

BRE-X IN HINDSIGHT: WHAT WE KNOW ABOUT THE BUSANG GOLD FRAUD

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ABSTRACT

This paper examines the events surrounding the Bre-X scam in the early to mid-1990s, setting out what we know and don't know. It concludes that the Busang fraud was primarily the product of human greed.

The lure of gold has always created frenzy. Historically, the individual had to actually find the gold to become wealthy. This is no longer the case. Now, an individual can invest in a company which does the searching. In this scenario, the greatest gains may come before the actual deposit is discovered. The hype that accompanies such investments sometimes crosses the line into outright fraud. Such is the case with Bre-X, a Canadian mining stock, that purportedly found the largest gold deposit in the world. In fact, there was little or no gold. Some people, including insiders, became quite wealthy from the stock-play. It is a story predicated on greed, deliberate negligence and naivete. Critiques claim, there were three Bre-Xs. First, the high profile Canadian entity headed by Paul Kavanagh and Rolly Francisco; second, the Indonesian Bre-X headed by John Felderhof and Michael DeGuzman; and third, the Canadian promotion arm headed by David Walsh and Steve McAnulty.¹ Incompetence and blind eyes prevailed at all levels. It is our conclusion that, while a prudent investor should have seen what was coming, the lust for quick and easy wealth proved irresistible for many.

We begin with background. Prior to Indonesia's independence in 1949 there was some mining activity. However, World War II and the subsequent independence movement crippled the industry.² The first president Sukarno's policy, or lack thereof, damaged the economy. By 1966 mining production had fallen below pre-war levels.³

General Suharto staged a military coup against the ineffective Sukarno and took over. This corrupt family ruled for over thirty years. Riches came in the form of kickbacks, legislated monopolies, and high percentage cuts in lucrative foreign businesses. If a business was doing well, the Suhartos wanted a piece of it. As John Felderhof later argued, "we found too much gold, so now it has become a question of national interest."⁴ Suharto implemented a "New Order" in 1968 which aimed at rebuilding the economy.⁵ Under his reforms, the economy flourished.⁶

The "New Order" included reforming foreign capital investment laws and the Mining Law of 1967. Required permits come in three sections: a SIPP, a CoW, and a long term contract. The SIPP allows a company to do preliminary explorations such as soil samples. The SIPP specifically restricts drilling and core extractions. Once the company proves the

claim has some potential, a CoW is granted, which is needed to begin large scale explorations. It was required for companies to drill and remove core samples. It generally lasts a year and must be renewed. After the company has constructed a mine and established good rapport with the government, a long term permit is granted. The foreign company must also relinquish twenty percent ownership to an Indonesian business.

Busang was not Bre-X's discovery. The land beside the Busang Creek on the Kalimantan Island (Borneo) was investigated by several companies long before Bre-X came along. Westralian Atan Minerals (PT WAM) acquired the claim, originally called Maura Atan, in 1987 and received a SIPP permit which allowed preliminary land exploration. Initial results ranged from 4 grams to 27.3 grams of gold per tonne. Since any concentration over 2 grams is significant, it seemed to be a lucrative claim.⁷

Maura Atan was renamed Busang. Exploration warranted soil samples, taken in a grid pattern. Trenches were then dug along the grid. Three trenches showed extraordinary results ranging from 10 to 15 grams of gold per tonne. The results were reported in Westralian's annual report and were also picked up by Montague Gold which had acquired Westralian. The results prompted a US\$60,000 drilling project.⁸

The results were discouraging. Although 17 of the 19 holes found gold, the results were very poor, showing 1 to 3 grams of gold per tonne. The samples showed a narrow, shallow resource without any pattern. It seemed Busang could not be developed into a productive mine. The property sat dormant while Montague attempted to get rid of it. William McLucas gained control of Montague, which included Busang, in 1991.

Peter Howe, heavily involved in the mining industry, was a catalyst in the Bre-X equation. McLucas appealed to Howe's expertise to help sell Busang. Howe proved useful providing both sellers and a buyer for Busang. Howe opened a mining consultant firm in Canada in 1960. Within ten years, he opened an office in Australia, then finally in Indonesia. Howe proved his worth by finding both sellers and a buyer for Busang.

John Felderhof and Michale DeGuzman were the Bre-X geologists. Felderhof was born in 1940 in The Netherlands. He graduated from Dalhousie University in 1962 with a degree in geology. Felderhof and a fellow geologist discovered the Ok Tedi copper deposit in Papua New Guinea in 1968. This was a significant find and propelled Felderhof into international mining circles. According to Howe, "Felderhof proved to be a good geologist". Howe hired Felderhof in 1974 and, for the next fifteen years, Felderhof worked on projects that stretched from South Africa to Indonesia.

Felderhof moved to Indonesia in the early 1980s, where he explored properties for Howe's Jason Mining Ltd. Howe paid his employees primarily in stock options. Jason did well in the 1980s, and so Felderhof was worth millions (on paper). However, the 1987 stock market crash hit junior mining companies hard. Jason was no exception and Felderhof's paper fortune diminished to pennies almost over night.

Felderhof returned to Jakarta in the early 1990s where he served as general manager for a mining company that eventually went bankrupt.⁹ Felderhof was not paid and was reduced to living off the charity of friends.

Michael DeGuzman was born in 1956. He graduated with a geology degree in Manila in 1977 and two years later with an M.A. He began working at Benguet Consolidated Inc, where the CEO Birl Worley remembered, "DeGuzman was a keen observer ... he could observe things that most geologists could not." He said that riches¹⁰ was to be the world's best geologist. Worley depicted DeGuzman as his "star employee."

Benguet proved to be a corrupt environment. DeGuzman refused to join in the corruption, and left Benguet in late 1987. Worley attempted to persuade him to return, but DeGuzman said "he couldn't work under those people." That year DeGuzman left the Philippines tired of the corruption.

DeGuzman went to Indonesia looking to discover the next biggest mineral deposit, but because he was a Filipino, he was relegated to menial labor tasks. In 1987, DeGuzman was working for Howe at Mirah. Mirah was one of Felderhof's projects with Jason-Pelsart. It was here the two first met and developed their friendship. In the early 1990s, like Felderhof, DeGuzman was left unemployed and unpaid. By the time McLucas approached the pair to sell the Busang property both were desperate for work. They were aware the sale would not be easy. The property had poor preliminary results and a half a dozen rejection letters from other mining firms. In addition, the mining industry was in a slump and not many companies were interested in buying.

In late 1992, Felderhof sent DeGuzman to Busang to find a deposit worth selling. DeGuzman did exactly that. After spending four days at the Busang site, he was able to write a more persuasive report than those who had previously investigated the site. Using the same core samples, he estimated a resource of "20 million tonnes with a gold content of more than two grams from the surface to a depth of fifty meters".¹¹ It also estimated the underground mine to be up to 60 million tons with a gold content exceeding 3.5 grams per tonne to a depth of 150 meters. The only explanation for this report is that he hoped the "deposit" would keep him employed.

Even if there was gold, they still needed to find a buyer. In March 1993 fortune struck. Felderhof received a phone call from his old and naive friend David Walsh who asked for a list of Indonesian property. Felderhof's reply hyped a claim called Busang.

David Walsh lived by two philosophies, "Other people's brains ... Other people's money."¹² This is certainly a good explanation of what a successful entrepreneur might do, but, in Walsh's case, it is not clear he had the ability to appreciate what brains others were bringing to his ventures. He was only seventeen, when he joined Eastern Trust Co., a brokerage firm, trading stocks. When he was faulted for not detecting a fraud, he left.

Within a year, he rejoined the financial services sector, this time at Midland Walwyn. Walsh worked in the institutional equities trading department and, at one point, had

commissions as high as \$200,000 per year. In 1982 Walsh asked Midland Walwyn if he could relocate to Calgary to establish an institutional stock trading desk. The company allowed the transfer and Walsh headed west. Unfortunately, he reached Calgary just as recession hit Alberta. While many companies and households were going bankrupt, Walsh tried to sell stock. His efforts were not successful and, after a year, Midland Walwyn cut his salary in half to \$2,000 a month.

The following year he quit and sued Midland Walwyn for \$110,000. Terms of the out-of-court settlement were never released. At the close of 1983 Walsh found himself in Calgary with a young family and no job. He next decided to try his hand at running his own public company. Walsh formed Bresea, a combination of his sons' names, Brett and Sean. Bresea was an exploration company focusing on oil and gas claims. The company raised enough money to purchase some prospective claims, but none yielded results.

That same year Walsh met Australian mining giant, Peter Howe at a barbecue in Sydney. Felderhof was there and, as he launched into tales of Indonesia's undiscovered mineral wealth, Walsh listened in awe. He soon accompanied Felderhof to Indonesia to explore these lands. Nothing developed immediately, but, over the next ten years, Felderhof kept in touch with Walsh and occasionally visited him in Calgary.

Walsh incorporated Bre-X Minerals Ltd. in February 1989 and listed it on the Alberta Stock Exchange. The company name came from his older son, Brett and 'X' for exploration. Shares opened at 30 cents. Over the next four years, the shares drifted between 14 and 30 cents. Walsh opened his 1991 letter to shareholders, "Yes, we are still in business."

By the end of 1991, Walsh's strain had intensified. He barely earned \$1,000 per month. His wife had quit her job. The family survived on cash advances from credit cards. In all, the Walsh had 15 credit cards from 8 banks in 4 cities. The family was also using a \$15,000 line of credit and a loan from the Royal Bank. In 1992, Walsh declared personal bankruptcy with debts exceeding \$200,000.

By early 1993 Bresea and Bre-X seemed at the end of the line. Walsh had one last hope. On April 2, he sent a letter to John Felderhof, inquiring about potential land claims in Indonesia. A With Canadian companies exploring in Latin America, Africa ... thought I would see what is up in Indonesia. "I want to put some romance into both companies ASAP." Felderhof welcomed the opportunity.¹³

Barely three weeks later Felderhof met Walsh in Jakarta.¹⁴ At the end of the evening, Walsh agreed to purchase Busang. On April 25, Felderhof wrote Montague stating he had found "a Canadian company to whom I have a very good chance of selling Maura Atan [Busang]." At the same time, Felderhof faxed Walsh urging him to act fast and confirm their deal to acquire Busang. Walsh responded on May 3, 1993, "Please proceed with arrangements to acquire Maura Atan CoW." On May 6, Bre-X announced it had acquired the Busang property for US \$80,100.¹⁵

Felderhof withheld information from the beginning. First, he did not disclose previous drilling results. Second, he was aware that DeGuzman's resume contained false information. DeGuzman credited himself with discovering the Dizon mine actually found in 1936. His former employer Birl Worley stated that DeGuzman helped drill the mine, however, "his involvement did not represent a discovery!"¹⁶ Third, the CoW for Maura Atan was not in good standing with the Indonesian government. "It will take some work to convince the mines department that serious work will soon commence." Finally, Felderhof secured lucrative positions for both himself and DeGuzman in the Busang project. It is suspicious for a middleman to seek employment from the property buyer on the property he is trying to unload.

Felderhof assumed full control. He chose the drilling company, the assay labs, and the staff: himself as General Manager, DeGuzman as Chief Geologist, and Cesar Puspos as Senior Geologist in charge of all field operations.

There were questions from the beginning. It was unusual that, for a small operation, one team refused to consult or discuss decisions with the other. Walsh deferred all matters relating to geology to Felderhof. "The roles that I played and John played were very well defined ... I did not have any influence or say in what went on in Indonesia."¹⁷ The obvious result was the Canadian team's isolation from the activities of the Indonesian project. Such activities included the salting operation, kick-backs from the drilling company, and the illegal acquisition of Busang II and Busang III.

Bre-X began drilling in October 1993. The first two holes produced insignificant amounts of gold, which prompted Felderhof to consider shutting down the project. "We almost shut down the project ... then we made a hit," recounts DeGuzman. The third hole reported significant gold. However, both Strathcona and Freeport later confirmed the gold in Bre-X hole 3 was foreign. The gold was a man-made copper and gold alloy, which does not occur in nature. It was also in the shape of tiny spiral shavings.

The fourth hole showed equally impressive grades of gold. However, it, too, was salted with alluvial gold acquired locally. Alluvial gold is found in river beds. It is seldom found in primary deposits.¹⁸ This should have been a red flag to the various metallurgists who studied Bre-X gold.

Bre-X employed other unusual practices. Bre-X hired an onsite metallurgist, but a metallurgist is not required on site. DeGuzman hired Jerry Alo because he supposedly possessed special metallurgist skills. However, according to Birl Worley, "Alo did not have the credentials of a metallurgist ... he also knew how to goof up samples." There were previous cases at Benguet when Alo had understated mineralization results, claiming a sample had less than 1 oz when the actual value was over 64 oz. Then, Alo and his colleagues would sell the "excess" minerals. Alo had also been guilty of salting samples and stealing from Benguet. It is surprising that the "honest" DeGuzman would hire someone known for dishonesty, especially for an apparently unnecessary position.¹⁹

Another unusual practice was to sample the entire core, instead of splitting it. This is highly suspicious since most companies split the core in half and retaining the other part for later examination or re-assaying. Testing the entire core means the results cannot be duplicated.

Bre-X began drilling in the southeast zone of Busang in May 1994. The results were impressive at 4.5 grams per tonne. The southeast zone, dubbed Busang II, was acquired in March 1994. In 1995, Bre-X bought its final piece of land in Busang, known as Busang III.²⁰ In acquiring Busang II and III, Felderhof shut out Merukh, one of its 10% partners. Because Indonesian law stipulates that all foreign companies must relinquish provide 20% ownership to local businesses, Felderhof's actions were illegal.

In February 1996, Merukh called Warren Beckwith, former executive of Westralian PT, to inquire about the ownership papers for Busang. The company had been thinking of selling a portion of its 10% of Bre-X to Placer Dome. However Beckwith had stumbled upon something else, Merukh had been dealt out of Busang II and Busang III. Syakerani was given 10% while Bre-X retained the other 90%. Beckwith offered to help Merukh by financing its legal costs in exchange for a piece of the south east zone. Merukh began threatening legal action and approaching influential friends in order to create problems for Bre-X.

The "professionals" did not correct the situation. Dr. Paul Kavanagh joined the Bre-X Board of Directors in March 1994.²¹ As the former head of exploration at Barrick Gold Corp, Kavanagh added legitimacy to Bre-X. Kavanagh had recently retired and taken an interest in the small junior mining company.²² He first became aware of Bre-X in the summer of 1993 when some of its assay results were published in the *Northern Miner*. He phoned Walsh, on behalf of Barrick, inquiring about Busang. Walsh claimed he wasn't interested in a senior partner at the time. However, a week later, Walsh phoned back and invited Barrick to visit Busang. Barrick's interest tripled the Bre-X stock price from 50 cents to \$1.50 in early 1994.²³

Barrick had offered to buy 500,000 shares at market value and 500,000 above market value to finance drilling. On February 10, 1994, Bre-X told reporters the deal with Barrick was off without informing Barrick. This should have set off alarm bells. Instead, he joined the Board of Directors. His appointment led to Bre-X employing its first Toronto underwriter, Loewen Odaatje McCutcheon Ltd (LOM).²⁴

LOM analyst Robert Van Doom agreed to sell 300,000 units for Bre-X at \$1.50 a piece. Each unit consisted of one share and half a warrant; a whole warrant allowed the holder to buy an additional share for \$1.75 at any time during the next two years. Because the stock was currently selling at \$1.85, LOM offered a good price and the shares were moved within a day. Walsh collected a check for just over \$4 million dollars On May 2, 1994.²⁵

Two years later (February 19, 1996) Bre-X appointed Rolando Francisco as executive vice-president. As the former chief financial officer of Lac Minerals, Francisco had

extensive experience in the mining industry. Francisco was born in 1950 in Manila, Philippines. His Filipino background provided insight into conducting business in the region. In addition, Francisco was experienced in dealing with investment bankers and understood how to finance large scale projects. Francisco was a hard working and honest employee that helped Bre-X during the ownership crisis and the Strathcona investigation.²⁶ As it turns out both Kavanagh and Francisco were too willing to accept Walsh and Felderhof's management.

On April 12, 1995, Bre-X gained more momentum with reported results from drilling in the northern area of the Southeast zone. Hole 52 yielded grams per tonne at 196 meters. On June 20, Bre-X issued a press release announcing "visual analysis had confirmed a deposit considerably larger than originally anticipated." The Southeast zone turned out to be far richer than the central zone with BSSE holes at 6.38 grams and 6.5 grams of gold per tonne. According to Felderhof, "The Central zone pales in comparison to the potential of the Southeast, and the Busang project in its entirety has the potential of becoming one of the world's great ore bodies." The stock continued to rise hitting \$8 in July 10, 1995.

Recent history indicated that major discoveries were sometimes made by unlikely individuals. Ontario Hemlo gold deposits were discovered by Murray Pezim.²⁷ Robert Friedland of Diamond Field discovered a large nickel deposit at Voisey's Bay in Labrador.²⁸ Pezim and Friedland were not respected in the mining community. Neither was Walsh, but the analysts were determined not to miss this one.

Dorothy Atkinson, initially at Pacific International Securities predicted shares would hit \$20 within the next six to twelve months. Atkinson, like so many others had bought into Bre-X's enormous, yet unfounded predictions.²⁹ Michael Schaefer began promoting the stock in the respected "Global Gold Stock Report". Schaefer labeled the Busang deposit as "a once in a lifetime situation." He believed the stock would go up to \$40 from its \$13 position. He also predicted Busang to hold at least 10 million ounces.³⁰

However the analyst that propelled Bre-X to a multi-billion dollar company was Egizio Bianchini of Nesbitt Burns. On September 5, 1995, Bianchini began covering Bre-X. He endorsed the company to his 1,200 stockbrokers every morning. Bianchini was probably the most successful analyst in gold stocks at the time with a history of picking winners and detecting scams. He labeled Felderhof and the Bre-X team as "competent technically." He also predicted the stock would reach \$21 within a year, when it was \$14. It hit that mark within three weeks.³¹

By October 1995, Canada's ten major gold company analysts were in a bidding war, out-doing each other's estimates of the Busang reserve and target stock prices. The Bre-X stock was up to \$51.25 on November 21 from \$14 in September. In the following month the stock rose to \$146.50, a more than ten-fold increase in three months. Atkinson predicted 70 million ounces of gold (February 25, 1996) and Bre-X shares eventually worth \$270.³² Bre-X itself edited Nesbitt Burns reports by eliminating negative comments before posting them on the internet.³³

Later that year Walsh invited analysts and Bre-X supporters to visit the Busang property. Walsh was selective in his invitations, abiding by Felderhof's approval.³⁴ There were two junkets, one in June and the other in July 1996. Felderhof, DeGuzman, Alo, and Puspos provided a tour of the facilities and the site. However, the analysts were never shown the Samrinda facility where all the samples were taken before they were transported to the lab. The groups were also carefully guarded and restricted from certain areas. At one point, DeGuzman and Puspos blatantly lied about a sample on site. According to Vivian Danielson, "the trip was more about intangibles ... about what might still be out there than what was already in hand."³⁵

There were others who were skeptical almost from the beginning. Dale Hendrick was a geologist-engineer, both well-respected and experienced. He had met an Australian geologist in Jakarta on February 16, 1995, who claimed he had worked on the Busang reserve with Westralian until 1989. He reported that Westralian had found, "diddly-squat." The Australian showed him the drilling plan for Bre-X and claimed, "they are a bunch of crooks." Alarmed, Hendrick visited the Bre-X Jakarta office, where "the office was a dump and the guy running it was a weirdo." Hendrick dumped his stock when he returned to Toronto.³⁶

Peter Kennedy, a *Financial Post* columnist, began questioning Bre-X's unorthodox assay techniques after the Prospectors Developer Association (PDA) convention in March 1996. As a columnist, his articles had some influence on stock holders. One article entitled, "Skepticism over Its Test Methods Could Delay Bre-X's Developments," caused the stock to drop \$4 to \$144 on Monday March 25.³⁷ Felderhof's response was "A little knowledge can be more dangerous than none at all I do not have time to educate on every subject."³⁸

Bre-X applied for a listing on the Toronto Stock Exchange in April 1996. A month earlier many investors felt a wave of reassurance when they heard Busang had hired Killborn PT to conduct a independent study before the listing was approved by the TSE. Killborn hired Normet Pty to conduct a metallurgist study on the gold found in the Busang deposit. Killborn was a reliable firm, but they only used samples that Bre-X had given them. No independent drilling was done in the Killborn study. As such, it only confirmed that there was gold in the tampered Bre-X samples. The study also produced a report detailing the possible size of the reserve. According to Killborn, "the reported gold assay results were understated by as much as 12.9%."³⁹

What was more interesting was that Normet Pty found a red flag, alluvial gold in a primary deposit.⁴⁰ When Normet approached Felderhof with the findings, the Dutch geologist attempted to explain the anomaly by stating oxidizing agents in the soil create a situation that is similar to a river bed, creating what seems like alluvial gold. However, Normet never found oxidizing agents in the Busang soil, so this theory did not seem possible. Normet were not obliged to make its findings public.

Bre-X was listed on Canada's most prestigious stock market the TSE on April 23, 1996. The company was not required to provide a new or even updated prospectus. In addition,

Bre-X did not have to disclose the independent studies that were conducted on the reserve by Normet Pty and Killborn. Nor did the Stock Exchange send a consultant to visit the property.⁴¹ According to Rowland Fleming TSE president, "Bre-X met and exceeded all requirements for a listing." Unfortunately, most requirements were based on capitalization. Of course the TSE listing gave Bre-X increased respectability for there are certain regulatory requirements that have to be met before it's Toronto-listed, so in a way there was added due diligence on this company.⁴² The stock listed on April 23, 1996, at \$184 and rose to \$187.5 within minutes. In May 1996, investors voted for a 10-1 split in shares to maintain affordability and encourage growth.

Bre-X was accepted on the NASDAQ exchange on August 19, 1996. It had put in an application in November 1995 to be listed. Bre-X falsified several statements regarding ownership on the Securities and Exchange commission application. The stock opened at \$24.70 a share.

Despite the ownership disputes and bidding war, Bre-X was promoted to Canada's most prestigious index, the TSE 300. This is unusual because securities regulations stipulate a company must be listed for at least a year to be considered for the index. The exchange made an exception because of the size of Bre-X and its excellent performance record. Of course, they still didn't have any revenue. According to Bob Siphthorpe, an analyst for Yorkton Securities, "they were throwing out the rule book for this one."

Bre-X had been operating under a SIPP and it expired on July 25, 1996. In fact they should have had an CoW long before this. Merukh had been hard at work, lobbying the government not to renew the permit until the ownership dispute over Busang II and Busang III was settled. Bre-X agreed to discuss the dispute on July 30, 1996. Meanwhile, Bre-X failed to disclose the ownership situation to the public. In August, the NASDAQ exchange listed Bre-X without any knowledge of the pending ownership crisis. The Bre-X executives kept this material information to themselves, while cashing out on their stock options. Walsh and his wife sold \$13.7 million, McAnulty sold \$37.6 million and Felderhof and his wife sold \$22.9 million. In late September, Bre-X reached its all time high at \$28 a share or \$280 pre-split. Shortly thereafter, Bre-X was listed on the TSE 300. News of the expired SIPP and dispute over Busang II and III still were not disclosed.

The public was alerted to the ownership crisis on October 4, 1996 in a *Globe and Mail* article. The information was not a press release, but rather an investigative piece done by two eager journalists who received a leak about the expired SIPP in August. The article detailed Bre-X's expired work permit and Merukh's situation. The article caused the TSE computer system to crash after 90 minutes of trading the following day. However, during those 90 minutes, \$510 million had been shaved off the Bre-X price. In September 1996, Bre-X choose an American investment bank J.P. Morgan to handle the ownership dispute.

Barrick Gold had been trying to acquire the Busang reserve since early 1996. The mining giant had intended to launch a hostile bid for the company in May 1996. However, when Peter Munk, Barrick's CEO, hired private investigators to find information on Bre-X,

they found many unsettling facts: Walsh's unimpressive history, ownership problems, and discrepancies in the gold content of the Busang reserve. Barrick remained interested but chose a more indirect and secretive approach. Munk convinced Suharto's daughter Tutut to influence the government to swing a deal with Barrick. In exchange, Barrick would give all construction contracts to Tutut's companies.

Tutut prompted her friend, a former mining minister, to set up a meeting between Barrick, Bre-X and the Indonesian government on November 14, 1996. The meeting basically forced Bre-X to forge a partnership with Barrick. The deadline for the agreement, granting Barrick 75% ownership of Busang was December 4, 1996. Under the contract, the government would be left with only 10% ownership.

The December deadline came and passed. At the beginning of December, there was a meeting at Tapos cattle ranch outside Jakarta. Only Suharto, his close confidant Bob Hasan and Billy Bob Moffett, CEO of Freeport McMoRan, were invited. Both Hasan and Moffett urged the President to seek other prospective buyers for Busang. In January, Suharto appealed to his friend Hasan to clean up the Bre-X mess. Hasan had become a mediator for family disputes since Suharto's wife's death.

Hasan didn't like Barrick's tactics. He began encouraging other companies to bid for Bre-X. Others stepped forward, but the ultimate decision was between Barrick and Freeport. Unlike Munk, Moffett remained indifferent and uninvolved in the bidding war. The obvious choice was Barrick.

On February 17, 1997, Freeport McMoRan announced it was to acquire 15% of Busang, while the government was to retain 40%, both directly and indirectly through Suharto's holding company Nusamba, Bre-X would keep the remaining 45%. This arrangement was most beneficial to the government and Hasan. All parties seemed pleased, including Bre-X which ended up with double what Barrick offered.⁴³ The market reacted when the deal was announced, dropping the Bre-X price to \$20.80. Meanwhile, Freeport had already left for Busang to start its due diligence survey.⁴⁴

While the fight for control raged, a suspicious fire at the Busang camp destroyed three buildings, including the Geology-Surveying-Drafting office and the Administration office on January 23, 1997. The fire started in the Geology Survey-Drafting, office located adjacent to the core shack. The core shack housed the only remains of core samples. The fire occurred immediately after Barrick conducted its due diligence survey.

The fire occurred around 5 AM. Alo and Puspos felt the fire started due to a power overload from the air conditioner and photocopier. However, Michael Leverman, a Canadian geologist and an electrician, believed such an explanation was unlikely to be true because the fire occurred at night when the power load would have been low.⁴⁵

Even more problematic was the hasty clean up the next day before a formal investigation was conducted. The police were not called. While the Canadian geologists attempted to seal off the area and preserve the integrity of the scene for investigative purposes, Jerry

Alo brought in a bulldozer and leveled the site. Apparently numerous irreplaceable files were lost, including surface geology and geochemistry maps.

DeGuzman was not on site at the time. He faxed Felderhof about the fire almost a week later. He began the letter, "Sorry to disturb you, but our geology building got burned last week." Such casual treatment of a significant fire is aging key information and equipment was suspicious.

Just when David Walsh and John Felderhof would be honored as (Canadian) Prospectors of the Year at the Prospector and Developers Association Convention on March 10, 1997, the end approached. It should have been the highlight of their careers. However, that same evening, they received a phone call from Freeport McMoRan. Freeport's first assay results showed insignificant amounts of gold. Freeport demanded an explanation. Walsh handed the phone to Felderhof, claiming he was only the "money guy." Felderhof said that DeGuzman would be the only one who could clear up the "misunderstanding." DeGuzman was sent back to Busang to resolve the problem. No one could have predicted what was to happen next.

Michael DeGuzman killed himself nine days later by jumping out of a helicopter over the jungles of Borneo. After leaving Toronto, he spent four days at a Singapore hospital. During that time, he visited a bank and inquired about opening a Singapore account. He left for Indonesia on March 17. He arrived in Jakarta but did not contact any of his close friends. Instead, he contacted one of his newer employees, Rudy Vega and asked that Vega meet him in Balikpapan. Balikpapan was a route stop on the way to Busang. DeGuzman mentioned to Vega he had some urgent issues to discuss regarding Freeport's findings.

DeGuzman reached Balikpapan on March 18, 1997. Rudy Vega claimed DeGuzman was in high spirits. On the way to the hotel, they stopped at a store where DeGuzman bought some new clothes, cough syrup and a pad of paper. That evening, the pair went to a karaoke bar where they sang songs and drank until the early hours of the morning.

The next morning DeGuzman proceeded to the airport to catch a flight to Samarinda. He spoke to Lilas, one of his wives, and made plans for her birthday and their first wedding anniversary the following week. At 11 AM DeGuzman boarded the plane to Busang alone. Vega did not accompany him. DeGuzman showed no emotion or depression prior to boarding. Seventeen minutes into the flight, he slid the door open and jumped to his death in the Borneo jungle. Alo identified the partly decomposed body two days later when it was found face down 150 meters from where DeGuzman was said to have jumped.⁴⁶ There were unusual aspects of DeGuzman's death. First, DeGuzman bought a new pair of pants and changed before he boarded the helicopter. Second, DeGuzman wrote a suicide note, misspelling one of his wife's name several times. Third, he addressed one note to Bernhard Leode, a distant co-worker, instead of one of his close Filipino co-workers. Fourth, his suicide note blames Hepatitis B and severe back pains as the factors causing him to take his life. However, DeGuzman had a curable bout of hepatitis B and had endured severe knee pain most of his life. He had had fourteen bouts

of malaria, but continued to work without complaint or concern. Pain had never crippled DeGuzman's activities -- let alone given him reason to end his life. Fifth, after two days of intensive searching, DeGuzman's body could not be found. Then, it appeared in the middle of the initial search area. Sixth, the body was so badly decomposed that DeGuzman could not be identified by fingerprint. Furthermore, DeGuzman lost all his teeth as a child, so dental records could not be used. As such, Alo's identification was based on clothing alone. Perhaps DeGuzman staged his own suicide.⁴⁷

The news of DeGuzman's death was very unsettling. Alarm bells finally went off for Paul Kavanagh and Rolly Francisco. They retained Strathcona Mineral Consultants, headed by Graham Farquharson, to conduct an independent study of the situation.⁴⁸ After five days of browsing through reports and talking with Bre-X and Freeport officials, Strathcona recommended issuing a press release stating that "the potential gold deposit in Busang had been overstated." Kavanagh objected claiming Strathcona had not even seen the Busang property. If Strathcona turned out to be wrong, the effects would be disastrous. However, Strathcona believed that not informing investors of the situation, would allow more people to buy into what appeared to be a fraud.

At 5:30 AM on March 26, 1997, Rolly Francisco received a call from Farquharson. Farquharson informed Rolly of his findings and recommended a press release. Francisco authorized the press release and the \$900,000 budget to conduct independent drilling. That morning, Bre-X stock dropped from \$15.80 to \$2.50. Walsh, along with other Bre-X board members, waited nervously for six weeks for Strathcona to release its preliminary report -- silently praying it would confirm the gold deposit.

Farquharson presented his report to the Bre-X board on May 3, 1997. He barely got two sentences out before those present scrambled for the reports. Walsh then asked him to leave for a short time to give the board some privacy to digest the results. No one anticipated the first sentence, "We very much regret having to express the firm opinion that an economic gold deposit has not been identified in the South East Zone of the Busang property, and is unlikely to be."⁴⁹

Farquharson returned to find board members in shock. "The scene was emotional and there were many outbursts." Strathcona released the results later that night, and they were immediately posted on the Internet. The stock was delisted on the NASDAQ on May 6, 1997 closing at 60 cents. The TSE and ASE delisted the stock on May 7, 1997. What was once a \$6 billion company had vanished into disgrace.⁵⁰

Finger pointing began almost immediately. Many critics turned to Canada's lax securities policies, claiming stricter disclosure policies and listing requirements would have detected the fraud.

Two weeks earlier (April 17, 1997) Francisco and Kavanagh hired the Forensic Investigative Associates to conduct an investigation into the salting scam that was dubbed "without precedent in the history of mining." A year later FIA DeGuzman acted with Cesar Puspos and others including Jerry Alo.⁵¹ Vivian Danielson disagrees: "The theory

does not wash in Indonesian or Canadian mining circles. When the Busang saga began, the Filipino geologists were nothing more than lowly paid field hands. They are now being portrayed as criminal masterminds of the world's biggest gold scam. Something doesn't quite add up."⁵²

It is uncertain if Felderhof was aware of the salting scam. If he did not know, he should have. Busang was supposedly the largest gold mine ever discovered, yet Felderhof spent less and less time there as the estimated reserves increased. Furthermore, he did not cooperate with Forensic Associates during their investigation.⁵³ Forensic Associates believes Walsh (and the other Canadian employees) did not know. Again, he should have. DeGuzman and Walsh are dead (massive heart attack in 1998), Felderhof is in his sanctuary on the Cayman Islands, and the four Filipino geologists live beyond legal reach in the Philippines. It is not certain we will ever know what happened.

The Bre-X scandal was easily the biggest mining fraud in Canadian history. This report focused on the significant events in the scandal from 1989 to 1997. Strict regulations and harsh punishments might deter such behavior, but the root of the problem remains incurable: Bre-X is a story about pure human greed.

ENDNOTES

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4. Brian Hutchinson, *Fool's Gold: The making of a global mining fraud*, Toronto: 1998, p. 204.
5. Danielson and Whyte, p. 35.
6. Douglas Goold and Andrew Willis, *The Bre-X Fraud*, Toronto: McClelland and Stewart, 1997., p. 77.
7. *Ibid.*, p. 40.
8. Danielson and Whyte, p. 53.
9. *Ibid.*, pp. 48-9.
10. *Ibid.*, pp. 57-8.
11. *Ibid.*, p. 63
12. Hutchinson, p. 95.
13. Forensic Investigative Associate, *FIA Interim Report of Investigation into Tampering with Bre-X Minerals Ltd. Busing Core Samples, October 3, 1997*, pp. 11, 339.
14. Danielson & Whyte, p. 65.
15. Diane Francis, *Bre-X: The Inside Story*, Toronto: Firefly Books, 1998, p. 41.
16. FIA, p. 30.
17. FIA, p. 41.
18. Danielson and Whyte, p. 23.
19. *Ibid.*, p. 70
20. Francis, p. 36

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22. *Ibid.*, pp. 78-9
23. Francis, p. 63-4
24. *Ibid.*, p. 65
25. Goold and Willis, p. 46.
26. Danielson and Whyte, p. 113
27. *Ibid.*, p. 108.
28. Goold and Willis, p. 73.
29. *Ibid.*, p. 57.
30. *Ibid.*, p. 58.
31. *Ibid.*, pp. 58-9.
32. *Ibid.*, p. 63.
33. *Ibid.*, p. 61.
34. Danielson and Whyte, p. 117.
35. *Ibid.*, pp. 120-3
36. Francis, p. 84-7
37. *Ibid.*, p. 88
38. *Ibid.*, p. 104 paperback edition.
39. *Ibid.*, p. 93
40. FIA, p. 94
41. Danielson and Whyte, p. 118.
42. Goold and Willis, p. 64.
43. *Ibid.*, p.108-37
44. Francis, p. 133
45. FIA, p. 125.
46. Goold and Willis, p. 180-90
47. FIA, pp. 169-70.
48. Danielson and Whyte, p. 185.
49. Goold and Willis, p. 218
50. *Ibid.*, pp. 220-1
51. FIA, Executive Summary, pp. 2-3.
52. Danielson and Whyte, p. 250.
53. FIA, p. 421.