes.
>
> MS. COLE: Is this indeed a monthly statement for that account?
>
> MR. JUDGE: Yes.
>
> MS. COLE: And can you tell us what the first activity, if any, was in this account?
>
> MR. JUDGE: The first activity occurred February the 20th of '96 and it was the receipt of 384,000 shares of Bre-X Minerals Limited.
>
> ...
>
> MS. COLE: And do you recall actually looking at the certificate when you received it?
>
> MR. JUDGE: I do actually, yes.
>
> MS. COLE: And did you notice who this share certificate was registered to?
>
> MR. JUDGE: Yes, I did.
>
> MS. COLE: And who was it registered to?
>
> MR. JUDGE: Mr. John B. Felderhof.

Transcript: May 11, 2005, pages 11-12

David testified:

> MS. DAVID: One hundred and seventy-eight thousand is the number of shares that Mr. Felderhof acquired through the exercise of options, and those shares went into his personal account at Nesbitt Burns. The remaining shares, totalling

384,000, were also acquired through the exercise of options and those shares went into the Grays Inn account J & I at Deacon Capital.

Transcript: April 11, 2005, page 10

Also in Exhibit 776, page 5, David sets out that on 20-Feb-1996 the Deacon/Grays Inn J&I account number 34962A-3 received 384,000 Bre-X shares and continuing in the column "*Information Obtained*" it states:

> Felderhof exercises 384, 000 options on 2/Jan/96 (209,000 @ $0.40, 55,000 @ $1.50 & 120,000 @ $5.05.
> Montreal Trust issued certificate #C-2020 in Felderhof's name on 10/Jan/96.
> Certificate #C-2020 rec'd into a/c #34962A-3 on 20/Feb/96 through Michael Judge

With respect to the submission in paragraph 163 that "*(ii) Felderhof reported sales of Bre-X shares from the Grays Inn J&I account in his insider reports*" there is evidence found at paragraphs 191-202 briefly reviewed below.

Felderhof's insider reports are found in Exhibit 780. In Felderhof's Insider Report of February 10, 1996 Felderhof lists the 384,000 shares acquired on January 2, 1996. These are the 384,000 shares deposited into the Deacon/Grays Inn J&I account on February 20, 1996.

Felderhof's March 4, 1996 Insider Report reports the sale of 20,000 shares leaving a balance of 364,000 shares in the Deacon/Grays Inn J&I account. The 20,000 shares were sold in late February 1996 which was before the charge periods. Felderhof's May 30, 1996 Insider Report reports the stock split on the 364,000 Bre-X Shares as 3,276,000 shares acquired for a total of 3,640,000 shares (10 to 1 split). There are no further Insider Reports after May 30, 1996 for the Deacon/Grays Inn J&I transactions.

The Deacon monthly statements for Grays Inn J&I account are found in Exhibit 779. The statement dated February 29, 1996 shows 384,000 Bre-X shares received and a total of 20,000 sold. The March 31, 1996 and April 30, 1996 statements show a balance of 364,000 Bre-X shares. After the 10 to 1 split, the May 31, 1996 statement shows a balance of 3,640,000 Bre-X shares. As the Defence points out, there is a discrepancy in the dates of the transactions with respect to the 20,000 shares sold as reported in the monthly statements and insider reports but it is not significant and I am satisfied they are the same sales.

Exhibit S5 Volume I: paragraphs 195-197

As noted above I find that John Felderhof was the beneficial owner of the Deacon/Grays Inn J&I account. There is a substantial amount of evidence that Felderhof was the beneficial owner. John Felderhof is the client being referred to in the "*Insider Information*" part of the application. John Felderhof exercised his options with respect to 384,000 Bre-X shares. John Felderhof paid Bre-X for the shares. The share certificate was in John Felderhof's name. John Felderhof signed the back of the share certificate. The share certificate was deposited into the Deacon/Grays Inn J&I account.

Bre-X's T.S.E. listing statement in March 1996 stated Felderhof was the beneficial owner of 384,000 shares. Felderhof reported the acquisition of the 384,000 Bre-X shares, the sale of 20,000 of those shares and the 10 to 1 stock split of the remaining 364,000 shares in his Insider Reports.

The submissions of the Defence were that the Deacon/Grays Inn J&I account was not beneficially owned by Felderhof but that in any event the O.S.C. has not proven that Felderhof gave instructions to sell any shares. In Exhibit S3 Tab C, paragraphs 11-12 the Defence submits:

> Para. 11. With respect to the Deacon Account, there is no evidence before this Court as to who directed the trading in that account. As Mr. Judge confirmed during cross-examination, all of his instructions came from Barclays, and he did not know who was instructing Barclays.
>
> Para. 12. Again, the failure of the OSC to call any witness from Barclays to establish on whose instructions they were placing orders with Deacon is critical. As there are no written trading instructions in evidence for this account, there is a complete lack of any evidence as to who sold securities of Bre-X in that account.

The O.S.C. case for the Deacon/Grays Inn J & I account is not as strong as the case for the Nesbitt Burns account. Unlike with the Nesbitt Burns account, with respect to the Deacon/Grays Inn J & I account there is no direct evidence of any instruction from Felderhof for any trade (the instructions came from Barclays), there is no evidence of any correspondence from a broker to Felderhof about any trades, there is no evidence that the monthly statements were sent directly to Felderhof or were received by Felderhof, there is no evidence of any standing orders from Felderhof to sell, there is no evidence of any instructions from Felderhof to suspend any standing orders, there are no insider reports with respect to any trades after the charge periods started and no insider reports after the May 30, 1996 report which reported the stock split.

But on the evidence discussed above with respect to which I found that Felderhof was the beneficial owner of the account and keeping in mind the purposes and principles of the *Securities Act* and the statement of Farley J. in paragraph 77 of Woods discussed above at

page 413 of these reasons, I find that the O.S.C. have proven beyond a reasonable doubt that Felderhof sold the shares in the Deacons/Grays Inn J & I account within the meaning of s.76(1) of the *Securities Act*.

There is no issue Felderhof's Bre-X shares were sold through the Deacon/Grays Inn J & I account. They were John Felderhof's shares as acknowledge in his insider trading reports. Felderhof was the client referred to in the application. It would be speculation not based on any evidence before me to find that there is a doubt raised that this was a discretionary or managed account and that Felderhof did not sell his own shares in his own beneficial account. On the evidence, the issue of a discretionary or managed account is simply not before me.

FINDING

I am satisfied beyond a reasonable doubt that on the circumstantial evidence discussed above that John Felderhof sold Bre-X securities through the Deacon/Grays Inn J & I account as listed in paragraphs 458 and 513 of Exhibit S5, Volume I.

When Did Felderhof Give Instructions To Sell

In addition to submitting that the O.S.C. has to prove that Felderhof gave instructions to sell on each and every occasion of a sale to prove that Felderhof traded within the meaning of S.76(1), the Defence also submits the O.S.C. must prove when Felderhof

gave the instructions in order to prove a breach of s.76(1). In oral submissions the Defence stated:

> MR. RICHARD: And I'll just start with giving a summary of what I submit would be the analysis, and that's for each sale of shares that we have to deal with, as we've mentioned many times, there are four different charge periods and in each charge period the total sales are lumped together. It's not that in charge period one there was one sale of shares. I believe the charge is that 100,000 shares were sold. That 100,000 is actually a number of smaller trades spread out over a number of days.
>
> So for each of the sales, what the OSC must prove is first, that Mr. Felderhof gave instructions for the sale. And what is significant about that is the determination of that timing of giving the instructions for the sale because, Your Honour, in my submission, what's necessary for the analysis is determining when the instruction was given because that is the point in time when we must analyze the further steps, being what was the knowledge of the individual at the time that the instruction was given, in particular, what was the knowledge with respect to the alleged material fact at the time that the instruction was given?
>
> And carrying on with the points as we've laid them out in our factum, it's also necessary to determine at that point in time was the alleged material fact a fact? Mr. Richter has covered many of the issues on that point, in particular, the first three particulars and some of the difficulties that can arise from the particulars not being clear facts.
>
> The next point would be at that time when the instruction is given, were the alleged material facts material? And I think that is where we come in a bit to your question to Mr. Richter. If it's determined when the instruction was given we have a point in time, clearly letters or events that may have happened subsequent to that aren't going to be part of the analysis at the time of the instruction.
>
> And then finally, we look at at [sic] that point in time, when the instruction was given, was there general disclosure of the alleged material facts? And we had set those out in our factum, but I simply wanted to go back and make it clear that in my submission that needs to be done for each and every sale of shares that occurred.
>
> ...
>
> So what I propose to do, Your Honour, is turn to the first charge period, to go through some of the points that I've raised and, in a sense, an example of the analysis to be done for each particular sale – and again, that analysis is proving that Mr. Felderhof gave an instruction. And what's necessary there is to determine

when the instruction was given, because the rest of the points all flow from that particular point in time. And it's where there can be, I submit, a danger of potentially drawing inferences as to when instructions may have been given. So that it's necessary to prove that Mr. Felderhof gave an instruction and at the time of the instruction it's necessary for the OSC to prove that Mr. Felderhof had knowledge of an alleged material fact, that at that time the alleged material fact was indeed a fact, and at that time the alleged material fact was material, and at that time the alleged material fact was undisclosed.

...

And so what I think you have to do, and I think technically you have to do it for every single trade, but for ease of this discussion, let's talk about every single day in which there was a trade. If you find that Mr. Felderhof traded or Grey's Inn traded on a particular day in the charge period and he traded because you find, notwithstanding Mr. Richard's arguments, that he put in the "sell" order, then the next stage of the inquiry is what was the state of the case on that day? So whenever the person who's alleged to have engaged in insider trading places an order, it crystallizes, in my submission, the analysis.

As Justice Farley said in Woods, the essence of this alleged offence is that somebody who has inside knowledge is cheating because he's using that knowledge to sell stock. Well, it goes without saying that if the trade order goes in on May 1st, 1996, then in terms of understanding the case, anything that happened after May 1st, indeed anything that happened 10 minutes after the order goes in, cannot be part of the prosecution for that trade.

Transcript: August 24, 2006, pages 85, 97, 111

Contrary to the above submission Farley J. in Woods states: "*The offence then is in essence not a question of using insider information but of buying or selling securities of a company while possessed of insider information.*"

Section 76(1) states in part "*sell securities...with the knowledge of a material fact...that has not been generally disclosed.*"

The connection made in S.76(1) is between the knowledge of a material fact not generally disclosed and the sale and not between the knowledge of a material fact not generally disclosed and when Felderhof gave the instructions to sell.

Witness Not Called By The O.S.C.

The Defence on numerous occasions has submitted that a weakness in the O.S.C. case is that many witnesses on the O.S.C. witness lists were not called to testify.

Transcript: August 22, 2006, pages 57-58
Transcript: August 24, 2006, pages 92, 95

The O.S.C. submissions are found starting at page 60 of the transcript of August 29, 2006:

> MS. COLE: Your Honour, the defence has also suggested that somehow the OSC has failed in not calling some of the witnesses that the OSC promised in its opening statement that it would call, and Barbara Horn was one of those witnesses, Your Honour. The defence suggests that Barbara Horn could tell the Court who directed the trades and it's our position that you cannot draw an adverse inference from our decision not to call Barbara Horn or any of the other witnesses.
>
> Your Honour, the law is that where a witness is equally available to both parties, an adverse inference cannot be drawn from the party's decision not to call a particular witness. So in other words, you can't infer, from our decision not to call Barbara Horn, that she would have testified that Mr. Felderhof did not direct the trade. And the authority for this principle, Your Honour, is R. v. Jolivet and King and Merrill. I'm just going to pass this up, Your Honour, I'm not going to take you through it, and I've also given you an excerpt from Sopinka on evidence on this point.
>
> ...
>
> MS. COLE: Your Honour, the Crown has an obligation to disclose what witnesses it's going to call and what we anticipate those witnesses will say, and we fulfilled that obligation.

Now, when the trial resumed in 2004, we decided in order to complete this trial in an efficient and timely way, we would not call some of the witnesses that were on the original witness list, and one of those witnesses was Barbara Horn. And in making that decision we considered the fact that going forward, any documents admitted into evidence in this trial would be on consent and therefore capable of the proof of their contents. And you'll recall, Your Honour, that's not how the trial originally proceeded.

Mr. Marrocco and I also considered whether the particular point would be or was adequately covered by another witness. And obviously we can't compel witnesses who are outside of Canada or who are otherwise not amenable to the process.

And you'll recall, Your Honour – well, I hope you'll recall, in December 2004 – I'm sure you will when you go back to the transcript – in December 2004, after Mr. Francisco completed his evidence there was some discussion about the OSC's decision not to call some of the witnesses on the original witness list. And the reference for that, Your Honour, is December 8th, 2004, the discussion is at pages 64 to 71.

THE COURT: December 8, '04, pages –

MS. COLE: - 64 to 71. And in that discussion, the defence asked us to keep the witnesses that we had removed from the list under summons because they wanted to consider whether they would call the witnesses. We did that, Your Honour, and we confirmed by letter that it had been done. And in fact, the defence did call some of the witnesses who were on our original list. You'll recall that the Crown had originally expressed an intention to call witnesses from Kilborn and Barrick. We did not, but the defence called Paul Semple of Kilborn and Peter Munk of Barrick.

THE COURT: Peter Munk was not under subpoena by the Crown.

MS. COLE: Well, the agreement was, Your Honour, that either we would keep them under summons, or whatever arrangement had been made –

THE COURT: I am sorry, summons.

MS. COLE: And I believe that there were three individuals from Kilborn –sorry, three individuals from Barrick who were on the original list, Davidson, Garver, and I can't recall the third one. And there's certainly, as you'll recall from some of the meetings we had about scheduling Peter Munk's testimony, there was a relationship with counsel for Barrick and there was an agreement that individuals from Barrick would be made available if required. So Your Honour, all of that to simply say that you can't draw an adverse inference from the fact that we didn't call some of the witnesses to get this trial on and completed in an efficient manner.

Transcript: August 29, 2006, pages 60-63

In R. v. Jolivet [2000] S.C.J. No. 28, the Supreme Court of Canada states at page 8:

> [T]he Crown is under no obligation to call a witness it considers unnecessary to the prosecution's case.

At page 10,

> Crown counsel is entitled to have a trial strategy and to modify it as the trial unfolds, provided that the modification does not result in unfairness to the accused.

Continuing on page 10 under the heading:

> 3. Was the Jury Entitled to Draw an Adverse Inference from the Crown's Failure to Call Bourgade?
>
> Para. 22 Cook, supra, listed some possible options to rectify any prejudice created by the Crown's failure to [page766] call a witness. These included a defence comment on that failure in its closing jury address. The purpose of making such a comment to the jury is inevitably to invite the jury to draw an adverse inference against the Crown's case. The questions at this point are, therefore, What circumstances justify such a comment, and What is the precise content of the adverse inference against the Crown's case that the defence is entitled to request?
>
> Para. 23 Put at its highest, the Crown's failure to call Bourgade could in theory have led the jury to draw the adverse inference that Bourgade's testimony, if called, would have been unfavourable to the Crown. In my view, there was no basis to ask the jury to draw such a strong inference in this case.
>
> Para. 24 Neither the defence nor the Crown have suggested that Bourgade would in fact have offered exculpatory evidence. The "adverse inference" principle is derived from ordinary logic and experience, and is not intended to punish a party who exercises its right not to call the witness by imposing an "adverse inference" which a trial judge in possession of the explanation for the decision considers to be wholly unjustified.
>
> Para. 25 The general rule developed in civil cases respecting adverse inferences from failure to tender a witness goes back at least to Blatch v. Archer (1774), 1 Cowp. 63, 98 E.R. 969, where, at p. 65, Lord Mansfield stated:

> It is certainly a maxim that all evidence is to be weighed according to the proof which it was in the power of one side to have produced, and in the power of the other to have contradicted.

Para. 26 The principle applies in criminal cases, but with due regard to the division of responsibilities between the Crown and the defence, as explained below. It is subject to many conditions. The party against whom the adverse inference is sought may, for example, give a satisfactory explanation for the failure to call the witness as explained in R. v. Rooke (1988), 40 C.C.C. (3d) 484 (B.C.C.A.), at [page767] p. 513, quoting Wigmore on Evidence (Chadbourn rev. 1979), vol. 2, at para. 290:

> In any event, the party affected by the inference may of course explain it away by showing circumstances which otherwise account for his failure to produce the witness. There should be no limitation upon this right to explain, except that the trial judge is to be satisfied that the circumstances thus offered would, in ordinary logic and experience, furnish a plausible reason for nonproduction. [Italics in original; underlining added.]

Para. 27 The party in question may have no special access to the potential witness. On the other hand, the "missing proof" may lie in the "peculiar power" of the party against whom the adverse inference is sought to be drawn: Graves v. United States, 150 U.S. 118 (1893), at p. 121. In the latter case there is a stronger basis for an adverse inference.

Para. 28 One must also be precise about the exact nature of the "adverse inference" sought to be drawn. In J. Sopinka, S. N. Lederman and A. W. Bryant, The Law of Evidence in Canada (2nd ed. 1999), at p. 297, para. 6.321, it is pointed out that the failure to call evidence may, depending on the circumstances, amount "to an implied admission that the evidence of the absent witness would be contrary to the party's case, or at least would not support it" (emphasis added), as stated in the civil case of Murray v. Saskatoon, [1952] 2 D.L.R. 499 (Sask. C.A.), at p. 506. The circumstances in which trial counsel decide not to call a particular witness may restrict the nature of the appropriate "adverse inference". Experienced trial lawyers will often decide against calling an available witness because the point has been adequately covered by another witness, or an honest witness has a poor demeanour, or other factors unrelated to the truth of the testimony. Other jurisdictions also recognize that in many cases the most that can be inferred is that the testimony would not have been helpful to a party, not necessarily that it would have been adverse: United States v. Hines, 470 F.2d 225 (3rd Cir. 1972), at p. 230, certiorari denied, 410 U.S. 968 (1973); and the Australian cases of Duke Group Ltd. (in Liquidation) v. Pilmer & Ors, [1998] A.S.O.U. 6529 (QL), [page768] and O'Donnell v. Reichard, [1975] V.R. 916 (S.C.), at p. 929.

> Para. 29 Applying these principles to the present facts, I think that if Crown counsel's explanation of his change of intention is accepted, the Crown acted in accordance with its ethical responsibilities, and an adverse inference that Bourgade would have given evidence unfavourable to the Crown would not be justified. If nothing had been said about Bourgade to the jury, that would have been an end to the matter. The complicating factor is that Crown counsel, despite his misgivings, twice announced to the jury that Bourgade would be called, and these announcements perhaps led the jury to anticipate that the Crown's case was stronger than it turned out to be. It is because of those announcements that I think a defence comment would have been appropriate.
>
> Para. 30 Crown counsel's comment had produced an element of prejudice by asserting the existence of corroborative evidence. An adverse inference of "unhelpfulness" would have been a fair result of the Crown's failure to substantiate its assertion.

I accept the O.S.C.'s explanation noted above. I draw no adverse inference. The Defence of course, can argue, as it has, that by not calling a particular witness the O.S.C. has not proven a particular matter.

Element (C) The Defendant Had Knowledge Of Material Information About The Public Company

Material Fact

The term "*material fact*" is defined in s.1(1) of the *Securities Act*:

> "material fact", where used in relation to securities issued or proposed to be issued, means a fact that significantly affects, or would reasonably be expected to have a significant effect on, the market price or value of such securities;

In the following cases the courts deal with the meaning of material fact, material change and material information.

I have already reviewed Woods above at pages 394-396.

In Pezim v. British Columbia (Superintendent of Brokers) [1994] S.C.J. No. 58 (S.C.C.) (QL), the Supreme Court of Canada states at page 23:

> Para. 79. Both "material change" and "material fact" are defined in s. 1 of the Act. They are defined in terms of the significance of their impact on the market price or value of the securities of an issuer. The definition of "material fact" is broader than that of "material change"; it encompasses any fact that can "reasonably be expected to significantly affect" the market price or value of the securities of an issuer, and not only changes in the "business, operations, assets or ownership of the issuer" that would reasonably be expected to have such an effect.
>
> ...
>
> Para. 81. Sections 67 and 68 of the Act also reflect the differences between a material change and a material fact. As Victor P. Alboini points out in Securities Law and Practice, 2nd ed., vol. 2 (1984), at p. 18-13, "[t]he concept of 'material change' should be distinguished from that of 'material fact'. Undisclosed material facts concerning a reporting issuer may not require timely disclosure...although they do restrict trading". Under the timely disclosure provision of the Act, s. 67, only material changes require that a press release be issued and that a report be filed. In contrast, under the insider trading provision, s. 68, a person who is in a special relationship with a reporting issuer is prohibited from buying or selling securities of the issuer when the person knows of either a material change or a material fact which has not been publicly disclosed.

In Re: Royal Trustco Ltd. (1981), 2 O.S.C.B. 322C (Ont. Sec. Comm.), the Divisional Court states at page 6:

> There is no question that s.75(1) of the Act is intended to prevent disclosure by persons in the position of White and Scholes of material facts before they have been generally disclosed. In my opinion, the information disclosed fell easily within the category of material facts within the context of the legislation and in the prevailing circumstances. That the appellants could not guarantee that the known holders of Trustco's shares would not sell or deposit their shares does not reduce the disclosure to a level less than fact. It was made clearly to encourage the officers of the bank not to sell or deposit the 10% of the outstanding shares of Trustco that it had acquired after earlier representations to it by White and Scholes and it achieved that purpose. Having in mind the general object of s.75, which is to prevent improper or unfair disclosure, I do not think the term "fact" should be read super-critically. In my opinion, the information was sufficiently factual or a sufficient alteration of circumstances to be a material "change" to fall

within the section. In my opinion the Commission was justified in holding that the section had been breached.

In R. v. Fingold [1999] O.J. No. 369 (QL), the Ontario Court of Justice (General Division) states at page 13:

> Para. 56. The appellant contends that it was the trial judge who erred in applying too low a standard in his objective test of the point at which information amounting to "facts" first came to the "knowledge" of the Commission. I agree that "facts" must mean more than mere rumour or gossip on the street or even an "overpowering suspicion". It must be information obtained from an identifiable source which might reasonably be expected to have such information and obtained in circumstances which would tend to support the accuracy and reliability of the information given. Similarly, "knowledge" does not require proof or verification to constitute knowledge. The trial judge referred to the definition of "knowledge" in Black's Law Dictionary which is cited above. One cannot deny knowledge when information given under oath supported by documentary evidence by a person who has first hand knowledge is received.

In Re: YBM Magnex International Inc. (2003), 26 O.S.C.B. 5285 (Ont. Sec. Comm.) (QL), the Ontario Securities Commission states starting at page 24:

> The Materiality Assessment
>
> [89] Disclosure in securities markets encourages investing and therefore growth. Disclosure protects investors, aids in ensuring that securities markets operate in a free and open manner and ensures that a security will nearly correspond to its actual value. Too much disclosure or information overload can be counter-productive. The boundaries are identified by the concept of "material facts". The definition appears straightforward but its assessment is nuanced.
>
> [90] Assessments of materiality are not to be judged against the standard of perfection or with the benefit of hindsight. It is not a science and involves the exercise of judgement and common sense; Core Mark International Inc. v. 162093 Canada Ltd. (8 June 1989) Toronto 1220/89 at 4-5 (Ont. H.C.)
>
> [91] The test for materiality in the Act is objective and is one of market impact. An investor wants to know facts that would reasonably be expected to significantly affect the market price or value of the securities. The investor is an economic being and materiality must be viewed from the perspective of the trading markets, that is, the buying, selling or holding of securities. Price in an

open market normally reflects all available information. YBM was not a thinly traded stock. As such, its price more likely reflected the information disclosed to the public market. Full disclosure of adverse information may lower the price but it does not shut out a security from the market.

[92] There was extensive reference to the U.S. law on materiality. The reasonable investor test or substantial likelihood test is found in TSC Industries, Inc. v. Northway, Inc., 426 U.S. 438 (1976) (TSC Industries). Generally, for historic information like past financial results or completed business transactions this test frames the materiality assessment. When facts point to a future event, the U.S. courts have applied the probability/magnitude test; Basic Inc. v. Levinson, 485 U.S. 224 (1988). This test analyses the current value of information as it effects the price of securities discounted by the chances of it occurring. This test has been applied by the Commission in Re Sheridan (1993), 16 O.S.C.B. 6345, and in Re Donnini (2002), 25 O.S.C.B. 6225 (Donnini).

[93] Disclosure is contextual. In the U.S. this has been identified as the total mix of information test; TSC Industries at 449. It seems sensible that the respondents must take into account the import of all extant disclosures, positive or negative, in order to assess whether a fact is material.

[94] Materiality is a question of mixed law and fact, i.e. do the facts satisfy the legal test? Some facts are material on their own. When one or more facts do not appear to be material on their own, materiality must also be considered in light of all the facts available to the persons responsible for the assessment.

[95] The materiality assessment in this case involves a consideration of whether material facts respecting the mandate, information obtained by and findings of the Special Committee were omitted from the disclosure documents. Would the disclosure of such information translate into market gains or losses? In our opinion, the critical question is whether certain undisclosed facts contained in the Special Committee Report would have revealed that YBM was, at the time, exposed to risks that would reasonably be expected to have a significant effect on the value of YBM's securities if disclosed.

[96] Peterson refers to U.S. law for the principle that uncharged criminal conduct or unadjudicated violations of the law generally need not be disclosed. U.S. v. Mathews, 787 F.2d 38 (2d Cir. 1986); SEC v. Chicago Helicopter Industries, 1980 U.S. Dist. Lexis 17214 (N.D. Ill. 1980). This is in reference to the allegation that the company had confirmed it was the subject/target of an ongoing highly sensitive criminal investigation by U.S. law enforcement authorities.

[97] According to John M. Fedders, "Qualitative Materiality: The Birth, Struggles, and Demise of an Unworkable Standard" (1988) 48 Cath. U. L. Rev. 41 at 89:

> The rule is that corporations need not disclose unadjudicated violations of law or antisocial or unethical conduct unless the information is quantitatively significant to investors and alters the total mix of information made available. The compelled disclosure of uncharged and unadjudicated criminal conduct would violate the Fifth Amendment.

[98] The allegation in this case is not whether YBM was engaged in money laundering or some other criminal activity. There is also no allegation that any of the respondents believed the company was a fraud or was not a real company. The evidence regarding the U.S. investigation and possible criminal associations of the founding shareholders and board knowledge is relevant, according to staff, because it demonstrates that the risks facing YBM were real and were readily identifiable through reasonable investigation and diligence.

[99] The U.S. case law with respect to such disclosure is caught up in Fifth Amendment issues related to self-incrimination and testimonial compulsion. There were no such arguments in this case.

[100] In our opinion, the events in this case are extraordinary in nature, the disclosure of which would likely have a significant effect on the market price or value of the securities. The cases referred to by staff and the respondents generally involved insider trading, credible merger negotiations, proxy statements or uncharged and unadjudicated violations of the law. These cases present discrete events in which the materiality analysis is quite straightforward. Such is not the case herein. Would the disclosure of these facts likely affect the market price or value of its securities?

[101] In this regard, we agree with the respondents that the application of the probability/magnitude test to the investigation by U.S. law enforcement agencies as a discrete event is problematic. In essence, the fact of the investigation was incapable of the application of the probability/magnitude test. Probability could not be determined with perfect certainty. However, this does not mean that a fact cannot meet the test for materiality set out in the Act. One should not lose sight of the forest for the trees by assessing the materiality of individual facts piecemeal when the broader factual context suggests a risk faced by an issuer. Some facts may be material on their own, while others may only be material in the context of other facts. The probability/magnitude test is useful in assessing the occurrence of a future event, but common sense must prevail. The broader factual context, or total mix, must not be overlooked when the risk facing the company is a current one.

In Donnini (Re) (2002), 25 O.S.C.B. 6225, the Ontario Securities Commission states at page 33:

> Para. 152. In *S.E.C. v. Mayhew*, 121 F. 3d 44 (U.S. 2nd Cir. Conn. 1997) (*Mayhew*), the United States Court of Appeals for the Second Circuit applied *Texas Gulf Sulphur*, *TSC Industries* and *Basic* with respect to the probability/magnitude test. Citing *Texas Gulf Sulphur*, the court noted, at 52, that "a major factor in determining whether information was material is the importance attached to it by those who knew about it." *Mayhew* concerned a securities trader who had received inside information in respective of a potential merger and traded on the basis of that information. Based on the facts, the court employed a contextual approach and held, at 52, that, "Although Mayhew was not given the specific details of the merger, a lesser level of specificity is required because he knew the information came from an insider and that the merger discussions were actual and serious." Accordingly, the Court concluded that the information at issue was material. In our case, Donnini may not have been aware of all the specifics of the negotiation but he knew it was being undertaken at the highest level at Yorkton and KCA and that Paterson was keen, while KCA was in need of further financing and interested: he knew that the negotiations were actual and serious.

Donnini appealed at the Divisional Court and then cross appealed at the Ontario Court of Appeal. In dismissing Donnini's cross appeal on the liability issue the Ontario Court of Appeal states in Donnini v. Ontario Securities Commission, 76 O.R. (3d) 43 at pages 7-8:

> Para.46. Donnini made a submission in oral argument before this court, which he conceded he had not advanced in front of the Commission or the Divisional Court; nor did he make it in his cross-appeal factum. The argument was that the Commission had paid only "lip service" to the wording of s. 76(1) of the Act. The words "material fact", which anchor s. 76(1), are defined as "a fact that would reasonably be expected to have a significant effect on the market price or value of the securities". Donnini asserts that the Commission did not analyze whether his trading in KCA shares on February 29 and March 1 met this standard.
>
> Para. 47. I disagree. I note that the argument has nothing to do with the Divisional Court's reasons; it ignores them and returns to the Commission's decision. In addition, on an objective basis (which the definition of "material fact" commands), the sheer volume of Donnini's trades on February 29 and March 1 (29.3 and [page53]24.2 per cent of the market for KCA shares, respectively), and the Commission's description of Donnini's motivation for his trades on those days ("Donnini acted in the same manner that a hedge fund intending to participate in the second special warrants financing might have behaved"), support only one conclusion -- Donnini's activity easily came within the definition of "material fact".

In Re Donnini the Ontario Securities Commission also states at page 25:

> Para. 110. The key questions before us were: (i) whether information concerning the second special warrants financing was material, (ii) whether the information constituted a fact, and (iii) whether Donnini's knowledge of the information was knowledge of a material fact. With respect to the first two questions, however, under the Act there is only one determination: is the information a "material fact"? In making this determination, we considered it useful, as a preliminary step, to analyze the questions of when material information may be considered to be established as a "fact", and what is "material".

I find the Ontario Securities Commission approach above to be useful and of assistance in the case at bar and I propose to follow a similar approach. Has the O.S.C. proven the alleged particular? Is the alleged material information established as a "*fact*" ? Is it "*material*" ?

I will now deal with the first question: Has the O.S.C. proven the alleged particulars?

Proof Of The Alleged Particulars

Two of the witnesses called by the O.S.C. with respect to the particulars were Michael Sharwood and Thomas Goin.

Michael Sharwood

The O.S.C. called Michael Sharwood, an Australian corporate lawyer, to give expert evidence and to testify as a fact witness.

Michael Sharwood was "*qualified as an expert in corporate, commercial and securities law in Australia particularly with respect to mining companies.*"

Transcript: May 2, 2005, page 17

The Defence agrees with paragraphs 232-236 of the O.S.C. written submissions Exhibit S5 Volume I:

> Para. 232. Sharwood obtained his honours degree in geology in 1961. He also obtained a masters degree in geology and subsequently worked as a geologist in Canada and Australia. He then completed his law degree and was admitted to the Australian Bar as a solicitor in 1977.
>
> **The Defence agrees.**
>
> Para. 233. Sharwood practises in the area of natural resources law in Australia. He worked on a number of transactions involving mining, oil, gas and financing when he was employed in Canada. He has extensive experience in both small and large scale commercial transactions in Australia, Indonesia, Papua New Guinea, Canada and the United States.
>
> **The Defence agrees.**
>
> Para. 234. Bre-X retained Sharwood on June 13, 1996 to assist in its acquisition of WRPL an Australian public company. This work included the due diligence investigation of WRPL and its assets to find out, among other things, the chain of title to PT WAM.
>
> **The Defence agrees.**
>
> Para. 235. Sharwood performed the due diligence, completed the transaction and delivered a report to Bre-X in July 1996. Bre-X subsequently asked Sharwood to further assist it with other issues surrounding its ownership.
>
> **The Defence agrees.**
>
> Para. 236. In January 1997, Sharwood delivered a report in which he expanded on his conclusions in his previous report and added a short description of title to Busang II (Southeast Zone).
>
> **The Defence agrees.**

Also at paragraph 38 of Exhibit S12 the Defence and O.S.C. state:

> Para. 38. As part of his retainer with Bre-X, Mr. Sharwood conducted extensive due diligence with respect to Bre-X's acquisition of an interest in Busang I and other issues. At the conclusion of his work, Mr. Sharwood delivered to Bre-X a lengthy report dated January 31, 1997 setting out the results of his due diligence

(the "Sharwood Report"). Mr. Sharwood also delivered a due diligence report to Bre-X on July 22, 1996 (the "July Sharwood Report").

Exhibit 302, Report on the title of Bre-X Minerals Ltd. to the Busang 1 and Busang 2 gold project in Indonesia dated January 31, 1997 (the "Sharwood Report")
Exhibit 56, July Sharwood Report, dated July 22, 1996

The OSC admits that Bre-X retained Sharwood on June 13, 1996 to assist in its acquisition of WRPL an Australian public company. This work included the due diligence investigation of WRPL and its assets to find out, among other things, the chain of title to PT WAM. Sharwood performed the due diligence, completed the transaction and delivered a report to Bre-X in July 1996.

Bre-X subsequently asked Sharwood to further assist it with other issues surrounding its ownership. In January 1997, Sharwood delivered a report in which he expanded on his conclusions in his previous report and added a short description of title to Busang II (Southeast Zone).

Sharwood delivered his due diligence report on July 22, 1996 and his final report on January 31, 1997.

Exhibit 56
Exhibit 302
Exhibit 858
Transcript: May 2, 2005, page 17
Exhibit S5 Volume I: paragraphs 231-236
Exhibit S12: paragraphs 34, 35, 38

Thomas Goin

The O.S.C. called Thomas Goin, a foreign legal advisor with the law firm of Mochtar, Karuwin & Komar (MKK) in Jakarta, Indonesia, to give expert evidence. The expert opinion, Exhibit 1001, is signed by MKK but has been referred to as Goin's opinion. Thomas Goin was qualified to give expert evidence in two areas:

1. "Indonesia law as it relates to mineral resources, especially gold," and
2. "Corporate and commercial law in Indonesia."

Transcript: July 19, 2005, pages 2-11
R. v. Felderhof [2005] O.J. No. 5996

Thomas Goin received a Juris Doctor degree from the University of California in 1976 and in that same year was admitted to practice in California courts. Thomas Goin has been a foreign legal adviser at M.K.K. in Indonesia since 1984.

Transcript: July 19, 2005, pages 2-11
Exhibit S12: paragraph 29
Exhibit S5 Volume I: paragraphs 215-219

Contract of Work (COW)

In paragraphs 220-230 of Exhibit S5 the O.S.C. sets out in general terms the way in which a foreign company like Bre-X can survey, explore, conduct feasibility studies, construct mining facilities, and conduct mining, processing and marketing operations in Indonesia. I note the Defence comments to each of those paragraphs. The Defence does not disagree in any substantial way and the Defence comments do not affect anything of significance in this case, except with respect to paragraph 220 and the issue of the KP's which are relevant to Particular 5.

> Para. 220 In Indonesia, mineral resources, including gold, belong to the state and are to be used for the welfare of the Indonesian people. The only way that a foreign company like Bre-X can invest in mineral rights or conduct mining exploration activity of any kind in Indonesia is through a mining authorization known as a COW.
>
> **The Defence agrees with the exception that it is not the only way a foreign company can invest in mineral rights and conduct mining exploration activity.**
>
> Para. 221 The foreign company must enter into a joint venture agreement (JVA) with at least one Indonesian company and apply for a COW.

The OSC cites no evidence. The Defence agrees that in 1987 there was a requirement that a foreign company include an Indonesian partner in a COW application. As of 1994, this was no longer a requirement. It is also usual that the parties enter into a joint venture agreement, but this is not mandatory.

Para. 222 There are several stages in the COW application process:

- application,
- approval in principle,
- negotiation,
- initialling of the COW,
- consultation with the parliamentary committee and the Foreign Investment Review Board (BKPM), and
- approval; where the Minister of the DOME and the President of Indonesia sign the COW.

The Defence agrees with the exception that the President does not sign the COW, but rather the President authorizes the Minister to sign the COW.

Para. 223 If the area identified in the COW application is available and the Director General of the DOME has no objections, he will approve the COW application in principle.

The Defence agrees.

Para. 224 The DOME and the applicant then negotiate the terms of the COW with the DOME, which negotiations can take several months.

The Defence agrees that negotiations could occur, but the practice (as Pak Ridwan testified) is that the applicant is entitled to seek clarification of the provisions of the draft COW, not to negotiate changes to it.

Para. 225 Once the DOME and the applicant are satisfied with the draft COW, the applicant and the DOME initial it.

The Defence agrees.

Para. 226 The Minister of Mines and Energy consults with a committee made up of the Parliament of Dewan Perwakilan Rakya (DPR) and the Foreign Investment Review Board (the Badan Koordinasi Penanaman Modal or BKPM). If the DPR and BKPM have no objections, each will recommend the application to the President of Indonesia.

The Defence agrees. Both the Parliament and the BKPM recommended Bre-X's COW applications for Busang II and III.

Para. 227 When the COW is ready to be signed, the applicants must form a PMA company to sign the COW. When establishing a PMA company, the applicants must sign a deed of establishment incorporating the articles of association. The

articles of association must be approved by the Minister of Justice. The PMA company is then incorporated as a separate legal entity.

The Defence agrees.

Para. 228 The President of Indonesia will then authorize the Minister of Mines and Energy to sign the COW on behalf of the Indonesian government.

The Defence agrees.

Para. 229 Once the COW is signed, the PMA company is directly responsible to the Indonesian government to fulfill the obligations under the COW.

The Defence agrees that it is the PMA company that contracts with the Indonesian government, not the shareholders of the PMA company.

Para. 230 By signing the COW, the Indonesian government gives the PMA company certain contractual rights to conduct mining activities in a certain area. The PMA company does not obtain any ownership interest in the mineral ores or any subsurface land rights.

The Defence agrees.

Exhibit S5 Volume I: paragraphs 220-230
Exhibit S12: paragraph 26

Goin describes Indonesian mining law in his opinion Exhibit 1001 at pages 1-20. Sharwood also does in pages 1-6 of his opinion Exhibit 858. It must be remembered, as his disclaimer sets out, that Sharwood is not qualified to practice law in Indonesia and he was not qualified to testify as an expert in Indonesia law. Pages 1-6 of Exhibit 858 provide background information to understanding his opinion.

PT WAM

PT WAM is the PMA company that signed the COW for Busang I.

On March 30, 1987, WRPL entered into a joint venture agreement with two Indonesian companies PT KG and PT SAP to explore and exploit the mineral resources in Busang I.

Exhibit 899
Exhibit S5 Volume I: paragraph 237
Exhibit S12: paragraph 27

PT KG was controlled by Dr. Jusuf Merukh, an Indonesian businessman and former politician. PT SAP was controlled by Haji Syakerani, an Indonesian businessman. Merukh also owned a percentage of PT SAP.

Exhibit S5 Volume I: paragraph 328

The JVA, Exhibit 899, s. 3, sets out the participating interests of the parties as WRPL: 80%; PT KG: 10%; PT SAP: 10%.

Exhibit 899
Exhibit S5 Volume I: paragraph 243
Exhibit S12: paragraph 27

The PT WAM COW was granted on December 21, 1987 over Busang I and other areas.

Exhibit 859: Tab B1.1(a)
Exhibit S5 Volume I: paragraph 244

Particular 1: That Due To A Failure To Comply With Contractual Obligations Owed To The Indonesian Government And The Shareholders Of PT Westralian Atan Minerals ("PT WAM"), Bre-X Had Not Secured Its Interest In The Property Known As Busang I

What Is The "Interest" In Busang I Allegedly Not Secured?

The O.S.C.'s position is that the "*interest*" in Busang I required to be secured was the legal ownership of the PT WAM shares. The Defendant position is that a beneficial interest in the PT WAM shares was sufficient.

In the O.S.C. written submissions, although not in oral submissions, the O.S.C. concedes Bre-X secured its interest in Busang I when it secured legal ownership to the PT WAM shares on July 27, 1996 by purchasing WRPL through MPNL.

Exhibit S5 Volume I: paragraphs 207- 209, 263, 267, 278, 279

In paragraph 207, Exhibit S5 Volume I which is the first paragraph in the O.S.C. lengthy discussion of Particular 1, the O.S.C. states "*Bre-X did not secure its interest in Busang I until July 27, 1996*" conceding that Bre-X secured its interest in Busang I on July 27, 1996 and that Particular 1 thereby ended on July 27, 1996. In oral submissions the O.S.C. takes a different inconsistent position arguing that Particular 1 does not end on July 27, 1996 but continues throughout the charge periods. The oral submissions are also not consistent with the Information and Particulars which were drafted by the O.S.C. wherein Particular 1 is a "*material fact*" referred to in count 1 and in count 2 which cover the charge periods up to July 26, 1996 but is not a material fact for counts 3 and 4 which cover charge periods after the July 27, 1996 date, commencing August 1, 1996 and ending September 10, 1996.

It is obvious from the way the Information and Particulars were drafted that the position of the O.S.C. was that Particular 1 ended on July 27, 1996 when "*Bre-X finally secured legal ownership to the PT WAM shares.*"

Exhibit S5 Volume I: paragraph 278
Transcript: August 30, 2006, pages 49-53, 66

The Defence concedes Bre-X had beneficial ownership but not legal ownership of the PT WAM shares until July 27, 1996.

Exhibit S12: paragraphs 41-43, 45, 46
Exhibit S5 Volume I: paragraphs 211, 249, 261, 263, 266, 267, 274-279

"Not Secured Its Interest"

In paragraphs 213-214 of Exhibit S5 Volume I the O.S.C. and Defence state:

> Para. 213. At paragraph 24 of the Defence closing argument, it states that "there is no definition in the particulars as to what the nature of the interest was that Bre-X had to acquire in Busang I in order to secure its interest in Busang I".
>
> **The Defence agrees.**
>
> Para. 214. In August 1999, the Defence brought a motion for Particulars for Counts 1-4. The motion was settled on consent.
>
> **The Defence agrees that a motion for particulars was brought and that particulars for counts 1 – 4 were provided by the OSC. This does not relieve the OSC from the burden of proving the particulars in the form that the OSC provided them. Dr. Juneja used the particulars as they are, without change, as well as the alleged consequences of the particulars.**

In oral submissions the OSC stated:

> MS. COLE: Okay, so my point, Your Honour, I think that that closes the inquiry. The fact that there was motion for particulars, the particulars were given, Mr. Groia indicated he was content. He was certainly aware of his right to – his client's right to bring on another motion if he wanted to.

Transcript: August 29, 2006, page 90

I agree with the Defence that the fact that the motion for particulars was settled on consent does not relieve the O.S.C. from the burden of proving the particulars in the form that the O.S.C. provided them.

Exhibit S5 Volume I: paragraphs 213-214
Exhibit S12: paragraph 24
Transcript: August 22, 2006, page 63
Transcript: August 29, 2006, pages 87-103
Transcript: August 30, 2006, pages 4-12

Bre-X Press Release Dated May 6, 1993

On May 6, 1993, Bre-X issued a press release stating in part:

> BRE-X MINERALS LTD. is pleased to report that it has entered the Pacific "Rim of Fire" as a potential gold and base metal miner.
>
> ...
>
> Mr. Walsh went on to say: "Subject to funding and director's approval, the man credited as co-discoverer of the large Ok Tedi copper gold mine in Papua New Guinea, John B. Felderhof, P. Geol., has agreed to head BRE-X's Indonesian exploration offices as General Manager. Mr. Felderhof, also credited with the discovery of four mineral properties in Indonesia of which one is in production, two scheduled to go into production and one at the feasibility stage, and thirteen years of experience in the country, has assembled an experienced team of three senior geologists with extensive experience in Indonesia and the Phillippines to join the BRE-X exploration forces."
>
> In an interview from Jakarta, Mr. Felderhof stated: "The development of projects concentrating on epithermal gold and porphyry gold copper in the Tertiary Volcanic Corridor (Rim of Fire) and massive sulphides will be the focus of our activities."
>
> Mr. Walsh continued: "Initially, BRE-X has an agreement in principle to acquire an 80% working interest in a gold project in East Kalimantan, Indonesia.

Exhibit 6
Exhibit S5 Volume I: paragraph 210

BRE-X FIRST ATTEMPT TO SECURE ITS INTEREST IN BUSANG I: THE 1993 OPTION AGREEMENT

On July 20, 1993 Bre-X purchased a one year option from WRPL to sell and purchase

80% of the total shares of PT WAM.

Exhibit 830
Exhibit S12: paragraph 28
Exhibit S5 Volume I: paragraphs 248, 264-273

Press Release Dated July 19, 1993

On July 19, 1993 Bre-X issued a press release stating in part.

> BRE-X MNERALS LTD. is pleased to report the successful acquisition of an 80% working interest in an advanced gold project in East Kalimantan, Indonesia.

Exhibit 6
Exhibit S5 Volume I: paragraph 210

The disclosure in the press releases changed from "*an agreement in principle to acquire an 80% working interest in a gold project*" in May 1993 to "*the successful acquisition of an 80% working interest in an advanced gold project*" in July 1993 after the option agreement.

In its commentary to paragraph 207, above, of Exhibit S5 Volume I the Defence submits that Bre-X had "*not disclosed*" that Bre-X had "*secured its legal interest*" but "*disclosed... that it had an 80% interest in Busang I*". The Defence is referring to the press release of July 19, 1993, which announced "*the successful acquisition of a 80% working interest*".

Exhibit 6

The Defence is correct that that press release does not announce that Bre-X secured its "*legal interest" but "an 80% working interest.*"

Consents and Approvals

To complete the 1993 option agreement would have required the approvals of the Indonesian government and of the Indonesian partners. This is conceded by the Defence.

Exhibit S12: paragraphs 30, 31, 39
Exhibit S5 Volume I: paragraphs 250, 256, 258

The Defence also concedes Bre-X did not get the necessary approvals from the Indonesian government nor the Indonesian partners. The Defence concedes this transaction was not completed and there was no transfer of the PT WAM shares to Bre-X. As discussed later in these reasons the Defence submits no approvals from the Indonesian government nor partners were required for an "*off shore*" transaction that the Defence submits later occurred in July 1995.

The Defence agrees with the O.S.C. submission in Exhibit S5 Volume I paragraph 252:

> Para. 252. Sharwood advised Bre-X that the July 20, 1993 option agreement to transfer 80% of the total shares of PT WAM was invalid. Therefore, WRPL's shares in PT WAM were not transferred for three reasons:
>
> - The first reason was that because the **transfer or the condition precedent in the agreement had not been satisfied** within the prescribed period of 12 months and all **regulatory and statutory approvals had not been obtained**.
>
> - The second reason is that there was **no evidence of any share register of PT WAM** and accordingly **no evidence of any registration of a transfer of shares.**
>
> - The third reason is that the Articles of Association of PT WAM as a prerequisite to transferring any shares in PT WAM the **transfer requires the approval of two members of the Direksi.** The Direksi is the Board of Directors. [emphasis added by the O.S.C.]

The Defence agrees that Mr. Sharwood said the option agreement was ineffective to transfer the shares. He stated that it was ineffective for the three reasons listed above. The shares were not transferred, but rather Bre-X conducted an offshore transaction in compliance with Indonesian law and the COW. There was no failure to comply with contractual obligations owed to the Indonesian government in connection with the offshore transaction. Mr. Sharwood was not qualified as an expert on Indonesian law.

Exhibit S5 Volume I: paragraphs 252, 253
Exhibit S12: paragraphs 39, 40

The O.S.C. discusses the various requirements of consents needed from the Indonesian government and Indonesian partners for Bre-X to transfer the shares of PT WAM and the fact that those consents were not obtained in Exhibit S5 Volume I, paragraphs 212, 245-260, 265, 270-273 and Exhibit 12, paragraphs 29, 30.

As noted above the Defence conceded Bre-X did not receive these necessary approvals to complete the option agreement to transfer the shares of PT WAM to Bre-X. The option agreement was never completed and Bre-X then attempted to secure an interest in the shares of PT WAM by purchasing MPNL in 1995.

BRE-X SECOND ATTEMPT TO SECURE ITS INTEREST IN BUSANG I: THE 1995 BRE-X PURCHASE OF MPNL

The O.S.C. submissions with respect to Indonesian government and partner consents can only be applicable to the 1993 option agreement and not the 1995 Bre-X purchase of MPNL. The O.S.C. concedes Bre-X obtained a beneficial but not a legal interest in the PT WAM shares through the 1995 purchase of MPNL although no consents were given for that transaction. The O.S.C. also concedes Bre-X secured legal ownership of the PT WAM shares on July 27, 1996 by purchasing WRPL through MPNL although no consents were given for that transaction as well.

Subject to the discussion above on pages 455-456 with respect to the O.S.C. oral submissions, the O.S.C. position as reflected in the O.S.C written submissions and in the

O.S.C. wording of the Information and Particulars that Particular 1 ends on July 27, 1996 and that Bre-X had then secured its interest in Busang I as of that date and as noted above this was done without any government or partner consent.

Exhibit S5 Volume I: paragraphs 207-209, 212, 265, 266, 267, 275-280
Exhibit S12: paragraphs 28-33, 38-46

Goin

In Goin's expert report Exhibit 1001, he states at paragraph 35:

> Para. 35. The above ministerial approvals are required only in the case where there is a direct transfer of the existing shares of the PMA company. Thus, a transfer of shares by a shareholder of P.T. Westralian Atan Minerals would have been subject to these ministerial approvals. On the other hand, where there is an indirect acquisition, e.g. through a change in the ownership of a shareholder of a PMA company, no formal approvals are legally required, though we advise our clients that notification of the change of control is considered good business practice. The acquisition by Bre-X of shares of Westralian Resource Projects Limited, a shareholder of P. T. Westralian Atan Minerals, as Bre-X Minerals Ltd. ("Bre-X") claims occurred (see Supp., Tab 2), would not have required these ministerial consents.

In this trial an indirect acquisition has also be referred to as an off shore transaction. Such a transaction did not require ministerial approval.

Exhibit 1001: paragraph 35
Exhibit S12: paragraphs 30-33

Sharwood

Sharwood also gave an opinion about this indirect acquisition. Paragraph B1.2(d) of Exhibit 858, Sharwood's expert report states:

> B1.2(d) There is evidence in the materials examined (and this is discussed in section B 2.2) of dealings in the WRPL PT WAM Shares whereby they were transferred ultimately to MPNL. These dealings pre-date the 1993 sale transfer and conveyance to Bre-X, and therefore cast further doubt on the validity of that transaction. Probably (but there is no supporting evidence in the materials

examined) for this reason, in 1995 all of the issued shares in MPNL were acquired by Bre-X A (see section B 3.2(b)) in order to achieve indirectly what had been intended to be achieved directly.

Exhibit 302
Exhibit 858
Exhibit 828
Exhibit S12: paragraphs 40-43

With respect to the 1995 Bre-X purchase of MPNL Sharwood concludes at Exhibit 858 B2.4(b):

> B2.4(b) Subject only to the Merukh Option, the documents reviewed lead to the conclusions that:
>
> (i) WRPL has since the date of the WAM COW been, and at present is, the registered holder of 80% of the issued shares in PT WAM; and
>
> (ii) MPNL is probably (although the matter is not without doubt) the beneficial holder (under Australian equitable principles) of 80% of the issued shares in PT WAM by virtue of the section B 2.3 arrangements as well as by reason of the agreements referred to in section B.2.2(b)(ii) and section B2.2(e). The latter (whereby WAPL purported to sell the WRPL PT WAM Shares to MPNL) post-dates the correspondence from MGNL to Soebagjo referred to in section B.2.2(e) and therefore supports the chain of beneficial title to the WRPL PT WAM Shares from WRPL to WAPL and ultimately to MPNL.

Exhibit 302
Exhibit 858
Exhibit 828
Exhibit S12: paragraphs 40-43

The uncompleted 1993 option agreement did not give Bre-X a secured interest in Busang I. The 1995 Bre-X purchase of MPNL gave Bre-X a beneficial interest but not legal title to WRPL's shares in PT WAM.

As noted above the Defence submits a beneficial interest in the PT WAM shares was sufficient to secure Bre-X's interest in Busang I. The O.S.C. written submissions (also

see pages 455-456 above for the O.S.C. oral submissions to the contrary) state that Bre-X secured its interest in Busang I only when it secured legal ownership of the PT WAM shares on July 27, 1996.

What Is The Nature Of This Beneficial Interest?

As stated in Exhibit 858 it is an interest "*under Australian equitable principles.*"

Sharwood testified in chief:

> MR. SHARWOOD: What we are seeing on the left-hand side is the outcome of two transactions which I discovered during the coarse of my investigations. The first transaction is the one referred to in the note. In fact, it was a sequence of transactions taking place between a series of Australian companies and in one case a Singapore incorporated company. The ultimate result of which I concluded to be that beneficial ownership as understood in Australian law to 80% of the shares in PT WAM had passed from W.R.P.L. to a company called Montague Pacific NL, passing on the way through a Singapore company called Westralian Atan, A-t-a-n, private limited.
>
> MR. MARROCCO: Now beneficial ownership, in Australian law what do you mean when you say "beneficial ownership"?
>
> MR. SHARWOOD: It meant that the legal owner was the trustee of the beneficial ownership, or held the shares in trust for the benefit of the beneficial owner.
>
> MR. MARROCCO: And was Montague Pacific an Australian corporation?
>
> MR. SHARWOOD: Yes, it was.
>
> MR. MARROCCO: And I think you said W.R.P.L. was also an Australian corporation?
>
> MR. SHARWOOD: Yes, it was.
>
> MR. MARROCCO: And did Australian law at that time recognize the distinction between legal ownership and beneficial ownership?
>
> MR. SHARWOOD: Yes, it does, did and it does.

Transcript: May 2, 2005, pages 43-44
Exhibit S12: paragraph 43

In cross-examination Sharwood was asked about his statement in Exhibit 883, a fax from Sharwood to Arthur Anderson:

> MR. GROIA: "Australian law recognizes the equitable concept of beneficial interests so that if a party was the holder of shares on the record but held the shares completely for the benefit of another party the other party is recognized as holding an interest in the shares. Such an interest is proprietary in nature and is said to be the beneficial interest. The beneficial interest carries with it all of the rights and incidents of ownership so that the party which holds the shares on the record is bound to deal with the shares as directed by the holder of the beneficial interest. The holder on the records is, in effect, relegated to the role of a formal holder of the title to the shares and must do as the beneficial holder directs in relation to the shares.
> Now as at that time, was that an accurate description or definition of beneficial interest as you understood it?
>
> MR. SHARWOOD: Yes.
>
> MR. GROIA: So before the beneficial title and the legal title were married together Bre-X had the beneficial interest as described here with respect to the PT WAM shares, correct?
>
> MR. SHARWOOD: M.P.N.L. did and Bre-X owned M.P.N.L., yes.
>
> MR. GROIA: Yes. So that was the interest that Bre-X held, you concluded that Bre-X held when Bre-X was listed on the Toronto Stock Exchange in April of 1996?
>
> MR. SHARWOOD: Yes.
>
> MR. GROIA: And it's also the interest that you concluded Bre-X held when the stock split in May of 1996?
>
> MR. SHARWOOD: Yes.
>
> MR. GROIA: And it was married up with the legal title, as we put it, on July 27, 1996, when the closing of the Waverly transaction occurred?
>
> MR. SHARWOOD: Yes.
>
> MR. GROIA: Okay.
>
> MR. SHARWOOD: There was always the question, of course, whether that beneficial interest would be recognized by the authorities in Indonesia.

MR. GROIA: Yes. But W.R.P.L. and M.P.N.L. were both Australian companies, correct?

MR. SHARWOOD: Yes.

MR. GROIA: And the beneficial interest, as you have described it here, you were describing it was understood under Australian law, correct?

MR. SHARWOOD: Correct.

MR. GROIA: Okay. As far as the Indonesian Government was concerned W.R.P.L. had been the owner on the record the entire time, correct?

MR. SHARWOOD: Yes.

Transcript: May 4, 2005, pages 60-61
Exhibit 883
Exhibit S12: paragraph 46

Immediately following the excerpt in Exhibit 883 put to Sharwood above in cross-examination is the following paragraph:

> We understand that Indonesian law does not recognize any equivalent concept of beneficial interests as such. Accordingly, any transfer of shares in PT WAM would only be effective upon execution of a notary deed and registration of the share transfer in the records of PT WAM. Any agreement between Westralian Resource Projects Limited (WRPL) and MPNL to transfer title to the shares in PT WAM will not be effective to transfer any interest in the PT WAM shares from WRPL to MPNL unless and until the formal notary deed is executed and the transfer is registered.

Exhibit 883

The paragraph above reflects Sharwood's testimony "*that Indonesian law does not recognize any equivalent concept of beneficial interests as much.*"

Goin also testified that beneficial interests are not recognized under Indonesian law.

There is no evidence that Bre-X would be required to go before an Indonesian court to enforce their interest in Busang. In fact, as noted below the applicable courts were those in Australia where beneficial interests were recognized.

Sharwood testified that Bre-X would have to apply to courts in Australia to enforce their rights:

> MS. COLE: You were asked in cross-examination about whether or not Bre-X held a beneficial interest in PT WAM on or about April 22nd when it was listed on the Toronto Stock Exchange and you were also asked whether Bre-X held that same beneficial interest in PT WAM when the stock split on May the 22nd. And you testified, if I understood, that Bre-X did, in fact, have this beneficial interest. I am wondering if you can tell us what rights did Bre-X have in April/May, 1996, as the beneficial owner of that 80% interest in PT WAM?
>
> MR. SHARWOOD: Bre-X through a chain of subsidiaries notably Bre-X Amsterdam Minerals BV was the shareholder, the sole shareholder of Montague Pacific which in turn, by reason of transactions entered into between WRPL, a Singapore company called Wetralian Atan PT Limited and a subsequent transaction between WRPL and Montague acquired beneficial rights to 80% of the shares in PT WAM subject only to the Merukh option.
>
> MS. COLE: And what were those beneficial rights that you have described?
>
> MR. SHARWOOD: Well they are the ordinary rights of a beneficiary under a trust. That is the right to have the asset dealt with by the trustee at the direction of the beneficiary.
>
> MS. COLE: And can I take it from that that they don't have the right to deal with the active director?
>
> MR. SHARWOOD: Correct.
>
> MS. COLE: And how would they enforce that right to have the asset dealt with in accordance with their wishes by the trustee?
>
> MR. SHARWOOD: By application to the courts probably in Western Australian, but somewhere in Australia.

Transcript: May 10, 2006, pages 127-128
Exhibit S5 Volume I: paragraphs 276, 277
Exhibit S12: paragraph 41

As seen above in Exhibit 858 B2.4 (b) (ii) Sharwood's report states that:

> MPNL is probably (although the matter is not without doubt) the beneficial holder (under Australian equitable principles) of 80% of the issued shares in PT WAM...

Exhibit 858 is Sharwood's final 31 January 1997 report. The same paragraph is found in Sharwood's 22 July 1996 report, Exhibit 56. But in a letter dated July 25, 1996, Exhibit 890, to the solicitor for Waverly (McLucas claim), Sharwood had an edited copy of the report sent stating that "*MPNL is the beneficial owner*" leaving out "*probably (although the matter is not without doubt).*"

Exhibit 56
Exhibit 858
Exhibit 890
Exhibit S12: paragraph 45

Sharwood agreed this was "*more bullish than the wording... to Bre-X.*" He testified he did not remember why it was revised that way.

Transcript: May 4, 2005, pages 119-120

Although in commenting on paragraphs 42 and 45 of Exhibit S12, the O.S.C. highlights "*probably (although the matter is not without doubt)*", in its written submissions the O.S.C. makes no submissions that the beneficial interest "*is not without doubt*" but simply states that Bre-X had a beneficial interest in the shares of PT WAM. See paragraphs 276, 277, 279 of Exhibit S5 Volume I.

Felderhof's Knowledge Of Bre-X's Interest

Sharwood testified Bre-X held this beneficial interest when Bre-X was listed on the Toronto Stock Exchange in April of 1996.

Transcript: May 4, 2005, page 60
Exhibit S12: paragraph 46

Felderhof did not know of this beneficial interest until Sharwood's opinion. Felderhof's stated belief to Rolando Francisco was that any opposing claim (McLucas claim) to Bre-X's interest was "*bogus*". See pages 475-479 of these reasons for Francisco's evidence.

Transcript: March 1, 2001, page 109

Rolando Francisco was Senior Vice President, Chief Financial Officer and a director of Gold Corp. before joining Bre-X in April 1996 as Executive Vice-President, Chief Financial Officer and a director. Francisco's curriculum vitae is Exhibit 106.

Exhibit 106
Transcript: November 29, 2000, pages 101-103
Transcript: November 30, 2000, pages 20-27

July 28, 1996 Press Release

The July 28, 1996 Bre-X press release stated:

> Bre-X...announced today that an agreement has been reached with Montague Gold NL whereby the completion of a previous transfer to Bre-X by Montague of it's interests in certain mining exploration joint ventures in Indonesia has been successfully concluded. This transaction completes the transfer to Bre-X the full and legal beneficial ownership of the Busang I project commonly known as the Central Zone. This further agreement is designed to clarify and remove any doubts over the ownership of Bre-X's interest. In consideration for entering into this subsequent agreement Montague has received payment of US$5.6 million and a net smelter royalty of one quarter of one percent of Bre-X's share of production after three million ounces of Gold have been produced from the Central Zone.

Exhibit 6

In paragraph 209 of Exhibit S5 Volume I the O.S.C. submits this is "*the first time Bre-X disclosed that there was any doubt about its ownership in Busang I.*"

Exhibit S5 Volume I: paragraph 209

I read that press release not as a concession by Bre-X that there was in fact a doubt about the ownership of Bre-X's interest but as removing any doubts that had previously been expressed such as the Levesque Beaubien analyst report dated June 7, 1996 reporting on "*Rumours*" about a "*Lawsuit*" by an "*Australian company [that] owned 80% of the Central Zone up to October 1993*".

Exhibit 434B: pages 119-120

As discussed later (page 475-479), Francisco believed Waverly's allegations (McLucas claim) to be a "*nuisance*", "*without merit*" and "*false*" and he agreed with Felderhof that they were "*bogus*". This is not a belief that there were in fact any "*doubts over the ownership of Bre-X's interest*".

Transcript: December 7, 2000, pages 28, 51-52
Transcript: March 1, 2001, pages 108-112

December 13, 1995 Felderhof Fax to MacDonald

On December 13, 1995, Felderhof wrote to MacDonald:

> Last but perhaps of over-riding importance that you are to carry on and conclude at the soonest with the Montague Group to secure incontestable tenure rights for Bre-X in PT.WAM.

Exhibit 1043: Tab 929
Exhibit S5 Volume I: paragraph 282

I see this as a reference to a situation similar to what eventually actually occurred as disclosed in the July 28, 1996 press release; that is, the completion of the previous transfer to Bre-X by Montague of its interests in PT WAM.

As noted above, Francisco testified Felderhof's stated belief was that Montague's claim was "*bogus*". Francisco believed it to be "*without merit*", "*false*" and a "*nuisance*". Such a claim is not a claim that makes Bre-X's rights contestable.

Transcript: December 7, 2000, pages 28, 51-52
Transcript: March 1, 2001, pages 108-112

MacDonald's Briefing Memorandum For Rolando Francisco

On April 13, 1996 Felderhof faxed MacDonald:

> 'Shareholders' agreement, go through this with Roly and Mike Bird on Tuesday morning and any other outstanding corporate matters including WAM you both should brief him?

Exhibit 1042: Tab 1123
Exhibit S5 Volume I: paragraph 284

In April 1996 Francisco went to Indonesia and met with MacDonald and other Bre-X personnel. He met with MacDonald for three or four days. He later met with Felderhof.

Exhibit S5 Volume I: paragraph 283

In paragraph 287 of Exhibit S5 Volume I the O.S.C. submits and the Defence agrees:

> Para. 287. MacDonald told Francisco that Felderhof was the "head of the entire operations in Indonesia" and that MacDonald, Bernard Leode, Bre-X Controller, de Guzman and Bird reported to Felderhof.
>
> **The Defence agrees.**

In paragraph 285 of Exhibit S5 Volume I the O.S.C. and Defence submit:

Para. 285. MacDonald gave Francisco a briefing memorandum dealing with the current status of Bre-X affairs in Indonesia.

The Defence agrees that Mr. MacDonald gave Mr. Francisco a briefing memorandum. However, the briefing memo is not evidence in this proceeding.

Exhibit S5 Volume I: paragraph 285
Exhibit 15
Exhibit 16

In the Exhibit Chart Exhibit S16, created jointly by the O.S.C. and Defence, the O.S.C. and Defence agreed that the two iterations of MacDonald's briefing memorandum put in through Francisco, Exhibit 15 and Exhibit 16, were admissible for the state of mind of the witness Francisco and not for the truth of its contents. At the end of the prosecution's case the O.S.C. brought an application to admit a number of documents as business records for the truth of their contents including Exhibit 15, Exhibit 16 and Exhibit 1114(i) which was a third iteration of the memorandum. On September 22, 2005, I ruled Exhibit 15, 16 and 1114(i) to be inadmissible under s.35 of the *Ontario Evidence Act.*

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Francisco's state of mind is not relevant to Felderhof's state of mind but Francisco's discussions with Felderhof about the MacDonald memo and the ownership of 80% of PT WAM are relevant to Felderhof's knowledge of those ownership issues.

Francisco's state of mind is not evidence with respect to the issue of the status of Bre-X's ownership of 80% of PT WAM but Francisco's discussions with Felderhof or more specifically Felderhof's statements may be some evidence going to prove the status of Bre-X's ownership.

The discussions that occurred between Felderhof and Francisco in Indonesia shortly after Francisco started working for Bre-X occurred before the charge periods began.

The O.S.C. submissions with respect to Francisco's evidence are found at Exhibit S5 Volume I paragraphs 289-294:

> Para. 289. After they returned from Busang, Felderhof and Francisco discussed the ownership issues surrounding PT WAM.
>
> **The Defence agrees that Mr. Francisco and Mr. Felderhof discussed "the issue of McLucas and the PT WAM question" in Jakarta. (Evidence of Mr. Francisco, December 4, 2000, Vol. 27, page 84)**
>
> Para. 290. Francisco showed Felderhof the MacDonald briefing memorandum. They reviewed and discussed the ownership of PT WAM. Felderhof indicated that he thought that the acquisition of PT WAM had already been completed, and that he was unhappy that Walsh had not yet succeeded in completing this.
>
> **The Defence agrees that Mr. Felderhof told Mr. Francisco that in Mr. Felderhof's view, "Bre-X had already completed the transaction with respect to the PT WAM". (Evidence of Mr. Francisco, December 7, 2000, Vol. 30, page 45)**
>
> Para. 291. Felderhof told Francisco that Bre-X bought an 80% interest in PT WAM and that PT WAM was owned or controlled by a company called Waverley.
>
> **The Defence agrees that Mr. Francisco used the term "Waverley" when he was referring to matters that took place in 1992 and 1993. The correct company was MGNL. Mr. Francisco also said that the company who owned or controlled PT WAM had been owned or controlled by "Waverley". Mr. Francisco went on to describe the company as "Waverley Finance, or the company that had that 80% interest in PT WAM". (Evidence of Mr. Francisco, December 4, 2000, Vol. 27, pages 88 – 89)**
>
> Para. 292. Francisco testified that based on the description he was given, the company that Bre-X bought to acquire 80% of PT WAM was not the right company.
>
> **The Defence agrees that Mr. Francisco said that based on the briefing memorandum given to him by Mr. MacDonald, the company that Bre-X bought to acquire the 80% interest in PT WAM was not the right company as represented by "Waverley". (Evidence of Mr. Francisco, December 4, 2000, Vol. 27, page 93)**
>
> Para. 293. During this visit to Indonesia in April 1996, Francisco warned Felderhof that it would be difficult for him [Francisco] to negotiate with a

potential joint venture partner on the Busang property if there were outstanding ownership issues with Busang I that could potentially affect Busang II and Busang III.

The Defence agrees that Mr. Francisco said:

"I told him or advised him that it would be difficult for me, as the major mandate being to negotiate with a potential joint venture partner on Busang property, that if there are issues, rightly or wrongly, that were still outstanding in connection with the ownership of Busang I, which could potentially jump to Busang II or Busang III, that I do not know, so I said I would not be able to begin first to officially engage J.P. Morgan as the financial – as a financial advisor, as well as the Republic National Bank of New York, as what we then call corporate advisors, because there are these subjects that are – that had been brought up by – through several individuals, by Mr. McLucas. And I said I still had to negotiate the PMA and just – and you're aware of how it is to negotiate things over there in Indonesia".

Para. 294. Francisco told Felderhof and Walsh that he would be delayed in retaining financial advisers because he did not want to continue negotiating with others knowing that there were outstanding ownership issues.

The Defence agrees that Mr. Francisco said he would be delayed because of Mr. McLucas' claims. Mr. Francisco also concluded shortly after this that Mr. McLucas' claim was a nuisance. (Evidence of Mr. Francisco, December 13, 2000, Vol. 33, pages 91-92)

Exhibit S5 Volume I: paragraphs 289-294

Felderhof told Francisco that *"[i]n his view, at that point, that Bre-X had already completed the transaction with respect to the PT WAM"* and that *"he was sort of unhappy with the way he believed this was handled by Mr. Walsh and now he was unhappy that things like this are happening and should have been done a long time ago."*

Transcript: December 7, 2000, page 45

Felderhof was unhappy because he believed that the transaction that was finally completed in July 27, 1996 should already have been completed by April of 1996. This

transaction was completed on July 27, 1996 by settling a "*bogus*", "*false*", "*nuisance*" claim that was "*without merit*".

Francisco's stated concerns with respect to negotiating with a potential joint venture partner (Exhibit S5 Volume I: paragraph 293) and retaining financial advisers (Exhibit S5 Volume I: paragraph 294) are related to his state of mind based on MacDonald's briefing memo which was not admitted for the truth of its contents.

Those concerns are not based on what he came to believe were the true state of affairs that the McLucas claim was "*false*", "*without merit*" and a "*nuisance*" only.

Transcript: December 7, 2000, pages 28, 51-52
Transcript: March 1, 2001, pages 108-112

END OF PARTICULAR 1: JULY 27, 1996

As noted above, in the written submissions the O.S.C. concedes that Bre-X secured its interest in Busang I on July 27, 1996 (see pages 455-456 for contrary oral position) when the Waverley or McLucas transaction was completed effectively merging Bre-X's legal and beneficial interest in the PT WAM shares.

Exhibit S5 Volume I: paragraphs 278, 279

Francisco described the Waverley transaction in his evidence:

> MR. FRANCISCO: Well, Mr. McLucas and I – it took only approximately five, six minutes, or maybe even less, to arrive into an agreement, although verbal at that point, but it was an agreement and we shook hands and we agreed that we would – that he would get his lawyers to start the process and that I would hire an Australian lawyer to do the work for Bre-X and that they would be in contact with each other in Sydney.

And at that point, we went back to the group and I believe I advised the group that Mr. McLucas and I had reached, at that point, an agreement to settle all the issues related to the delay in the completion of the transaction on PT. WAM, including all other allegations against Mr. Felderhof that was being made by Mr. McLucas.

...

MR. FRANCISCO: Well I – what came to my mind right at the very moment – I'm saying this to you so that you would have a clearer understanding why I – what I discussed with Mr. Felderhof, after the group dispersed.

What came to my mind at that very moment when Mr. McLucas agreed for a consideration of six million dollars, was that Mr. McLucas, in part – and I don't remember if I had brought it up in one of your –as an answer in one of your questions. Mr. McLucas had also alleged that he may have a potential interest on Busang II. So when – at that moment, when he and I were together alone negotiation and he agreed to settle for a consideration of six million dollars and I said to myself, "The company had a market value," meaning Bre-X, "had a market value of, I believe, somewhere around four or five billion dollars and here he was, if his claim or his allegations were, in fact, true, why would he settle for just six million dollars?"

So I just would like to put that in your mind, so that I can answer your question more clearly –

MR. NASTER: Yes.

MR. FRANCISCO: - why I said that.

THE COURT: Just so I have it clear then –

MR. NASTER: Certainly.

THE COURT: - so the settlement that was reached between Mr. Francisco and Mr. McLucas, included that alleged claim to Busang II?

MR. NASTER: Is that correct, sir?

MR. FRANCISCO: It's overall, Your Honour.

THE COURT: The settlement was for everything?

THE WITNESS: For everything, Your Honour. Alleged or unalleged, whatever, this is an absolute of claims from both sides.

So bearing that in mind, I – when Mr. Felderhof had that subsequent discussion in the lounge, I was second guessing myself. I questioned myself – maybe I paid too much – not me, I don't have that kind of money, meaning the company.

Maybe I paid too much, six million dollars. If his allegations were true, why would he settle for six million.

...

MR. GROIA: And in general terms, in both of those instances, essentially what the board decided was that until the transaction with McLucas was completed, there was nothing to disclose, is that fair?

MR. FRANCISCO: Maybe, sir, yes.

MR. GROIA: There were all these innuendo and allegations floating around that you wanted to get to the bottom of, so you went to meet with Mr. McLucas and you made a deal with him in ten minutes for six million dollars and that was the end of the matter.

MR. FRANCISCO: Well, I thought it was just a nuisance, after I had had the chance to meet with Mr. McLucas.

MR. GROIA: Would you agree with me, sir, that a nuisance claim is synonymous with a claim that's not material?

MR. FRANCISCO: I think I heard a word from one of my colleagues that it was a "bogus claim".

MR. GROIA: A "bogus claim."

MR. FRANCISCO: That was a word I heard from one of my colleagues.

MR. GROIA: Was that a member of the legal fraternity or another colleague?

MR. FRANCISCO: No, no, no, it's from Mr. Felderhof.

MR. GROIA: And you agreed with that.

MR. FRANCISCO: Well, after – at first, when I met with Mr. McLucas, I think I expressed to the Crown in my earlier testimony, that – and you know the circumstances of the allegations of Mr. McLucas, one of which was he believed that he was misled by Mr. Felderhof as to the potential of Busang and also an issue of incomplete transaction in there, and after I met with Mr. McLucas and closed – and had a handshake with him, I asked myself, you know, maybe I overpaid because – when I say "I," it's the company. I don't have the money, six million dollars, because if I were Mr. McLucas, if I were him and if my

allegations were strong and if I really believed in my allegations, I would have asked for the entire Busang property, not just for six million dollars, considering the fact that the market capitalization of Bre-X was in the billions of dollars, at least four or five billion dollars at that time.

So therefore, how could you – yes, Mr. Felderhof was right to say it was a bogus claim and for me I say it's a nuisance claim.

MR. GROIA: Was it ever described to you as a frivolous claim?

MR. FRANCISCO: I have heard of the word, but I don't know if it was in that context.

MR. GROIA: Did you consider –

MR. FRANCISCO: I think the word I heard was "without merit."

MR. GROIA: "Without merit."

MR. FRANCISCO: Yes, sir.

MR. GROIA: Would you agree with me, sir, as a director of a public company, a bogus claim is not a material fact?

MR. FRANCISCO: Well, if I look on the definition of "bogus" in the dictionary, it may be that will help. But what's the definition of "bogus"? I mean –

MR. GROIA: Phony, or false, or –

MR. FRANCISCO: Well, it's false. So it's not a material fact, it's false. If we believe it's false, in my view, without being a securities lawyer, if it's false, it's false.

MR. GROIA: And that view was shared by the other directors.

MR. FRANCISCO: I believe so.

MR. GROIA: Any by your advisors.

MR. FRANCISCO: I believe so, sir.

MR. GROIA: And by your legal advisors – they were consulted and gave you advice about whether there was a need to disclose this bogus claim.

MR. FRANCISCO: I believe so, sir.

...

MR. GROIA: Did you follow a similar process in reaching the conclusion that the McLucas claim was not material?

MR. FRANCSICO: I think we did an extensive due diligence on that.

MR. GROIA: And had extensive discussions with the lawyers about materiality question.

MR. FRANCISCO: All – and lawyers and other consultants.

MR. GROIA: And other consultants.

MR. FRANCISCO: Yes, sir.

MR. GROIA: And the board, as a group, reached a decision that the McLucas claim was not material.

MR. FRANCISCO: Are we talking of Jusef Merukh or McLucas?

MR. GROIA: No, McLucas, I say.

MR. FRANCISCO: Yes, sir.

MR. GROIA: So you reached a collective decision as a group that the McLucas claim was not material.

MR. FRANCISCO: Well, we did not have a formal board meeting –

MR. GROIA: Yes, sir.

MR. FRANCISCO: - to approve that, but at that time, don't forget, I was just new with the company and faced with this thing. It was just barely a month and a half that I had been with the company at that time.

MR. GROIA: And, of course, you met face to face with Mr. McLucas and negotiated the deal.

MR. FRANCISCO: Yes, I did. Yes.

MR. GROIA: And based on that face to face discussion and that ten minute negotiation, did that cause you to change your opinion that this was a bogus claim and not material?

MR. FRANCISCO: No, I think it reenforced [sic] that concept that it's a nuisance claim.

MR. GROIA: And that meeting and that opinion, where your view was reinforced, had nothing to do with Mr. Felderhof, correct? You sat across the table from Mr. McLucas and you cut a deal and you walked away think this was a bogus claim, independent of anything you'd been told by Mr. Felderhof.

MR. FRANCISCO: Yes.

Transcript: December 7, 2000, pages 28, 51
Transcript: March 1, 2001, pages 108, 111

It took only approximately five or six minutes and six million dollars to settle all issues between Bre-X and the Waverley group of companies with respect to Busang I and II and III. Francisco questioned why McLucas would settle for so little if Waverley's alleged interest in Busang was true. Francisco believed Waverley's claim was a "*nuisance claim*", "*false*", "*without merit*", "*bogus*", and not a material fact. Francisco testified his face to face discussion with McLucas did not change his opinion but reinforced it that it was a nuisance claim. Francisco was an O.S.C. witness whose creditability and ability as a corporate executive and director was not questioned by any party.

No Effect On Operations of Busang

The completion of the Waverley (McLucas) transaction had no effect on the operations at Busang. It was simply the settlement of a nuisance claim.

The Intention Of The Montague Companies

The understanding and intention of the Montague Companies was that Bre-X had ultimate control of 80% of the PT WAM shares and Montague Gold intended to conclude the transaction, although perhaps with some additional benefits for themselves.

Exhibit 888 is a fax dated July 3, 1995 from Hedderwick as executive director of Montague Gold to KPMG:

> We write to advise you that the ownership of Montague Pacific NL (MGP) has changed. MGP was an 100% subsidiary of Montague Gold NL and is now owned and controlled by Bre-X Minerals Amsterdam NV (Bre-X).
>
> PT Westralian Atan Minerals (PT WAM) is 80% owned by MGP and thus is also ultimately controlled by Bre-X.
>
> You kindly audited and provided an accounting service for PT WAM from its incorporation in 1988 and the representatives of Bre-X in Indonesia require access to all PT WAM accounting, audit and tax return records you may have in your possession.
>
> Please accept this letter as our authority to you to make available to Mr. John Felderhof of Bre-X, or his stated representative, all records you have to hand as Bre-X are now the ultimate major shareholder and manager of PT WAM.

In Exhibit 1044, Tab 1038, Hedderwick faxes David Walsh on February 16, 1996:

> As you will know from various faxes, I am working with Montague Gold NL to establish the best means to conclude the transfer. We are slightly hampered by our lack of understanding of the problem which has not been fully explained. John Felderhof's fax of 12 February does not make much sense to us, and the manner is totally unnecessary bearing in mind your fax to me of 5 December.
>
> David, we have a concern about what you, or Bre-X, were told in 1993 that made you so excited about Busang compared to what we were told at the same time by the same person who was then being paid by Montague, particularly in view of the fact that Montague Gold NL and its controlling shareholder, Waverly Mining Finance plc had ample funds available at that time.

O.S.C. Position Re Beneficial Interests

I note the O.S.C.'s different views of beneficial interests. In the O.S.C.'s submissions, Felderhof's beneficial ownership of the Grays Inn J & I account was sufficient to prove that trading in the account was Felderhof's trading, but Bre-X's beneficial interest in the PT WAM shares was not sufficient to secure its interest in Busang I.

Merukh Option

On January 12, 1996, Felderhof faxed MacDonald stating in part: "*Mike Bird to draw up resolution stating that option agreement with Indonesian partner(s) are hereby cancelled*" indicating Felderhof's awareness of an alleged option agreement by Merukh.

Exhibit 1043: tab 971
Exhibit S5 Volume I: paragraphs 295-296

A Merukh option for an additional 20% of PT WAM discussed in Sharwood's opinion, Exhibit 858, would have decreased the percentage of Bre-X's interest in Busang I.

Exhibit 858
Exhibit S5 Volume I: paragraphs 239-243

In his expert opinion, Exhibit 858, B2.5(e)(i), Sharwood states: "*it is reasonable but not conclusive to infer that the Merukh Option was also terminated*".

Exhibit 858
Exhibit S5 Volume I: paragraphs 295, 296

It is difficult to reconcile the O.S.C. submission that the Merukh option is relevant to Particular 1 with the O.S.C. position reflected in the O.S.C. written submissions (see also pages 455-456) and in the O.S.C. wording of the Information and Particulars that Particular 1 ends on July 27, 1996 when Bre-X completed the purchase of WRPL

because the purchase of WRPL did not have anything to do with the Merukh option and would not have affected it.

As discussed below Particular 1 alleges Bre-X did not secure its interest in Busang I because of a failure to obtain consents or approvals from the Indonesian government and shareholders of PT WAM. The Merukh option, if it existed, is a separate matter.

FINDING

Francisco was told several times by Walsh that "*everything was 'immaculate' throughout the company.*" It was not, but that does not mean the O.S.C. has proven Particular 1 beyond a reasonable doubt.

Transcript: November 30, 2000, page 6

Particular 1 states that Bre-X had not secured its interest in Busang I "*due to a failure to comply with contractual obligations owed to the Indonesian government and the shareholders of PT Westralian Atan Minerals.*"

On the O.S.C.'s presentation of the case and on all of the evidence, the contractual obligations referred to were the consents or approvals required from the Indonesian government and shareholders of PT WAM for a direct purchase of the shares of PT WAM. No consents or approvals were required for an indirect acquisition of the shares of PT WAM by purchasing the shares of the company (WRPL) that owned the shares of PT WAM as was finally completed on July 27, 2006.

Assuming that Bre-X had not secured its interest, on the evidence, that would not be due to a failure to comply with contractual obligations owed to the Indonesian government and shareholders of PT WAM but due to a failure to complete the indirect or "*off shore*" acquisition of an interest in Busang I.

Bre-X, through MPNL, held a beneficial interest in the shares of PT WAM. Michael Sharwood, the expert called by the O.S.C., agreed that a beneficial "*interest is proprietary in nature...*" and that:

> The beneficial interest carries with it all of the rights and incidents of ownership so that the party which holds the shares on the record is bound to deal with the shares as directed by the holder of the beneficial interest. The holder on the record is in effect relegated to the role of a formal holder of the title to the shares and must do as the beneficial holder directs in relation to the shares.

Exhibit 883
Exhibit S12: paragraph 46
Transcript: May 4, 2005, pages 60-61

The evidence that Bre-X had secured a beneficial interest in Busang I raises a reasonable doubt that the O.S.C. has proven Particular 1 that Bre-X had not secured its interest.

The only difference in the state of affairs before July 27, 1996 when Bre-X had a beneficial interest but the O.S.C. alleges it had not secured its interest in Busang I and after July 27, 1996 when the O.S.C. concedes that Bre-X had secured its interest (Exhibit S5 Volume I, paragraph 207 but see pages 455-456 above) was the completion of the McLucas transaction.

I have a reasonable doubt that the settlement of this "*false*", "*bogus*", "*nuisance*" claim "*without merit*" on July 27, 1996 is sufficient to distinguish the state of affairs in any meaningful way between the time before and after July 27, 1996.

Exhibit S5 Volume I: paragraphs 207-209, 263, 267, 278, 279

There is a reasonable doubt that the O.S.C. has proven Particular 1.

PARTICULAR 2: THAT BRE-X HAD MISLEAD THE INDONESIAN GOVERNMENT RESPECTING THE ACQUISITION OF AN 80% INTEREST IN PT WAM

The February 13, 1996 Bre-X Letter To D.O.M.E.

On January 25, 1996, Dr. Kavanagh and de Guzman met with representatives of the

Indonesian Department of Mines and Energy (D.O.M.E.).

Transcript: February 28, 2005, pages 97-98
Exhibit 577: pages 87-88
Exhibit S5 Volume I: paragraph 302

In a memorandum to Felderhof dated January 26, 1996 de Guzman wrote:

> With reference to "feedback" from the Mines Department during yesterday's presentation, listed below are critical items which must be addressed immediately...
>
> B. Immediate Actions Required....
>
> 2. Official letter to Mines Department pertaining to Bre-X Minerals Limited ownership of Westralian Project Resources Limited. GCD with MCB assistance (as needed).

Exhibit 418
Exhibit S5 Volume I: paragraph 303

In a letter dated February 13, 1996, Felderhof wrote to the D.O.M.E.:

> We are pleased to confirm that Bre-X Minerals Ltd. of Alberta, Canada through its 100% owned subsidiary Montague Pacific NL of Perth, Australia is presently the ultimate parent company of Westralian Resource Project Ltd. of Sydney, Australia, which is the registered foreign holder of 80% or 800,000 shares in PT. Westralian Atan Minerals (the "Company").

Exhibit 1044: Tab 1017

Sharwood testified that the statement that Bre-X through MPNL was the "*ultimate parent company*" of WRPL was "*not correct*":

> MR. SHARWOOD: The statement is not correct because at that time Montague Pacific was not the holding company of W.R.P.L. W.R.P.L. was held 100% by Waverley Mining Finance.
>
> MR. MARROCCO: So is it correct that Bre-X owned –that Montague Pacific at this point in time, February 13th, '96, was a 100% owned subsidiary of Bre-X.
>
> MR. SHARWOOD: Yes. As indicated in the charts we looked at earlier, Bre-X through Bre-X Amsterdam had acquired Montague Pacific in July, 1995.
>
> MR. MARROCCO: And the part of it that is false is the assertion then, is it the assertion that Montague Pacific is the ultimate parent of W.R.P.L.?
>
> MR. SHARWOOD: Correct.

Transcript: May 2, 2005, page 97

The Defence concedes that MPNL was not the ultimate parent company of WRPL:

> MR. RICHTER: Now, in that first paragraph, by the date of this letter, Bre-X had acquired 100 percent of Montague Pacific. It was not at that time the ultimate parent company of WRPL.
>
> ...
>
> The issue, as I understand it, is that at the time as it turned out, Montague Pacific was not the ultimate parent company of WRPL.
>
> Mr. Sharwood testified that by that day WRPL was out [sic] 100 percent owned by Waverley and not by Montague Pacific. And Waverley was Mr. McLucas' company. On the other hand, as Mr. Sharwood testified by the date of this letter Bre-X had acquired beneficial ownership of PT WAM. So while the details of the letter are incorrect, the effect of what the transactions that had occurred both before and after Bre-X got that option, the effect of the transaction was that Bre-X was the beneficial owner. So it's not totally off the mark. It's true that the

Indonesian Government didn't recognize beneficial ownership, but the letter is not completely wrong with respect to Bre-X having the 80% interest in PT WAM.

Transcript: August 23, 2006, pages 38-39

Evidence That Indonesian Government Misled

The Defence submits that by failing to call any witnesses from the Indonesian Department of Mines to testify that they were misled, the O.S.C. has failed to prove beyond a reasonable doubt that the Indonesian government was misled.

Exhibit S12: paragraph 52
Exhibit S5 Volume I: paragraph 301
Transcript: August 23, 2006, pages 54-56, 81

The O.S.C. submits it was not necessary for the O.S.C. to call a witness from the Indonesian government to testify they were misled.

Transcript: August 30, 2006, pages 26-27

FINDING

There is no direct evidence that the Indonesian government was misled.

"*Mislead*" is defined in the Canadian Oxford Dictionary as follows:

> **Mislead**: "*cause (a person) to have a wrong idea or impression about something.*"

The statement to the Indonesian Government that Bre-X through MPNL was the ultimate parent company of WRPL was not correct. It was misleading.

The only logical inference is that the recipient of a statement that is not correct or wrong will "*have a wrong idea or impression*" that Bre-X through MPNL was the ultimate parent company of WRPL, which was the registered owner of 80% of PT WAM. It was not necessary to call a witness from the D.O.M.E. to say the Indonesian government was misled.

The O.S.C. has proven Particular 2 subject to issues of Felderhof's knowledge, whether the fact is material, general disclosure, and defences of due diligence.

Materiality

Materiality will be discussed again later in this judgement in the context of analyzing Dr. Juneja's evidence. The following evidence of and submissions with respect to Ridwan, Goin and Sharwood also touches on materiality. It also touches on whether Felderhof had knowledge that Bre-X mislead the Indonesian government as opposed to knowledge that a letter was set to the Indonesian government which turned out to have incorrect information.

Ridwan Mahmud (Pak Ridwan)

Pak Ridwan testified on behalf of the Defence as an expert witness and as a fact witness. Ridwan was a former senior official with the Indonesian Department of Mines and Energy. The O.S.C. consented to Ridwan being qualified as an expert witness in practices and procedures of the D.O.M.E. and as an expert in Indonesian mining law subject to cross examination to determine the weight to be given his evidence.

Ridwan received a Bachelor of Science in mining engineering in 1958 from Queen's University, in Kingston, Ontario. He received a Master of Mining Engineering in 1959 from the Institute of Technology in Bandung, Indonesia. In 1970 he received a Bachelor of Economics from the University of Indonesia. Ridwan's curriculum vitae is Exhibit 1256.

Exhibit 1256
Exhibit S12: paragraph 53
Exhibit S5 Volume I: paragraph 310
Transcript: November 28, 2005, pages 1-13

Ridwan testified there was no penalty for not notifying the D.O.M.E. of an offshore transaction. A letter notifying the D.O.M.E. of such a transaction would be referred to as a courtesy letter. Ridwan described the February 13, 1996 letter to the D.O.M.E. above as a courtesy letter.

Exhibit 1044: Tab 1017
Exhibit S12: paragraph 50
Transcript: November 28, 2005, pages 96-100

On cross-examination Ridwan agreed that the D.O.M.E. would be concerned if it received a false letter.

Exhibit S5 Volume I: paragraph 311
Transcript: November 29, 2005, page 117

If there were mistakes in the letter the D.O.M.E. would call the company or ask a company representative to attend to explain and correct the mistake. If the mistake was considered serious the D.O.M.E. could issue a warning letter requiring the mistake to be corrected within 180 days.

Exhibit S12: paragraph 56

Transcript: November 28, 2005, pages 96-100

Although Ridwan described the February 13, 1996 letter as a courtesy letter there is evidence the D.O.M.E. requested this letter. In Exhibit 418 discussed above, de Guzman referred to the letter as a critical item requiring immediate action by way of an official letter to the D.O.M.E. In Exhibit 419 and Exhibit 1044, Tab 1022, Felderhof states the matter is urgent.

Exhibit S12: paragraph 56
Exhibit 418
Exhibit 419
Exhibit 1044: tab 1022

Goin

Goin testified:

> MR. GOIN: If I understand the question correctly, it's whether statements which were not deliberately false but may have been incorrect, whether that would have necessarily resulted in cancellation of a license. I think the answer is "No". As it's stated here, it's within the discretion of the Government office and the reaction that they would have to the nature of the falsehood.
>
> MR. RICHTER: Yes. And if I can put it this way, the scenario you were given by the O.S.C. is what I'll call the worst case scenario, which is that there was a deliberate attempt to mislead and conceal. I guess what my question was getting at is if it was not a deliberate attempt to mislead and conceal, but an inadvertent error made in good faith, presumably you wouldn't be any worse off than in the scenario where you were deliberately attempting to mislead and conceal. Is that a fair statement?
>
> MR. GOIN: It's a fair statement that you would not be in any worse position, but again, I think, regardless of the issue about whether it's deliberate or intentional, the issue for this is whether – what impact does that have on the regulator in terms

of the Department of Mines policy, not some abstract concept of whether it's correct or not.

As you could see from the amount of paperwork and the reports that are required, the Department of Mines relies on the truthfulness of the contractors.

MR. RICHTER: Yes.

MR. GOIN: And so they may be somewhat surprised to find out that somebody is not, or has not been reporting truthfully.

But again, as this dealt with issues regarding ownership and offshore transfers were not considered to be unlawful, that's an area where certainly the Department of Mines would have discretion.

MR. RICHTER: Yes. And if Bre-X discovered that an error had been made in communication with the Department of Mines, I assume that that's something that could be corrected with the Department of Mines.

MR. GOIN: I mean that would be our recommendation that they do correct it. Whether it could be corrected, that would depend on the Department of Mines.

Transcript: July 25, 2005, pages 35-36
Exhibit S5 Volume I: paragraphs 307- 308

Goin Conference Call With O.S.C. On April 21, 1999

There was a conference call between Goin and the O.S.C. on April 21, 1999. Goin's memo to file with respect to that call, Exhibit 1015 dated April 23, 1999, states the following:

2. False statements: Assume a company submitted incorrect statements in applications for a license. Would such activity constitute a criminal activity? Further research would be needed to determine whether such activity constitutes a criminal act under the criminal code, but there may be some criminal sanctions under the 1934 company regulation. The principal legal affect of submitting false statements is that the government agency would have grounds to deny or to revoke [t]he request for a license.

The hypothetical was presented that a company submitted false applications on the manner in which it acquired an interest in an existing contract of work. The purpose of the false statement was to conceal the fact that the foreign investor did

not get the necessary approvals to transfer the interest in the contract of work. The question was whether false statements of this type would be grounds to revoke or deny an application. I replied that it may be entirely in the discretion of the government agency. If the government agency is satisfied with the identity of the foreign investor (e.g. capability, etc.), the mere fact of a false statement of this type may not result in revocation of the license.

Exhibit 1015
Exhibit S12: paragraphs 64-65

The August 14, 1996 Bre-X Letter To D.O.M.E.

Bre-X sent a letter to the D.O.M.E. on August 14, 1996 signed by Felderhof in response to a telephone call from an employee of the D.O.M.E., Nurselah Adiwanata. The letter was prepared by Sharwood's office.

Exhibit 79
Exhibit S12: paragraphs 57-59

The O.S.C. position is that the August letter is not relevant and that it is not relying on the August letter as part of Particular 2. The O.S.C. is relying on the February 13, 1996 letter only to prove the allegation in Particular 2 that Bre-X misled the Indonesian government respecting the acquisition of an 80% interest in PT WAM.

Exhibit S12: paragraphs 57-61
Transcript: August 30, 2006, page 25

The Defence is relying on the August letter as being a clarification of the February letter.

Exhibit S12: paragraph 61

Ridwan testified the August letter clarified the February letter.

Transcript: November 28, 2005, page 98
Exhibit S12: paragraph 61

Goin testified any error in the February letter could be corrected. He testified the August letter provided updating information and that it would be an appropriate way to correct information.

Transcript: July 25, 2005, pages 28-41
Exhibit S12: paragraph 61

Sharwood's evidence was that to the best of his knowledge the February 1996 letter was never corrected.

Transcript: May 10, 2005
Exhibit S5: paragraph 309
Exhibit S12: paragraph 56

The August letter drafted by Sharwood's office and reviewed by Sharwood repeats the statement in the February letter that Bre-X was the ultimate parent company of WRPL. That statement was not correct at the time of the February letter but by the time of the August letter, as the letter sets out, the McLucas transaction had been completed transferring all of the issued shares in WRPL to Bre-X making Bre-X in fact the ultimate parent company of WRPL.

The August letter also "*reiterated... that Bre-X has at all relevant times since July 1993 been beneficially entitled to all of the issued share capital of MPNL and WRPL and, thereby, to the control and ownership of the shares [of PT.WAM]*".

Exhibit 79
Exhibit 1044: tab 1017

FELDERHOF'S KNOWLEDGE

Counts 1 to 4 require the O.S.C. to prove beyond a reasonable doubt that Felderhof sold Bre-X shares "*with knowledge of a material fact.*"

With respect to Particular 2 the O.S.C. must prove beyond a reasonable doubt that Felderhof sold Bre-X shares "*with knowledge of [the] material fact*" "*that Bre-X had misled the Indonesian government respecting the acquisition of an 80% interest in PT WAM.*"

Knowledge is an integral part of the actus reus of insider trading charges and must be proved by the O.S.C. beyond a reasonable doubt. Given the wording of Particular 2 it is not sufficient for the O.S.C. to prove that Felderhof knew that Bre-X sent a letter to the Indonesian government (Felderhof signed the letter) and to prove that the letter contained misleading information (Sharwood testified it was not correct). The O.S.C. must prove beyond a reasonable doubt that Felderhof knew that Bre-X misled the Indonesian government.

Felderhof Faxes To And From The Beckwith Group Of Companies

In and around the time of the February 13, 1996 letter from Felderhof to the D.O.M.E. there are two faxes from Felderhof to Kernaghan and a response from Hedderwick to Walsh, a copy of which was received by Felderhof dated February 12, 14 and 16, 1996 respectively.

Exhibit 419
Exhibit 1044: tab 1022
Exhibit 1044: tab 1083

The February 12, 1996 fax from Felderhof to Kernaghan states:

> I am clearly at loss as to why it has taken 18 months to transfer the ownership. This is unbelievable. With regards to your fax to Greg MacDonald dated 30 January 1996, I fail to understand what tax implications has to do with Bre-X's request that you state that Bre-X is the legitimate owner. Please not that in the option agreement the purchase price was US$ 80,000 which consisted of US$ 40,000 direct payment to Montaque and US$ 40,000 in outstanding land taxes payable to the Indonesian Department of Mines. Also that there were no outstanding liabilities. Unfortunately we have paid a number of these e.g. $20,000 for outstanding taxes in Montaque Pacific Australia and US$ 120,000 on outstanding provincial taxes. Now it turns out that Montaque Pacific is not the real owner. Quite frankly, my mind boggles and my board of directors are on my back.
>
> Four our audit and Indonesian Mines Department we require a letter from Montaque that Bre-X through Montaque Pacific is the legitimate owner of Westralian Resource Projects Limited which in turn holds the foreign shareholding in the PT. Westralian Maura Atan concession. It would be appreciated if you could formulate such a letter as soon as possible as time if [sic] running out.

Exhibit 419

The February 14, 1996 fax from Felderhof to Kernaghan states:

> Please see attached to Mines Department stating that we are legitimate owners of PT. WAM. They will require as a back up a formal letter from Montague as per my fax dated 12 February 1996 on this subject. This matter is URGENT.

Exhibit 1044: tab 1022

The February 16, 1996 fax from Hedderwick to Walsh states (also discussed above at page 481 of these reasons):

> As you will know from various faxes, I am working with Montague Gold NL to establish the best means to conclude the transfer. We are slightly hampered by our lack of understanding of the problem which has not been fully explained. John Felderhof's fax of 12 February does not make much sense to us, and the manner is totally unnecessary bearing in mind your fax to me of 5 December.
>
> David, we have a concern about what you, or Bre-X, were told in 1993 that made you so excited about Busang compared to what we were told at the same time by the same person who was then being paid by Montague, particularly in view of

the fact that Montague Gold NL and its controlling shareholder, Waverley Mining Finance plc had ample funds available at that time.

Exhibit 1044: tab 1038

O.S.C. Position

With respect to the February 12, 1996 fax specifically but also generally with respect to the other correspondence the O.S.C. states at paragraph 304 of Exhibit S5 Volume I:

> Para. 304 On February 12, 1996, Felderhof sent Kernaghan a fax that acknowledged that MPNL did not own the shares of WRPL. Despite this acknowledgment, Felderhof asked Kernaghan to send a letter from MPNL to the DOME and Bre-X auditors telling them that Bre-X, through MPNL, owned an 80% interest in PT WAM, which was untrue.
>
> ...
>
> **There are a number of minor errors in this quote. The Defence does not agree that Mr. Felderhof acknowledges that MPNL did not own the shares in PT WAM. An innocent interpretation of this letter is that Mr. Felderhof is responding to an assertion that MPNL is not the owner. By essentially repeating the assertion "Now it turns out Montague Pacific is not the real owner", the letter shows surprise at the assertion, not acceptance of it. The second paragraph of the letter confirms that Mr. Felderhof believed that MPNL owned the shares and he wanted Mr. Kernaghan to confirm his belief.**

Exhibit S5 Volume I: paragraph 304

In oral submission the O.S.C. stated:

> On February 12th, Mr. Felderhof sent Wayne Kernaghan a fax that acknowledged that MPNL did not own shares in WRPL. And despite this acknowledgment, Mr. Felderhof asked Kernaghan to send a letter from MPNL to the Department of Mines and to Bre-X auditors, telling them that Bre-X, through MPNL, owns that 80% interest in PT WAM, which was untrue.
>
> ...
>
> But I think that this is really quite straightforward. Mr. Felderhof writes to the Department of Mines and gives them information that he knows to be false, and

the next day he writes to Kernaghan and essentially asks him to back him up in this falsehood.

I think what's important here is that Mr. Felderhof knows this is false information. I would go even further and say that he actually knows that it's material. And we don't have to prove that, we just have to prove he's in possession of information. But I would say that this is evidence of wilful blindness, that he knew this information was material, and I suggest that to you because of the absolute importance of the relationship with the relationship with the Department of Mines. The Department of Mines has asked for this information and I suggest that it's exactly what I just suggested to you a minute ago, that they want to know who they're dealing with. They want to know who the foreign interest is.

I'm going to suggest that Mr. Felderhof knew that what he told the Mines had to be accurate and it had to be substantiated. And that's why he kept writing Kernaghan saying, "Send me a letter. I need back-up. This is important. It's urgent." I'm going to suggest that Mr. Felderhof knew that it wasn't good enough to tell the Department of Mines "The paperwork's messy. We haven't figured it out yet."

I'm going to suggest, Your Honour, that the relationship with the Department of Mines was absolutely critical, again coming back to one of our two important facts, Busang was the only significant asset that they had.

The Department of Mines is in a position where they have complete discretion over whether Bre-X will be granted a COW.

Transcript: August 30, 2006, pages 24-26

Defence Position

With respect to paragraph 304 of Exhibit S5 Volume I and the February 12, 1996 fax the

Defence comments:

> **The Defence does not agree that Mr. Felderhof acknowledges that MPNL did not own the shares in PT WAM. An innocent interpretation of this letter is that Mr. Felderhof is responding to an assertion that MPNL is not the owner. By essentially repeating the assertion "Now it turns out Montague Pacific is not the real owner", the letter shows surprise at the assertion, not acceptance of it. The second paragraph of the letter confirms that Mr. Felderhof believed that MPNL owned the shares and he wanted Mr. Kernaghan to confirm his belief.**

Exhibit S5 Volume I: paragraph 304

And with respect to the February 16, 1996 fax the Defence comments:

> **The Defence agrees that Mr. Felderhof received a copy of this letter. This letter is indicative of Mr. McLucas' nuisance claim. Based on Mr. Francisco's conclusions in May 1996, the truthfulness of this letter is questionable.**

Exhibit S5 Volume I: paragraph 306

As noted above in the discussion of Particular 1, in Francisco's opinion McLucas' claim was a "*nuisance*", "*false*" and not a material fact. Francisco agreed with Felderhof that the claim was "*bogus*".

In their oral submissions the Defence states there are two ways to interpret the letters of February 12, 13 and 14, 2006: the sinister O.S.C. interpretation and an innocent interpretation:

> And in my submissions, there's another interpretation which I'll call the innocent interpretation. It goes something like this: Start with the February 12th letter from Mr. Felderhof to Mr. Kernaghan. It goes something like this: "Dear Wayne, can't believe it's taken you 18 months to finish transferring this ownership. Your records are a mess and I wish you would get your act together. We've paid all this money, now you're telling us that Montague Pacific doesn't own the PT WAM shares. Since you told us when we bought Montague Pacific that they did own the PT WAM shares, you'll forgive us if we're a little skeptical. Based on what we've been ale [sic] to figure out, we think the Montague Pacific owns WRPL which owns the PT WAM shares and please confirm for our auditor and the Department of Mines that that's correct."
> The on February 13th Mr. Felderhof writes a letter to the Department of Mines and he says:
>
> > "We are pleased to confirm that Bre-X...through its 100% owned subsidiary Montague Pacific...is presently the ultimate parent company of WRPL..."

> Which holds the PT WAares [sic]. And the words "is presently" are there to indicate that that's what we believe at the moment. "This situation is fluid, the situation is a mess, and if it turns out that that's wrong, we'll send you another letter, we'll let you know, but that's what we think right now."
> And then on the 16th [sic] he sends a letter to Mr. Kernaghan reminding him that he would like to have this letter confirming what they believe and what they've told to the Department of Mines.
> So there are two interpretations. And in my submission, there's no reason to conclude this letter was sent with deliberate intention of misleading the Department of Mines. You have Mr. Sharwood's evidence about what an absolute mess these records were and Mr. Sharwood is a very experienced, very capable lawyer dealing with Australian corporate mining and securities law. He spent an extensive amount of time reviewing all of these documents and records and agreed the documents were a mess. He wasn't able to reach any absolutely firm conclusions, although he did reach conclusions which are set out in his report. And in my submission, it's being a little unkind to Mr. Felderhof, the geologist, to suggest that he should have known and understood all of this stuff, he should have done what really only a lawyer could do, which was all of that corporate due diligence that Bre-X paid Mr. Sharwood to do, and that he should have reached the conclusions that Mr. Sharwood reached after the extensive work that he and his firm did. And that work, you may recall, hadn't been done yet by February because Mr. Sharwood hadn't been retained yet, work hadn't been started.

Transcript: August 23, 2006, pages 44-46
Exhibit S12: paragraph 55

With respect to Felderhof's knowledge and the O.S.C.'s burden the Defence submits:

> The final point with respect to this particular –well, first let me deal with the issue of Mr. Felderhof's knowledge. The O.S.C. has to prove beyond a reasonable doubt part of its case that Mr. Felderhof had knowledge of the alleged material fact which is that he, or that Bre-X had misled the Department of Mines. That requires the O.S.C. to prove not only that Mr. Felderhof – he obviously knew he sent the letter or signed them –has to prove not only that he knew the letter was misleading, but also that he knew that the Department of Mines had been misled, based on the wording of that particular. It's my submission the O.S.C. has not provided evidence to establish that level of knowledge.
>
> And it gets back to my comment earlier this morning, that even Mr. Sharwood, after all his due diligence, said it was a mess. The records of KPMG were a mess.

Transcript: August 23, 2006, page 73

The Defence also point to Exhibit 888 (reproduced above at pages 480-481), a letter dated July 3, 1995 from Montague Gold signed by Hedderwick stating to PT WAM's auditing and accounting service:

> PT Westralian Atan Minerals (PT WAM) is 80% owned by MGP and thus is also ultimately controlled by Bre-X.

Exhibit 888

FINDING

I do not agree with the Defence submission that by stating that Bre-X through MPNL "*is presently*" the ultimate parent company of WRPL that that indicates a present belief that, if wrong, can simply be corrected in a future letter. The letter to the D.O.M.E. is a statement that Bre-X through MPNL is the "*ultimate parent company*" of WRPL. It is not a conditional statement.

On the other hand there is evidence raising a reasonable doubt with respect to the O.S.C. submission that Felderhof knew Bre-X had misled the Indonesian government.

In Exhibit 888 dated July 3, 1995 Hedderwick stated PT WAM was ultimately controlled by Bre-X.

Felderhof's position in his faxes to Kernaghan on February 12 and 14, 1996 (Exhibit 419 and Exhibit 1044 , Tab 1022) that Bre-X is the "*legitimate*" owner is also somewhat supported by Hedderwick's fax of February 16, 1996 (Exhibit 1044: Tab 1038) stating that *"[a]s you will know from various faxes, I am working with Montague Gold NL to establish the best means to conclude the transfer.*"

In the February 12, 1996 fax (Exhibit 419) Felderhof asks Kernaghan to state "*that Bre-X through Montague Pacific is the legitimate owner of Westralian Resource Projects Limited which in turn holds the foreign shareholding in the PT Westralian Maura Atan concession*".

Exhibit 419

In the February 14, 1996 (Exhibit 1044: Tab 1022) fax to Kernaghan Felderhof refers to the February 13, 1996 fax to the D.O.M.E. (Exhibit 1044: Tab 1017) and incorrectly states that that fax to the D.O.M.E. stated that Bre-X was the "*legitimate*" owners of PT WAM. Felderhof did not differentiate between being the "*ultimate parent company*" (Exhibit 1044: tab 1017) which is not correct and being the "*legitimate*" owner or beneficial holder which was true.

Exhibit 1044: Tab 1022
Exhibit 1044: Tab 1017

In Sharwood's opinion (Exhibit 858, Exhibit 79) Bre-X through MPNL was the beneficial holder of 80% of the issued shares of PT WAM. This is not dissimilar to Felderhof's statements in Exhibit 419 and Exhibit 1044, Tab 1022 that Bre-X is the "*legitimate*" owner of WRPL/PT WAM.

It is not that Felderhof should benefit from being wrong and imprecise in his various statements but these statements by and to Felderhof about the status of the Bre-X acquisition of an 80% interest in PT WAM are relevant to whether the O.S.C. has proven beyond a reasonable doubt that Felderhof had knowledge that Bre-X had "misled" the Indonesian government.

The letter to the D.O.M.E. was signed by Felderhof and de Guzman but prepared, it appears from Exhibit 418, by Greg MacDonald with Mike Bird's assistance (as needed). Given the correspondence received by Felderhof and Bre-X from the Beckwith group of companies referred to above, and Felderhof's stated belief that Bre-X was the "*legitimate*" owner through MPNL of WRPL which owned 80% of PT WAM, and the transactions discussed above in Particular 1 where Bre-X in fact had a beneficial interest in PT WAM, the O.S.C. has not proven beyond a reasonable doubt that Felderhof knew that Bre-X had misled the Indonesian government. Felderhof had knowledge that Bre-X sent the February 13, 1996 letter to the Indonesian government. There was evidence the letter contained information that was not correct. But there is a reasonable doubt Felderhof knew the Indonesian government was misled because there is a reasonable doubt that Felderhof believed Bre-X was the legitimate owner of PT WAM and therefore was not misleading the Indonesian government.

Exhibit 418
Exhibit 888
Exhibit 1044: tab 1038
Exhibit 858: page 24
Exhibit 79

Particular 3: That Bre-X Had Unjustly Excluded PT KG, And/Or PT SAP, And/Or Jusuf Merukh, From Obtaining An Interest In The Property Known As Busang II

Merukh Not Included In Bre-X Busang II Cow Application

The Defence concedes that Jusuf Merukh was not included in Bre-X's application for a COW over Busang II. The issue is whether the exclusion was unjust.

Exhibit S5 Volume I: paragraphs 314- 315

The Defence also concedes that Merukh was not included in the steps leading up to the COW application.

The Defence agrees with the following O.S.C. submissions:

> Para. 334. A KP is a mining authorization only available to Indonesians.
>
> **The Defence agrees.**
>
> Para. 335. On February 2, 1994, Ahmad Yani, Director of CV Sri Rahayu, submitted an application to the DOME for three general survey KPs. Yani was Syakerani's son.
>
> **The Defence agrees. The OSC has failed to mention that Mr. Felderhof had previously explored the area covered by Busang I and II while working with Jason Mining in the 1980's. (See paragraphs 82 and 83 of the Written Closing Argument of the Defence)**
>
> Para. 336. On February 6, 1995, the DOME granted three general survey KPs to CV Sri Rahayu.
>
> **The Defence agrees.**
>
> ...
>
> **c) Bre-X and CV Sri Rahayu entered into a JVA on June 7, 1994 without Merukh**
>
> Para. 344. On June 7, 1994, Bre-X entered into a JVA with CV Sri Rahayu to develop the mining rights in the mineral resources in Busang II. Syakerani, a Director of CV Sri Rahayu and Felderhof for Bre-X signed the JVA.
>
> **The Defence agrees.**
>
> Para. 345. The JVA described the mining rights as three KP applications in process owned by CV Sri Rahayu. Bre-X had a 90% participating interest and CV Sri Rahayu had a 10% participating interest.
>
> **The Defence agrees.**
>
> **(d) Bre-X and PT Askatindo Karya Mineral entered into a JVA on September 10, 1994 without Merukh**

Para. 346. On September 10, 1994, Bre-X entered into a JVA with PT AKM to develop the mineral resources in the mining rights in Busang II.

The Defence agrees.

Para. 347. The JVA described the mining rights as those permitted under a general survey and an exploration KP. Yani signed the JVA as Director of PT AKM and Felderhof signed on behalf of Bre-X.

The Defence agrees that the "Mining Rights" were defined to include the general survey KPs and exploration KPs listed in the schedule and any other KP's applied for.

Para. 348. Of the eight general survey KPs held by PT AKM, five did not proceed. The mining rights in the remaining three general survey KPs were issued as DU1626, DU1627 and DU1628.

The Defence agrees.

Para. 349. On February 6, 1995, the DOME granted three general survey KPs for Busang II to Yani/CV Sri Rahayu: DU1626, DU1627 and DU1628.

The Defence agrees. PT AKM had taken over the application of CV Sri Rahayu.

Para. 350. Bre-X had a 90% interest and PT AKM had a 10% interest in these three general survey KPs.

The Defence agrees that Bre-X held a 90% interest in the joint venture and PT AKM held a 10% interest in the joint venture.

(e) Bre-X and PT AKM applied for a COW over Busang II without Merukh

Para. 351. On September 14, 1994, Bre-X and PT AKM applied for a COW over Busang II. Merukh was excluded from this application.

The Defence agrees that Mr. Merukh was not included in this COW application.

Para. 352. On March 17, 1995, the DOME approved in principle the Busang II COW application.

The Defence agrees.

Para. 353. The DOME subsequently initialled the draft COW.

The Defence agrees. This occurred in March 1996. (Exhibit 6, Tab 96(8), Bre-X Press Release dated March 28, 1996)

Exhibit S5 Volume I: paragraphs 334-336, 344-353

Goin

In Exhibit 1001 Goin states:

> Para. 128 (c). During a two month field exploration and mapping effort in August and September, 1993, employees of Bre-X (or acting under Bre-X's directions) working pursuant to the WAM Contract of Work collected promising samples from an area identified as the "New Prospect Area" which the reports indicated was outside the current COW area;
>
> (d). These reports prepared in October, 1993, recommended that the Contract of Work Area for WAM be extended to cover this new area (Tab 40), but due to licensing problems at WAM (Tab 41), consideration was given to alternatively obtaining KP's for this additional area;
>
> ...
>
> Para. 129. As provided in Section 6 of the Joint Venture Agreement, all survey and exploration information was to be owned by WAM. Section 6 only refers to information "in respect of the area subject of the KP", and one might argue that Busang II was outside this area. Nevertheless, the information was developed for WAM. Under general principles of law, WAM would own the rights to that information, even if the information was outside of the WAM Contract of Work Area.
>
> Para. 130. The use by one shareholder, manager or director of the survey and exploration information developed by or on behalf of WAM and its agents, raises significant legal questions under the Joint Venture Agreement and general principles of tort law, as well as the risk (which eventually came to pass) that the licensing process may be complicated by complaints submitted by the excluded shareholders of WAM.
>
> ...
>
> Para. 134. The exploitation of information developed by WAM for purposes which benefit only some, but not all, shareholders of WAM would not, in our view, be in good faith in that it did not reflect the collective rights of all shareholders to the benefits of the information. Evidence of affirmative bad faith is clear from Mr. Felderhof's June 21, 1994 facsimile to Mr. David Walsh (Tab 55) discussing the advantages to the new COW applications:
>
> "...we will have 90% instead of 80%"
>
> "...getting rid of a potential unsuitable Indonesian partner Jusuf Merukh."

In chief Goin testified:

MR. MARROCCO: So just in terms of the exclusion of Mr. Merukh, how did you analyze that particular issue?

MR. GOIN: The report summarizes some of the relevant facts, which would indicate that there may be issues regarding good faith, and that's contained at paragraph 128.

MR. MARROCCO: Just briefly, what are those issues in paragraph 128?

MR. GOIN: That both Mr. de Guzman and Mr. Felderhof were acting, at various times, initially before Bre-X was involved, but later after Bre-X was involved, on behalf of PT WAM in connection with submitting reports to the Government, or taking other action on behalf of PT WAM, that it appears as a result of a work program that was approved by the individuals and undertaken by Mr. Umar Olii, the identified information, which was attributed in the assay report to PT WAM, and that Mr. Felderhof and Mr. Umar Olii were also appointed by Westralian, the shareholder in PT WAM, that the parties involved recognized that at least – or suggested that one way to deal with this new information was to expand the Contract of Work area and in fact, that was an issue under consideration for a period of months it appears, until at least June of 1995, at which time it was decided to proceed with a separate Contract of Work, which would not include Mr. Merukh or the Indonesian shareholder of PT WAM, PT Krueng Gasui.

The issue there is where PT WAM has a proprietary information which is being used by one of the shareholders or by one of its agents or sub-agents, significant questions arise as to whether the person utilizing that information without offering it to PT WAM would be acting in good faith.

Transcript: July 20, 2005, pages 45-46
Exhibit S12: paragraph 86

Goin was cross-examined with respect to paragraph 134:

MR. RICHTER: ...Is that opinion that you expressed there based on your understanding that Bre-X applied for the Busang II and III Contracts of Work based on the 53 samples taken by Umar Olii in 1993?

MR. GOIN: It is based on the fact that PT WAM had acquired information in respect of the prospect known as the Southeast Zone or Busang II.

MR. RICHTER: Yes.

MR. GOIN: - and as such, the parties the PT WAM joint venture would not be able to go into that area without offering it to their other partners because they would be using that information obtained.

Transcript: July 26, 2005, pages 98-99
Exhibit S12: paragraph 87

O.S.C. Position

The O.S.C. position is that confidential proprietary exploration information developed by PT WAM, in particular 53 promising samples collected during the field exploration and mapping program in August and September 1993 from a "*New Prospect Area*" located within Busang II, was used by Bre-X to benefit itself by obtaining an interest in Busang II through it's COW application over Busang II, while excluding Merukh in breach of Bre-X's duty of good faith owed Merukh as another PT WAM shareholder.

"NEW PROSPECT AREA"

Evidence In Support Of The O.S.C. Position

The O.S.C. relies on Goin's opinion. Goin's opinion was based in part on some documentation which was not admitted as evidence in the trial.

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Exhibit S12: paragraph 78

I find the following admitted evidence to be sufficient to form the necessary basis for Goin's opinion.

On July 20, 1993 Bre-X purchased the one-year option, discussed earlier in my reasons with respect to Particular 1, for 80% of the shares of PT WAM.

Exhibit S5 Volume I: paragraph 269
Exhibit 830

In paragraphs 321-332 the O.S.C. sets out the evidence of what occurred in and around and after the July 1993 option agreement relevant to the O.S.C. allegation that Bre-X

improperly used PT WAM information. Those paragraphs with the Defence comments are reproduced below:

(b) Bre-X used confidential PT WAM information and resources to confirm mineralization in the SEZ

Para. 320. On July 18, 1993, Felderhof told Walsh that he had met with de Guzman and Umar Olii, Bre-X Senior Exploration Geologist, to discuss the work plan for Muara Atan COW, which was to start on August 1, 1993.

The Defence does not agree that Mr. Olii was a "Bre-X Senior Geologist".

Para. 321. On July 19, 1993, Bre-X issued a press release disclosing a two-month field program of detailed geological mapping and sampling to be conducted under Felderhof's supervision.

> With a funding recently completed, **a two month field program will commence August 1, 1993**, consisting of a detailed geological mapping and sampling followed by a 1,000m (metres) diamond drill program with the objective of delineating the potential of Busang, which is believed to contain an open pittable resource of 20 million tonnes @ +2gm/tonne gold (1,000,000 ounces of gold).
>
> **BRE-X will be operator of all its mineral exploration and development in Indonesia under the supervision of BRE-X's General Manager – Indonesia Operations, John B. Felderhof, P. Geol.**
>
> John Felderhof is credited as co-discoverer of the large Ok Tedi copper-gold mine in Papua New Guinea, and the discoverer of four mineral properties in Indonesia of which one is in production, two scheduled to go into production, and one at the feasibility stage. **With thirteen years of experience in the country, he has assembled an experienced team of three senior geologists with extensive experience in Indonesia and the Philippines to join the BRE-X exploration forces**. [emphasis added]

The Defence agrees that these quotes are accurate except that portions of the press release are left out between the first and second quoted paragraphs. The portion left out refers to an additional Bre-X project in Indonesia.

Para. 322. On August 3, 1993, Bre-X issued a press release disclosing that it was doing further mapping and sampling at Busang.

> The Muara Atan contract area encompasses 57,571 hectares with three prime prospects identified. The most advanced is the Busang prospect where work commenced August 1 1993. This will consist of further mapping and sampling to set up a 1,000m diamond drill program to establish drill indicated reserves. Prior work on this property, including 19 holes totalling 1,200m of drilling, indicated a geological potential, open pittable resource of 20 million tonnes at +2 gm/t. Bre-X Minerals will be operator.

The Defence agrees that this is an accurate quote from the press release.

Para. 323. On August 24, 1993, Umar Olii sent John Irvin, Manager, Indo Assay Labs, 53 rock samples.

> Herewith I am sending you a batch of 53 rock samples.

The Defence agrees.

Para. 324. On August 26, 1993, Felderhof thanked Umar Olii for his detailed fax and asked him when the assay results would be ready for Muara Atan (Busang I).

> *(1) Thank you for you detailed fax.*
>
> . . .
>
> *(5) When will assay results become available?*

The Defence agrees that this is an accurate partial quote. The subject of the fax is stated to be "Muara Atan". The fax does not state that the assay results are related to Busang I.

Para. 325. On September 6, 1993, IAL issued an assay certificate to Felderhof, PTWAM for 53 rock chips. The samples were identified in the assay certificate as BS00032 to BS00084 (total 53 samples).

The Defence agrees.

Para. 326. On September 9, 1993, Felderhof asked de Guzman and Tommy Olii, Bre-X Logistics Manager, when the results for the 53 channel samples would be available.

> *(2) When will results be available for the 53 channel samples?*
>
> . . .

Best Regards,
John

The Defence agrees that Tommy Olii was a "logistics manager", but not necessarily the "Bre-X Logistics Manager". The Defence agrees that this is an accurate partial quote from Mr. Felderhof's fax.

Para. 327. In October 1993, Umar Olii and Zufrein, Bre-X Senior Exploration Geologist, reported their August 1993 work in a report called "*Re Interpretation on the Geology and Gold Mineralization of Busang [P]rospect, Muara Atan COW.*"

> This progress report is prepared after a **one month detail geological mapping at Busang Prospect of Muara Atan COW in East Kalimantan.**
>
> The Busang prospect has been investigated by PT. Westralian Atan Minerals (WAM) which includes:
>
> - Rivers and creek traverses by tape and compass method for base maps.
> - Soil sampling along the ridges and spurs.
> - Brief geological mapping and
> - Drilling program of a total of 19 holes with total metrage of 1487.5 m.
>
> In 1992 Mike de Guzman visited the area and recognized that the area is still potential for exploration targets for gold deposits.
>
> **In July 1993 Bre-X Minerals of Canada, took the option on the Muara Atan COW and conducted detail geological mapping at 1:2,500 in Busang area as of August 1993.** [emphasis added]

The Defence agrees that there is a report prepared by Mr. Olii and Mr. Zuffrein. The Defence does not agree that either of these individuals were employees of Bre-X. The report does not indicate that it is a Bre-X report. There is no evidence as to when, or if, Mr. Felderhof received this report.

Para. 328. The objectives of the detailed geological mapping included:

> - To provide detailed surface geologic map of the prospect to be correlated to the existed drill holes information.
>
> - To give more understanding on the local geology of the area for drill targets interpretation.

- **To find new prospective area.** [emphasis added]

The Defence agrees that this is an accurate quote from the report. Mr. Olii's objectives are not consistent with the evidence from Mr. Felderhof, which was that the objective was to position diamond drill holes on the Busang project. (Exhibit 1032, Tab 78)

Para. 329. Umar Olii and Zufrein reported the discovery of a new mineralized area outside the PT WAM COW. They called this the "new prospect area":

> **On the eastern tributaries of the Busang river an altered mineralized zone of approximately 600m x 700m, trending on NE direction was found, and this area is referred to as new prospect area. The sample assay results used for the analyses of the Hg-Au relationship are mainly collected from this area, which lies outside the current COW.** [emphasis added]

The Defence agrees that this is almost an accurate quote (the last line should read "which lies outside current COW"). The OSC has not lead evidence to establish where the samples were actually from, who collected the samples, who apparently concluded that they were outside the COW or how it was apparently determined that the samples were from outside the PT WAM COW area. Pak Ridwan testified that COW boundaries can be off by as much as several hundred metres. (Evidence of Pak Ridwan, November 28, 2005, Vol. 142, pages 104-107)

Para. 330. Umar Olii and Zufrein stated that channel samples from the new prospect area averaged 3.86 g/t gold.

> **...higher grade gold mineralization of more than 2 gr/t Au was picked up from the 5.5 m channel samples, averaging 3.86 gr/t Au...the new prospect area lies outside the current contract of work area.** [emphasis added]

The Defence agrees that this is an accurate quote. The OSC has not lead evidence to establish where the samples were actually from, who collected the samples, who apparently concluded that they were outside the COW or how it was apparently determined that the samples were from outside the PT WAM COW area. Pak Ridwan testified that COW boundaries can be off by as much as several hundred metres. (Evidence of Pak Ridwan, November 28, 2005, Vol. 142, pages 104-107)

Para. 331. Umar Olii and Zufrein recommended that Bre-X apply to extend the area covered by the PT WAM COW because the new mineralized area was outside the existing COW.

> **Extension of COW application to cover the new prospect area should be organized as soon as possible,**

> **because this area is located outside the existing COW area covered by other non active COW**, which is expected will be terminated by the government by the end of this year or early next year. [emphasis added]

The Defence agrees that this is an almost accurate quote from the report (the third line should read "located outside the existing COW area and covered by other non". The OSC has not lead evidence to establish that the "new prospect area" was actually outside the PT WAM COW, who apparently concluded that it was outside the COW or how it was apparently determined that it was outside the PT WAM COW area. Pak Ridwan testified that COW boundaries can be off by as much as several hundred metres. (Evidence of Pak Ridwan, November 28, 2005, Vol. 142, pages 104-107)

Para. 332. On October 27, 1993, Umar Olii reiterated his recommendation that Bre-X apply to extend the PT WAM COW that he made in the earlier October 1993 report, stating:

> The **application of the COW extension should be follow up as soon as possible**, considering the fact if the previous COW has been officially terminated this area will be free and any company may lodge their KP or COW application. [emphasis added]

The Defence agrees that this is an almost accurate quote from the report (the second line should read "considering the fact that if the previous COW". The OSC alleges that this recommendation was made to Bre-X, however, the report does not indicate who the report was prepared for. The OSC also alleges that Bre-X had no interest in PT WAM at all at this time. Mr. Olii does not appear to be involved with PT WAM or Bre-X in any way following this report. There is no evidence as to when, or if, Mr. Felderhof received this report.

Defence Position And The Defence Comments On O.S.C Position

A key issue in the Defence position is whether the evidence establishes that the "*new prospect area*" was in the Southeast Zone (Busang II) and led first to the three KPs over the Southeast Zone and eventually to Bre-X's COW application over the Southeast Zone. Below I discuss the Defence comments with respect to some of the O.S.C. submissions in the paragraphs reproduced above.

Paragraph 324

The Defence comments that the fax, Exhibit 1032, Tab 124, does not state that the assay results are related to Busang I but Olii's and Zuffrein's report of the August work refers to "*one month detail geological mapping at Busang Prospect of Maura Atan Cow*".

Exhibit S5 Volume I: paragraph 327
Exhibit 785

Also the Bre-X July 19, 1993 press release disclosing the two month field program refers to "*delineating the potential of Busang*".

Exhibit S5Volume I: paragraph 321
Exhibit 6

The Bre-X August 3, 1993 press release also refers to Busang and sampling.

Exhibit S5 Volume I: paragraph 322
Exhibit 6

Umar Olii who had commenced work at Busang on August 1, 1993 sent these 53 samples on August 24, 1993 to Indo Assay.

Exhibit S5 Volume I: paragraph 323
Exhibit 1108

On the evidence discussed above and below the 53 samples sent were from the "*new prospect area*" collected during Olii's work at Busang.

Exhibit S5 Volume I: paragraph 330
Exhibit 785

Paragraph 325

The Defence agrees with this paragraph. The September 6, 1993 IAL assay certificates for the 53 samples from the "*new prospect area*" list the client as:

"*CLIENT: PT Westralian Atan Minerals*

PROJECT:
REFRENCE: JB Felderhof 25/8/93"

This is more evidence that the exploration information was developed by PT WAM and was the property of PT WAM.

Exhibit 599

Paragraph 327

The Defence does not agree Olii and Zuffrein were employees of Bre-X.

Olii and Zuffrein were senior exploration geologists doing geological mapping of Busang.

Exhibit 785

The July 19, 1993 Bre-X press release reporting Bre-X's acquisition of an 80% working interest in PT WAM and announcing the two month field program at Busang I, set out that Bre-X's "*mineral exploration and development in Indonesian [would be] under the supervision of Bre-X's General Manager -Indonesian Operations, John B. Felderhof.*"

Exhibit 6

Olii and Zuffrein were working under the supervision of Felderhof.

The Defence submits in its comments to paragraph 327 and 332 that there is no evidence when or if Felderhof received this report.

As noted above work described in the report was done under the supervision of Felderhof.

Exhibit 1032, Tab 124 is an example of Felderhof's ongoing interest in the work, receiving detailed reports and asking about assay results.

Again in Exhibit 1032, Tab 138, Felderhof is asking about the assay results.

Exhibit 1032: Tab 124, Tab 138

Paragraph 328

The Defence comments that one of the objectives of the detailed geological mapping set out in Olii's report "*to find new prospective area*" was not consistent with Felderhof's July 18, 1999 fax to Walsh, Exhibit 1032, tab 78. The work done by Olii and Zuffrein was done under the supervision of Felderhof as noted above. Felderhof's supervision would first and foremost involve setting out the objectives.

In any event what is important is that as the report states that a "*new prospective area*" was found.

Paragraphs 329, 330 and 331

The Defence submission with respect to these paragraphs is that the O.S.C. has not lead evidence to establish that the "*new prospect area*" was actually outside the PT WAM.

The Defence also submits the O.S.C. did "*not lead evidence to establish where the samples were actually from, who collected the samples, who apparently concluded they*

were outside the COW or how it was apparently determined that the samples were from outside the PT WAM COW area."

Exhibit S5 Volume I: paragraphs 329-331
Exhibit S12: paragraphs 79-81, 87
Transcript: August 23, 2006, pages 93-105

COW Boundaries

The Defence points to the evidence of Ridwan and Goin to establish the difficulties of determining exact COW boundaries.

Ridwan

Ridwan testified that in 1993, prior to the use of G.P.S., COW boundaries were determined using "*quite a primitive method*" and could "*deviate several hundred meters*".

Transcript: November 28, 2005, pages 102-105
Exhibit S12: paragraph 81

Ridwan is not a senior exploration geologist as were Olii and Zuffrein.

Exhibit 785

Goin

Goin testified on cross-examination:

> MR. RICHTER: Okay. It's my understanding that standing in the middle of a jungle, it's actually very difficult to know where a boundary is located. Do you have any knowledge of that?
>
> MR. GOIN: I would expect that would be true.
>
> MR. RICHTER: Okay. Are you familiar with the surveying requirements in fixing the boundaries for a Contract of Work?
>
> MR. GOIN: No. Only to the extent that recently there's been a change of the method of surveying and now they're using a GSP system of measuring.

Transcript: July 26, 2005, page 104
Exhibit S12: paragraph 80

As a lawyer Goin has no real expertise in the area of COW boundaries.

Goin testified he relied on the conclusions in the original reports by Olii and Zuffrein concluding that the 53 samples were from outside the PT WAM area.

Transcript: July 26, 2005, pages 105-106
Exhibit S12: paragraph 79

Olii and Zuffrein

With respect to Olii's and Zuffrein's statement that the "*new prospect area*" was "*outside the existing COW Area and covered by other non active COW*," I find the following to be of importance. Olii and Zuffrein were senior exploration geologists with experience in Indonesia. The report refers to the use of maps and compasses. The objectives include mapping and finding new prospective areas. Olii and Zuffrein determined, the "*new prospect area*" was outside the existing COW. There was no apparent doubt in that conclusion. The conclusion was not conditional.

The fact the "*new prospect area*" was outside the PT WAM COW was a significant and not a casual matter and required action. In the recommendation section of the report, Olii and Zuffrein state "*Extension of COW application to cover the new prospect area should be organized as soon as possible because this area is located outside the existing COW area and covered by other non active COW, which is expected will be terminated by the government by the end of this year or early next year.*"

Olli and Zuffrein were not only aware that the new prospect area was outside the existing COW but had also determined that it was covered by another non-active COW.

Exhibit 1003: Tab 40
Exhibit 785
Transcript: August 30, 2006, page 39

FINDING

On the evidence, I find the "*new prospect area*" was outside the PT WAM COW area.

DID THE NEW PROSPECT AREA LEAD TO COW APPLICATION OVER BUSANG II

The second part of the enquiry is whether the exploration information from the "*new prospect area*" led to Bre-X's COW application over Busang II.

Jason Mining

The Defence position is that Bre-X's COW application over Busang II was not the result of Olii's and Zuffrein's exploration work in the "*new prospect area*" but the result of Felderhof's prior knowledge of the prospectivity of Busang II. The Defence position is set out in paragraphs 82 and 83 of Exhibit S12 and pages 106-117 of the transcript of August 23, 2006.

The Defence submits and the O.S.C. comments as follows in paragraphs 82-83:

> Para. 82. There was some evidence that Mr. Felderhof had previously explored the area that was covered by the Busang II COW application, and that he had independently recognized the prospectivity of the area long before Bre-X became involved in Busang I. Mr. Sharwood testified that at a meeting on July 29, 1996, at the Bre-X office in Jakarta, Mr. Felderhof told Mr. Sharwood that Mr. Felderhof had made an application for a COW over the Southeast Zone through a company called "Jason Mining", but that Mr. Felderhof had abandoned the

application because of a number of pre-existing KPs. Mr. Felderhof also told Mr. Sharwood at that meeting that the continuity between the Central Zone (in Busang I) and the Southeast Zone was established working backwards from the Southeast Zone to the Central Zone and not the other way around.

Evidence of Mr. Sharwood, Volume 107, page 84
Evidence of Mr. Sharwood, Volume 108, pages 99-100

The OSC denies this paragraph. Felderhof's statements are relevant for the purpose of establishing the information that Sharwood was given i.e. Sharwood's state of mind when he issued his report(s). Felderhof's statements are not admissible for the truth of the facts however because they are hearsay.

Para. 83. Mr. Felderhof's statements to Mr. Sharwood in 1996 are supported by the evidence in this trial. Exhibit 1007 is a copy of the "Proposed Contract of Work Area" for PT Atanindo Mas Perdana and Jason Lebong Padang Limited. This map was produced from Crown disclosure. A comparison of this map with the map marked as Exhibit 1006, setting out the PT WAM COW area, shows that the Jason proposed COW area included what became Block V of the PT WAM COW, as well as at least some of Busang II. Further, the quarterly report for Jason Mining Limited dated January 29, 1987 refers to a COW application over an area in Atan, East Kalimantan, and Mr. Felderhof wrote to Mr. Syakerani on or about January 31, 1986 (though the fax line suggests that the letter was faxed on February 3, 1987) stating that, among other things, Jason's COW application had been initialled that day.

Exhibit 1007, Map, P.T. Atanindo Mas Perdana and Jason Lebong Padang Limited
Exhibit 1006, Map, P.T. Westralian Atan Minerals
Exhibit 1199, Report by Jason Mining Limited entitled "Quarterly Report to December 31, 1986 to the Australian Associated Stock Exchange Under Section 3B(5) of the Listing Requirements", dated January 29, 1987
Exhibit 877, Letter dated January 31, 1986

The OSC denies this paragraph. The OSC admits these exhibits state what they state.

Exhibit S12: paragraphs 82-83
Transcript: August 23, 2006, page 110

I agree with the O.S.C. submission that Felderhof statements to Sharwood are hearsay and are not proof of the truth of the contents.

The maps, Jason's quarterly report and Felderhof's fax to Syakerani referred to in paragraph 83 of Exhibit S12 are evidence that Jason had proposed a COW over an area that included at least some of Busang II prior to the creation of PT WAM.
There is some evidence supporting Felderhof's statement to Sharwood that Felderhof recognized the prospectively of the area (Busang II) before PT WAM came into existence.
But In any event, even if there was information acquired previously which could have given an independent basis for applying for a COW over the Southeast Zone or Busang II, in Goin's opinion there would still be a duty of good faith if subsequent information was developed on behalf of PT WAM as occurred here with the 53 samples in the "*new prospect area*".

Goin testified:

> MR. RICHTER: Assume that Mr. Felderhof independently acquired information about the prospectivity of the area that fell within the Busang II and III Contract of Work applications, and that he acquired that information before PT WAM even came into existence, before any he had any involvement with PT WAM joint venture, I take it that that information that Mr. Felderhof had would not be the property of PT WAM.
>
> MR. GOIN: No, that is correct.
>
> MR. RICHTER: And so if that information were used by Bre-X or one of its companies to pursue a Contract of Work application over Busang II and III, that would not be exploitation of proprietary information belonging to PT WAM.

MR. GOIN: No. Although in analyzing the good faith duty, I think you have two distinct – different situations.

...

MR. GOIN: Now, assume that there were – that PT WAM did develop information on the Southeast Zone as a result of its work activity.

MR. RICHTER: Yes.

MR. GOIN: In that case, any party even though they may have had an independent basis to go into the Southeast Zone, they would, in our view, be in breach of the duty of good faith because they would, if you will, conflicted themselves out by participating in the PT WAM and having developed that information.

Transcript: July 27, 2005, pages 31-32

Dr. Kavanagh

The Defence also relies on Dr. Kavanagh's evidence to rebut the O.S.C. submission that that Busang II COW application was the result of Olii's and Zuffrein's exploration work in the "*new prospect area*". The O.S.C. admits the Defence position in paragraph 84 of Exhibit S12:

> Para. 84. In addition, Dr. Kavanagh testified that it was common to apply for ground surrounding an exploration site, and that in fact it might be poor practice for an exploration geologist to not think of doing so. On March 24, 1994, just one week after joining Bre-X, Dr. Kavanagh sent a fax to Mr. Felderhof inquiring who owned the surrounding ground and asking whether it could be acquired.
>
> **Evidence of Dr. Kavanagh, Volume 79, pages 31-32**
> **Evidence of Dr. Kavanagh, Volume 74, pages 14-15**
> **Exhibit 550, Letter dated March 24, 1994**

The OSC admits that on cross-examination Kavanagh was asked about his March 24, 1994 fax to Felderhof, in which he asked "Who owns the ground (mining rights) between and around Busang Blocks II, IV and V? Can it be acquired?"

Kavanagh agreed that it is pretty common for exploration geologists to want to stake or acquire as much land as possible around an exploration site. He agreed it would have been poor practice for Mr. Felderhof not to have thought about staking the parcels of land referred to if they were available.

Kavanagh's evidence is cited out of context because Olii was exploring outside of the PT WAM COW. There is no evidence of any efforts to stake or acquire that area prior to exploring it.

Exhibit S12: paragraph 84

There is no direct evidence that Dr. Kavanagh's "*best practice*" position is what Bre-X was attempting to do in applying for the Busang II COW. Neither does the circumstantial evidence support that position.

Dr. Kavanagh's "*best practices*" approach of applying for ground surrounding an exploration site as being the reason for applying for a COW over Busang II is also not consistent with the hearsay statement made by Felderhof to Sharwood noted above, on which the Defence asks the court to rely, that Felderhof had prior knowledge through Jason Mining of the prospectivity of the Southeast Zone and that that was the basis for applying for a COW over Busang II.

The "*best practices*" argument means applying for surrounding ground not because of present information but to cover possible future developments. The Jason Mining

argument means applying for surrounding ground because of present knowledge of prospectivity.

Bre-X's Busang II Application Was At Least In Part Related To Favourable Assay Results In The New Prospect Area

By Option Deed dated July 20 1993 Bre-X purchased a one year option from WRPL for 80% of the total shares of PT WAM.

Exhibit 830

In and around the date of the Option Deed commencing August 1, 1993, Bre-X undertook the two month field program in the Central Zone and the "*new prospect area*".

On August 24, 1993 Olii sent I.A.L. 53 samples. On September 6, 1993 I.A.L. released encouraging assay results from the 53 samples. Olii and Zuffrein recommended in October 1993 to extend the PT WAM COW application as soon as possible to the "*new prospect area*".

Exhibit S5 Volume I: paragraphs 323-326, 330
Exhibit 1003: Tab 40
Exhibit 785

On February 2, 1994 applications for the 3 KPs covering the Southeast Zone were submitted to the D.O.M.E. This was the first step leading to Bre-X's COW application for Busang II.

Exhibit 874
Exhibit S5 Volume I: paragraphs 334-336, 344-353

FINDING

The above sequence of events establishes a circumstantial case connecting Bre-X's Busang II COW application to the favourable assay results obtained from the "*new prospect area*".

There is some evidence that the Busang II COW application was related to both the PT WAM information about the 53 samples and to the Jason Mining information.
As noted above Goin's expert opinion was that there would still be a duty of good faith where there was previously acquired independent information and additional, perhaps simply confirmatory information developed on behalf of PT WAM as there was here.
Transcript: July 27, 2005, pages 31-32

I find that in breaching it's duty of good faith Bre-X had unjustly excluded Merukh from obtaining an interest in Busang II.

O.S.C. Secondary Submissions That Bre-X Unjustly Excluded Merukh

In addition to the O.S.C.'s primary submissions relying on Goin's expert evidence that Bre-X unjustly excluded Merukh, the O.S.C. also secondarily relied on the evidence of Ridwan, Sharwood, Munk, Dr. Kavanagh and Dr. Juneja in Exhibit S14 and Exhibit S5 Volume I paragraphs 339-343, 389-390.
Having found in favour of the O.S.C. in respect of the primary submissions, the secondary arguments become less significant.

I find these secondary arguments to have little merit largely for the reasons set out by the Defence in Exhibit S7, the Defence comments to the paragraphs listed above in Exhibit S5 Volume I, and paragraphs 42-45 of Exhibit S4.

Several other issues raised by the Defence are dealt with here before proceeding with an analysis of Felderhof's knowledge.

Attempts to Contact Merukh And Merukh's Bad Reputation

In paragraphs 67-69 of Exhibit S12 the Defence sets out Bre-X's attempts to contact Merukh and advise him of Bre-X's option over the PT WAM COW. There was no evidence of any Merukh response.

Exhibit S12: paragraphs 67-69

In paragraphs 71-72 the Defence sets out Ridwan's evidence that Merukh had a very bad reputation with that D.O.M.E. and that the D.O.M.E. would be reluctant to deal with Merukh.

Exhibit S12: paragraphs 67-72, 74-75

The O.S.C. comments with respect to these paragraphs have merit. In any event, these Defence submissions, in and of themselves are not valid reasons not to include Merukh in

an application for Busang II because in Goin's expert opinion even a potentially unsuitable partner must be treated with good faith.

Transcript: July 20, 2005, page 51

Difference In Merukh's Claim And The O.S.C. Approach At Trial

In paragraphs 73-77 of Exhibit S12 the Defence submits Merukh's claims and the O.S.C.'s case at trial were different. In fact there may be some question whether there is any evidence that Merukh even knew about the 53 samples taken from the "*new prospect area*" on which the O.S.C. relies.

But the O.S.C. is not restricted in presenting it's case by Merukh's claim at the time. In any event whatever the O.S.C. theory is with respect to Particular 3 the onus is on the O.S.C. to prove the alleged particular beyond a reasonable doubt and the fact that Merukh's claim is different is a fact that may be taken into consideration in that determination.

Transcript: August 23, 2006, pages 86-91

Kartini Opinion

Kartini, Muljadi & Rekan are an Indonesian law firm that prepared a legal opinion at the request of Sharwood acting for Bre-X.

The Kartini opinions are dated September 27, 1996 and September 30, 1996.

The Kartini opinion concluded Merukh did not have valid claims against Bre-X.

Exhibit S12: paragraphs 88-89
Exhibit 129

Exhibit 852

Goin did not agree with Kartini's opinion. In paragraph 137 of Exhibit 1001, Goin's expert opinion states in part:

> Para. 137. We have reviewed the draft opinion dated September 27 of the Law Offices of Kartini Muljadi, a highly respected law firm in Jakarta with whom we have worked on numerous occasions (Tab 60). In that opinion, there is a discussion of good faith and confidential information, but as the opinion admits, they were not made aware of certain confidential information, such as the information on the 53 samples identified by Mr. Umar Olii during his 1993 field survey...

Exhibit 1001: paragraph 137

The Kartini opinion, as was noted above with respect to information relied on by Sharwood, is based in part on hearsay.

In paragraph 34 on page 8 of Exhibit 129 the Kartini opinion states:

> We are instructed that the application for Busang 2 was made because the ground became available and not because of any particular information Bre-X may have received from PT WAM. In fact Mr. Felderhof had sought a contract of work in respect of ground including Busang 1 and 2 prior to any application being made for the PT WAM COW. However Jason Mining, the company which made the original application, did not proceed with its application because at the time a draft contract of work was prepared for initialing, it was expressed to be subject to certain KP's which were subsequently converted into the PT WAM COW.

Exhibit 129: paragraph 34

In paragraph 10 on page 15 of Exhibit 129 the Kartini opinion states:

> The connection between Busang 1 and 2 was established working back from the drilling results carried out in 1995 on the Busang 2 ground.

The statements relied upon by Kartini are hearsay and not otherwise proven.

The Kartini opinion on the other hand does not take into consideration the 53 samples from the "*new prospect area*" on which the O.S.C. and Goin's opinion rely.

Exhibit 129
Exhibit 852
Exhibit 1001

In paragraph 88 of Exhibit S12, the Defence also submits that at the time of Merukh's allegation Bre-X had the benefit of the Kartini's opinion. Merukh's original allegations were made starting in May 1993, sometime before the Kartini opinion's dated September 27 and 30, 1996. Also importantly the Kartini opinions postdated the end of the charge periods with respect to the insider trading counts, September 10, 1996.

Exhibit S12: paragraphs 73-76, 88
Exhibit 129
Exhibit 852

SUMMARY OF FINDING

I repeat in conclusion that I find that the O.S.C. has proven beyond a reasonable doubt that Bre-X used confidential proprietary exploration information developed by PT WAM, the 53 promising samples from the "*new prospect area*" located within Busang II, to benefit itself in breach of its duty of good faith owed Merukh by applying for a new COW over Busang II without including Merukh.

The O.S.C. has proven that Bre-X unjustly excluded Merukh.

As noted above I accept Goin's evidence that Bre-X breached it's duty of good faith to Merukh by using PT WAM information even where there was prior independent information which by itself could have formed the basis for a COW application.

FELDERHOF'S KNOWLEDGE

There are two issues. Has the O.S.C. proven beyond a reasonable doubt first that Felderhof knew Merukh was excluded and second that Felderhof knew Merukh was unjustly excluded.

Felderhof Knew Merukh Was Excluded From Busang II

As noted earlier the Defence concedes Merukh was not included in the Busang II COW application and there is no issue that Felderhof knew that Merukh was not included.

Transcript: August 23, 2006, pages 118-120

Did Felderhof Know That Merukh Was Unjustly Excluded From Busang II

The general discussion in Particular 2 under the heading "*Felderhof's Knowledge*" on pages 493-494 is applicable to Particular 3.

With respect to Particular 3 that O.S.C. must prove that Felderhof had knowledge that Bre-X unjustly excluded Merukh.

Given the wording of Particular 3 it is not sufficient for the O.S.C. to prove beyond a reasonable doubt that Merukh was excluded (as the O.S.C. has) and that the exclusion was unjust because the exclusion was in breach of Bre-X's duty of good faith (as I have

found the O.S.C. has). The O.S.C. must prove beyond a reasonable doubt that Felderhof knew the exclusion was unjust.

O.S.C. Position

With respect to Felderhof's knowledge, the O.S.C. reviewed evidence under the heading "*Felderhof knew that Merukh was excluded*". There are no O.S.C. submissions specifically and directly about Felderhof's knowledge that Merukh was "*unjustly*" excluded except perhaps the reference to the June 21, 1994 fax from Felderhof to Walsh.

Exhibit S5 Volume I: page 89, paragraphs 354-377
Exhibit 1035: Tab 326

There are other O.S.C. submissions, if accepted, from which it may be argued that an inference be drawn that Felderhof knew the exclusion was unjust. For example, paragraphs 526 of Exhibit S5 Volume I where the O.S.C. alleges Felderhof first acknowledged Merukh's interest in Busang II on April 19, 1994.

Exhibit S5 Volume I: paragraphs 356, 361, 383
Exhibit 1035: Tab 326
Exhibit 1034: Tab 279

These various submissions are discussed below.

With respect to Felderhof's knowledge under the heading noted above, "*Felderhof knew that Merukh was excluded*", the O.S.C. relied on various faxes from Felderhof indicating on several occasions his desire to buy out Merukh and then Felderhof's decision to apply for a COW over Busang II without buying out Merukh nor offering to include him.

Exhibit S5 Volume I: paragraph 355

The faxes from Felderhof on which the O.S.C. relies are found in the following paragraphs of Exhibit S5 Volume I. Corrections to the O.S.C. quotes (pointed out by the Defence) to conform with the actual exhibits are found in square brackets. The added emphasis was done by the O.S.C. in the O.S.C. submissions Exhibit 9.

Para. 356. Felderhof first acknowledged Merukh's interest in Busang II on April 19, 1994, when he told Jonathan Nassey that he wanted to buy out Merukh.

> *(b) I do not wish at this stage to apply for a new COW but incorporate into existing COW which is fourth generation. Terms under fifth generation e.g. tax is not as good as under fourth generation.*
>
> *(c)* ***Because of this I would like Syakerani to be our only partner in Busang.***
>
> ***I would like to buy Joseph Meruk [sic] out.*** *Ask Syakerani to negotiate a cash settlement. *But just ask his opinion how much it would cost to buy Joseph out. Once I know the amount I will be able to pay Syakerani a substantial [agent] fee if the price is right. Please discuss with him asap.* [emphasis added]

The Defence agrees that this is an accurate quote with the exception that the word "agent" is omitted from the second last line between "substantial" and "fee". The fax does not acknowledge Mr. Merukh's interest in Busang II. In fact, it acknowledges the opposite. Because neither PT, KG nor Mr. Merukh had an interest in Busang II, if the Busang I COW was somehow going to be extended to cover Busang II (because the fifth generation COWs were not as favourable as the forth generation), then Mr. Merukh would have to be bought out of the Busang I COW.

Para. 357. Felderhof repeated his desire to buy out Merukh in his April 23, 1994 letter to Nassey.

> *(3) I do not wish to terminate Busang COW at this stage. As previously mentioned to you the terms of the 5th generation COW are detrimental. The existing terms under 4 generation are much more favourable.* ***I wish to buy Joseph Merukh out*** *and have asked Syakerani to give me an estimate on how much this will be.* [emphasis added]

The Defence agrees that this is an accurate quote from Mr. Felderhof's fax. The Defence agrees that Bre-X considered buying out Mr. Merukh's interest in Busang I at a time when the fifth generation COW was applicable.

Para. 358. On April 28, 1994, Felderhof told Syakerani it would be better for Syakerani and Bre-X to buy Merukh out now rather than later.

> *(4) It would be beneficial for both you and Bre-X to buy Josef [sic] Merukh shares out now rather than later.* [emphasis added]

The Defence agrees that after explaining to Mr. Syakerani his concerns with Mr. Syakerani's suggestion of applying for a new COW (the then current fifth generation COW), Mr. Felderhof suggested that another way would be to apply to extend the Busang I COW. This would require Mr. Merukh to be bought out because he had no interest at all in Busang II.

Para. 359. On June 10, 1994, Felderhof told Walsh and McAnulty that he intended to apply for a new COW, which would give them a 90% interest instead of 80%.

> *We will end up with 90% instead of 80%. This would simplify transfer from Montague. All they would have to do [is to] notify Mines Dept that they wish to relinquish the area. However, please notify Montague that you will be exercising your option eg taking up the area.*

The Defence agrees that this is an accurate quote, with the exception that the second line should read "All they would have to do is to notify". There is no evidence as to exactly when the sixth generation COW became applicable, but it is known that when Bre-X and PT AKM applied for a new COW in September 1994, it was already the sixth generation.

Para. 360. On June 20, 1994, Felderhof told de Guzman that the new COW was dangerous and that they could lose their area of interest if they didn't play ball with Syakerani or the DOME.

> *NEW COW – I think that this is dangerous. I believe that we could probably lose our area of interest if we don't play ball with Syakerani or Mine Dept. Could expose ourselves to a [lot] of upfront money. Suggest that we let Mike Bird handle all this in conjunction with you, Jonathan and myself.*

The Defence agrees that this is an accurate quote with the exception that the word "cut" in the third line is actually "lot". This fax would also indicate that Bre-X and Mr. Felderhof considered a number of possibilities and changed views in the months prior to the Busang II COW application being submitted. One issue that was never present was the view that Mr. Merukh ever had an interest in Busang II.

Para. 361. On June 21, 1994, Felderhof told Walsh that he wanted to get rid of a potential unsuitable Indonesian partner, Merukh.

> *As discussed with you there are a number of advantages applying for new COW*
>
> *(3) we will have 90% instead of 80%*
> *(4)* ***getting rid of a potential unsuitable Indonesian partner, Jusuf Merukh***
> [emphasis added]

The Defence agrees that this is almost an accurate quote (the first line should read "a number of advantages applying"). Mr. Felderhof did not state that he wanted to get rid of a potential unsuitable partner, but rather that it would be an advantage. Based on Pak Ridwan's evidence (as discussed at paragraphs 71 – 72 of the Written Closing Argument of the Defence), it would appear that Mr. Merukh was an unsuitable partner.

Para. 362. On June 23, 1994, Felderhof told Syakerani that he was moving ahead with the COW application.

> *Thank you for your fax regarding application over relinquished area. We are moving ahead on COW application. Mr. David Walsh is getting material together to be courier to our office.*
>
> *In the meantime I suggest that if possible you submit the map to Mine Dept with area as drawn by Mike de Guzman. I appreciate that matter is of importance and that we need to act immediately.*

The Defence agrees that this is an accurate quote. Mr. Felderhof told Mr. Syakerani that Bre-X was moving ahead with the COW application.

Para. 363. On June 27, 1994, Felderhof told Syakerani that Walsh would raise the new COW issue at the June 30, 1994 Bre-X board meeting.

> *I have discussed the new COW over Busang area with our President Mr. David Walsh. He will bring the matter up at board meeting [on] 30 June 94 and I will contact you shortly thereafter regarding your proposed terms.*

The Defence agrees that this is almost an accurate quote (the word "in" in the second last line should be "on"). There is no evidence as to the "terms" from Mr. Syakerani that Mr. Felderhof referred to. This highlights an important issue when reviewing the correspondence: there may be gaps in the documentary record.

Para. 364. There is no evidence that this matter was ever brought up at a board meeting or that Felderhof told Walsh or other board members that Merukh had a right to participate in Busang II.

The Defence agrees. Further, there is no evidence that it was not brought up at a board meeting. The Defence agrees that Mr. Felderhof did not tell anyone that Mr. Merukh had a right to participate in Busang II. Mr. Merukh had no such right.

Para. 365. On the same day, Felderhof admitted to Walsh that he was misleading Syakerani by telling him that there was a board meeting.

> *The board meeting re Syakerani is my input to play for time etc.*

The Defence agrees that this is an accurate quote. The Defence disagrees that anything was done to mislead Mr. Syakerani. There is no evidence that the issue was not brought up at a board meeting.

Para. 366. On June 27, 1994, Felderhof told Bird that a map covering the area in the proposed COW had been prepared and hopefully submitted to the DOME.

> *A map of proposed area COW has been prepared and hopefully already submitted to Mines Dept. by Syakerani.*

The Defence agrees that this is an accurate quote.

...

Para. 383. Goin testified that the June 21, 1994 letter from Felderhof to Walsh is evidence of bad faith.

> *As discussed with you there are a number of advantages of applying for new COW*
>
> *(3) we will have 90% instead of 80%*
> *(4)* ***getting rid of a potential unsuitable Indonesian partner, Jusuf Merukh*** [emphasis added]

The Defence agrees that Mr. Goin repeated MKK's view that this fax was evidence of bad faith. This view was based on this fax being an attempt to get rid of a partner that had a right to participate in Busang II and III because exploration had been carried out outside of the PT WAM COW. This has not been proven. There is no evidence that it would be bad faith to seek to buy out a partner who had no right to be involved in Busang II or II.

Para. 384. Goin opined that even a potentially unsuitable partner must be treated with good faith.

The Defence agrees that Mr. Goin said this.

Exhibit S5 Volume I: paragraphs 356-366, 383-384

In Exhibit 1001, paragraph 134, Goin expressed his opinion with respect to the June 21, 1994 fax from Felderhof to Walsh, noted above in paragraphs 361 and 383:

> Evidence of affirmative bad faith is clear from Mr. Felderhof's June 21, 1994 facsimile to Mr. David Walsh (Tab 55) discussing the advantages to the new COW applications:
>
> > "...we will have 90% instead of 80%"
> >
> > "...getting rid of a potential unsuitable Indonesian partner Jusuf Merukh."

Exhibit 1001: paragraph 134
Exhibit S5 Volume I: paragraphs 356-366, 383-384

Goin testified:

> MR. MARROCCO: And on paragraph 134, your conclusion there is?
>
> MR. GOIN: We conclude that the exploitation of information developed by WAM for the purposes which benefits some, but not all shareholders would not be in good faith because it does not reflect the collective rights of all shareholders to the benefits of that information. We do not have any evidence that Mr. Merukh or his company was aware of this, or that reports were made, or that he consented in any way to this.
>
> MR. MARROCCO: And then you say there:
> "Evidence of affirmative bad faith is clear."
> What items to you rely on?
>
> MR. GOIN: Well, the quotation in the facsimile from Mr. Felderhof and Mr. Walsh, where he is trying to get rid of an unsuitable partner, Jusef Merukh; in other words, he is looking at his personal interests, rather than the duties to disclose the information and to negotiate with him to buy him out if necessary, but to make a joint decision within the context of the PT WAM.

MR. MARROCCO: I take it – is it true under Indonesian law that even if a person was unsuitable as a partner, but was, in fact, a partner, that they would still have to be treated as a partner?

MR. GOIN: That's true, assuming that the unsuitable was not something that would cause the partnership arrangement to terminate.

Transcript: July 20, 2005, page 51

The O.S.C. position is that Felderhof's stated desire to buy out Merukh is an acknowledgement that Merukh had an interest in Busang II. The O.S.C. submits Felderhof's decision then not to extend the PT WAM COW but to apply for a new COW over Busang II without buying out Merukh or offering to include him in the Busang II COW giving Bre-X "*90% instead of 80%*" of Busang II and getting "*rid of a potential unsuitable Indonesian partner, Jusef Merukh was "clear*" "*[e]vidence of affirmative bad faith.*"

Defence Position

The Defence position is that because of the way Particular 3 is framed, the O.S.C. must prove that Felderhof knew that Merukh was excluded, that Felderhof knew the exclusion was unjust and that Felderhof knew the exclusion was unjust by Indonesian law. As noted, there is no issue that Felderhof knew Merukh was excluded.

Transcript: August 23, 2006, pages 118-120

I agree that the O.S.C. has to prove beyond a reasonable doubt that Felderhof knew that Merukh was unjustly excluded. For the purposes of this judgement it is not necessary for me to determine whether the Crown must specifically prove Felderhof knew it was unjust as a matter of Indonesian law.

The Defence position is that Felderhof never acknowledged that Merukh had an interest in Busang II as the O.S.C. states but that in fact the opposite is true. The Defence submits that Felderhof was always consistent in his belief that Merukh had no interest in Busang II and stated that belief to other officers and directors of Bre-X and to Bre-X's lawyers: Sharwood (who was asked about Felderhof's comments in chief by the O.S.C., transcript May 2, 2005, page 84) and Bennett Jones. The Defence position is that the faxes from Felderhof referred to by the O.S.C. are also consistent with that position.

The Defence position is that there were two ways to acquire Busang II: by extending the PT WAM COW to include Busang II or by applying for a new COW over Busang II. Applying for KP's over Busang II in the interim would secure Busang II for either of the two ways noted above.

The advantage of extending the PT WAM COW was that it was a fourth generation COW which had "*much more favourable*" terms (Exhibit 1034, tab 285) then the fifth generation COW applicable to new COW applications at the time.

The disadvantage of extending the PT WAM COW was that it would extend the interest of all shareholders in PT WAM (Busang I) to Busang II including Merukh but as Felderhof believed Merukh has no right to an interest in Busang II it would be necessary to either buy out Merukh's interest in PT WAM or give him an interest in Busang II to which he was not entitled.

The Defence submits the discussion about buying out Merukh's interest in PT WAM before extending the PT WAM COW was therefore in fact not an acknowledgement that because Merukh had an interest in Busang II as the O.S.C. submits but shows the opposite that because Merukh had no right to an interest in Busang II he needed to be bought out if the PT WAM COW was going to be extended or as noted above he would get an interest in Busang II to which he was not entitled.

The disadvantage of a new COW application for Busang II was that the terms of the applicable fifth generation COW were much less favourable then the terms of the fourth generation PT WAM COW.

The advantages of a new COW application would be that Merukh, who was unsuitable and who was not entitled to any interest in Busang II, would not be included and that Bre-X would get a 90% interest in Busang II instead of 80% as would have been the case if Bre-X had bought out Merukh's interest in PT WAM and then extended the PT WAM COW.

Felderhof and Bre-X eventually determined the best way to acquire Busang II was through a new COW application which by then was a sixth generation and not an unfavourable fifth generation COW.

Finding

My reading of the faxes, given the evidence of the surrounding circumstances, leads me to prefer the Defence position.

Exhibit S5 Volume I: paragraphs 356-366, 383-384
Exhibit S4: paragraphs 46-47

Dr. Kavanagh

With respect to the issue of Felderhof's knowledge, the O.S.C. also relied on Dr. Kavanagh's evidence. In paragraphs 370-376 of Exhibit S5 Volume I the O.S.C. discusses Dr. Kavanagh's view, expressed to Felderhof, that Bre-X should let the partners in Busang I have the same interest in Busang II and III.

Exhibit S5 Volume I: paragraphs 370-376

In cross-examination, Dr. Kavanagh agreed his view was not "*universally held by everyone in the industry*" and that he ultimately concurred in the decision to proceed with a 90% interest for Bre-X in Busang II and III.

Transcript: March 14, 2005, page 83

FINDING

Given my finding that I prefer the Defence interpretation of the faxes relied upon by the O.S.C. in proving Felderhof's knowledge; Felderhof's repeatedly stated belief that

Merukh was not entitled to any interest in Busang II; the evidence that through Jason Mining Felderhof had some prior independent knowledge of the prospectivity of Busang II; the evidence that Felderhof's opinion was supported and confirmed by legal opinion, Sharwood (although as with the Kartini opinion the weight is lessened because information came from Felderhof himself) and Kartini (although Kartini's opinion came after the charge period); the testimony of Ridwan that he advised Felderhof that the D.O.M.E. and Dr. Kuntoro had stated that Merukh's claim had no merit and that the D.O.M.E. would not be responding to it (Transcript: November 29, 2005, pages 11-17); and the fact that the Merukh's complaints to the Indonesian government (Exhibit 39, Exhibit 43(a), Exhibit 43(b), Exhibit 846) do not refer to the work by Olii in 1993 in the new prospect area on which the O.S.C. relies to prove Merukh's exclusion was unjust, I am not satisfied that the O.S.C. has proven beyond a reasonable doubt that Felderhof knew that Bre-X had unjustly excluded Merukh from Busang II.

Particular 4: That PT KG, And/Or PT SAP, And/Or Jusef Merukh, Had Issued A Complaint To The Indonesian Government And Bre-X Respecting Their Exclusion From Obtaining An Interest In The Exploration Of The Property Known As Busang II

Jusef Merukh made a number of complaints to Indonesian government officials. On May 28, 1996 Merukh complained to Dr. Kuntoro at the D.O.M.E. asking the D.O.M.E. to direct Bre-X to return the Southeast Zone area to the exploration area of the PT WAM COW.

On June 28, 1996 Francisco sent a copy of Merukh's May 28, 1996 complaint to Felderhof. The Defence concedes Merukh complained to the Indonesian government and that Felderhof knew of the complaint on June 28, 1996.

Exhibit S5 Volume I: paragraphs 463-464
Exhibit S12: paragraph 91
Exhibit 39

On June 25, 1996 Merukh wrote a second letter to Dr. Kuntoro. Merukh alleged that "*geological information obtained by PT. WAM [in 1988] demonstrated that the Busang mineralized Zone extended beyond the South-East boundary of the COW.*" The letter relied on Article 4.2 of the PT WAM COW in its request that the Southeast Zone be amalgamated into the PT WAM COW.

On July 2, 1996 Merukh's lawyers wrote to Bre-X in Jakarta enclosing the June 25, 1996 letter.

Exhibit S5 Volume I: paragraphs 467, 469-470
Exhibit S12: paragraph 92
Exhibit 43(a)
Exhibit 43(b)

On July 8, 1996 Felderhof sent a copy of the July 2, 1996, lawyers letter to Walsh.

Exhibit S5 Volume I: paragraph 475
Exhibit 45

On August 2, 1996 Merukh's lawyers wrote to Dr. Kuntoro reporting on their meeting with Bre-X on July 30, 1996 and renewing their formal requests that the two new COWS, including the one for the Southeast Zone or Busang II not be granted and that Bre-X be instructed to amalgamate the new areas with the PT. WAM COW.

Exhibit S12: paragraph 93
Exhibit 846

On February 18, 1997 Merukh wrote to the Minister of Mines applying under Article 4.2 of the PT WAM COW to amalgamate "*the Busang Project area... under the ownership... of PT WAM.*"

In that letter Merukh states "*we have written to the Ministry on the following dates:*

28 May 1996	*21 October 1996*
25 June 1996	22 October 1996
2 August 1996	*3 December 1996*
19 August 1996	*16 December 1996*
14 October 1996	*9 January 1993*".

Other then the letters discussed above the other letters listed in Exhibit 477 are not exhibits in this trial.

Exhibit S12: paragraph 94
Exhibit 477

The evidence of Sharwood, Goin and Ridwan was that Merukh's argument under Article 4.2 of the PT WAM COW had no merit.

Exhibit S5 Volume I: paragraph 467

FINDING

The O.S.C. has proven that Merukh complained to the Indonesian government that he was excluded from Busang II and that Felderhof had knowledge of the complaints.

Exhibit S3: Tab C, paragraph 35

Particular 5: That The Indonesian Government Had Cancelled The Preliminary Survey Permit Respecting The Property Known As Busang II

On March 17, 1995, Bre-X received approval in principle for the COW application over Busang II.

On June 6, 1995, Bre-X applied for a SIPP over Busang II. On July 20, 1995, the D.O.M.E. granted the SIPP for one year ending July 20, 1996. On June 20, 1996 Bre-X applied for an extension of the SIPP. On July 20, 1996 the SIPP was extended for a further year ending July 19, 1997.

On August 15, 1996, the D.O.M.E. cancelled the SIPP over Busang II *"[i]n connection with administration problems that have arisen which have not yet been resolved (finalized) by your partner, Bre-X"*.

There is no issue the Indonesian government cancelled the SIPP as alleged in Particular 5.

Exhibit S5 Volume I: paragraphs 530-531, 534-538, 541
Exhibit S12: paragraph 111
Exhibit S3: Tab C, paragraph 36

Felderhof's Knowledge

On or about August 15, 1996, Felderhof spoke to Francisco about the cancellation of the SIPP. Felderhof urged Francisco to call Ridwan right away because Ridwan would be able to give Francisco a better perspective on why the SIPP was cancelled.

On or about August 15, 1996, Felderhof told Francisco that the cancellation of the SIPP *"was just a shot across the bow"*. Francisco testified that what Felderhof meant by that

and what he told Francisco was that the Indonesian government was applying pressure on Bre-X to agree to enter a joint venture agreement with Barrick with respect to Busang.

Exhibit S5 Volume I: paragraph 343
Transcript: December 19, 2000, pages 97-100

FINDING

The O.S.C. has proven that the Indonesian government cancelled the SIPP on August 15, 1996 and that Felderhof had knowledge of the cancellation.

MATERIALITY

In 1996 the *Securities Act* in S.1(1) defined "*material fact*" as "*where used in relation to securities issued or proposed to be issued, means a fact that significantly affects, or would reasonably be expected to have a significant effect on, the market price or value of such securities.*"

Today the *Securities Act* defines "*material fact*" as: "*when used in relation to securities issued or proposed to be issued, means a fact that would reasonably be expected to have a significant effect on the market price or value of the securities.*"

Dr. Juneja

The O.S.C. called an expert, Dr. Juneja, to testify with respect to the first part of the definition in force in 1996 but now deleted: "*a fact that significantly affects....the market price or value of such securities*".

Dr. Juneja is Senior Vice President in the securities and financial services practice of National Economic Research Associate (N.E.R.A.) an economic consulting firm. Dr. Juneja's extensive curriculum vitae and experience are found at Exhibit 800A, Tab 1.

My ruling qualifying Dr. Juneja is at pages 2-7 of the April 14, 2005 transcript. I concluded: "*In summary, the witness is qualified as an expert in the fields of securities economics and assessment of materiality.*"

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Dr. Juneja conducted an event study. The Defence accepted the general validity of event studies but submits this event study was flawed.

Exhibit S5 Volume I: paragraphs 395-399
Exhibit 800

Dr. Juneja describes her event study in Exhibit 800.

In the hearing to qualify Dr. Juneja, the Defence objected to her being qualified, for among other reasons, the fact that Dr. Juneja's opinion of materiality related not to the particulars but, as asked by the O.S.C., to the particulars "*and their potential consequences*".

I ruled that objection went to the weight of the evidence and not admissibility.

In paragraph 145 of Exhibit S12 the Defence submits "*[t]his analysis was imposed upon N.E.R.A. by the O.S.C. and renders the work that N.E.R.A. did of no value to the materiality of the alleged undisclosed facts.*"

Transcript: April 14, 2005, page 6
Exhibit S12: paragraph 145

In it's commentary the O.S.C. denies paragraph 145 above and states "*The O.S.C. must prove beyond a reasonable doubt that Felderhof was in possession of material facts, which facts have been particularized in the information.*"

I agree the O.S.C. must prove beyond a reasonable doubt that Felderhof had knowledge of the material facts set out in the particulars to the information.
The issue is whether Dr. Juneja's analysis and opinion of the materiality of the particulars together with their potential consequences, following the instructions of the O.S.C., is sufficient evidence (without at this point considering the other Defence submissions attacking Dr. Juneja's opinion) to prove that the particulars are material facts.

The O.S.C.'s instructions (not those of Ms. Cole nor Mr. Marrocco (now Mr. Justice Marrocco)) to Dr. Juneja were clear in her opinion, Exhibit 800A, Dr. Juneja states at page 3:

> "I was asked by counsel to provide an opinion, based on my experience as an economist, as to whether the above facts (and their potential consequences) were material, as defined in the Ontario Securities Act. In arriving at my opinion, it was necessary...to answer the following questions: ...
>
> 2. Were these facts (and their consequences) material?..."

Dr. Juneja also testified to this on more than one occasion that the O.S.C. asked her "*to do an analysis of ...whether or not the particulars and their consequences were material*".

Transcript: April 18, 2005, page 16

DR. JUNEJA DOES NOT UNTANGLE PARTICULARS FROM THE ALLEGED POTENTIAL CONSEQUENCES NOR ANY ONE PARTICULAR FROM ANY OTHER PARTICULAR

On page 2 of in her opinion, Exhibit 800A, Dr. Juneja sets out the "*allegedly material facts, or Particulars*" found in the Particulars to the Information (set out above at page 393 of these reasons).

On page 3, Dr. Juneja continues:

> Each of these material facts, in turn, placed at risk Bre-X obtaining approval of its pending application for a Contract of Work ("COW") over Busang II and thereby jeopardized the likelihood of Bre-X securing a legal interest to the gold and the extent to which Bre-X could profit from the gold. [4] These were the potential consequences of the Particulars.

In footnote 4 Dr. Juneja states that the O.S.C. "*Overview of the Allegations Made by the Ontario Securities Commission Respecting Insider Trading by John Felderhof dated January 4, 2000, page 2*" was the source of what she states in her opinion "*were the potential consequences of the Particulars.*"

Throughout her report Dr. Juneja to refers to her analysis not of the particulars standing on their own but of the particulars together with their alleged consequences; for example (emphasis added) starting at page 3:

The facts only truly began to be revealed on October 4, 1996 **and related facts and developments** continued to be revealed until at least March 6, 1997.

...

Page 6:

The news of September 27, 1996 was followed by a series of revelations, relating to the five Particulars and **their consequences**, to emerge for the next six months. In order to answer the questions posed to me by counsel, I proceed in stages. The goals are to determine:

1. When, if ever, the full extent of the information regarding Bre-X's disputes with its local joint venture partners, the company's difficulties related to its efforts to establish clear legal and beneficial ownership of Busang I **and the ensuing consequences** to ownership to Busang II thereby became generally disclosed to the public.

2. Whether the information was material.

...

Page 10:

In order to determine whether the disclosures, misleading omissions, and misrepresentations concerning Bre-X's disputes with its local joint venture partners, the company's difficulties related to its efforts to establish clear legal and beneficial ownership of Busang I, **and the impact** of these factors on the company's investment in Busang II were material, I employed the event study technique.

...

Page 12:

As a result of an analysis of news stories, analyst reports, press releases, and regulatory filings on and by Bre-X, I have been able to identify those days upon which new information was released concerning Bre-X's disputes with its local joint venture partners, the company's difficulties related to its efforts to establish clear legal and beneficial ownership of Busang I **and subsequent developments** reflecting title and the pending COW for Busang II.

...

In order to test whether the information regarding Bre-X's disputes with its local joint venture partners, its difficulties in establishing clear ownership of Busang I, **and ensuing developments** regarding Busang II was material, I created a list of key dates (culled from the bold print items in Exhibit 3) on which any aspect of such information first became publicly known.

Exhibit 800A: pages 3, 6, 10, 12

The report variously refers to the consequences as "*consequences*", "*potential consequences*", "*ensuing consequences*", "*impact*", "*related facts and developments*", "*subsequent developments*" and "*ensuing developments*".

Exhibit 800A

Dr. Juneja repeats in her evidence that she was analyzing not the particulars on their own as alleged in counts 1 to 4 but the particulars and their consequences together:

> DR. JUNEJA: ...They asked me to assess the materiality of the information related to the particulars and resulting facts and consequences.

Transcript: April 14, 2005, page 7

> DR. JUNEJA: So what we did with this chronology is we read through the whole chronology, all the analysts reports that we had collected, and the SEC filings that we had collected, and also press releases that we had from Bre-X, and looked for information that related to any of the five particulars and their potential consequences.

Transcript: April 14, 2005, page 18

> DR. JUNEJA: What we're trying to get a handle on here is when the particulars and their consequences were disclosed to the market.

Transcript: April 14, 2005, page 24

> DR. JUNEJA: And in conjunction with the request from the OSC, I wasn't looking only at the five specific particulars, but also at the consequences of the particulars.

Transcript: April 28, 2005, page 21
Exhibit S12: paragraph 133

Dr. Juneja evidence is replete with such references.

Dr. Juneja's Evidence On April 14 And 19, 2005

Dr. Juneja further testified:

> MR. GROIA: Now, if I take you then to your report, page two, where you list the five material facts for particulars, I take it you conclude that each and every one of those five particulars also constitute a material fact.
>
> DR. JUNEJA: What I'm testing for is the materiality of the five particulars as a whole, and along with their consequences as a whole. I'm not testing for the materiality of any one individual fact.
>
> MR. GROIA: So when we look at the top of page four, item number 3, your evidence is that you're not expressing any opinion as to whether any one of those facts, or any one of those particulars, is or is not material.
>
> DR. JUNEJA: That's correct. The disclosures, for the most part, often related to more than one particular, or related to consequences of a combination of the particulars, and I did not disentangle the materiality of any one fact from the other.
>
> MR. GROIA: And did you disentangle the materiality of any one particular from related facts and developments?
>
> DR. JUNEJA: No, I did not.
>
> ...
>
> MR. GROIA: Is your evidence, Doctor Juneja, that in assessing these five particulars, you did not disentangle the five particulars from related facts and developments?
>
> DR. JUNEJA: No, I did not.

Transcript: April 19, 2005, pages 40-41

> DR JUNEJA: And I think some of the consequences of the particulars are, in substance, related, you know, to several of the particulars.

Transcript: April 14, 2005, pages 61-62

The onus on the O.S.C. is to prove the actus reas of Counts 1 to 4 beyond a reasonable doubt. Included in that is the requirement that the O.S.C. prove the particulars beyond a reasonable doubt. The O.S.C. must also prove that the particulars are material facts beyond a reasonable doubt.

Dr. Juneja's evidence does not prove beyond a reasonable doubt that any one particular is material. Dr. Juneja's evidence does not prove beyond a reasonable doubt that the particulars together are material. At it's highest, Dr. Juneja's evidence is that all "*five particulars as a whole...along with their consequences as a whole*" are material.

Dr. Juneja "*did not disentangle the materiality of any one fact [or particular] from ...[any] other*" fact or particular. Dr. Juneja did not "*disentangle the materiality of any one particular from related facts and developments*" or consequences.
Dr. Juneja did not "*disentangle the five particulars from related facts and developments*" or consequences. Dr. Juneja was "*not testing for the materiality of any one individual fact*" or particular. Dr. Juneja was "*not expressing any opinion as to whether any one of those facts, or any one of those particulars, is or is not material.*"
Transcript: April 19, 2005, pages 40-41

Significantly Dr. Juneja did not testify that because in her opinion the "*five particulars as a whole...along with their consequences as a whole*" were material that therefore the five particulars as a whole were material or that any one particular was material or that any two or three or four particulars were material.

It may be appropriate (or perhaps even essential) to consider the consequences of a fact in determining the materiality of that fact but in the end the evidence must be that the fact is a material fact. Significantly Dr. Juneja did not give such evidence.

S. 76(1) requires the O.S.C. to prove the material fact beyond a reasonable doubt. Dr. Juneja did not testify that the particulars were material facts. The particulars are the alleged material facts and are part of the information charging Felderhof with insider trading. The potential consequences are not part of the charges Felderhof is facing.

The O.S.C. alleged certain facts (the particulars) to be the material facts and is now purporting to prove other facts (the particulars and their potential consequences) or more precisely the "*five particulars as a whole... along with their consequences as a whole*" to be material.

Dr. Juneja's evidence as noted was that she did not test "*for the materiality of any one individual fact*" but that she tested for "*the materiality of the five particulars as a whole...along with their consequences as a whole*" and that she "*did not disentangle the given particulars [or any one particular] from related facts and developments*" (the

consequences) and that she did not "*disentangle the materiality of any one fact from...[any] other*" fact or particular.

O.S.C. Position

In paragraphs 429, 433, 437, 503 and 552 of Exhibit S5 Volume I the O.S.C. submits with respect to each particular that "*it has proven beyond a reasonable doubt that [that] Particular...was material*". I disagree. Dr. Juneja's evidence does not prove beyond a reasonable doubt that each particular was material. Dr. Juneja's evidence does not even prove beyond a reasonable doubt that the five particulars as a whole were material. Dr. Juneja's opinion was that "*the five particulars as a whole...along with their consequences as a whole*" were material.

Dr. Juneja's Evidence On April 28, 2005

The O.S.C. relies on the following testimony of Dr. Juneja to submit that Dr. Juneja did in fact separate particulars from consequences and did testify about the materiality of individual particulars:

> DR. JUNEJA: Well, you could look at Exhibit 3. But let me give you a little more information. If you look at the particular particulars –let's just talk about the particulars for a minute, rather than their consequences. The particular number two, for example, let's just look at that, about the method in which – let me just put this down for a minute. Particular number two is that they have misled the Indonesian Government respecting the acquisition of an 80% interest in PT WAM. Now, that particular, in and of itself, is revealed on October 4th. If you believe that particular, which I'm agnostic on, but let's assume that it's true, information about that is revealed on October 4th.
>
> COURT REPORTER: On October –
>
> DR. JUNEJA: - 4th. If you look at particular number three, that Bre-X had unjustly excluded PT Krueng Gasui, and/or PT Sungai Atan Perdana, and/or Jusef Merukh from obtaining an interest in the property known as Busang II, that

particular is revealed to the market on October 4th, when the first questions about the exclusion arise, on October 15th and 16th, when information comes out to the market about the 40% option, and October 18th, when there's information about meeting with Jusef Merukh to settle his complaint.

If you look at particular number four about Jusef Merukh having issued a complaint to the Indonesian Government and Bre-X respecting their exclusion from obtaining an interest in the exploration of the property known as Busang II, that information comes out on October 4th, when it's indicated to the market that such a complaint was filed, and then I think there would be amplifying information on the 15th and 16th that have to do with the 40% option, and on the 18th of October having to do with the potential Merukh settlement.

The particular number five has to do with the Government canceling the preliminary SIP and that is indicated to the market in a clear fashion on October 4th.

So let's just focus on those dates for a minute and not worry about the consequences of the particulars. The question then becomes, was that information material to the market? So I would point you to the dates of October 4th, 15th , 16th and 18th . All of those dates, 4th, 5th, the 16th and the 18th are indeed statistically significant. The 15th has some issues with it because there was no trading in Canada on the 14th, but if you look at the NASDAQ, which should be reasonable to do, we see that it is a statistically significant movement.

Now, this information is initially released in October and I think there's no question that the market is responding to this information and there are material movements. These are dates on which there is no other substantive news that would contaminate.

Now, subsequently it gets a little harder in terms of figuring out what the news is that's relating to the particulars in terms of pointing directly back to each of these particulars. Instead, what you then have is a whole series of events which are unleashed that have to do with whether or not they're going to get the COW, whether or not – how much of the mine they're going to have access to. And the first question then becomes, "Well, do we even care about those subsequent dates?" Because if we've looked at these initial dates, you've already got evidence that the particulars were material. However, when I did this analysis I wasn't focusing only on those initial dates. I didn't know how those would turn out. I didn't know if they'd be statistically significant or not. I wanted to get a sample of the dates on which material information came out, potentially – new information about the particulars came out to the market. And in conjunction with the request from the OSC, I wasn't looking only at the five specific particulars, but also at the consequences of the particulars.

...

MR. GROIA: And if we look at what you just gave as your explanation about the second and third and fourth particular, did I not understand your prior testimony to be that it was difficult, if not impossible, to isolate out these disclosures and relate them to specific particulars?

DR. JUNEJA: I can't tell you exactly what I've said over the past nine days, but my testimony would have been that there were many, many things released over this time period and that there was information that was related to the particulars, there was information that was related to the consequences of the particulars.

MR. GROIA: So you don't agree with me that when you just said to Judge Hryn that we should just focus on those early October dates and not worry about the consequences, you're not in agreement with me when I suggest to you you're contradicting your prior testimony.

DR. JUNEJA: What I was doing was answering Judge Hryn's question.

MR. GROIA: And in order to try and do that, I'm suggesting to you that your testimony is now contradicting what you said before when I took you through those dates several days ago in cross-examination. Would you agree with that?

DR. JUNEJA: No. My intent was not to contradict any prior testimony.

MR. GROIA: So is it possible, or is it not possible, to relate particular news stories to particular particulars?

DR. JUNEJA: It depends on the story. I think that there are some stories where it is clear that particular particulars are being revealed; however there are other stories where the consequences of particulars are being revealed. And certainly even in the stories that I've pointed to in October, that doesn't mean that there was nothing that the market was gleaning about the consequences of the particulars at the same time.

Transcript: April 28, 2005, pages 19-21, 23

In the last lines quoted above from page 21 Dr. Juneja concedes the news stories in October 1996 had information about the consequences of the particulars but to the extent that this evidence purports to comment on the materiality of individual particulars alone then this evidence contradicts Dr. Juneja's prior evidence, discussed above, found in

Exhibit 800A and in testimony on April 19, 2005 and on all those other occasions where the testimony consistently tied Dr. Juneja's opinion to an analysis of the particulars together with the consequences and not to an analysis of the particulars alone.

Dr. Juneja's prior evidence was clear that the O.S.C. instructions were to assume the particulars and to assume the consequences and to determine the materiality of the particulars together with their potential consequences. Dr. Juneja's evidence was that she did not disentangle the materiality of any one particular from any other particular or from the consequences. She testified she tested the materiality of the five particulars as a whole with their consequences as a whole. She testified she did not test for the materiality of any one individual particular.

In this segment of her testimony (April 28, 2005 pages 19-21, 23), Dr. Juneja purports (contrary to her prior evidence) to separate or disentangle the consequences from the particulars and to comment on the materiality of the particulars. In this evidence Dr. Juneja relies on news stories on October 4, 15, 16, and 18, 1996. A brief analysis of these news stories does not support Dr. Juneja's April 28, 2005 testimony.

The October 4, 1996 Globe and Mail article is a very important article for Dr. Juneja's opinion. In Exhibit 3 in Exhibit 800A, entitled the "*Chronology of News Stories Relating to the Particulars*", Dr. Juneja bolded key information which is clearly significant but related to consequences and not to the particulars per se. Examples of that is information in the October 4, 1996 article that the *"[a]uthorities in that country have launched an*

inquiry..." and that "*the Indonesian government said yesterday that Indonesia's President will not sign the license for Bre-X until the outstanding issues are resolved*" which is information clearly related to the consequences and not the particulars per se. That information would be virtually impossible to disentangle from the information about particulars and is consistent with her evidence on April 19, 2005 that she did not disentangle the materiality of the particulars from each other nor from the assumed consequences.

Exhibit 800A
Exhibit S5 Volume I: paragraph 404
Transcript: April 28, 2005, pages 19-21, 23

Dr. Juneja testified that the October 4, 1996 news story was relevant to establishing the materiality of Particulars 2, 3, 4, 5 but in addition to bolding consequences as noted above, Dr. Juneja also testified that she was in fact looking for the particulars and their consequences in the October 4, 1996 news story and not for particulars alone:

> DR. JUNEJA: So all the information that's revealed on that day, including the unbolded, is going to be relevant to the stock price. What we're trying to get a handle on here is when the particulars and their consequences were disclosed to the market.

Transcript: April 14, 2005, page 24

As noted above, in her April 28, 2005 testimony Dr. Juneja also refers to October 15, 16, and 18, 1996 in addition to October 4, 1996, as dates that purportedly also establish the materiality of Particular 3 and 4 without "*worry[ing] about the consequences of the particulars*" but that is contrary to her evidence on April 27, 2005 where she testified that

the news on October 15, 16 and 18, 1996 was related to the particulars and the consequences of the particulars and not to the particulars alone.

With respect to October 15 1996 news story, Dr. Juneja testified:

> DR. JUNEJA: ...When I noted that in my review of materials I said, "Well, I think this news on the 15th is actually pretty important, potentially important, potentially related to the particulars of the disclosure and potentially related to the consequences of the particulars.

Transcript: April 27, 2005, page 16

With respect to October 16 1996 news story, Dr. Juneja testified:

> DR. JUNEJA: My testimony is that there appeared to be new information regarding particulars and consequences to the market, and so I chose that as a key date.

Transcript: April 27, 2005, page 14

With respect to October 18, 1996 news story, Dr. Juneja testified:

> DR. JUNEJA: My evidence is that the meeting with Jusef Merukh that was reported in the press was potentially news that was related to the particulars and their consequences...

Transcript: April 27, 2005, page 27

FINDING

I find that this contradictory evidence given on April 28, 2005 does not assist me or at least leaves me with a substantial and reasonable doubt with respect to the April 28, 2005 evidence of the materiality of the particulars.

This evidence of April 28, 2005 places substantial reliance on what Dr. Juneja states is the first disclosure of the particulars and consequences on October 4, 1996 but Dr. Juneja did not take into account the Barrick manipulation that led to the "*news*" disclosed on October 4, 1996, as discussed later in these reasons at pages 561--571.

O.S.C. FAILS TO ESTABLISH POTENTIAL CONSEQUENCES FLOW FROM PARTICULARS

As noted above I find there is a reasonable doubt about Dr. Juneja's evidence that the particulars are material facts because, among other reasons, the evidence of materiality related to the particulars and their consequences combined and the evidence did not disentangle the materiality of the particulars from the materiality of the consequences.

But to even consider the purported evidence of the materiality of the particulars and their consequences as being evidence that the particulars are material, the O.S.C. would have to prove the consequences (as the O.S.C. is required to prove each of the particulars) and to prove that the consequences flowed from the particulars. The O.S.C. has also failed to prove these requirements.

As noted earlier Dr. Juneja was asked to assume the five particulars were true and to assume the potential consequences of the five particulars.

Transcript: April 19, 2005, pages 41-42, 87
Transcript: April 14, 2005, pages 20-22

The O.S.C. concedes that Dr. Juneja was asked to assume the consequences of the particulars but the O.S.C. also submits that Dr. Juneja "*reached an independent conclusion*" about the consequences of the particulars.

The O.S.C. refers to Dr. Juneja's evidence at pages 20-22 of the April 14, 2005 transcript:

> DR. JUNEJA: Well, as I said, we looked at the particulars closely and we also, in reading the chronology, determined that there were various potential consequences of the particulars, and we determined what those were as well, and those had to do with whether Bre-X had – how secure their interest was in the Busang properties and how likely it was that they were to receive a COW, and what share of the pie, so to speak, of the Busang properties, they would ultimately end up with, and what that ultimately implied is what the company would be worth. So we were looking for information relating to the particulars and those consequences throughout the chronology and throughout the other sources that we had, and what we've done here is bolded any such information within the text of the news stories. And we're really highlighting, I think, the key information as opposed to – there sometimes are amplified sentences, or something like that, but we're really highlighting the key information that's revealed in the story.
>
> MR. MARROCCO: So going back to our discussion earlier about the particulars, you noted those particulars in your report at page 2 and then you went on at page 3, you talked about the consequences of those particulars. I just want to make sure I understand your evidence – that you actually formed an independent conclusion of whether or not there were consequences of those particulars from reading this chronology?
>
> DR. JUNEJA: What I've been asked to do by the OSC is to assume the five particulars, and not independently –you know, I wasn't asked to do an independent assessment of the five particulars. I was also asked to assume that each of these allegedly material facts placed at risk Bre-X obtaining approval of its pending application for a COW over Busang II, and thereby jeopardizing, sorry-
>
> ...
>
> DR. JUNEJA: I was asked to assume that each of these particulars placed at risk Bre-X obtaining approval of its pending application for a COW over Busang II-
>
> MR. MARROCCO: Yes.

DR. JUNEJA: -- and thereby jeopardize the likelihood of Bre-X securing a legal interest to the gold, and jeopardizing the extent to which Bre-X could profit from the gold.

However, in reading the chronology and reading the materials from the analysts, it became clear to me that issues regarding the dispute with Jusef Merukh and how they'd acquired their 80 percent interest in PT WAM, and the complaint by Merukh to the Government, was indeed jeopardizing and affecting the likelihood of obtaining a COW, and it was indeed affecting the markets assessment of the extent to which Bre-X could profit from the gold.

THE COURT: Taking the market assessment.

DR. JUNEJA: Market's assessment, yes. As the market was learning about these events, you'd see in the news stories that they were commenting about how these events were affecting how much Bre-X would end up with in terms of their share of the pie.

Transcript: April 14, 2005, pages 20-22
Transcript: April 18, 2005, pages 13-14
Transcript: April 28, 2005, page 74
Exhibit S5 Volume I: paragraph 394

After giving the evidence above on April 14, 2005 which seems to suggest that Dr. Juneja was not just assuming but came to the conclusion herself that the potential consequences were related to the particulars, Dr. Juneja on April 19, 2005 reverts to saying that given guidance by the O.S.C., she was making an assumption that the stated consequences flowed from the particulars and again on April 20, 2005 Dr. Juneja testified "*what I did is assume the particulars, assume their consequences...*".

Transcript: April 19, 2005 page 87
Transcript: April 20, 2005, page 91

On the evidence there are other intervening factors, Barrick and the Indonesian government, which create real doubt that the potential consequences, set out on page 3 of

Exhibit 800A, and assumed by Dr. Juneja are the result of the particulars and not the result of those other factors.

Barrick Gold

The detailed evidence of Barrick's involvement in Indonesia is set out below. Dr. Juneja above does not testify that this evidence was considered in her conclusion that the potential consequences flowed from the particulars and were not the result of other factors.

Dr. Juneja was cross-examined generally about her knowledge of Barrick's involvement and activities in Indonesia and in the main that knowledge was limited to the news stories and analysts reports in her chronology. Dr. Juneja did not give appropriate consideration to Barrick's involvement. Exhibits 1289, 1292, 1318, 1319, 1303, 1322, 1313, discussed below, were disclosed by the O.S.C. to the Defence but were not part of Dr. Juneja's chronology which formed the basis of her opinion, Exhibit 800, and on which she depended to conclude that the potential consequences flowed from the particulars.

Transcript: April 18, 2005, pages 9-10, 14-15
Transcript: April 19, 2005, pages 87-90
Transcript: April 20, 2005, pages 50-52
Transcript: April 26, 2005, pages 83, 90
Transcript: April 27, 2005, pages 47, 57-58, 61-62, 74-102

Dr. Juneja was provided with the O.S.C. "*Overview of Allegations*" which had references to Barrick but Dr. Juneja testified that "*it wasn't really something that I considered in forming my opinion...*".

Transcript: April 18, 2005, pages 47-52

Barrick spent significant time, resources and substantial sums of money to obtain a share of the Busang gold deposit and to influence events and the Indonesian government in efforts to achieve that goal.

In Exhibit S12 paragraphs 129-131 the Defence sets out the documentary evidence and the evidence of Peter Munk that the Defence submits establishes Barrick's attempts to influence events in Barrick's favour to obtain a share of the Busang gold deposit.
In commentary on those submissions the O.S.C. sets out in detail the testimony of Peter Munk with respect to that documentary evidence.
Exhibit S12: paragraphs 129-131

The documentary record and the inferences that may be drawn from it, created contemporaneously, with some expectation of confidentiality and not for purposes of litigation deserves weight at least comparable to the weight given that oral testimony.

References in the documents to "*Big Bang*" or "*B.B.*" are references to Bre-X and Busang.

By the fall of 1995 Barrick was using Hany Salaam who "*was a good friend of President's Carter*", a "*trusted business contact*" and "*one of [Barrick's] associates in the region*" "*to use all his local contacts to give [Barrick] more information*" about Bre-X.

Exhibit 1289
Transcript: December 7, 2005, pages 44-45, 66-73

Exhibit S12: paragraph 130

On May 14, 1996 Munk set a fax to Salaam enclosing a report of the May 10, 1996

Bre-X Annual Meeting stating "*Please note page 4, paragraph marked.*"

The marked portion of the report stated:

> The company is in the final stages of acquiring the contract of works for B2, B3, Sable and Sangihe properties. The Contract of Work has been initialed by the Department of Mines. They are now in the final step of acquiring the signature from the President of Indonesia. They anticipate that the signature from the President will be coming within the next two to three weeks.

Exhibit 1292

On May 23, 1996 Neil MacLachlan faxed Munk regarding Big Bang:

> The two new COW applications are still pending and we understand that the review process will be slow.

Neil MacLachlan is an executive at Barrick.

Exhibit 1318

On July 29, 1996 Munk sent a fax to MacLachlan with a copy of the Bre-X July 28 press release. The following line in the press release is underlined and emphasized with an arrow:

> Government approvals of these Contracts of Work are anticipated in the near future.

Beside this line Peter Munk wrote the following line with two question marks:

> ? Is this the message they were given?

The fax reads:

> The last sentence from the enclosed press release referring to COW seems to be a total contradiction to what we have been told on this matter. Either Big Bang

officials do not seem to get the message – or we and they are being told two difference stories! I suspect Mr. Kuntoro's "softly softly" message is not getting through to B.B.

Our friends should use this official release by B.B. – and the obvious contradiction – to make sure that they are getting a clear signal. It would not take much more than a statement from the Ministry that their application for the COW will not be proceeded with unless a deal is completed within the next, say, ten days.

It is obvious that our objective can only be achieved if B.B. has been given the message in a loud and clear voice. It is also obvious that so far this has not happened. If all our friends want this transaction to happen – as we have all along been assured –then they must "grasp the nettle" and make it clear to B.B. where things stand.

It is also obvious that if B.B. were given a clear message we would have a deal done in a quick time frame, on a reasonable and fair basis to everyone involved and clearly serving Indonesia's best national interests.

I would appreciate if you could get the above points accepted by Walid Kurdi and our other friends.

Exhibit 1319

In Exhibit 1319 above, Munk refers to Walid Kurdi. Munk described Walid Kurdi as follows:

MR. MUNK: He is exactly that. He was a long term associate of Mr. Salaam. He is a Jordanian national, very highly placed within the Royal family and very much at home and familiar with the Indonesian and Brunei Malaysian scene as having been either the ambassador of Jordan in that region, or the person – I'm sorry – of the Royal family of Jordan.

MR. GROIA: Do you know if his wife is related to any of the royalty of Jordan?

MR. MUNK: Indeed that is a correct statement. His wife, Princess Royale – I think that's her name-was at that time the sister of the late King Hussein.

MR. GROIA: And if you were already using Mr. Salaam and Gulf Mineral Resources, why did Barrick ask them to seek the assistance of Mr. Walid Kurdi?

MR. MUNK: I don't know whether that's a correct description, Mr. Groia. I think that we were trying to expand our contacts continuously. The stakes became bigger. The complications became more complex. And Mr. Salaam himself recommended that we broaden our reach by bringing in people who are very highly regarded by the local establishment.

...

MR. MUNK: And so Mr. Kurdi was an outstanding advocate for our cause and I, even today, I am grateful to him for what he has done for us. He is an outstanding businessman, outstanding character and personality who is currently Chairman of the Jordanian Airways.

Transcript: December 7, 2005, pages 137-138, 147

On September 5, 1996, Munk wrote to Kurdi:

This is to confirm our arrangements as finalized this morning:

1. In recognition of your services over the past year and your expenses incurred in that connection, we shall pay you US$5 million on acquiring a majority position in the Busang C.O.W. in Indonesia.

2. In recognition of your accepting the position of exclusive adviser to our Indonesian company in case we are the operators of the Busang project, we will pay you a further US$5 million within six months of the final C.O.W. award.

3. You will enter into an agreement with us as adviser and consultant to us in connection with our Indonesian activities. Your remuneration will start at US$1 million per annum, escalating 5% annually, plus all your out-of-pocket expenses.

4. You have agreed to act exclusively for Barrick in the mining industry and keep all information on other matters on which you are consulted totally confidential and only for your own use, except when mutually agreed.

If the above reflects fully our understanding, I would appreciate your counter-signing a copy of this letter.

In closing, I wish to thank you for your outstanding assistance and support over the past year in our activities in Indonesia.

Exhibit 1299

On September 20, 1996, Munk wrote to Salaam:

> Dear Hany:
>
> Further to our telephone conversation, we hope to be able to get some help from our friends in Jakarata in the form of a statement. The reasons for the statement to be made could be, say, a response to the Financial Times article of September 18 in which Guzman claims, on behalf of Bre-X, to own the three contiguous COWs. A letter could even come from the Embassy stating that:
>
> > "Bre-X has not been granted the COWs; in fact, due to certain irregularities, a Committee has been formed under the Inspector General of Indonesia to review Bre-X's application."
>
> As an alternative, someone from the Ministry in Jakarta could issue a follow up statement to the Reuters news report of September 17 quoting the Director of Mining Industry Development, Mr. Rozik Soetjipto, and saying that:
>
> "In line with the new monitoring policy, a Special Committee has been formed by the Minister of Mining under the Inspector General to investigate irregularities in connection with the Bre-X application for the COWs."
>
> Even if we can't induce the government to make such statements – which, of course, should be made to prevent damaging Indonesia's capital market reputation by allowing innocent investors to buy securities without full knowledge of the facts – it could be arranged with an official of the Ministry (and Walid Kurdi suggested Adrian Ganto) to respond to a telephone question by a Canadian journalist along the same lines as quoted above.
>
> We also continue to believe it would be helpful to have the KPs canceled as that may force Bre-X to disclose that their SIPP has been canceled.
>
> Just some thoughts from us. Could you give me your views at your convenience?

Exhibit 1303

On October 4, 1996 the Globe and Mail published an article about Bre-X titled: "*Bre-X hits snag in Indonesia. Officials probe allegations miner left out partner in Busang property, broke law on reporting acquisition.*"

The article, Exhibit 131, contained information very similar to the suggestions made in Exhibit 1303, the September 20, 1996 letter above from Peter Munk to Hany Salaam.

Exhibit 1303, the letter, suggests different ways of putting out adverse information about Bre-X. One such suggestion is "*it could be arranged with an official of the Ministry...to respond to a telephone question by a Canadian journalist...*"
Exhibit 131, the news story, states: "*The Indonesian Ministry of Mines and Energy in Jakarta provided answers to a series of questions posed by the Globe and Mail*".

Exhibit 1303 suggests: "*A letter could even come from the Embassy...*" .
Exhibit 131 states: "*The answers were translated and forwarded by Mr. Ames...*" "*vice-consul for investments with the Indonesian consulate general in Toronto.*"

Exhibit 1303 suggests the kind of adverse information that could be disclosed about Bre-X. The suggestions in Exhibit 1303 include: "*Bre-X has not been granted the COWS; in fact, due to certain irregularities, a Committee has been formed under the Inspector General of Indonesia to review Bre-X's application.*"
Exhibit 131 announces very similar adverse information: "*Authorities in that country [Indonesia] have launched an inquiry that will examine an ownership dispute over a slice of its Busang property*" "*...[T]he Indonesian government said yesterday that Indonesia's President will not sign the license [Contract of Work] for Bre-X until the outstanding issues are resolved.*"

With respect to Exhibit 1303, the September 20, 1996 letter above from Peter Munk to Hany Salaam, Sharwood testified:

> MR. SHARWOOD: This correspondence that you showed me is certainly enlightening in the context of your question and suggests to me that Barrick was orchestrating the press.

Transcript: May 10, 2005, pages 51-52

With respect to Exhibit 1303, Ridwan testified:

> MR. MAHMUD: First, Barrick would like to see a statement made by the Minister of Mines that contracts of works of Busang. It's not going to be awarded to Bre-X. That is the key of this letter it seems to me because to respond to what Financial Times article on September 18. It is actually the right of the Ministry of Mines to respond. No one can dictate the Minister, especially the Director General who are in charge in this Contract of Work. And he also said, suggests, or not in this letter, if I understood, it will be helpful to have the KP's cancelled as they may force Bre-X to disclose that their SIPP has been cancelled. It seems to me that the gentleman who wrote this letter does not know the mining procedure, even does not know the mining law in Indonesia. It's not very easy for the Minister to cancel the KP's because the KP – first, it is a national company and every national company also have their backing, what we call it, in the Parliament. And also came, that fellow who owns this KP is also come to that particular area. Certainly the local Government will support him. I doubt if Barrick got the Contract of Work he will get support from the local people. He might be sabotaged. That is something that the sender of this letter does not realize. And it seems to me, since money play an important role, that everybody can be bought. That is, again, my personal philosophy. There is a rule that has to be obeyed and there is the ethics that have to be obeyed. I feel sorry to read this letter. A big company such as Barrick can interfere in what the Government should do or the Government should not do. Barrick is not a replacement of the Colonial Dutch Government. Plainly speaking, I am a little bit emotional to read this letter because it disturbs the structure, the procedure that we have established for more than 15 years just because of this guy. I don't care whether he is the richest man in the world. I don't care. But this is certainly interfere with the Indonesian Government's policy and also interfere with the rule in law that can be passed if you have money. I again reiterate, Indonesia is not the Banana Republic. There is 220 million people there. The area cover more than 2 million square kilometers. It's a big country. So please understand my feeling. Thank you.

Transcript: November 29, 2005, pages 37-38

As noted above, in Exhibit 1319 the letter from Munk to MacLachlan there is a reference to Dr. Kuntoro: "*I suspect Mr. Kuntoro's 'softly softly' message is not getting through to B.B.*"

Then on October 30, 1996, MacLachlan wrote Munk:

> The Minister of Mines has signed the Decree withdrawing the majority of the important powers and authority which he had previously delegated to the Director General of Mines (Dr. Kuntoro). The change is effective 17th October 1996.
>
> DELETED
>
> It is understood that the Ministry of Mines and Energey will shortly be calling a meeting of COW applicants to advise them of new procedures and the method by which the Department will be run in future and in particular, how exploration and mining applications will now be processed. Thus this news will soon become widely known, at least, within the mining community. A number of other foreign mining companies will have heard the news today.
>
> As I understand it, all decisions taken by Kuntoro prior to 17th October will stand but those made after that date will require the endorsement of the Minister.
>
> A copy of the signed Decree together with an English translation is attached.
>
> The initiative, which led to this development, came from our JV partner and Airlangga who some time ago expressed concern to the Minister at the degree of power which Kuntoro had been given and in the way that such authority was being exercised.
>
> I would recommend that you take this opportunity to encourage the local team by speaking to Walid Kurdi and congratulating him on the success of their efforts.

Exhibit 1322

On November 5, 1996, Munk wrote Kurdi:

> Further to our telephone conversation this morning, I have agreed to forward to you an advance as against the $5 million payment otherwise due to you under our letter agreement in the event Barrick acquired a majority position in the Busang

> COW in Indonesia. I am making this advance at this time based upon your report as to the status of the selection of Barrick Gold Corporation as the operator of the Busang Project. It is our mutual understanding that should the report prove to be incorrect, you will promptly return this advance to Barrick.
>
> As we discussed, this advance is expressly conditional on your certification that none of the funds will be utilized in any manner that contravenes the laws applicable to Barrick's operations, including, particularly, the United States Foreign Corrupt Practices Act. In view of the very high public profile of this matter (see enclosed articles), we must be especially vigilant that we can demonstrate that no funds advanced to our various Indonesian partners be applied in contravention of these laws. Please note your agreement and certification concerning the use of this advance in the space below.
>
> Again, please let me express our appreciation for the enormous efforts you have given during the past year as Barrick seeks to become established in Indonesia. Your assistance in presenting our credentials and your advice concerning our activities in Indonesia has been invaluable. We look forward to continuing to work with you on this matter.

Exhibit 1313

After being shown copies of what later became Exhibit 1319, 1299, 1303 and 1322,

Sharwood gave the following evidence:

> MR. RICHTER: And does this document and the other documents I have referred you to affect your view as to whether it was Merukh or Barrick who may have been behind the SIPP cancellation?
>
> MR. SHARWOOD: I can only repeat the answer I gave to a previous question along those lines. It is clear from the materials you are showing me that Barrick was involved. Whether or not they were in association with Merukh in some way, I have no way of telling.

Transcript: May 10, 2005, page 55

There is no direct evidence that Barrick was "*behind the SIPP cancellation*". There is support for Sharwood's opinion "*that Barrick was involved*" by implication from Exhibit 1303 where it is stated *"[w]e [Barrick] also continue to believe it would be helpful to*

have the KP's canceled". Exhibit 1303 implies the ability to make something happen, "*to have the KP's canceled*".

Exhibit 1321 is a letter from former President George Bush to President Suharto dated September 20, 1996. Exhibit 1324 is a letter from former Prime Minister Brian Mulroney to President Soeharto dated Janaury 24, 1997. Exhibits 1317, 1320, 1323 are other letters from Brian Mulroney to the Indonesian Minister of Mines and Energy.

FINDING

This evidence of Barrick's ability to influence events and the Indonesian government raises a reasonable doubt that the "*potential consequences*" flowed from the particulars and not from Barrick's substantial influence.

Dr. Juneja's opinion of materiality is dependent on those "*potential consequences*" being the result of the particulars and not the result of other factors.

Indonesian Government

In addition to giving insufficient weight to Barrick's involvement in the "*potential consequences*" discussed above, Dr. Juneja comes to doubtful conclusions about the relationship between the particulars, the Indonesian government and the potential consequences.

In their closing oral submissions the Defence states:

> MR. GROIA: ...when you are asked to assess the materiality of these five particulars and their consequences you have to do so against the context and the understanding that at the end of the day none of it really matters.
>
> ...
>
> MR. GROIA: ...especially in a country like Indonesia where I think I would say there is really only one material event, what was Suharto going to do. At the end of the day he was going to do whatever he wanted to do...

Transcript: August 25, 2005, pages 65, 38-39

Dr. Juneja does not agree with the Defence position. Dr. Juneja's opinion was that the consequences were related to the particulars in that the particulars created the opportunity for the Indonesian government, which it otherwise would not have had, to obtain a share of Busang and to impose on Bre-X the terms of how Busang was to be divided with a reduced share for Bre-X.

Dr. Juneja's evidence, in part, was a follows:

> MR. GROIA: So if we were to add to your report one additional assumption, that assumption being that the only fact that really mattered in this whole circumstance was what President Suharto felt like doing, then I take it that that assumption would contradict and perhaps neutralize the five assumptions which are to the contrary. Is that a fair assessment of your report?
>
> DR. JUNEJA: No.

Transcript: April 26, 2005, page 28

> ...
>
> DR. JUNEJA: ...It appears that certainly as news regarding the particulars was revealed to the market, a consequence of that was indeed the Government of Indonesia's involvement in putting at risk whether or not the COW would be approved, when it would be approved, and under what conditions, and so while in

the report I used that as an assumption, I think an independent reading of the materials would support that as well.

MR. GROIA: But you made that statement, I take it, without knowing what was going on behind the scenes.

DR. JUNEJA: In terms of what was going on behind the scenes, my knowledge of that is simply based on the press reports and analyst reports.

Transcript: April 18, 2005, pages 13-14

...

MR. GROIA: Did you have to look at the political realities of Indonesia as part of your event study?

DR. JUNEJA: What I had to look at was the political realities insomuch as any information about the Indonesia Government was reported in the publicly available news sources that I reviewed.

Transcript: April 19, 2005, page 48

...

DR. JUNEJA: They are connected in the following sense. There are five particulars that are listed on page 2 of my report. News that directly appears to reveal these particulars starts coming out on September 27th, 1996. At the same time as these particulars start being revealed directly to the market, a series of events is put into motion that appears to relate to this news which includes events that jeopardize the likelihood of Bre-X securing a legal interest to the gold and the extent to which they could profit from the gold, as well as the likelihood of their obtaining a COW. As time goes on news is revealed which relates directly to the five particulars in terms of information that comes out about the dispute with Merukh; the way in which Bre-X obtained its 80% interest; news about the cancellation of the SIPP and so forth. But at the same time there is also news coming out about things that are happening at the time as a result of these revelations and as a result of perhaps giving the Indonesian Government some ammunition or some basis with which to take the negotiations with Bre-X into a certain direction. So in reviewing the news stories that were coming out at the time, I took all of that into account.

MR. GROIA: Would you agree with me that the only thing that really mattered that could possibly affect Bre-X's title or the Contract of Work is what President Suharto decided to do?

DR. JUNEJA: I'm not sure what you mean by that in that President Suharto was the ultimate decision-maker. But in terms of the process whereby the decision would be made and the bottom line would be negotiated, there were certainly events that were happening that would be conducive to the Indonesian Government and to Suharto taking things in a different direction, or emphasizing certain things in terms of the process. There were various events that were occurring at the time.

Transcript: April 26, 2005, pages 25-27

...

MR. GROIA: So if, for example, hypothetically, Barrick had bribed the Government to launch the inquiry, what was reported in the newspaper was simply an explanation or an excuse for the inquiry. A real reason would have been the bribe in my hypothetical. Right?

DR. JUNEJA: If Barrick had bribed the Government and the alleged particulars are actually just something that the Government can use to follow a course of action and to confuse the issue but to make different things happen then they would have done otherwise, it's still possible that there are things going on behind the scene that aren't reported. What I am assessing and looking at is what the market was perceiving with regard to the particulars and their consequences.

Transcript: April 26, 2005, page 90

...

MR. GROIA: But again, I take it you would agree that the greediness, if I can call it that, of the Suharto family would be facts that would be unrelated to the particulars?

DR. JUNEJA: I think that the – if you are asking me to assume that the Suharto family is greedy, in and of itself that's unrelated to the particulars to the extent that that interacts with things that happen that are related to the particulars and that allow the Suharto family to undertake certain actions they might not have undertaken otherwise, then those may well be related to the particulars and maybe part of their greediness.

MR. GROIA: Or their greediness may have pre-existed and the issues related to Bre-X could have simply provided them with an excuse. Is that possible?

DR. JUNEJA: It's possible that the issues related to Bre-X may have provided them with an excuse and a method by which to undertake certain things that they may not have undertaken otherwise.

Transcript: April 26, 2005, pages 111-112

...

DR. JUNEJA: No. What I'm telling you is that once it became revealed to the market or apparent to the market that there was some strong probability that Bre-X had failed to comply with contractual obligations owed to the Indonesian Government, that Bre-X had not secured its interest in the property known as Busang I, that Bre-X had misled the Indonesian Government respecting the acquisition of its 80 percent interest, that there was some probability that they had unjustly excluded PT KG, PT SAP and/or Jusef Merukh from Busang II, and that PT KG, PT SAP and/or Jusef Merukh had issued a complaint to the Indonesian Government, and that the Indonesian Government had cancelled the preliminary SIP, that a series of events unfolded where the Indonesian Government started negotiating with Bre-X and demanding various conditions be met, and that over this six month time period, the share of the mine that Bre-X was ultimately going to have access too, was something that kept changing in terms of the perception of the market, and that this event on March 6th was that it was recorded on March 7th that on March 6th rumours had reached the market that whatever share had been settled on, was changing yet again.

Transcript: April 20, 2005, page 58

...

DR. JUNEJA: The answer to that question would be a repetition of the answer to the question that you asked me a bit earlier, and I think you may have asked me the same question, which is to the extent that Bre-X may have misled the Indonesian Government was one of the factors that began to be revealed to the market in October of '96, and that resulted in subsequent events whereby the Government of Indonesia got very heavily involved in determining what share of the market they would ultimately have. The rumours are simply a consequence and a follow on to that series of events.

Transcript: April 20, 2005, page 59

...

DR. JUNEJA: No, I'm not the only person who does that. I think that if you have any sort of professional experience and training in understanding and reading news related to a company, and if you were to read the chronology of events and the other publicly available information, it would be clear that any news that is a follow on to the events that occurred with the Government of Indonesia's involvement in determining what share of Busang II Bre-X would ultimately end up with, would be related to the consequences of the particulars.

...

DR. JUNEJA: Well, I think the question becomes once there is an official complaint filed with the Indonesian Government and there is a suggestion that Bre-X may have done things that are consistent with the particulars, it changes the backdrop in terms of what the Indonesian Government can claim and how the negotiations are going to proceed. At least that's what is revealed in the publicly available information.

Transcript: April 20, 2005, page 61

Dr. Juneja testified she reached her conclusion by reading the chronology and other publicly available information. Some of those news stories found in the chronology are briefly reviewed below:

10/4/96, Reuters News Service, Exhibit 800B, page 295

"The basic thing about this is you've got a C$5.5- or C$6-billion ($4 billion or $4.4-billion) ore deposit sitting right there and people want a part of the pie. That's what it comes down to," Fowler said.

10/5/96, The Globe and Mail, Exhibit 800B, pages 299-300

A number of money managers said they knew there were political risks involved with Bre-X's position in Indonesia. "We heard there was a risk, that there were a few things getting in the way of a COW," said John Zechner of Toronto-based J.Zechner & Associates Ltd." And there were some rumours that the Indonesian government wanted them to have a partner before it actually got signed, because it was such a major mining project. Maybe that's why [Bre-X] offered to sell more than 25 per cent [of the Busang deposit]."

...

Greg Bay of money manager M.K. Wong Associates Ltd. in Vancouver suggested that the Indonesian government and some of its rulers might be eager to get their hands on a slice of the ore body.

10/28/96, Reuters News Service, Exhibit 800B, pages 342-343

CANADA: BRE-X JOINS FORCES WITH SUHARTO'S SON, STOCK SOARS.
By Heather Scoffield
TORONTO (Reuter) – Canada's Bre-X Minerals Ltd., moved on Monday to resolve a dispute over its huge Busang gold discovery in Indonesia, forging an alliance with a company controlled by the eldest son of Indonesia's President

Suharto. "This is an important first step to the resolution of Bre-X's problems," said gold analyst John Ing of Maison Placements Canada.

...

"Having an arrangement with this fellow is a bonus," said Ing, the analyst. "The key in Indonesia is who you know." "They seemed to have teamed up with a partner with high standing," said mining analyst Michael Fowler of brokerage Levesque Beaubien Geoffrion.

10/28/96, Maclean's, Exhibit 800B, page 344

Some analysts say Bre-X is being blackmailed: it cannot mine the claim until it receives a licence from Indonesian authorities.

10/28/96, The Globe and Mail, Exhibit 800B, pages 348-350

Bre-X Minerals Ltd. has offered the son of Indonesia's President a stunning deal worth hundreds of millions of dollars to help settle its troubles in the Southeast Asian country. Shares in Bre-X soared almost 17 per cent yesterday after the Calgary-based company announced it has struck a strategic alliance with a private Indonesian company, PT Panutan Duta, which is controlled by President Suharto's eldest son.

...

Analysts were quick to peg the memorandum of understanding with the Indonesian concern as effectively buying off Indonesia's government, and expected Bre-X now to settle its troubles quickly, perhaps by the end of the week. "If you have any trouble understanding what it all means, I assume you also believe in the tooth fairy," Dough Leishman of Yorkton Securities Inc. said in a commentary to investors. "Welcome to Indonesia."

...

Asked weather it would be easier for a foreign company to get a COW if it had Mr. Suharto's son on board, Chaidir Siregar, head of the economics section at the Indonesian Embassy at Ottawa, replied: "It might be, yes. I think it's not only in Indonesia, it's all over the world. If you are very close to the power, it's easier for you. This is –what do you call it? –the nature of business."

...

"The company has finally realized that doing business in Indonesia is not like doing business in Canada," said an analyst close to the company and who, like others, spoke on condition that his name not be used. "The deal is better than I could have hoped for." Added a second analyst: "I think that Bre-X is dealing with the people now that they should have been dealing with in the first place. I think that's pretty clear. "They did everything legal, but they didn't do it under Indonesian customs. They missed talking to some very key people, and that's why

we ended up with the roadblock that we did. It's family-run over there."

...

He predicted –as did another analyst – that an "aggressive" Barrick Gold Corp. "is not going to lose this one." In his view, Bre-X will soon disappear from the picture entirely, in favour of the Suharto family and Toronto-based Barrick.

10/29/96, Dow Jones International News, Exhibit 800B, page 351

In recent years, many foreign companies have teamed up with Suharto's children. (The 75-year-old leader has three sons and three daughters, all of whom are in business.)

10/30/96, The Financial Post, Exhibit 800B, page 355-356

DEAL CAST SHADOW ON BRE X: US$40M to Indonesian president's son may be seen as bribe by potential partners that firm needs to develop huge deposit.

...

"What is going on in this deposit is clearly tainted," said Wesley Cragg, a professor of business ethics at York University in Toronto.

...

However, others say companies conducting deals outside North America must get used to the fact that business practices are often very different in other countries. "When in Rome, learn to speak Latin," one analyst said. Another said the advantages of acquiring an asset as potentially rich as Busang may override concerns about engaging in joint venture deals with powerful Indonesian families.

11/1/96, Reuters News Service, Exhibit 800B, page 360

Barrick Gold Corp. said on Friday that its association with a construction company run by the eldest daughter of the Indonesian president had nothing to do with the intrigue surrounding Bre-X Minerals, Ltd.

11/2/96, The Globe and Mail, Exhibit 800B, pages 365-368

If David Walsh and John Felderhof were not already so rich as to be practically above suspicion, more complaints might be heard about their offhand approach to corporate disclosure and insider trading. And if the situation were not so funny, more outrage might be expressed about the classic Third World shakedown the two new multimillionaires and their Calgary-based company have just gone through in Indonesia.

...

It was their fate to make one of the great gold strikes of modern times under the nose of one of the world's most famously corrupt governments, and to be none too quick to realize what they were up against.

...

Rather, it seems to have been a case of Mr. Walsh and Mr. Felderhof wondering why it was taking so long to get their mining permits firmed up, gradually realizing they would have to pay somebody, and then trying to figure out whom. Their search ended this week, and the payoff – er, consulting fee – is breathtaking.

...

The person to do business with turned out to be Sigit Harjojudanto, eldest son of President Suharto, the iron-fisted, sticky-fingered ex-general who has ruled the world's most populous archipelago for more than 30 years. Mr. Harjojudanto's job is to deliver the mining permits, signed and sealed by his father's government. If he does so, payments to a company he controls could easily exceed $ 1-billion by the time the last ounce of gold is extracted.

...

In Indonesia, the Suharto family has its hands in just about every facet of business, including toll roads, oil refineries, lumber, satellites, agriculture and hotels. The government has awarded billions of dollars in infrastructure contracts to companies with ties to the President's six offspring, making them fabulously wealthy. The family compact is so strong that critics have called Indonesia "the land of the rising sons and daughters." The President's late wife, Tien Suharto, was known as "Madame Tien Per Cent," for her habit of taking a cut of major deals. As it happens, Bre-X agreed to give up 10 per cent of its massive gold find, plus other incentives, for Mr. Harjojudanto's assistance. "You're dealing with a different type of business environment," said William McKee, president of Megastar Ventures Ltd., a Vancouver-based company with a 50-per-cent stake in a small property near Bre-X, "and if there's any success at all, it often catches the attention of the elite."

...

Foreigners who do business in Indonesia often report unexplained delays and bureaucratic flip-flops. "We thought we had one great, wonderful permit...but then we discovered we didn't have it," said John Pollock, president of Jonpol Explorations Ltd. of Toronto. "They say there was an oversight by the computer. "Faced with delays, companies often turn to well-placed Indonesians for assistance. Texas T Resources Inc. of Vancouver hired a retired Indonesian brigadier-general as a consultant. "It's definitely helpful," said Russ Bissett, Texas T's public relations chief. "Otherwise, you're dealing blind."

...

"I've never had to bribe anyone," said Peter Howe, whose Toronto-based consulting company, ACA Howe International Ltd., has been active in Indonesia since the 1970's. It is not entirely clear what happened to Bre-X, he said, "but something happened behind the scenes and some company got to somebody in Indonesia and stirred all this up...I guess if you're being clobbered by people that

are claiming things that aren't true, then you need the support of the government, and you can't get much higher than the President's son, of course."

11/25/96, Dow Jones Asian Equities Report, Exhibit 800B, page 419

Indonesia's Minister of Mines and Energy, I.B. Sudjana, has told prospective partners Canadian companies Bre-X Minerals and Barrick Gold Corp that the government would be receptive to a 10% percent stake in what is now being touted as the world's biggest gold mine in the hinterland of East Kalimantan.

...

The sources say it was at the same meeting Sudjana laid down the government's position that Barrick should acquire a 75% shareholding in the mine, leaving the remaining 25% in the hands of Bre-X and local partner Panutan Duta, the company owned by President Suharto's eldest son, Sigit Harjojudanto. In an intriguing contest between two members of the presidential family, Barrick's key ally is Sigit's older sister, Siti Hardijanti Rukmana, better known as Tutut, who is perhaps the most politically savvy of the Suharto children.

11/25/96, Dow Jones International News, Exhibit 800B, page 419

In asking for their 'consideration,' Sudjana is said to have reminded the two Canadian executives of the precedent set by Louisiana-based Freeport-McMoran Copper & Gold, which offered the government a 10% stake in the company's copper and gold mine back in the early 1970s.

11/26/96, Reuters News Service, Exhibit 800B, pages 423 - 424

Gold giant Barrick Gold Corp. is negotiating with Canada's Bre-X Minerals Ltd. to gain control of Bre-X's huge Busang gold discovery in Indonesia, the two companies said on Tuesday. The companies were negotiating under the "guidance" of the Indonesian government, which asked Bre-X to form a joint venture with Barrick, Bre-x said.

...

"This is a result of Barrick working very hard behind the scenes to circumvent Bre-X's sale process," one analyst said of the news.

...

To satisfy Indonesia, Bre-X would keep 25 percent of its stake and 75 percent would go to Toronto-based Barrick, the world's third largest gold producer. Bre-X said that the Indonesian government "would appreciate it if the parties could consider a 10 percent participation being given to the Indonesian government."

The Indonesian government wants Barrick and Bre-X to reach a deal by December 4 or else the government "will take steps to prevent a delay in the development" of Busang, Bre-X said.

...

With the Indonesian government guiding the Busang negotiations, Bre-X's powers to negotiate a favorable deal were curbed, analysts said.

...

Given the possible questions that may be raised over how Barrick obtained this special status, it will be essential that they are viewed as treating Bre-X shareholders fairly in any negotiations going forward," said an analyst who did not wish to be identified.

12/4/96, The Toronto Star, Exhibit 800B, page 484

"The only person who knows what's going to happen is the president of Indonesia," said Kevin Klassen of BPI Mutual Funds Inc. in Toronto.

...

"The government will decide as to the divvying up of the ore body."

12/13/96, The Financial Post, Exhibit 800B, page 587

Not much is clear in this comedy of errors. But one thing is: the matter will be resolved to the ultimate satisfaction of Suharto and his family.

12/16/96, Dow Jones International News, Exhibit 800B, page 607

Chorny fears the tiny mining firm is being forced into an unfavourable deal with Barrick, whose heavyweight political allies include Suharto's eldest daughter, Siti Hardijanti Rukmana, a prospective partner in the Busang venture, Bush and another international adviser, former Canadian Prime Minister Brian Mulroney. The Indonesian Government has imposed an ownership formula under which Barrick will effectively get 70% of the mine, Bre-X 20% and the Government 10%.

12/16/96, Dow Jones News Service, Exhibit 800B, page 607

Shareholders of embattled Bre-X Minerals Ltd. (BXMNF) have retained prominent Houston law firm Baker & Botts to represent their interests in the company's struggle with Barrick Gold Corp. (ABX) for control of Indonesia's giant Busang gold deposit. The move appears to raise the political stakes for former U.S. President

George Bush, an "honorary adviser" to Barrick's board of international adviser who has been under fire from American investors for endorsing a deal that precludes an open bidding process. One of the law firm's owners is James Baker, Bush's secretary of state.

12/17/96, The Financial Post, Exhibit 800B, page 611

About three weeks ago, the Indonesian government ordered Bre-X to cut a deal giving Barrick 75% of Bre-X's stake in Busang. Indonesia's state-owned tin mining company, PT Tambang Timah, is expected to take 10% of Busang, which is estimated to host at least 57 million ounces of gold. "This is a shotgun wedding if there is going to be one," said Yetter, who declined to say what legal strategy he might pursue.

...

However, he said final details won't be announced until the agreement is approved by the Indonesian government. "It's their law and their gold," said Borg, adding it may take several days for Indonesia to approve the complex deal.

1/15/97, Reuters News Service, Exhibit 800B, pages 683 - 685

Until this week, it seemed Barrick was the only company with a realistic chance of grabbing a share of the project. In November, the Indonesian government told Bre-X, which discovered the Busang gold find, to form a joint venture with Barrick and present their deal to the government for approval. A proposal was assembled last month and awaits the government's blessing. But the Indonesian government's edict spooked the international mining community and angered many Bre-X shareholders who felt their company had been forced to negotiate with a gun to its head. Some Bre-X shareholders hired high-profile lawyers to ensure their interests were protected in any eventual deal. Meanwhile, the Barrick-Bre-X arrangement spawned rampant rumors in the mining and investment communities, prompting observers to ask why [the] Busang deposit was not auctioned to the highest bidder, how Barrick acquired such a privileged position and who was calling the shots in hammering out a final deal. Barrick maintains it was chosen for its experience operating large gold mines, its environmental record and its strong financial position. Others cite Barrick's alliance with the influential daughter of Indonesia's President Suharto, and Barrick's high powered advisory board, which includes former Canadian Prime Brian Mulroney and former U.S. President George Bush.

...

Most observers agree on one thing: Indonesian President Suharto and his close officials and advisors hold the key to any conclusion of the Bre-X saga. "I think Placer and Barrick are waiting for some sort of signal," said Ing. "I think it's a waiting game."

...

Analysts said Indonesian officials were probably concerned about tarnishing their reputation in the international investment community and were seeking a way to allow other companies to bid on Busang without losing face.

1/15/97, The Globe and Mail, Exhibit 800B, pages 685- 687

Hasan may be Busang swing man. Suharto's pal said to be pushing for auction on rights to develop huge Indonesian deposit.
A golfing buddy of Indonesian President Suharto appears to be at the centre of the latest round of manoeuvring for Bre-X Minerals Ltd's massive Busang gold deposit.

...

Meanwhile, Mr. Hasan has acquired a stake in an Indonesian company that owns 10 per cent of the deposit. Analysts say he is encouraging the Indonesian government to drop the Barrick arrangement and open the bidding to more companies. Mr. Hasan's encouragement is believed to have led Vancouver's Placer Done Inc. to announce its $6.2 –billion merger proposal with Bre-X yesterday. Placer Dome's proposal includes a 40-per-cent share in the deposit for an array of Indonesian players, including the government and Mr. Hasan's company. That compares with the 10-per-cent cut the Indonesian government would receive under the Barrick arrangement.

...

Other shareholders say both companies are foolish to get into a bidding war over the deposit. "These companies must be desperate for reserves to bid for this thing in a corrupt nation said Harry Bingham a portfolio manager at Van Eck Associates in New York, which holds large blocks of shares in Barrick and Placer Dome. "Why are they taking the risk? They are just outbidding each other with Suharto."

1/15/97, The Toronto Star, Exhibit 800B, page 695

The rumble in the Indonesian jungle is all about who really controls a gold deposit which at current prices may be worth as much as $44 billion. It's also about a clash of cultures, laws and an object lesson in the perils of Third World politics, where personal and national interests combine in complex ways.

...

Complicating things is that Indonesia, which has been ruled by President Suharto and his family since to took power in a 1965 coup, is also considered one of the most corrupt countries in the world. That is the assessment of Transparency International, a Berlin-based organization, that compiles a corruption index based on surveys of international business executives.

2/14/97, The Financial Post, Exhibit 800B, pages 816-817

But only a few high-level officials in the Indonesian government know the details of any Busang deal or whether it is acceptable to the Indonesian ruler, President Suharto.

...

As a result, approval from Hasan is widely seen as vital before any deal is sent to Suharto for final approval. Placer Dome, among other observers, believes an unofficial, behind-the-scenes auction may well be taking place within the Indonesian government.

2/18/97, The Financial Post, Exhibit 800B, page 859-860

As expected, the deal calls for Bre-X to keep a 45% stake in Busang, with Freeport getting 15% of the find and the right to act as mine operator. Under the agreement, two Indonesian companies pick up 30% of the mine. The Indonesian government will get 10%.

...

"I think the whole thing smells," said a Toronto mining executive, adding the value of Bre-X's stake has been reduced by the fact that it doesn't get to operate the mine.

...

Although the Indonesian government did not express a view on the deal yesterday, it is expected to endorse the plan soon. That's because one of the Busang saga's key players, Mohamad "Bob" Hasan, is clearly backing the arrangement. Hasan controls the two Indonesian partner companies –PT Askatindo Karya Mineral and PT Amsya Lyna – and is a trusted confidante of Indonesian President Suharto. Hasan is thought to have brokered the Bre-X agreement with Freeport.

3/1/97, Canadian Business, Exhibit 800B, pages 939-940

We sent senior writer Brian Hutchinson to Indonesia in December to sort out the confusion. Hutchinson, who interviewed senior government officials, top Canadian mining executives and other insiders, discovered that Bre-X's only error was in being outmaneuvered. Hutchinson found that Barrick had begun lobbying top Indonesian officials early in 1996. Former US president George Bush, a member of Barrick's international advisory board, and former prime minister Brian Mulroney, a Barrick director, had both pressed Barrick's case with Indonesia. What's more, Barrick had entered into an alliance with the eldest daughter of Indonesia's President Suharto, the former army strongman who has ruled the country for 31 years. Barrick also struck deals with the children of other top Indonesian government officials. Bre-X's David Walsh had gotten lucky; Barrick's Peter Munk was being smart. Or so it seemed. But Hutchinson, whose

> remarkable story about the struggle for control of the goldfield begins on page 26, also discovered that the controversy had divided Indonesia –government technocrats who had administered a fair and transparent regulatory system for the mining industry for years were outraged that their efforts were being overturned to accommodate the greed and ambition of political figures. They were deeply concerned that desperately needed foreign investment and expertise would begin to flow away from Indonesia. "Of all the people I met in Indonesia while researching this story, the technocrats left the deepest impression," says Hutchinson. "One man was on the verge of tears as he sat in his office and described how three decades of solid mining law had been undermined in a matter of weeks, thanks to a handful of local politicians and some shortsighted Canadian businessmen." Now, it seems, fair play and an underdog's determination have won the day. Just hours before this issue went to press, Bre-X announced the creation of a new join-venture company that will develop and operate its Indonesian properties. Conspicuous by its absence is the name Barrick. Instead, Bre-X, its two Indonesian partners and the Republic of Indonesia are teamed with Freeport-McMoRan Copper & Gold Inc. of New Orleans.

These and other news articles in the chronology are hearsay and are not proof of their contents and are not admissible evidence of the Defence position that the particulars and their alleged consequences did not matter and that that the only thing that mattered was "*whatever [President Suharto] wanted to do.*"

Transcript: August 25, 2006, pages 38-39

That is not to say that there was no other evidence that Barrick had the ability to influence events and the Indonesian government; that Bre-X was being influenced by the Indonesian government to enter into an agreement with Barrick; that Placer Dome made an offer for involvement in Busang that was more profitable for Indonesian interests (40%) than the Barrick proposal (10%); that at the end Barrick and Merukh received no share of Busang and that at the end Busang was divided between Bre-X (45%), Freeport (15%), Indonesian government (10%), and Indonesian companies including Hasan (30%).

FINDING

These news stories on the other hand are very relevant to Dr. Juneja's opinion, because her opinion that the consequences flowed from the particulars is based on these and other similar news stories in the chronology.

These stories, on which Dr. Juneja depended, raise a reasonable doubt that the Indonesian government's involvement in dividing up Busang would have been any different if not for the particulars and therefore there is a reasonable doubt that the consequences flowed from the particulars. This in turn raises a reasonable doubt that Dr. Juneja's opinion assists in proving that the particulars are material facts given that her instructions from the O.S.C. was to test for the particulars and their consequences and given that Dr. Juneja did not disentangle the particulars from their alleged consequences.

Exhibit 800A
Transcript: April 19, 2005, pages 40-41

Dr. Juneja's opinion, based on reading the chronology, was that the consequences were related to the particulars in that the particulars created an opportunity for the Indonesian government, which it otherwise would not have had, to obtain a share of Busang and impose the terms for the division of Busang. An equally valid conclusion based on the reading of the chronology was that the particulars were not relevant to the Indonesian government's conduct and that what was relevant was that the Indonesian government wanted a share of what was potentially the world's largest gold deposit.

Corroboration for this conclusion may be found in what actually happened at the end. Bre-X's interest in Busang I was not relevant. Bre-X's statements to the Indonesian government about that interest was not relevant. The cancellation of the SIPP was not relevant. Merukh's claim and Merukh's complaints to the Indonesian government were not relevant. Merukh did not receive a share of Busang. Bre-X received a share of Busang although a reduced share to allow for the 40% that went to Indonesian interests.

Dr. Juneja did not have the advantage of also having considered the Barrick documents discussed above when she read the chronology and concluded that the potential consequences flowed from the particulars because the Barrick documents were not part of the chronology. A reading of the Barrick documents would have put the news stories reviewed above into a different light and raised a reasonable doubt that the potential consequences were in fact the result of the particulars and not the result of other factors: the Indonesian government's desire for a share of Busang and/or Barrick's influence. Dr. Juneja's evidence of materiality is based on her "*testing for materiality of the five particulars as a whole... along with their consequences as a whole.*" Given the reasonable doubt raised above that the assumed consequences flowed from the particulars and not other factors (the influence of Barrick and the Indonesian governments desire for a share of Busang), I find Dr. Juneja's opinion of materiality does not assist the O.S.C.
Transcript: April 19, 2005, pages 40-41

Chronology Is Hearsay And Not Evidence

As important as the above noted failure of Dr. Juneja to give proper consideration to the impact of Barrick's influence and the Indonesian government's desire for a share of

Busang when she gave her opinion that the potential consequences flowed from the particulars, is the failure of the O.S.C. to call admissible evidence that the potential consequences flowed from the particulars.

The chronology and analyst reports on which Dr. Juneja relied for her opinion are hearsay and not evidence of the truth of their contents.

Dr. Juneja testified "*in reading the chronology and reading the materials from the analysts, it became clear to one*" that the potential consequences flowed from the particulars.

Transcript: April 14, 2005, pages 21-22

Reading newspaper stories ("*the chronology*") and analyst reports may be proper methodology for an event study where facts may be assumed for the event study because they are otherwise proven at trial (as the O.S.C. attempted to do in this trial with respect to the particulars but has not done so with respect to the consequences), but I fail to see how hearsay evidence without other admissible evidence, is a sufficient evidentiary basis for the bald conclusion that the potential consequences in fact flowed from the particulars.

I also note that in her evidence Dr. Juneja does not in general otherwise give much weight to analysts' reports.

Transcript: April 27, 2005, pages 18-19, 104-105

Other Difficulties In Proof That Particulars Are Material Facts

Aside from the issue of consequences discussed above Dr. Juneja's evidence that she tested "*for the materiality of the five particulars as a whole*" causes other problems for the O.S.C. case. None of the Counts 1 to 4 relies on the materiality of the five particulars "*as a whole*". None of those counts rely on the materality of all five particulars but on three particulars (Counts 1 and 3) or four particulars (Counts 2 and 4).

And the combination of particulars is different for each count:

Count 1 includes Particulars 1, 2, 3

Count 2 includes Particulars 1, 2, 3, 4,

Count 3 includes Particulars 2, 3, 4,

Count 4 includes Particulars 2, 3, 4, 5

The O.S.C. position is that the O.S.C. is only required to prove that any one particular is a material fact for each of the counts and the Defence concedes that but how can evidence that purports to look only at the materiality of the "*five particulars as a whole*" (together with the potential consequences) without "*expressing any opinion as to whether any one of those facts, or any one of those particulars, is or is not material*" be evidence beyond a reasonable doubt that any one or two or three or four particulars is material.

Transcript: April 19, 2005, pages 40-41

I earlier found that the O.S.C. had not proven Particular 1 and that the O.S.C. cannot rely on Particular 2 and 3 because the O.S.C. did not prove Felderhof's knowledge of Particulars 2 and 3 beyond a reasonable doubt. Those findings not only entitle Felderhof

to an acquittal on Count 1 but also make the O.S.C. case more difficult to prove because the O.S.C. cannot rely on Particulars 1, 2, and 3 for any count.

The O.S.C. is required to prove that Particular 4 is a material fact if there is to be a conviction with respect to Counts 2 and 3 and to prove that Particulars 4 and/or 5 are material facts if there is to be a conviction with respect to Count 4.
The evidence of Dr. Juneja was that she was "*not expressing any opinion as to whether any one of those facts, or any one of those particulars, is or is not material.*" Dr. Juneja's opinion is not applicable to any one of the particulars because as she testified she was "*not testing for the materiality of any one individual fact*" or particular. Dr. Juneja was "*not expressing any opinion as to whether*" particulars 4 and/or 5 are material.
Transcript: April 19, 2005, pages 40-41

Although I have found that the O.S.C. has not proven Particular 1, Dr. Juneja's opinion of materiality includes Particular 1 and the alleged potential consequences of Particular 1. Because Dr. Juneja assumed the existence of all of the particulars and because Dr. Juneja did not disentangle the materiality of any one particular from the materiality of any other particular and did not disentangle the materiality of any one particular from the materiality of the consequences as a whole, I am not able to determine the result of taking Particular 1 out of Dr. Juneja's analysis except that it casts doubt on Dr. Juneja's analysis of materiality and casts doubt on the O.S.C. ability to meet it's onus to prove the material facts beyond a reasonable doubt.

Similar concerns apply when Particular 2 and 3, with respect to which Felderhof's knowledge has not been proven beyond a reasonable doubt, are taken out of Dr. Juneja's analysis.

Jusuf Merukh

An important part of Dr. Juneja's opinion as to the materiality of the particulars is the significance she puts on Merukh's claims to Busang and his complaints to the Indonesian government.

Exhibit 800A: page 6

But Ridwan testified that the D.O.M.E. took the position that there was no merit to Merukh's claim.

Transcript: November 29, 2005, pages 11-13

And as noted above at the end when a deal was made for Busang between the Indonesian government, the Indonesian partners, Freeport and Bre-X, Jusuf Merukh was excluded. Jusuf Merukh claims had no consequences. They were ignored by the Indonesian government.

Transcript: April 26, 2005, pages 27-28

CONCLUSION RE DR. JUNEJA'S EVIDENCE OF MATERIALITY

As noted earlier the definition of material facts includes "*a fact that significantly affects, or would reasonably be expected to have a significant effect on, the market price or value of such securities*". Dr. Juneja's evidence related to the first part of the test:

"*significantly affects*".

With respect to the first part of the test, I find that there is a reasonable doubt that Dr. Juneja's evidence establishes that the alleged material facts set out in the Particulars to the Information are in fact material.

THE SECOND PART OF THE MATERIAL FACT DEFINITION

The O.S.C. relies on the evidence below with respect to the second part of the material fact definition: "*would reasonably be expected to have a significant affect.*"

Dr. Kavanagh Re Particular 1

The O.S.C. relies on the evidence of Dr. Kavanagh with respect to the materiality of Particular 1 (Exhibit S5 Volume I, paragraphs 425-426). As I have found that the O.S.C. has not proven Particular 1 beyond a reasonable doubt this issue is moot but in any event the O.S.C.'s submissions are answered by the Defence in paragraphs 22-23 of Exhibit S4.

Exhibit S5: paragraphs 425-426
Exhibit S4: paragraphs 22-23

Dr. Kavanagh was also not qualified as an expert to give evidence as to materiality under the Ontario *Securities Act.*

R. v. Maxwell [1996] O.J. No. 4832

Peter Munk Re Particular 1

The O.S.C. also relies on the evidence of Munk with respect to the materiality of Particular 1 (Exhibit S5 Volume I, paragraph 427-428). As noted above given that the

O.S.C. has not proven Particular 1, this issue is moot. Peter Munk was also not qualified as an expert in materiality and he was not asked specifically about "*material fact*" as defined in the *Securities Act*.

The weight given to Munk's evidence cannot be disconnected from Barrick's involvement with Bre-X and the Indonesian government at the time as discussed at pages 561-571 of these reasons.

Exhibit S5 Volume I: paragraphs 427-428
Exhibit S4: paragraph 24
R. v. Maxwell, supra

Peter Munk/Michael Sharwood/Thomas Goin/Ridwan Mahmud Re Particular 5

The O.S.C. refers to the evidence of Munk, Sharwood, Goin and Mahmud under the heading "*Materiality of Particular 5*" (the SIPP cancellation) at paragraphs 547-551 of Exhibit S5 Volume I.

None were qualified as an expert in materiality and none were asked specifically about "*material fact*" as defined in the *Securities Act*.

Also as noted above the weight given Munk's evidence cannot be disconnected from Barrick's involvement with Bre-X and the Indonesian government.

The O.S.C. submissions have to be seen and weighed in the light of Sharwood's evidence in cross-examination, set out above, that it was "*clear from the materials...that Barrick was involved*" in the SIPP cancellation.

Exhibit S5 Volume I: paragraphs 547-551
Transcript: May 10, 2005, page 55

R. v. Maxwell, supra

FINDINGS

I find the above evidence does not establish that the alleged material facts set out in the particulars to the Information are in fact material.

CONCLUSION

Having found that the O.S.C. has not proven Particular 1 and not proven Felderhof's knowledge of Particular 2 and 3 beyond a reasonable doubt, Felderhof is found not guilty of Count 1 on that basis alone.

For the reasons given above the O.S.C. has not proven beyond a reasonable doubt that Particulars 1 through 5 are material facts, an essential element of the actus reus of the offence, and on that basis Felderhof is found not guilty of Counts 1 to 4.

John Felderhof is found not guilty on all counts.

Dated at Toronto, Ontario, this 31st day of July, 2007.

Mr. Justice P. Hryn