



Ontario
Securities
Commission

Commission des
valeurs mobilières
de l'Ontario

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**IN THE MATTER OF THE *SECURITIES ACT*,
R.S.O. 1990, c. S.5, AS AMENDED**

AND

**IN THE MATTER OF
REX DIAMOND MINING CORPORATION, SERGE MULLER
AND BENOIT HOLEMANS**

REASONS AND DECISION

Hearing: December 10, 11, 12, 13, 14, 2007
March 31, 2008

Decision: August 21, 2008

Panel: Wendell S. Wigle, Q.C. - Commissioner and Chair of the Panel
David L. Knight, FCA - Commissioner
Kevin J. Kelly - Commissioner

Counsel: John Corelli - For Staff of the Ontario Securities
Shauna Flynn Commission

Alistair Crawley - For Rex Diamond Mining Corporation,
Matthew Scott Serge Muller, and Benoit Holemans

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REASONS AND DECISION

I. OVERVIEW

A. Introduction

[1] This was a hearing before the Ontario Securities Commission (the “Commission”) to decide whether Rex Diamond Mining Corporation (“Rex”), Serge Muller (“Muller”) and Benoit Holemans (“Holemans”) (collectively, the “Respondents”) breached the *Securities Act*, R.S.O. 1990, c. S.5, as amended (the “Act”) and acted contrary to the public interest by: (1) failing to make timely disclosure of a material change in the business, operations and capital of Rex; and (2) providing misleading disclosure in public filings and (3) providing misleading information to Market Regulation Services Inc. (“RS”).

[2] This proceeding was commenced by a Statement of Allegations and Notice of Hearing, dated February 8, 2007. An Amended Statement of Allegations was issued on December 4, 2007. The parties agreed that this proceeding should be bifurcated; first a hearing on the merits; and second, if necessary, a hearing to address sanctions.

[3] This case relates to Rex’s diamond mining operations in Sierra Leone; specifically, mining lease 10/94 in the Kono District of Sierra Leone (the “Tongo Lease”) and mining lease 9/94 in the Pujehun District of Sierra Leone (the “Zimmi Lease”) (collectively, the “Leases”).

[4] There is no dispute that Rex did not issue news releases or file material change reports with respect to: (1) notices received from the Sierra Leone Government indicating that the Leases might be cancelled; and (2) the December 11, 2003 notice of tender (the “Notice of Tender”), which announced that the Sierra Leone Government was seeking tenders from mining companies with respect to the Tongo Diamond Field area. Rex previously held these mining rights pursuant to the Tongo Lease. Staff alleges that Rex breached section 75 of the Act by failing to issue news releases and file material change reports in respect of these events.

[5] As well, Staff takes the position that Rex breached section 75 of the Act by failing to file a material change report, though it did issue a news release, after the Sierra Leone Government issued the tender evaluation on March 30, 2004 (the “Tender Evaluation”), which declared that Koidu Holdings SA was granted mining rights to the Tongo Diamond Field area and stated that Rex’s Leases were cancelled in October 2003.

[6] In addition, Staff alleges that there was misleading disclosure in Rex’s public filings during the period of February 2003 to November 2003 inclusive with respect to Rex’s operations in Sierra Leone, and that the Respondents provided misleading statements to RS with respect to the Leases.

[7] On December 10, 2007, the hearing on the merits commenced and evidence was heard on December 10, 11, 12, 13 and 14, 2007. Following the close of evidence, we heard submissions on the merits on March 31, 2008.

B. Our Decision

[8] Upon reviewing all the evidence, the applicable law and the submissions made, we have concluded that:

(1) it is likely that there was a material change in the business, operations or capital of Rex when Rex received the following correspondence from the Government of Sierra Leone:

(a) the first warning letter dated January 3, 2003, which advised Rex that the Minerals Advisory Board recommended to the Minister of Mineral Resources that Rex's Leases be cancelled because Rex did not comply with the conditions set out in the Leases; and

(b) the second warning letter dated April 16, 2003, which advised Rex that its Leases were not in good standing and that Rex failed to honour its financial obligations;

(2) material changes did occur in the business, operations or capital of Rex when:

(a) Rex received the final notice warning letter dated June 4, 2003, from the Sierra Leone Government, which advised Rex that it had 90 days to comply with the conditions of the Leases or otherwise the Leases would be revoked;

(b) Rex became aware of the Notice of Tender on December 15, 2003; and

(c) the Government of Sierra Leone issued the Tender Evaluation on March 30, 2004.

(3) Rex should have issued news releases and filed material change reports following the events referred to in paragraphs (a) and (b), and should have filed a material change report as well as issuing a news release following the event described in paragraph (c). By failing to do so, Rex breached section 75 of the Act and acted contrary to the public interest;

(4) Rex acted contrary to the public interest by providing inaccurate and incomplete disclosure regarding its operations in Sierra Leone in each of its public filings of February 28, 2003, August 15, 2003 and November 28, 2003;

(5) Rex acted contrary to the public interest when it provided RS with an inaccurate and incomplete chronology of events; and

(6) Muller, as a director and the CEO of Rex, authorized or permitted, and Holemans, as the CFO of Rex, acquiesced in the conduct described in paragraphs (3) to (5) above, and thereby acted contrary to the public interest.

II. BACKGROUND

A. The Respondents

[9] The Respondents in this case are Rex, Muller and Holemans.

[10] Rex is a diamond mining company, originally established under the *Business Corporations Act* (Ontario) by Articles of Amalgamation dated September 14, 1995, and continued under the *Business Corporations Act* (Yukon) on July 31, 2000. Rex was listed on the Toronto Stock Exchange (“TSX”); however, effective October 2006 it is no longer trading on the TSX.

[11] Rex’s head offices are in Belgium and its mining operations are located in South Africa, Mauritania, Paraguay and Sierra Leone. Rex’s business is described in its Annual Information Forms of 2001, 2002 and 2003 as follows:

Rex Diamond Mining Corporation is a vertically integrated diamond company with significant grass roots exploration in Mauritania, development projects in Sierra Leone, mining operations in South Africa, marketing and polishing in Antwerp and on-line retailing of diamonds and diamond jewelry. The corporate offices and decision-making centre of Rex are located in Antwerp, the capital of the diamond industry, handling over 80% of the world’s rough diamond trade.

[12] It is Rex’s operations in Sierra Leone that are the focus of Staff’s Allegations.

[13] Muller is Rex’s Chief Executive Officer (“CEO”) and a Director. He is a Belgian citizen and resides in Zurich, Switzerland. He is also the founder and largest shareholder of Rex. Muller has over 40 years of experience working in the diamond industry. Muller began working in his family’s diamond business when it held a “sight” at De Beers. As a sightholder, Muller’s family was one of a few select customers of De Beers that were invited to “see” and buy diamonds from De Beers. In 1980 the diamond market crashed, and sightholders experienced significant losses on their diamond purchases when De Beers refused to drop their prices. At this time, Muller became directly involved with finding alternative sources of diamonds, and as a result, he became involved with purchasing rough diamonds on the open market in Sierra Leone and South Africa.

[14] Holemans is Rex’s Chief Financial Officer (“CFO”). He is a Belgian citizen and resides in Antwerp, Belgium. He began working for Rex in 1995 and by 1997 he became Rex’s CFO.

B. The Allegations

[15] It is alleged by Staff that Rex contravened section 75 of the Act and engaged in conduct contrary to the public interest by:

(1) failing to issue news releases or file material change reports forthwith disclosing the correspondence of the Sierra Leone Government received by Rex on January 3, 2003, April 16, 2003 and June 4, 2003, and the risk that the Sierra

Leone Government would cancel Rex's Leases. According to Staff, this risk would have been clear to Rex on January 3, 2003, and in any event, by no later than June 4, 2003;

(2) failing to issue a news release or file a material change report forthwith disclosing the issuance of December 11, 2003 Notice of Tender, of which Rex became aware on December 15, 2003, and the effect this would have on the business and operations of Rex;

(3) failing to file a material change report forthwith disclosing that on March 30, 2004, the Sierra Leone Government issued the Tender Evaluation, which announced that the Leases held by Rex had been cancelled, and the effect this would have on the business and operations of Rex.

[16] Further, it is alleged that Muller as a director and the CEO of Rex and Holemans as Rex's CFO acted contrary to the public interest by authorizing, permitting or acquiescing in Rex's non-compliance with section 75 of the Act.

[17] In addition, it is alleged that Rex acted contrary to the public interest by providing misleading disclosure regarding its operations in Sierra Leone in each of its public filings of February 28, 2003, August 15, 2003 and November 28, 2003 and that Muller and Holemans, as officers and directors of Rex, authorized, permitted or acquiesced in Rex's provision of misleading disclosure in its public filings.

[18] During opening statements, Staff made some clarifications with respect to their allegations set out in paragraphs 14 and 15 in the Statement of Allegations, which relate to Rex's diamond trading business and Rex's Management Discussion and Analysis ("MD&A") filed November 28, 2003. Specifically, Staff stated "I'm not relying on that allegation about the rough diamonds. That's not going to be a part of [the] case before you". As a result, Staff explained that paragraph 15 of the Statement of Allegations should be amended by having the second sentence struck out as follows:

15. The information contained in the MD&A was misleading. ~~The "first shipment" of diamonds did not come from the properties covered by the Leases.~~ Further, it does not appear that there was a reasonable basis for Rex to state that imports were expected to reach a level of \$2 million per month within a year. Rex's imports did not reach a level of \$2 million per month. Rex never commenced any actual mining operations on the properties covered by the Leases.

[19] It is also alleged that Muller and Holemans authorized, permitted or acquiesced in Rex's provision of misleading information to RS. Staff alleges that the chronology of events provided to RS by Rex ("Rex's Chronology") contained misleading information and omitted key facts with respect to the Leases.

III. THE ISSUES

[20] Staff's allegations raise the following issues for our determination:

(1) did a material change occur in the business, operations or capital of Rex when:

(a) Rex received correspondence dated January 3, 2003, April 16, 2003 and June 4, 2003, from the Sierra Leone Government, with respect to the risk of the cancellation of the Leases?

(b) Rex became aware of the Notice of Tender on December 15, 2003?

(c) the Government of Sierra Leone issued the Tender Evaluation on March 30, 2004?

(2) if a material change did occur, did Muller in his capacity as a director and CEO of Rex and Holemans in his capacity as Rex's CFO, authorize, acquiesce in or permit a breach by Rex of section 75 contrary to the public interest?

(3) did the Respondents act contrary to the public interest by providing misleading disclosure regarding its operations in Sierra Leone in each of its public filings of February 28, 2003, August 15, 2003 and November 28, 2003?

(4) did the Respondents act contrary to the public interest by misleading RS by providing an incomplete chronology?

IV. THE EVIDENCE

A. The Chronology of Events

[21] While the Statement of Allegations refers to events that took place in 2003 and 2004, it is necessary to examine the detailed history of Rex's operations in Sierra Leone to gain a comprehensive understanding of the events surrounding the Leases. The following section outlines the chronology of events in this matter.

1. Muller Acquires Mining Rights in Sierra Leone

[22] By 1987, Muller had arrangements with the Sierra Leone Government to purchase rough diamonds directly from the government-controlled National Diamond Mining Corporation ("NDMC"). Over time, Muller also became involved in financing production and controlling security at the mines in order to preserve his supply of diamonds.

[23] In the 1990s, the political situation in Sierra Leone deteriorated with a military overthrow of the Government and the privatization of mines. In exchange for \$2 million owed to Muller by the NDMC, the new government offered Muller mining rights in the areas known as Tongo and Zimmi. As a result, in 1994, Muller obtained four mining leases:

1. ML 7/94: Block 13 in Kono (the "Block 13 Lease");
2. ML 8/94: No. 12 Slimes Dam and Tailings in Kono (the "Slimes Dam Lease");

3. ML 9/94: the Zimmi Lease; and
4. ML 10/94: the Tongo Lease.

2. 1995: Rex was Established

[24] In 1995, Rex was established in Ontario by Articles of Amalgamation which joined Kimberlex Resources Ltd. and Speer Darrow Management Inc.

[25] Muller received shares in Rex in exchange for transferring his interest in the South African mines and the four mining leases in Sierra Leone. This is how Rex came into ownership of the Leases at issue in this proceeding.

3. 1996: Rex Loses the Block 13 Lease

[26] In 1996, Rex lost ownership of the Block 13 Lease. According to correspondence to the Government of Sierra Leone from Rex's lawyer, dated April 10, 1996, the Government of Sierra Leone reissued the Block 13 Lease to a third party because Rex did not comply with its obligation to pursue mining activities. Rex took the position that such activities were impossible at the time owing to a *force majeure* in that area.

4. 1997: The Military Coup

[27] In May of 1997, there was an outbreak of hostilities and civil war in Sierra Leone which led to a military coup (the "Military Coup"). As a result, a *force majeure* was declared in Sierra Leone.

[28] Rex's Prospectus, dated August 27, 1997 (the "1997 Prospectus"), described the Military Coup as follows:

On May 25, 1997, the 14-month-old civilian government of Sierra Leone was overthrown by a military coup and the Armed Forces Revolutionary Council ("AFRC") assumed power. Since the coup, there have been reports of widespread looting in the capital of Freetown, many foreign nationals have been evacuated and there has been several armed clashes among the AFRC and various Sierra Leone groups as well as between Nigerian peacekeeping troops based in Sierra Leone and local forces supportive of the coup.

[29] Rex reacted to the Military Coup by temporarily halting all operations in Sierra Leone and withdrawing all expatriate employees.

[30] In its 1997 Prospectus, Rex warned investors that there was "no guarantee" the political situation in the country would stabilize and that Rex did not know "when or if the Corporation will be able to resume operations".

[31] However, in the 1997 Prospectus, Rex assured investors that:

Although the May 1997 political disruptions in Sierra Leone has delayed the implementation of Rex's operations in the country, Rex is confident that the importance of future diamond revenues to Sierra Leone, will likely see normalization of the business climate in the near future.

[32] The 1997 Prospectus also explained the status of the Leases and assured investors that despite the Military Coup, Rex intended to maintain its interests in Sierra Leone and had made appropriate arrangements with the respective Chieftain Councils and representatives of the land-owning families with respect to the surface rights applicable to the Leases.

5. Description of the Leases in the 1997 Prospectus

[33] Despite the Military Coup, the 1997 Prospectus positively described the properties of the Leases.

[34] With respect to the Tongo Lease, it was noted that four kimberlite dyke zones were discovered on this property.

[35] With respect to the Zimmi Lease, it was noted that it was an alluvial diamond property. The 1997 Prospectus described the property covered by the Zimmi Lease as follows:

Geological reports based upon sampling programs carried out on the property indicate that the property contains deposits of large stones of high quality ... The Corporation believes that the Zimmi property has the potential to produce alluvial diamonds at surface and the high grade paleo channels and other geophysical features indicate the possibility of kimberlite.

[36] The 1997 Prospectus also stated that Sierra Leone "has produced, and continues to produce many of the world's finest largest diamonds, the great majority from alluvial deposits".

6. The Rombouts Report

[37] The description of the properties covered by the Leases in the 1997 Prospectus was consistent with a report prepared in 1997 by Dr. Luc Rombouts (then a consulting geologist for Rex) (the "Rombouts Report").

[38] The Rombouts Report concluded that:

- with respect to the area covered by the Tongo Lease:
 - the Tongo kimberlite dykes may constitute a diamond resource worth US\$1.65 billion down to a depth of 500 metres and US\$3.31 billion if mining proceeded to a depth of 1,000 metres;
 - the Tongo Lease area covers the most important diamond-bearing kimberlite dykes zones: Lando, Kundu, Tongo and Peyima. The Rombouts

Report states that these kimberlite dykes contain high quality gem stones, and the Lando kimberlite dyke is the richest and longest dyke and is a very attractive mining target; and

- assuming an average value of US\$175/carats for the Tongo diamonds, the ore should have an average value content of US\$140/tonne.
- with respect to the area covered by the Zimmi Lease:
 - deeper alluvial gravels may be present underneath the present floodplain. The deeper channels should be explored and their diamond content quantified. The resources in the deeper channels of the Morro valley may amount to several million cubic metres. Kimberlites are known just across the border in Liberia but could also be present on the Sierra Leonean side of the border. The Zimmi region has good diamond-bearing kimberlite exploration potential.

7. 1998: President Kabbah Returns to Power in Sierra Leone

[39] By May of 1998, the government fell and the government led by President Kabbah returned to power, albeit with some continuing political instability.

[40] Once the Kabbah government came back into power in Sierra Leone, Rex corresponded through its solicitors with the Government of Sierra Leone by letters dated May 19, 1998, June 4, 1998 and July 24, 1998, to determine the amounts it owed by way of rent and fees with respect to the Leases.

[41] In addition, by letters dated July 23, 1998 and August 10, 1998, Rex informed the Government of Sierra Leone that it wished to relinquish its mining rights with respect to the Slimes Dam Lease.

[42] On August 18, 1998, Rex received correspondence from the Government of Sierra Leone Mines Division, Ministry of Mineral Resources, stating that rent payments for the Slimes Dam Lease, Zimmi Lease and Tongo Lease amounted to US\$285,597.50. Rex subsequently paid US\$276,120.00 to the Sierra Leone Government for the rents of the Leases covering the periods March 1, 1997 to February 28, 1998 and March 1, 1998 until February 28, 1999. This amount excluded the Slimes Dam Lease which Rex relinquished.

[43] In addition, on August 18, 1998, Rex issued a news release stating that the Ministry of Mineral Resources of Sierra Leone gave written reconfirmation of Rex's Leases.

[44] By letter dated August 20, 1998, A. B. Omadachi, the Major for the Chief of Defence Staff of the Armed Forces of the Republic of Sierra Leone corresponded with Rex to inform Rex that it was cleared to carry out mining activities in the regions of Tongo and Zimmi and that these areas were safe.

[45] On November 30, 1998, Rex corresponded with the Minister of the Ministry of Mineral Resources in Sierra Leone to inform the Minister that due to the current security

situation in the region, Rex had been unable to operate. The Ministry of Mineral Resources acknowledged this in a letter dated December 30, 1998 and expressed hope that Rex would be able to start mining operations in the Zimmi and Tongo regions when the security situation improved.

8. 1999: The Peace Treaty

[46] On July 13, 1999, a Peace Treaty was signed between the Government of Sierra Leone and the Revolutionary United Front.

[47] At this time, Rex informed shareholders in its Consolidated Financial Statements for the years ended March 31, 1999 and 1998 that normal mining operations could commence in the near future but there was no assurance that this would happen.

[48] Rex also informed its shareholders via its website that Rex's Leases were still in good standing. On June 28, 1999, Holemans wrote:

The government has reconfirmed the good standing of our concessions one year ago and again three months ago (see also <http://www.rexmining.com>). The leases have all been paid for and we have consciously chosen not to make use of the "Force Majeure" clause during the war in order to avoid any possible discussion about our legal standing.

Our aim is to develop an industrial mining operation in Sierra Leone requiring both capital and technical know-how, these are otherwise not available in the country. We are not interested in the small alluvial diggings, but in the Tongo Fields underground reserves and in the underdeveloped Zimmi Fields. We enjoy the support of the local population and the Paramount Chiefs in the surrounding villages who want to improve the living conditions in their communities.

[49] At this time, Rex's shareholders wrote to Rex to express concern that the drop in Rex's share price might be attributable to the jeopardy of the Leases in Sierra Leone. Rex assured investors that the Leases were still in good standing.

9. 2002: A More Stable Situation

[50] By letter dated March 18, 2002, the Director of Mines, A. R. Wurie, informed Rex that the *force majeure* was "officially lifted" on January 18, 2002. This letter also required Rex to comply with the Leases and commence mining operations. The Director specified that:

This letter also serves as a notice for your company to put in place the necessary modalities for the resumption of the kimberlite operations within the time frame prescribed above.

Failure to take necessary action to regularize and/or update your obligations as required, will result to the Ministry's assumption that you are no longer interested in the Licence.

[51] In return, Rex provided the Government of Sierra Leone with a Work Programme and signed an agreement with the Makpele Chiefdom to access the Zimmi property for mining.

[52] However, in its Consolidated Financial Statements for the years ended March 31, 2002 and 2001, Rex still cautioned that:

The Company is subject to the considerations and risks of operating in South Africa, Sierra Leone and Mauritania. These include risks associated with the political and economic environment, foreign currency exchange and changes in legislation.

10. The 2002 Annual Information Form and 2002 Annual Report

[53] The 2002 Annual Information Form ("2002 AIF") along with the 2002 Annual Report also described Rex's outlook in Mauritania, South Africa and Sierra Leone at this time.

[54] With respect to Mauritania, the cost of holding exploration licences increased, Rex reduced its number of exploration permits, there were no important new discoveries and Rex slowly started to reduce expenses in Mauritania. Specifically, the 2002 Annual Report stated:

... no mineral resource or reserve has been identified on any of the Mauritania properties and there can be no assurance that future exploration will result in the discovery of an economically viable mineral resource or mineral reserve.

[55] With respect to South Africa, it was noted that only one mine was in production and that the other two were on "care and maintenance". In addition, the 2002 Annual Report explained that Rex incurred a net loss of \$9.0 million and this was mainly due to a decrease in Rex's diamond production in South Africa. This decrease in diamond production was the result of excessive rainfall and flooding of Rex's South African mines.

[56] With respect to Sierra Leone, the news was more positive. In its 2002 AIF, Rex referred to the increase in peace and stability in Sierra Leone:

Security and stability is now gradually returning to Sierra Leone and the management believes that it will be in a position to resume its activities in Sierra Leone in the near future.

11. The October 1, 2002 News Release and the Fauvilla MOU

[57] On October 1, 2002, Rex issued a news release to announce that it had entered into a Memorandum of Understanding with Fauvilla Ltd. to operate alluvial diamond production on Rex's Zimmi property (the "Fauvilla MOU").

[58] Pursuant to the Fauvilla MOU:

... Fauvilla has agreed to invest US\$5,000,000 to begin operations on the "Zimmi" property. Rex will, however, retain 100% of the concession rights to the property. Fauvilla, a diamond mining company operating alluvial mines in West Africa, has also agreed to commence mining activities on "Zimmi" within 90 days. All costs associated with mining operations will be paid by Fauvilla. Rex and Fauvilla will also share the costs of development projects for the local community on the "Zimmi" property.

[59] In addition, the October 1, 2002 news release also mentioned that Rex completed a private placement to raise funds for Rex's operations in South Africa.

12. The January 3, 2003 Warning Letter

[60] By letter dated January 3, 2003, U. B. Kamara, for the Director of Mines, wrote to Rex to inform Rex that the Minerals Advisory Board recommended that the Minister of Mineral Resources terminate the Leases.

[61] The letter explained that this recommendation came about because Rex did not commence operations on the areas covered by the Leases and as a result, illicit mining was taking place.

[62] Specifically the January 3, 2003 letter stated:

Moreover, despite the general calm situation in the country since the beginning of 2002 and the various notices sent to your company to start activities to bring these properties to production, you have steadfastly failed to do so and instead resorted to mobilizing people in high places to influence my office not to take action against your company for its blatant default of the provisions of the Mines and Mineral's Act and its Mining Leases.

In view of the above and the several breaches of the terms of your leases, the Minerals Advisory Board has recommended to the Minister of Mineral Resources that your two leases in Pujehun ML 9/94 and Tongo MI 10/94 be terminated.

13. Rex's Response and Actions Subsequent to the January 3, 2003 Warning Letter

[63] In response to the January 3, 2003 letter, a letter was sent on Rex's behalf by Zeev Morgenstern ("Morgenstern"), Rex's Managing Director, on January 7, 2003 to the Chief

of the Makpele Chiefdom to confirm Rex's support of operating in the Makpele Chiefdom. This letter set out Rex's commitment to undertake a number of development projects in the Makpele Chiefdom.

[64] In return, the Makpele Chiefdom wrote to the Sierra Leone Government by letters dated January 7 and January 10, 2003 to support Rex's operations.

[65] By letter dated January 14, 2003, the Sierra Leone National Policy Advisory Committee ("NPAC") informed Rex that it was given another chance before the Leases would be terminated and imposed conditions on Rex. The NPAC stated:

... the NPAC advises that Rex Mining Company be given one last chance to demonstrate its commitment and serious intentions by starting operations at its two mining concessions ML9/94 at Zimmi and ML10/94 at Tongo indicating when it intends to commence such operations. The Company should be requested to submit a detailed work programme, and an indication of actions to be undertaken within specific timeframes.

[66] Also, on January 14, 2003, Rex wrote to the Director of Mines of the Ministry of Mineral Resources to address the issues raised by the January 3, 2003 letter and to inform the Sierra Leone Government of mining operations steps being taken by Rex in connection with the property under the Leases.

[67] In addition, the Minister of Mineral Resources wrote to Rex on January 21, 2003 to remind Rex that a comprehensive "Work Programme" covering the conduct of all Rex's operations on the Leases needed to be submitted within two weeks.

[68] On February 3, 2003, Rex submitted its comprehensive "Work Programme" to the Ministry of Mineral Resources. At the same time, Rex also requested that:

[the] Ministry [furnish] us with the necessary figures in order to facilitate our payment of Lease rent covering both Zimmi and Tongo which said payments will be effected *immediately* upon receipt of the said figures. [emphasis from original]

[69] On February 7, 2003, M. S. Deen, the Minister of Mineral Resources, wrote to Rex advising Rex that they accepted Rex's "Work Programme" in principle, and that Rex owed a total of US\$282,000 on the Leases for the period of January 19, 2002 to January 18, 2004.

14. Rex's MD&A and News Release Filed February 28, 2003

[70] Rex's MD&A filed February 28, 2003, indicated that Rex was engaging in operations in Sierra Leone. The "Outlook" section stated that:

In Sierra Leone heavy mining equipment is currently being moved into the Zimmi concession while the mining camp is being established. Dr. Luc Rombouts will head a team of geologists to conduct a geophysical and topographical survey in Tongo Fields in preparation for a drilling

programme. The drilling programme planned for later in the year is to outline and quantify the diamond resources present in the kimberlite dykes.

[71] In addition, Rex issued a news release on February 28, 2003, which confirmed that “[in] Sierra Leone, Rex’s partner, Fauvilla Ltd., is moving heavy mining equipment onto the Zimmi concession while the mining camp is being established”.

15. The April 16, 2003 Warning Letter

[72] On April 16, 2003, A. R. Wurie, the Director of Mines for the Ministry of Mineral Resources wrote to Rex to inform it that the Leases were not in good standing. In particular, Rex did not fulfill its financial obligations under the Leases; however, it was recognized that Rex did start geological survey activities with respect to the Tongo Lease.

[73] Specifically, the Director of Mines gave Rex the following warning:

In light of these activities, the Rex Mining Corporation has definitely contravened Section 100 (1) & (2) of the Mining and Minerals Act, a situation this Ministry and indeed Cabinet will not entertain much longer.

You are therefore advised in your Company’s interest to honour your financial obligations without further delay in order to avoid any unpleasant decisions that Government may take to redress the situation.

16. The June 4, 2003 Warning Letter

[74] On June 4, 2003, M. S. Deen, the Minister of Mineral Resources, gave final notice to Rex that in 90 days Rex’s Leases would be cancelled because Rex did not embark on any meaningful operations on the property covered by the Leases. M. S. Deen explained that an inspection of the area covered by the Leases revealed that only artisanal mining was taking place on the area covered by the Zimmi Lease, and that this was inadequate mining activity which did not conform with Rex’s comprehensive “Work Programme”. The following reasons were given to support the final notice:

So far, field inspections undertaken by no less a person than my Deputy Minister, on the instructions of Government, has clearly revealed that your operations in Zimmi are nothing more than extensive and intensive artisanal mining involving over 600 diggers apparently working under the usual “support system”. We do appreciate your contribution to the Local Community in terms of employment, but you will agree with me that this type of mining is definitely not in consonance with the trial mining envisaged in your work programme. A well defined mining cut preferably with the use of earthmoving equipment and the treatment of extracted gravel in a mobile washing plant, would have been the most appropriate mining method employed by a Company of your status.

You will recall that several assurances were given to the Director of Mines, in earlier correspondence that your Company would commence

mining operations in accordance with your work programme in the first quarter of 2003, but so far no progress has been made in that direction even after you received my letter [dated February 7, 2003]

[75] Consequently, Rex was given 90 days notice to take appropriate action to fulfill its obligations under the Leases, otherwise the Government of Sierra Leone would be left with no alternative but to cancel Rex's Leases. The Minister of Mineral Resources emphasized that Rex's failure to meet its obligations under the Leases violated subsection 31 (1) and (2) of Sierra Leone's Mines and Minerals Act and that:

... if after Ninety (90) days notice, your company fails to take appropriate action to fulfill its obligations under its licences, Government will be left with no alternative but to cancel the Mining Leases ML 9/94 and ML 10/94 held by Rex Mining Corporation ...

[76] The June 4, 2003 letter also required Rex within 90 days to: (1) submit a full report of the artisanal mining now being carried out including disposal of the diamonds recovered in that mining activity; (2) provide a report on the basic geophysical prospecting undertaken on the property of the Tongo Lease; and (3) provide a more detailed work programme for the area under the Leases.

17. The July 28, 2003 Letter to Shareholders

[77] The July 28, 2003 letter to shareholders contained in Rex's 2003 Annual Report did not mention the correspondence from the Government of Sierra Leone relating to the Leases. With respect to Sierra Leone, all that was mentioned was that:

... a team of geologists has been surveying the Tongo Fields Kimberlites in Sierra Leone, The subcontracting arrangement reached for the development of Zimmy [*sic*] in Sierra Leone is proceeding at a frustratingly slow pace.

[78] In contrast, approximately a page and half of the July 28, 2003 letter to shareholders discussed negative information about the status of the South Africa operations, in particular, the problems with currency appreciation, mining accidents and legislation changes in South Africa. Overall, the letter to shareholders emphasized that it was a challenging year for Rex's operations.

18. The August 15, 2003 Annual Information Form

[79] On August 15, 2003, Rex filed its 2003 Annual Information Form (the "2003 AIF"). Under "Trends", Rex stated:

Peace and stability are returning to West Africa. This bodes well for the economic development of the sub-region and the rebuilding of industrial diamond mining in Sierra Leone, Guinea and Liberia.

[80] Under the "Description of the Business", Rex described the Sierra Leone properties as follows:

... the Corporation holds two diamond-mining leases in Sierra Leone (the “Sierra Leone Properties”). As a result of political instability, the Corporation has halted operations in Sierra Leone (see “Sierra Leone Properties”) but has a Memorandum of Understanding with Fauvilla Ltd. to start operations on the Zimmi alluvial property.

[81] In addition, the 2003 AIF stated:

Security and stability is now gradually returning to Sierra Leone and management believes that it will be in a position to resume its activities in Sierra Leone in the near future.

[82] The 2003 AIF also favourably described the property covered by the Leases. With respect to the Zimmi Lease Rex stated that:

The Corporation believes that the Zimmi property has the potential to produce alluvial diamonds at surface and that high-grade paleo channels and other geophysical features indicate the possibility of a primary kimberlite source. Under the MOU, Fauvilla has agreed to invest US\$5,000,000 to begin operations on the “Zimmi property”.

[83] With respect to the Tongo Lease, the 2003 AIF stated:

The Tongo dykes are reputedly among the highest grade diamond-bearing dykes in the world. During fiscal 2003 a team was set up to start surveying the Tongo dyke system and a ground magnetic survey was carried out, as well as a topographical survey, allowing a better definition of the extent of the kimberlite dykes.

[84] As for Rex’s operations in Mauritania, the 2003 AIF states that Rex reduced its diamond exploration holdings in that country. The seven permits Rex held were reduced to three, while only 2 applications for permits were made.

[85] With respect to South Africa, Rex’s operations continued to struggle at this time.

19. Rex’s MD&A Filed November 28, 2003

[86] Rex’s MD&A filed November 28, 2003 contained positive information about Sierra Leone. It announced that a private placement had been completed and that “[the] gross proceeds of Cdn\$3.6 million will be used to build up the rough supply from Sierra Leone and for general working capital purposes.”

[87] The MD&A filed November 28, 2003 also discussed shipments of diamonds from Sierra Leone and Rex’s expected output:

The first shipment to Rex Antwerp of Sierra Leone rough diamonds have been sold in Antwerp during the month of November. Sierra Leone sales were strong, with high prices obtained, as the diamond market is in short supply. Imports from Sierra Leone are expected to reach a sustained level

of \$2 million per month within a year, thereby compensating for the currency exchange related losses of the South African operations.

[88] The “Outlook” section of Rex’s MD&A filed November 28, 2003 also addressed problems that Rex’s South African operations were experiencing. In particular, strikes in Rex’s South African mines affected Rex’s operations as well as currency fluctuations of the South African Rand.

[89] Rex’s MD&A filed November 28, 2003 made no mention of the cancellation of the Leases or the threat of cancellation from the Government of Sierra Leone relating to the Leases.

20. December 2003: The Notice of Tender and the Fauvilla Letter

[90] On December 11, 2003 the Sierra Leone Government posted the Notice of Tender for the Tongo diamond field on its website <http://www.statehouse-sl.org/> (the “Statehouse Website”). The Notice of Tender reads as follows:

The Sierra Leone Government announces that the Tongo Diamond Field area, which was previously held by Rex Mining Company, is now open to tender for mining companies to explore for diamonds in Kimberlite dyke zones. The alluvials around Tongo have produced an estimated 15 million carats of 95% gem quality over the past 50 or so years. Up to 80 carat stones have been recovered but they are generally smaller but clearer than at Koidu.

[91] There is no record that Rex received written notification of the Notice of Tender or that the Leases were cancelled.

[92] The Evidence presented at the hearing revealed that Rex became aware of the Notice of Tender by a letter sent by fax from Fauvilla, dated December 15, 2003 (the “Fauvilla Letter”). The Fauvilla Letter informed Rex that:

The Government of Sierra Leone has now formally issued a tender “for mining companies to explore for diamonds in Kimberlite dyke zones” in the Tongo Diamond Field area, “which was previously held by Rex Mining Company” to quote the official announcement.

[93] Further, the Fauvilla Letter inquired whether Rex could provide assurances whether the Leases were in good standing, whether they were cancelled, and whether there was any other information that “may materially impact the status of the aforementioned MOU and the value of the MOU as one of Fauvilla’s assets”.

[94] Muller questioned Morgenstern about the letter; however, the evidence shows that no action was taken with respect to the Fauvilla Letter.

21. January 2004 – The E-Mail Correspondence

[95] During January 2004, Rex received a number of e-mails with respect to the Notice of Tender.

[96] On January 23, 2004, Stephen Lay (“Lay”), a mining engineer hired by Rex wrote:

Just to let you know that I have had a couple of enquiries about the Tongo field. In both cases they have said that Rex does not hold the licence any more and the [Government] is re-tendering it.

[97] In response on January 26, 2004, Holemans replied that the “re-tendering is a rumor”. During his testimony, Holemans explained that this response was based on Muller’s explanation that “... there is nothing really going on, it is a rumor...”, despite the fact that the Notice of Tender was posted on the Sierra Leone website since December 11, 2003.

[98] On January 30, 2004, Rombouts wrote an e-mail to Muller to inform him of the following:

The government of Sierra Leone has put out a tender for the sale of the Tongo property. For more details see the Sierra Leone government website at: www.statehouse-sl.org/min-ten-dec11.html. It is specifically mentioned that the property was previously held by Rex. *What do we have to do with this? A formal complaint to the government, a Press release (this is material information if confirmed) or any other ideas?* [emphasis added]

[99] Muller responded to this e-mail on January 31, 2004 and stated:

I am aware of this offer. We have however until the 29 feb 2004 [sic] to pay our lease and this whole tender is cancelled. Of course the deposits of 5.000 USD in order to tender will not be returned. We will receive a formal letter from the Ministry of Mines on Monday to request the payment until that date. I find that the boys in SL jumped the gun, they must be either hungry or angry.

[100] We note that with respect to the February 29, 2004 date mentioned above, we were not provided with any other evidence that the Government of Sierra Leone gave Rex a deadline of February 29, 2004. At this time, Muller was involved in efforts to reinstate Rex’s Leases; however, his testimony revealed that reinstatement discussions with the Sierra Leone Government were oral and not in writing.

22. February 2004 to March 2004

i. Rex’s Negotiations with the Sierra Leone Government with Respect to the Leases

[101] According to Rex’s Chronology which was provided to RS, in February 2004 discussions commenced with the Government of Sierra Leone regarding “the purported revocation and tender”.

[102] At the hearing we were not provided with any documentation with respect to the “revocation and tender” negotiations. Specifically, Rex’s Chronology states:

Discussions continue throughout the month with Mohamed Deen, the Minister of Mineral Resources of Sierra Leone and Rashid A. Wurie, the Director of Mines, Ministry of Mineral Resources of Sierra Leone. *The discussions are informal and undocumented.* The Company is verbally informed that the tender is not likely to go ahead. [emphasis added]

ii. Shareholder Inquiries and Comments

[103] During the period of February 2004 to March 2004 a number of inquiries and comments were made about Rex and its Leases on the Stockhouse website <http://www.stockhouse.com>, which is an internet website used by investors and interested parties to post information on securities (the “Stockhouse Website”). In particular, the following posts were made on the website:

- “We were told over and over again that the company would resume their activity once peace was established. That time has come but Rex has abandoned its plans.” (Posted February 5, 2004);
- “Walking away from the Sierra Leone permits makes absolutely no sense. These permits were held and religiously paid for each year even during the height of the civil war back in 2000. The company repeatedly stated that they would return to the country once peace was established. We are at that inflection point now.” (Posted February 5, 2004);
- “In reaction on the previous article about the licences in Sierra Leone, somebody of [sic] the Belgian chatsite received an e-mail back from Rex that RXD has made an agreement with the Sierra Leone government and that news will be out in the coming days. That could explain the volume and price rise.” (Posted February 18, 2004); and
- “It seems these guys don’t think anything material is PR worthy at all and I wonder (especially given the wild price and trading swings) how long it will be before the OSC and TSE yank the carpet.” (Posted March 3, 2004)

iii. RS’s Investigation into Rex’s Conduct

[104] Contact between RS and Rex commenced on February 19, 2004. On that date, RS had identified unusual trading patterns and contacted Rex’s Canadian counsel to ask whether any information could account for the increase in share price. Counsel for Rex advised RS that there was a private placement in the works and that he would verify with Rex whether there was any other cause for the increase in share price.

[105] On February 24, 2004 RS again contacted Rex’s Canadian counsel upon identifying fluctuation in Rex’s share price. Specifically, Rex’s opening price on February 23, 2004 was \$1.20 per share and on February 24, 2004 Rex’s shares opened at a price of \$0.96 per share. Counsel for Rex advised RS that he was only aware of a private placement that was subject to a close on March 22, 2004, and that he had verified with Rex that there were no other corporate developments.

iv. The February 2004 Trading Data

[106] As referred to in the comments posted on the Stockhouse Website, the value of Rex's shares and the trading volume fluctuated significantly during February 2004.

[107] For the two week period commencing February 16, 2004, the volume of Rex shares traded varied from day to day. For example, on February 18, 2004 the daily volume was 135,443 and on February 19, 2004, the daily volume was 828,651. In comparison, a year earlier during February 2003 the daily volume never exceeded 73,350, and for the month of January 2004, the daily volume never exceeded 100,120. Overall, the trading data provided in evidence revealed that the volume of shares traded increased significantly.

[108] During this same period the price of Rex's shares fluctuated from as low as \$0.93 per share (on February 16, 2004) to as high as \$1.25 per share (on February 19, 2004).

[109] In addition, the number of trades executed also increased dramatically. For example, on February 19 and 20, 2004, 204 and 129 trades were executed respectively. This is a huge variation in comparison to the daily number of trades which took place in January 2004, which never exceeded more than 25 trades in a day. Comparatively, in February 2003, the number of trades never exceeded 17 on a single day.

23. March 30, 2004: The Tender Evaluation

i. The Sierra Leone Government Gives Public Notice of the Tongo Diamond Field Tender Evaluation

[110] On March 30, 2004, the Sierra Leone Government issued the Tender Evaluation.

[111] The Tender Evaluation stated that:

The Government of Sierra Leone originally granted a Mining Lease for the Tongo Diamond Field to Rex Diamond Mining Corporation Limited, a small diamond mining and exploration company with its head office in Antwerp in February 1994.

[112] The Tender Evaluation also explained why the Leases had been revoked:

Following the official declaration of peace, announced in early 2002, companies that had been active in Sierra Leone prior to the war were invited to continue their work. ... A letter issued by the Ministry of Mines to exploration and mining companies in mid 2002 required them to confirm that they would restart their operations or give up their mineral rights. Rex Mining failed to commit sufficient resources to their exploration programmes. *As a result the Government cancelled their Tongo and Zimmi mining leases in October 2003.* [emphasis added]

[113] The Tender Evaluation declared Koidu Holdings SA as the winner of the Tongo diamond rights.

[114] Rex was not notified in any way by the Government of Sierra Leone of the Tender Evaluation. The Tender Evaluation was posted on the Government of Sierra Leone's Statehouse Website, but it was not posted on the website of the Ministry of Natural Resources of Sierra Leone.

ii. Rex's April 2, 2004 News Release in Response to the Tender Evaluation

[115] On April 2, 2004, Rex's management first became aware of the March 30, 2004 internet posting of the Tender Evaluation.

[116] As a result, Rex issued a news release on April 2, 2004 (the "April News Release"). The April News Release acknowledged that Rex learned that its Leases had been cancelled:

The Government of Sierra Leone has announced that it has cancelled Rex's diamond mining leases. To date no formal cancellation notice has been forwarded to Rex. Negotiations were being held for a reinstatement until yesterday.

[117] Further, the April News Release also contained a quote from Muller which explained that:

In 1997 Rex was the first company to resume operations in Sierra Leone after a long period of a brutal civil war. Force majeure was lifted in 2002 and in 2003 Rex had a team of geologists surveying the diamond deposits in view of commencing drilling in 2004. The decision of the government is opportunistic and arbitrary in nature. Rex has spent more than US \$6 million in Sierra Leone over a period of 8 years; only 3 years were stable and peaceful and secure operations possible. This move is not only unwarranted, unjust and unjustified, but it will diminish the possibility for Tongo fissures ever to be developed. This will needlessly raise the risk profile of the country and debase that standard of law and title in Sierra Leone. Rex is in the business of producing diamonds from underground kimberlite fissures in South Africa. Rex's strategy provides for the transfer of technology, know-how and experience in underground fissure mining gained in South Africa to Sierra Leone. These fundamental factors confirm Rex to be the most appropriate developer for the Tongo fissures. This precipitous resolution is ill advised and prejudicially motivated.

24. Rex's Share Performance Subsequent to the Tender Evaluation

[118] The highest number of trades for the month of April 2004 was 109 and that occurred on April 2, 2004, the day Rex issued the April News Release, which disclosed the existence of the Tender Evaluation. For the rest of the month of April the number of

trades did not exceed 39 per day. Investors reacted and the number of trades increased when knowledge of the Tender Evaluation was made public by Rex.

[119] On April 2, 2004, Rex's shares opened at \$0.60 and on that same day Rex's shares traded for as low as \$0.45, before closing at \$0.57. Previously, on April 1, 2004, (prior to the April News Release) the opening price of Rex's shares was \$0.74.

[120] During the first two weeks of April 2004, the volume of shares traded also fluctuated greatly. On April 2, 2004, the daily volume of shares was 511,630, which was the high for all of April 2004. This was uncharacteristically high compared to the daily volume for the rest of April 2004 which varied between a low of 13,190 (on April 6, 2004) to a high of 149,400 (on April 5, 2004).

25. April 2004 to August 2004: Rex Seeks Reinstatement of the Leases

[121] Subsequent to the April News Release, Muller and Morgenstern continued to correspond with the Government of Sierra Leone to try to reinstate the Leases to Rex.

[122] By letters dated April 5, 2004 and April 15, 2004, Rex wrote to the Minister of Ministry of Mines and Mineral Resources to request the reinstatement of the Zimmi Lease. The April 5, 2004 letter was signed by a representative of Rex and the April 15, 2004 letter was signed by Muller. Both letters stated that the Leases were "unfortunately withdrawn some time ago", but emphasized the "very cordial relationship between the Rex Mining Company and the people of Makpele Chiefdom and the fact that the Company is now fully ready in cash and materials for any mining operation".

[123] In addition, the Makpele Chiefdom corresponded with the Minister of the Ministry of Mines and Mineral Resources by letters dated May 5, 2004 and August 10, 2004 to support the reinstatement of the Zimmi Lease.

[124] On May 24, 2004, the Ministry of Mineral Resources wrote to the Makpele Chiefdom to explain its decision to cancel the Leases. According to the Ministry of Mineral Resources:

[Rex] held onto this licence for over Nine (9) years without exercising its obligations under that Licence in spite of several notices from this Ministry even after the expiration of the force majeure in January 2002.

This persistent inaction on the part of Rex resulted in the invocation of the relevant provisions of the Mines and Mineral Act, which was reinforced by a Cabinet decision, to extend the period for remedying the offences and eventually to cancel the Rex Mining Lease in October 2003.

[125] By letter dated June 1, 2004, the Minister of Mineral Resources informed the Makpele Chiefdom that the Ministry cannot cancel the decision taken by Cabinet to cancel the Leases. The Ministry further suggested by letter dated June 7, 2004, that the Makpele Chiefdom should encourage Rex to pay the outstanding fees of \$282,000.

[126] By letter dated June 23, 2004, the Ministry of Mineral Resources advised Rex that it owed a total of US\$141,000.00 for the Leases. In addition, Rex was informed that the Sierra Leone Government would only consider the appeal by the Makpele Chiefdom to reinstate the Leases after Rex effected full payment of the amounts owing.

[127] On July 23, 2004, Muller on behalf of Rex wrote to the Director of Mines, A.C. Wurie, of the Ministry of Mineral Resources, requesting that the Ministry reconsider their demand that Rex pay outstanding rents on the Leases. Rex reminded the Ministry that all prospecting/exploration and/or mining companies enjoyed the benefits of suspension of their obligations under their respective licenses throughout the *force majeure* period until January 18, 2002. Rex explained that:

Since the force majeure period covered the period for which we already paid the lease rents, it is but reasonable to believe that our obligations (financial and technical) under the licence remained suspended until the 18th January 2002 after which the suspension should have been lifted.

In light of the foregoing, the period for which the rents were paid, should have been rescheduled to take effect from 18th January 2002 in which case our payment should now cover the periods 18th January – 17th January 2003 and 18th January 2003 - 17th January 2004, thus eliminating the payment of any arrears of Mining Lease Rents by our Company.

[128] By letter dated August 4, 2004, the Director of Mines, A.C. Wurie, of the Ministry of Mineral Resources advised Rex that its indebtedness to the Government is now US\$126,000, in light of the reduction to the Zimmi Lease. The Ministry also articulated its position with respect to several prior contested issues as follows:

- (i) during the periods for which the Tongo lease rent was paid, the area was occupied by rebels and all of Rex's obligations under that license should have been suspended until January 18, 2002 when peace was officially announced;
- (ii) in the case of Zimmi, the area was not occupied by rebels, and was therefore accessible;
- (iii) although Rex honoured its financial obligation, Rex continuously defaulted on its technical obligation to conduct explorations and
- (iv) the cancellation of Rex's Zimmi and Tongo Leases stands as a result of the company's failure to honour its obligations set out in the Leases.

26. October 2004: RS's Inquiries Regarding the April News Release

[129] On October 6, 2004, RS wrote to Rex to inform them that RS was conducting a review of the trading in the shares of Rex and that this was prompted by Rex's April News Release. In particular, RS requested Rex to provide a chronology of events leading up to the April News Release.

[130] In addition, RS also requested that Rex provide the following information:

- State when Rex first became aware that the Government of Sierra Leone cancelled their diamond mining leases. Who notified Rex that the Government had taken such action?
- A chronological listing of all events and developments, including but not limited to, meetings, telephone conversations and correspondence, from the date when discussions or communications commenced regarding the events announced until the time of the press release on April 2, 2004. In your response, please include dates, names of individuals involved, their business affiliations, their role in the events announced, and a brief summary of significant matter discussed.

[131] On October 28, 2004, Muller responded to RS's request, and provided RS with Rex's Chronology of the relevant events.

B. The Witnesses

[132] During the hearing, we heard and considered evidence from four witnesses. Staff called two witnesses Arlene Cristello ("Cristello"), a senior investigative trading analyst with RS, and Shauna Flynn ("Flynn"), an investigation counsel with the Commission. The Respondents called two witnesses, Muller and Holemans.

1. Cristello

[133] Cristello gave testimony regarding the chronology of events surrounding the cancellation of the Leases and RS's investigation into those events.

i. The RS Investigation

[134] In April 2004, Cristello was assigned to review Rex's conduct. Her involvement began after Rex issued the April News Release, which announced that Rex became aware that the Government of Sierra Leone cancelled the Tongo Lease.

[135] On October 6, 2004, Cristello addressed a letter to Muller, requesting a chronology of information leading up to the April News Release in order to determine at what point in time Rex was made aware that the Leases had been cancelled.

[136] On October 28, 2004, on behalf of Rex, Muller corresponded with RS and provided a chronology of the events with respect to Rex's Leases and Rex's policy respecting disclosure to RS. Cristello explained that the policy stated that materiality determinations/assessments were to be made by the CEO, the CFO, and the chief geologist.

[137] On November 18, 2004, Cristello sent her report to the TSX and the Commission recommending investigation into possible insider trading and timely disclosure violations.

ii. Analysis of Trading Data Relating to the April News Release

[138] Cristello gave testimony relating to the trading data for Rex in the context of the April News Release. Cristello explained that the trading price data for March 30, 2004, preceding the news release, showed a downward price movement which triggered RS to request information from Rex Diamond. According to Cristello, the trading data of April 2, 2004, following the news release, then showed a significant decrease in the price of Rex shares and a significant increase in trading volume.

[139] On the issue of trading price, on cross-examination Cristello speculated that the downward price movement could have been attributable to the issuance of the April News Release since the stock would likely have opened following the issuance of the news release.

[140] On the issue of trading volume specifically, Cristello testified that volume was significant because it was well above what would be considered the normal daily trading volume since the average daily volume during April 2004 was 57,524 shares.

iii. Disclosure Made to RS

[141] Cristello testified that a number of documents were not presented to RS by Rex during the course of their investigation. They include:

- the letter from U.B. Kamara, Director of Mines, dated January 3, 2003, which advised Rex, “[I]n view of the several breaches of the terms of your leases, the Mineral Advisory Board has recommended to the Minister of Mineral Resources that the leases be terminated”;
- the letter from A.R. Wurie, Director of Mines, dated April 16, 2003 to Rex, which advised of continued breaches and warned the company to “honour financial obligations”;
- the letter from M.S. Deen, Minister of Mineral Resources, dated June 4, 2003 to Rex issuing final notice that the Leases would be terminated in 90 days if Rex did not comply with the requests of the Sierra Leone Government; and
- the letter from Fauvilla, dated December 15, 2003, written by Yigal Shapiro to Muller advising that the Government has issued the Tender.

[142] Cristello explained that these documents were relevant and important to determine the exact date when Rex was made aware of the cancellation of the Leases and that RS would have expected to receive them in response to their October 6, 2004 letter.

[143] Failure to disclose these documents left RS with the impression that Rex had not become aware of the cancellation of the Leases until January 30, 2004. In fact, Cristello emphasized that RS was not aware of any communications between Rex and the Sierra Leone Government prior to January 30, 2004.

[144] The chronology provided by Rex to RS was incomplete and relied on by Cristello as a complete account of events and used to produce her analysis of the Rex file.

iv. Cancellation of the Leases

[145] With respect to the cancellation of the Leases, Cristello explained that from her understanding of the Sierra Leone Government's Notice of Tender dated December 11, 2003, the Leases were cancelled in October 2003. However, she had difficulty reconciling the various dates which were either hand-written or printed on the Notice of Tender version which was retrieved from the Statehouse website.

v. Disclosure in the Public Filings

[146] On the issue of disclosure, Cristello explained that upon review of several public filings, she grew concerned over the lack of disclosure regarding Sierra Leone and the Leases.

2. Flynn

[147] Flynn gave testimony relating to the documents submitted to the Commission by Rex and Staff's voluntary interviews with Muller and Holemans.

i. Staff's Investigation

[148] Flynn testified that Staff's investigation began with a letter dated June 6, 2005 in which she asked for all documents relating to the Sierra Leone properties for the period August 1, 2003 to April 4, 2004. Flynn testified that Staff received documentation through Rex's counsel on June 29, 2005, as well as at the voluntary interviews of Muller and Holemans, and subsequent to those interviews through answers to undertakings.

[149] Flynn testified that Staff did not obtain any information from the Government of Sierra Leone, nor were any requests made to the Government of Sierra Leone.

ii. Review of Correspondence Relating to the Cancellation of Leases

[150] In her testimony, Flynn reviewed correspondence between the Government of Sierra Leone and Rex as well as other documents relevant to the cancellation of the Leases. Her testimony described below helped to provide insight with respect to Rex's actions.

[151] Flynn testified that Rex made no reference in its chronology to the letters from March 18, 2002 to August 23, 2003. However, during cross-examination Flynn testified that correspondence dated from January 3, 2003 to June 4, 2003 was provided on a voluntarily basis by Rex to the Commission on June 29, 2005. Flynn further testified that these documents were provided in response to Staff's inquiry dated June 6, 2005.

[152] Flynn testified that she asked Muller why the information contained in the letters dated March 18, 2002 and January 3, 2003 was not disclosed, and she stated that Muller replied that since negotiations with the government were ongoing, Rex's officers determined that the information was not material and did not require disclosure.

[153] With respect to the Notice of Tender, Flynn testified that she received a copy of the Notice both from Rex and from RS but that it was unclear when it was posted: the Notice itself it is dated December 5, 2003; the printout attached, which seems to be an overview of news and information in Sierra Leone dates the Notice at December 11, 2003; and the chronology provided by Rex dates the Notice at December 10, 2003. Flynn testified that she did not determine the exact date but assumed that it was either posted on December 10 or 11, 2003. For the purpose of our Analysis we accept that that Notice of Tender was posted on December 11, 2003 and this is reflected in our chronology of events set out above.

[154] Flynn also reviewed a letter addressed to Muller dated December 15, 2003, written by Yigal Shapira on behalf of Fauvilla advising that the Sierra Leone Government had issued the Notice of Tender. Flynn testified that she asked Muller why this letter was not referred to in the chronology provided to RS. Muller explained that the letter was not provided at that time because it had been filed incorrectly and recovered during his review of the file for the purpose of the civil proceedings against Fauvilla. In cross-examination, Flynn further testified that the letter was indeed provided to Staff on a voluntary basis upon its recovery.

[155] Flynn also questioned Muller about the e-mail correspondence that took place in January 2004. Flynn testified that when asked to explain the basis for the e-mail correspondence, Muller had stated in his interview that Holemans had come to him for an answer, that he had then gone to both Morgenstern and A. R. Wurie to inquire further, and that Wurie had told him: "It's all about the mining leases and that they refuse to pay. We will cancel the tendering if we come to an agreement." Flynn testified that she inquired as to whether Muller had any documentation confirming the discussion with Wurie and that Muller advised that he did not have anything of the sort in writing.

[156] In addition, during her testimony, Flynn pointed out that the chronology provided by Rex to RS (and its representation that the company first became aware of the tender on January 30, 2004), it is not consistent with other documents, including the Fauvilla letter.

iii. Review of Documents Relating to Disclosure

[157] Flynn also reviewed various public documents and correspondence between the Government of Sierra Leone and Rex relevant to the disclosure of information relating to the cancellation of the leases.

[158] Flynn reviewed Rex's Consolidated Financial Statements for the years ended March 31, 2003 and 2002 and testified that they did not make any mention of the correspondence that was passing between the Sierra Leone Government and Rex regarding the possible cancellation of the Leases. In cross-examination, Flynn testified that the document does, in a footnote halfway down the page, contain general cautionary language that operations may or may not start up on the properties; however, there was still no mention of any specific risks.

[159] Further, Flynn reviewed the 2003 AIF and testified that it did not indicate that the Leases were the subject of correspondence with the government regarding their possible cancellation. In fact she explained that the document states that Rex holds the leases until February 28, 2019. In cross-examination, Flynn testified that the document included cautionary language concerning the prospects in Sierra Leone, but again there is no mention of any specific risks that existed at the time the 2003 AIF was filed.

[160] Similarly, Flynn reviewed Rex's Annual Report filed August 19, 2003 and testified that it did not have any indication as to the correspondence that was passing between the Government of Sierra Leone and Rex regarding possible cancellation of the leases. During cross-examination, Flynn testified that Muller disclosed to shareholders on page 3 of the Annual Report that the arrangement with Fauvilla regarding Zimmi was not proceeding as hoped.

iv. Rent Pre-Payments

[161] Flynn reviewed in detail the issue of the rent pre-payments from 1997-1999 (when she explained that Rex chose not to take advantage of the *force majeure* clause but later tried to invoke the clause to recover the lease payments).

[162] To summarize, Rex paid \$276,122 in rent for the Leases for the period 1997-1999 despite not being engaged in actual mining in Sierra Leone during this time due to the *force majeure*. In its fiscal 1999 financial statements, Rex wrote down its mining assets and capitalized mining costs by \$3,145,904, leaving only a net carrying value of \$400,000 on its books for containerized and secured mining equipment on the ground in Sierra Leone.

3. Muller

[163] Muller's testimony focused on explaining how the Sierra Leone Government operates, and the type of approach that the Sierra Leone Government takes in its business dealings. The relevant excerpts of his testimony relating to the correspondence with respect to the cancellation of the Leases and content of the public disclosure documents are summarized below.

i. Review of the Correspondence Relating to the Cancellation of the Leases

[164] First, Muller reviewed the letter dated March 18, 2002 from the Sierra Leone Government to Rex, which advised the company that the *force majeure* was lifted. Muller testified that the letter was provided to Rex a couple of months later (July not March) which demonstrates inconsistency within the Government of Sierra Leone's records. Further, Muller explained that a team had been put in place to do the work and stated his view that the fact that the letter was sent to Rex not even a year after the *force majeure* was lifted signals that it was simply a malicious letter.

[165] Muller also reviewed the January 3, 2003 warning letter that the Leases were at risk of being terminated. Muller testified that "this is a typical letter that Usman Kamara would issue in order to try to extract from you something". Muller further

emphasized that “it’s not because [the letter] says so that it means so”. He explained that action was not taken immediately upon receipt of this letter because “you never give a guy like this anything because he is corrupt”. According to Muller, the January 3, 2003 warning letter was just a threat. He also stated that Morgenstern advised him that Usman was making trouble again and reminded him that it was not the first letter of that kind that Rex had received. Finally, Muller added “on a letter like that, the only thing you do is call the Director of Mines [who] tells you to disregard it”. Muller testified that he did indeed call Wurie, the Director of Mines that same day.

[166] Muller also reviewed the correspondence from Rex in February 2003 relating to Rex’s Work Programme and the outstanding payment on the Leases. Muller explained that Morgenstern sent this letter without consulting him. He testified that he asked Morgenstern to fix this problem because Rex had already paid the rent on the Leases. Muller explained that this letter was not an issue of importance to him since Sierra Leone was relatively low in importance and value for the company and that in his opinion this was understood by Rex’s shareholders.

[167] Muller’s testimony also addressed the April 16, 2003 warning letter. According to Muller, Wurie sent this letter because Wurie was likely coming under pressure from the Sierra Leone Government to ensure that the payments on the Leases were made. Muller explained that he did not disclose this letter because Rex had already paid the amounts owing on the Leases and was engaged in a negotiating process with the Sierra Leone Government. Muller explained that “the dispute itself between Rex and the Government is not sufficient to disclose”. As for the Final Notice letter dated June 4, 2003 Muller testified that the response was made locally by Morgenstern.

[168] With respect to the Fauvilla Letter, Muller testified that he sought Morgenstern’s opinion locally regarding who to deal with on this and that Morgenstern replied, “It’s just a letter of intimidation. Don’t ever give it attention. They just want to get you to back off after the court case that you are filing against them”. As a result, Muller emphasized that this letter was not given attention and that it went into the “Fauvilla file”, not the Sierra Leone file, and that it only resurfaced in the process of civil proceedings with Fauvilla in Israel. He added that neither the Fauvilla Letter nor the Notice of Tender were discussed at board meetings.

[169] In his testimony, Muller also addressed the e-mail correspondence that was exchanged in January of 2004, in particular the e-mail from Rombouts which raised the issue of materiality. Muller testified that Rombouts was simply “questioning whether the information was material” and that he did not engage in discussions with Rombouts about this matter because he felt that it was a temporary problem that could be solved by negotiation. Muller concluded that it was a matter of judgment and that he personally decided that it was not material information requiring disclosure.

[170] Muller also testified that when Holemans sought his advice with respect to the risk of the cancellation of the Leases, he called Wurie who in turn advised him, “it’s all about the mining leases that you refuse to pay. We will cancel the tendering if we come to an agreement”. Muller emphasized that he wrote to Rombouts exactly what Wurie had

[171] With respect to the Tender Evaluation, Muller testified that he was not given direct notice of it and that it was the first time, to his knowledge, that a document like this was issued on the website of the Sierra Leone State House.

ii. Review of Documents Relating to Disclosure

[172] According to Muller, the risk of the cancellation of the Leases was a matter to be negotiated with the Sierra Leone Government, and as a result it was of no relevance and it was not mentioned in the February 28, 2003 news release. He explained that Rex had disagreements with the Sierra Leone Government on numerous occasions which had been successfully settled and in his view the threat of the cancellation of the Leases was an issue that could be settled with the Sierra Leone Government. He also testified that the issue was a material fact, but not material enough to stand on its own in a news release; however, the fact that a camp was being set up in order to mine was indeed worthy of disclosure and this was mentioned in the February 28, 2003 news release.

[173] With respect to the 2003 AIF, Muller gave the following explanation during his voluntary interview with Staff:

My personal view at the time was that I wasn't willing to go and spend capital into Sierra Leone because I didn't think the country was safe and stable enough ... However, on exploration, on surveying with Luc Rombouts under Tongo properties, I was willing to spend money. I brought in Fauvilla because Fauvilla claimed and they undertook to spend money that I wasn't willing to spend there.

[174] Muller also emphasized that the 2003 AIF contained cautionary language. In his words:

it's a very measured statement ... we do not promise to make big things, we resume activities. It's a very measured and very gradual wording and it reflects what my thinking at the time was. Don't rush into it. Go step by step. There's no need to go and spend extra money here. The ground is still warm. This is a war zone still.

[175] Further, Muller explained that Rombouts presented a program to the Sierra Leone Government, got approval for it, then organized logistics. Then the team carried on work for a few months.

[176] Muller also reviewed the MD&A filed November 28, 2003. He explained that the shipments of diamonds related to an agreement with Kassin Basma, not to Rex's mining activities/operations. He further explained that this agreement between Rex and

Basma was not disclosed in public documents because it was “a verbal agreement with a trader”. In addition, Muller explained his reasoning behind the wording of the MD&A as follows:

In the ten years that Rex is a company, we always said that we are a company that is active in all the facets of the diamond trade, namely, exploration, mining, production and trade. ... we never disclosed that we produced from these mines, just the opposite. We said that we moved equipment with Fauvilla. We did not say that Fauvilla produced the diamond. ... Between survey on Tongo Fields, moving equipment with Fauvilla and production coming to Antwerp, there's a big gap, and there's nothing in between. So it's no one to jump that gap and say that we tried to mislead anybody by saying that we produced something, diamonds – we imported diamonds from Sierra Leone.

[177] Further, Muller testified that Rex expected imports of rough diamonds from Sierra Leone to reach a sustained level of \$2 million dollars per year, and that he was dealing with the number one or number two diamond exporter in Sierra Leone whom he believed could easily provide the volume necessary for Rex to be importing \$2 million per month within a year.

[178] Muller also reviewed Rex's news release dated April 2, 2004 announcing the Tender Evaluation and provided explanations for alleged misrepresentations regarding the company's investment in Sierra Leone. According to Muller, operations were not commenced in Sierra Leone because, although peace and stability returned to the region, it was still a very risky region.

4. Holemans

[179] The relevant excerpts of Holemans' testimony relating to the correspondence with respect to the cancellation of the Leases and content of the documents containing the public disclosure, are summarized below.

i. Review of the Correspondence Relating to the Cancellation of the Leases

[180] With respect to the January 3, 2003 warning letter, Holemans testified that he did not personally see or have any discussions regarding this letter, but stated that Muller and Morgenstern would have been aware of it. He added that in hindsight he did not know why a news release would not have been issued; however, Holemans conceded that although it was his and Muller's responsibility to make materiality assessments, he did not know why a news release was not issued at the time.

[181] With respect to the April 16, 2003 warning letter, Holemans testified that Rex did not pay the rents after specifically requesting rent figures because Muller had said that the rents were covered by the 1997 and 1998 pre-payments. He also added that Sierra Leone was “minor when you look to the whole group of operations” of Rex, and that Muller concluded that the information was not material. Holemans testified: “everything

regarding Sierra Leone was totally Serge's hands. If he decided not to give this to me or bring it to my attention, I follow what he thinks on that."

[182] Holemans also testified that some of the correspondence from the Sierra Leone Government was never brought to his attention. For example, Holemans testified that the final notice letter dated June 4, 2003, the Notice of Tender and the Fauvilla Letter were not brought to his attention, and he did not know about them at the time.

[183] Holemans also testified with respect to the e-mail he sent to Lay on January 23, 2004. He explained that he told Lay the re-tendering was a "rumour" because this is what Muller instructed him to write. He added that Muller did not provide him any basis for that answer, despite the fact that the Notice of Tender had been posted on the Sierra Leone Government website since December 11, 2003; nevertheless, Holemans did not recall asking any further questions or discussing the matter with either Muller or Morgenstern.

[184] Holemans also informed us that he reviewed Rombouts' e-mail sent on January 31, 2004, which alerted Rex to the Notice of Tender and inquired whether this was material information. Holemans testified that he discussed the matter with Muller, and was aware of Muller's response that this was just a matter of paying the amounts outstanding on the Leases.

[185] With respect to the Tender Evaluation, Holemans testified that he became aware of it sometime in April, through his own searches on the internet. He also reviewed Rex's April News Release, which acknowledged the Tender Evaluation. Holemans testified that on April 2, 2004 the issue was 'material' because by then it was a fact that the leases had been cancelled, not withstanding his personal view that Sierra Leone was not important. He stated, "I went to [Muller], I said, now it's material because now we really lost it ..." but Muller's reasoning throughout this time was that you don't have to issue a news release for every rumour.

[186] The transcript of Holemans' voluntary interview also stated that although Holemans would not have known that the cancellation of the Leases was a fact until April 2, 2004, Muller and Morgenstern would have known that it was a fact at a much earlier stage – through the series of letters dated January 3, 2003, April 16, 2003, and June 4, 2003.

[187] Further, Holemans added that Muller was engaged in negotiations with the Sierra Leone Government on this issue and that he was taken by surprise by news of the cancellation of the Leases. Finally, he noted a 'mistake' in the Rex news release where it is stated, "the Government of Sierra Leone has announced that it has cancelled Rex mining leases" (plural). He stated that reference should only be made to the Tongo Lease (singular).

ii. Review of Documents Relating to Disclosure

[188] Holemans reviewed the 2003 AIF and testified that there was a general understanding that since President Kabbah had returned to Sierra Leone stability would

follow. He explained that the correspondence from the government regarding the cancellation of the Leases was not discussed in the public filings because he “did not have that information at that time”.

[189] With respect to the MD&A filed February 28, 2003, Holemans testified that it referred to the Fauvilla MOU and the equipment which was purchased for \$350,000. He explained that the drilling program was never commenced because it was too expensive to carry out and this was not disclosed by Rex because they did not feel that it was material at the time.

[190] Holemans also reviewed Rex’s MD&A filed November 28, 2003. He testified that the representations about diamond purchases were arrived at with the diamond buyer in Sierra Leone, together with Muller and Morgenstern.

V. ANALYSIS

A. Did a Material Change Occur in the Business, Operations or Capital of Rex?

1. The Statutory Regime

[191] In this case, the Amended Statement of Allegations relates to conduct which took place in 2003 and 2004. The relevant sections of the Act which were in force at that time are set out in “Schedule A” of our Reasons and Decision.

2. Disclosure Obligations Under the Act

[192] Section 75 of the Act creates a disclosure obligation for reporting issuers when a material change occurs. Subsection 75(1) of the Act provides that “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”. Subsection 75(2) requires the reporting issuer to file a report of a material change “as soon as practicable and in any event within ten days of the date on which the change occurs”.

[193] The Act is supplemented by National Policy 51-201 – Disclosure Standards (“NP 51-201”). Subsection 4.2(2) states that “... if there is any doubt about whether particular information is material, we encourage companies to err on the side of materiality and release information publicly”.

[194] The definition of “material change” is set out in subsection 1(1) of the Act as follows:

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 any of the securities of the issuer.

[195] This definition can be broken down into two separate parts: the first part requires determining whether a change took place, and the second part requires assessing

whether the change would reasonably be expected to have a significant effect on the price/value of the securities.

[196] The first part of the “material change” definition distinguishes a “material change” from a “material fact”. Basically, not all material facts are significant enough to be classified as a change in the business, operations or capital of an issuer. As explained by the Commission in *Re AiT* (2008), 31 O.S.C.B. 712 at para. 210:

Not all material facts will be significant enough to constitute a change in the business, operations or capital of the issuer, and therefore be a material change. The Act makes an important distinction between the definitions of a material fact and a material change in subsection 1(1). This distinction is fundamental to the various requirements under the Act since certain disclosure requirements are triggered by the occurrence of a material change (but not a material fact).

[197] Therefore, we must consider the events that took place and determine whether they are sufficient to constitute a material change or whether they are simply material facts which do not have to be disclosed pursuant to section 75 of the Act. This is imperative because material changes and material facts trigger different legal obligations:

For example, only in the event of a material change does section 75 of the Act require an issuer to issue a news release and also file with the Commission a material change report on a timely basis, or alternatively file a confidential material change report with the Commission. In contrast, section 76 of the Act does not require disclosure of either material changes or material facts, but prohibits anyone from purchasing or selling securities with knowledge of a material fact or material change that has not been generally disclosed to the public. (*Re AiT*, *supra* at para. 210)

[198] Further the Commission emphasized in *Re AiT* that:

The legislation clearly differentiates between material changes and material facts, setting up different disclosure obligations and restrictions for each. It clearly contemplated that issuers might be aware of a material fact and insiders must be prevented from trading with such knowledge (section 76 of the Act). However, the existence of a material fact alone does not give rise to the disclosure obligation under section 75 of the Act. (at para. 213)

[199] The second part of the “material change” definition is referred to as the market impact test. Section 4.1 of NP 51-201 confirms that the definition of “material change” is based on a market impact test. As explained by the Commission in *Re YBM Magnex et al.* (2003), 26 O.S.C.B. 5285:

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 securities. (at para. 91)

[200] Section 4.2 of NP 51-201 also recognizes that a determination of materiality is not always straightforward and there is no “simple bright-line standard or test”. This has also been recently confirmed by the Commission in *Re AiT* where the Commission explained that:

We agree that there is no “bright-line test”. Instead, the assessment of whether a material change has taken place will depend on the circumstances and series of events that took place. This is because the determination of a material change is a question of mixed fact and law (*Re YBM Magnex et al., supra* at para. 94). This determination requires ascertaining whether the existing facts fulfill the legal test. Each case will be unique, and the specific facts and circumstances will vary case by case. Since the fact scenarios will differ in all cases, it is impossible to articulate a bright-line test that will apply in all circumstances. (at para. 215)

[201] The assessment of whether a material change has occurred is a fact specific exercise. It is for this reason that we have set out an extremely detailed chronology of events above in order to provide a clear timeline of all the relevant facts. This fact intensive approach is consistent with the approach the Commission adopted in *Re AiT*, which was articulated as follows:

... the determination of whether a material change occurred requires ascertaining whether the series of events that took place during the Relevant Period constitute a material change. As a result, this requires an in depth analysis of the facts in this case. (at para. 225)

[202] The parties also relied on American case law with respect to materiality. We note however, that the legal concepts found in American law are not worded identically to the Ontario Statute. Specifically, the Commission explained in *Re AiT* that:

... the law in the United States does not include the concept of a "material change" as defined in our Act. The probability/magnitude test was formulated as an appropriate test for determining the materiality of speculative or contingent information. Although the American probability/magnitude test may be useful with respect to materiality, it is not particularly useful in determining whether a change has occurred, which is crucial in this case. As a result, we are wary of quoting and adhering to the American case law, especially when the American law does not incorporate the concept of a "material change" as the Ontario statute does. (at para. 207)

3. Best Disclosure Practices

[203] The Commission has often emphasized that disclosure forms the cornerstone of securities regulation (*Re Philip Services Corp.* (2006), 29 O.S.C.B. 3971 at para. 7). It benefits the capital markets because:

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 ... (*Re YBM Magnex et. al.*, *supra* at para. 89)

[204] The purposes of the Act set out in section 1.1 to: (1) provide protection to investors from unfair, improper or fraudulent practices, and (2) foster fair and efficient capital markets and confidence in capital markets, are largely achieved through truthful and accurate disclosure. This is because enforcing requirements for timely, accurate and efficient disclosure is one of the primary means of fulfilling the Act's statutory purposes (see section 2.1 of the Act). As explained by the Commission in *Re AiT*:

... through timely disclosure, fairness can be achieved for all investors participating in the capital markets. Disclosure serves to level the playing field such that all investors have access to the same information upon which to make investment decisions. (at para. 199)

[205] Because disclosure plays such an important role in ensuring that the capital markets are functioning on current, truthful and accurate information, it is essential that all market participants follow best disclosure practices. As explained by the Commission in *Re YBM Magnex et al.*, *supra* at paragraph 518, disclosure "enhances fairness of the market". In order for disclosure to accomplish its objectives, the information made public by issuers needs to be accurate. Premature and undesirable disclosure is unhelpful and does not enhance informed decision making in the capital markets.

[206] NP 51-201 provides guidance on best disclosure practices. Subsection 2.2(2) of NP 51-201 is of importance in our analysis and states:

Announcement of material changes should be factual and balanced. Unfavourable news must be disclosed just as promptly and completely as favourable news. Companies that disclose positive news but withhold negative news could find their disclosure practices subject to scrutiny by securities regulators. A company's press release should contain enough detail to enable the media and investors to understand the substance and importance of the change it is disclosing.

[207] Subsection 2.2(2) of NP 51-201 clarifies the type and quality of information that should be disclosed. It is highly important the right kind of information is made public because otherwise inadequate disclosure will trigger incorrect market signals.

[208] Further guidance is also given in section 4.3 of NP 51-201, which provides examples of potential material information. For the purposes of the present case, the following examples of potential material information are relevant:

- any development that affects the company's resources, technology, products or markets;
- major disputes or disputes with major contractors or suppliers; and
- significant new contracts, products, patents or services or significant losses of contracts or business

[209] Furthermore, best disclosure practices dictate that when in doubt, an issuer should err on the side of disclosure. This is established in NP 51-201 at subsection 4.2(2) and in the Commission's case law:

The concept of material change, like that of material fact, requires an exercise of judgment. If the decision is borderline, then the information should be considered material and disclosed. In our opinion, a supercritical interpretation of the meaning of material change does not support the goal of promoting disclosure or protecting the investing public. (*Re YBM Magnex et al.*, *supra* at para. 518)

4. Assessment of the Evidence

i. The Warning Letters dated January 3, 2003, April 16, 2003 and June 4, 2003

[210] On January 3, 2003 and April 16, 2003, Rex was warned by the Sierra Leone Government that the Leases were at risk of being cancelled. Then on June 5, 2003 the Sierra Leone Government sent an additional warning letter giving Rex 90 days notice that the Leases would be terminated if Rex did not comply with the Sierra Leone Government's conditions.

[211] We find that by the time Rex received the final notice warning letter dated June 5, 2003, and probably earlier in 2003, there was a very possible risk that the Leases would be cancelled by the Government of Sierra Leone, and this should have been communicated to the public by means of a material change report pursuant to section 75 of the Act. This is evident from the correspondence that was put into evidence before us. For example, the warning letters dated January 3, 2003, April 16, 2003 and June 4, 2003 all advised Rex that if it continued to fail to comply with the obligations set out in the Leases, the Leases would be revoked. The Notice of Tender issued December 11, 2003, reinforced the risk that Rex's Leases were in danger and the Tender Evaluation dated March 30, 2004, confirmed that Rex did indeed lose the Leases.

[212] Clearly, the risk was high that the Leases would be cancelled, otherwise Rex would not have engaged in the efforts it did to rectify the situation. In particular, Morgenstern, on behalf of Rex, contacted the Makpele Chiefdom to seek support from them and the Makpele did in fact support Rex and provided letters to the Sierra Leone Government to attempt to persuade the Government to allow Rex to keep the Leases. Also, Morgenstern, on behalf of Rex, sent correspondence to the Sierra Leone Government in February 2003 to ascertain the amounts owing on the Leases in order to take steps to make payments on the Leases.

[213] In our view, the Leases constituted an important asset to Rex as the public filings made reference to their high potential value. In addition, the Rombouts Report described the Tongo Lease as having a potential value to Rex of US\$1,654 billion if mined to a depth of 500 metres, and US\$3.31 billion if mined down to a 1,000 metres depth. Potential values in the range of billions of dollars undoubtedly establish that the Tongo Lease was an important asset.

[214] The value of mining assets is highly relevant in a material change determination as established by the Supreme Court of Canada in *Pezim v. British Columbia (Superintendent of Brokers)*, [1994] 2 S.C.R. 557, where the Court stated:

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. (at para. 87)

[215] The Leases had a high potential value to Rex, and developments concerning them would be of interest to shareholders. The fact that the Leases along with their high potential was at risk of being lost should have been disclosed in a material change report.

[216] In its public filings, Rex's disclosure with respect to Sierra Leone tended to be generally optimistic. While Rex's public filings did refer to the existence of some political uncertainty in Sierra Leone, Rex's public disclosure had an optimistic tone. A review of the evidence shows that the outlook was not entirely positive and the letters dated January 3, 2003, April 16, 2003 and June 4, 2003 involved a very possible risk to Rex's assets – the Leases. Without these Leases, Rex did not have the ability to produce diamonds in Sierra Leone. On this point, the Respondents took the position that a deal with Basma provided Rex with rough diamonds to export back to Belgium, but the evidence at the hearing revealed that this deal did not work out and Basma was corrupt. Therefore, Rex really needed the Leases in order to have access to rough diamonds.

ii. The Notice of Tender

[217] The Notice of Tender was issued on December 11, 2003. It clearly stated that it applied to mining areas previously belonging to Rex, which signaled that Rex's Leases had been revoked.

[218] As Staff pointed out to us in their submissions, "if investors are justifiably concerned about the estimated mineral content of mining property, so too must they be entitled to know whether the company holds that asset at all." The public should have been informed after Rex found out about the Notice of Tender which clearly indicated that Rex lost the Leases. That affected Rex's operations because it would no longer have legal entitlement to access the land and extract diamonds. We agree with Staff that "the loss of the Sierra Leone Leases eliminated any potential for Rex to generate future revenue from those operations" and in our view this constitutes a change in Rex's operations.

[219] Indeed, the Notice of Tender was significant in the minds of Rex's shareholders. During February and March 2004 investors made inquiries to Rex regarding the status of the Leases and postings about the status of the Leases were made by investors on the Stockhouse Website.

[220] Not only was there a failure to disclose the dispute regarding the Leases, but also there was a failure to disclose the loss of the Leases altogether after Rex learned about the Notice of Tender.

iii. The Tender Evaluation

[221] Similar to the Notice of Tender, the Tender Evaluation signaled that a change occurred in Rex's operations and assets because it established that the Leases once belonging to Rex had been officially transferred to another company. Rex's ability to operate in Sierra Leone was significantly changed.

iv. Market Impact

[222] It is evident that the risk that the Leases could be cancelled – and especially the actual cancellation of the Leases – constituted a change in Rex's business.

[223] The issue before us now is to determine whether this change was “material”. In other words, is it reasonable to expect that there would be a significant effect on the market price or value of any of the securities of the issuer? We find that it was reasonable to expect a significant market impact for the reasons described below.

[224] The Notice of Tender was issued on or about December 11, 2003. It clearly stated that the property in question formerly belonged to Rex. Following the Notice of Tender in December 2003, in February 2004, rumours started to circulate about Rex's Leases and a number of queries and comments were posted on the internet and made reference to Rex's share price.

[225] At the same time fluctuations in the value of Rex's shares were occurring. As well the volume of shares traded and number of trades per day varied significantly from the norm.

[226] These day to day variations in the opening and closing prices of Rex's shares and the high trading volume were not the norm in Rex's daily trading patterns. This prompted RS to contact Rex on February 19, 2004 to inquire what events could possibly be triggering such huge share price fluctuations.

[227] In our view, abnormal fluctuations in share prices, volume and the number of trades per day demonstrate market impact, and indicate that the market is reacting to something. Investors reacted and trading activity, especially volume and number of trades per day increased. In our view this demonstrates that investors had an interest in Rex's operations in Sierra Leone, and they traded accordingly when they became aware of rumours regarding Sierra Leone. Indeed, after all these fluctuations in Rex's share price were taking place, an investor posted a comment on a website in early March commenting that there were wild price and trading swings and Rex had not disclosed any “PR worthy” information.

[228] The Tender Evaluation was issued on March 30, 2004. This made it official that Rex had lost the Leases. Rex issued a news release on April 2, 2004 to disclose this information to the public, and following the April News Release, Rex's share price

fluctuated and the volume of shares traded was very high on April 2 and 5. To summarize, upon finding out about the cancellation of the Leases, the market reacted as follows:

- from April 1, 2004 to April 2, 2004, the opening price in Rex's shares decreased by 18.92%; and
- from April 1, 2004 to April 2, 2004, the closing price in Rex's shares decreased by 18.57%.

[229] The above numbers show that the market reacted to the announcement that Rex had lost its Leases. This shows that the investing public thought the Leases had important value to Rex.

[230] In their defence, the Respondents argued that Sierra Leone was not material and that the Leases were not the focus of Rex's activities at the time. The Respondents take the position that the Leases in Sierra Leone were "interesting but not material". We do not accept this submission. The Rombouts Report favourably described the area covered by the Leases as potentially having extremely high value. In addition, in an e-mail dated January 30, 2004, Rombouts mentioned that information with respect to the cancellation of the Leases "... is material information if confirmed...". The evidence also shows that Rex went through a lot of effort to negotiate with the Sierra Leone Government to have the Leases reinstated. Previously, when Rex lost a lease that did not have as important a value, they did not bother with such efforts, as in the case with the Block 13 Lease.

[231] The Respondents also submitted that:

An analysis of the trading in shares of Rex in relation to news or events concerning Rex's mining leases in Sierra Leon reveals that, with the possible exception of news of the military coup on May 25, 1997, news or events relating to Rex's mining leases in Sierra Leone had no discernible affect on the Rex share price, and certainly had no "significant effect".

[232] We do not accept this submission. On April 2, 2003, there was an approximate 18% decrease in the value of Rex's shares accompanied by a very high volume of trading, when news of the Tender Evaluation and loss of the Leases became known to the public. In our view the market was reacting to the announcement that Rex lost the Leases.

[233] In addition, at this time, Rex's public filings mentioned that Rex's operations in South Africa were not performing well due to floods and a workers' strike. The outlook for Mauritania was also bleak. However, Rex never provided negative information about Sierra Leone. Conversely, in its 2003 AIF, Rex stated that peace and stability were returning to Sierra Leone and the impression was given that mining activities would soon resume as Rex had entered into the Fauvilla MOU. The MD&A filed on November 28, 2003 also focused on diamond shipments from Sierra Leone. Looked at as a whole, we find that the public filings show that Sierra Leone had a positive outlook and was important to Rex's future, especially considering that Rex's

operations in South Africa and Mauritania were on the decline. As a result, we find that the Sierra Leone operations were material to Rex and that a reasonable investor would read the public filings and information about Sierra Leone as being positive for Rex.

[234] We find it problematic that Rex had knowledge of the fact that it could potentially lose its Leases and Rex never revealed the final notice warning letter dated June 5, 2003 to the public. In our view, Rex should have issued a material change report when it initially learned that there was a risk that it would lose the Leases. This is because the loss of a right to mine for diamonds would impact the operations of a diamond exploration company such as Rex and this in turn would affect Rex's ability to generate profit and share price would be affected accordingly.

B. If a material change did occur, did Muller in his capacity as a director and the CEO of Rex and Holemans in his capacity as Rex's CFO, authorize, acquiesce in or permit a breach by Rex of section 75 thereby acting contrary to the public interest?

1. Overview

[235] In our view, both Muller in his capacity as a director and the CEO of Rex and Holemans in his capacity as CFO, authorized, permitted or acquiesced in Rex's breach of section 75 of the Act. However, we recognize that Holemans' conduct is not as blameworthy as Muller's conduct since Holemans lacked awareness of many of the events that transpired. This is explained further below.

2. Muller

[236] The testimony at the hearing revealed that Muller's opinion was given deference and that he determined that the Notice of Tender was not material. However, we note that at this same time others feared or recognized that it was in fact material. For example:

- Rombouts raised the issue of materiality to Rex in his e-mail dated January 30, 2004; and
- the Fauvilla Letter made reference to the fact that the Notice of Tender may materially impact the Fauvilla MOU and Rex's operations in Sierra Leone.

[237] Despite having knowledge of Rombouts' e-mail and the Fauvilla Letter, Muller unilaterally decided not to issue a material change report. Muller's actions concern us because he withheld important information about a change to Rex's assets, namely a Notice of Tender announced that Rex lost its Leases. The evidence demonstrates that Muller disregarded the correspondence he received from the Sierra Leone Government between January and June 2003 and he did not share this information with Holemans.

[238] Muller's testimony also revealed that Muller relied on his personal discretion when he made decisions with respect to disclosing information about the Leases to Holemans and to the public. Muller emphasized that he knew what was appropriate in the

circumstances based on his experience in business dealings with officials from the Government of Sierra Leone. While we recognize that Muller has an in-depth understanding and knowledge of the mining business and significant experience dealing with the Sierra Leone Government, Muller's judgment as to what information should or should not be disclosed cannot take precedence over the disclosure obligations set out in the Act. As established by the Supreme Court of Canada, the business judgment rule does not apply to decisions regarding disclosure:

... disclosure is a matter of legal obligation. The Business Judgment Rule is a concept well-developed in the context of *business* decisions but should not be used to qualify or undermine the duty of disclosure. (*Kerr v. Danier Leather Inc.*, [2007] 3 S.C.R. 331 at para. 54)

[239] The evidence demonstrates that Muller withheld information with respect to the cancellation of the Leases from Holemans and the public. As a result, we find that he authorized and permitted Rex to violate section 75 of the Act and thereby acted contrary to the public interest.

3. Holemans

[240] The evidence revealed that Holemans did not possess the same amount of information with respect to the problems relating to the Leases as Muller did. Holeman's knowledge was the following:

- matters relating to Sierra Leone and the Leases were in Muller's hands, and issues were brought to Holemans' attention only when Muller thought it was necessary;
- he did not personally see or have any discussions regarding the January 3, 2003 warning letter, the final notice letter dated June 4, 2003, the Notice of Tender and the Fauvilla Letter at the relevant times. Muller did not bring these documents to Holemans' attention;
- with respect to the April 16, 2003 warning letter, Holemans followed Muller's instructions that the rent payments did not have to be made because the rents were covered by the 1997 and 1998 pre-payments;
- with respect to the e-mail to Lay, Holeman's actions were based on Muller's instructions; and
- Holemans was surprised when he found out that the Leases were cancelled because Muller gave him the impression that problems with the Leases such as the rent payments were being negotiated with the Sierra Leone Government.

[241] Regardless of his limited knowledge of some of the events surrounding the Leases, Holemans was the CFO of Rex. As CFO, he occupied a position of authority, responsibility and trust within the company. He was ultimately responsible for Rex's financial reporting obligations and was named in Rex's disclosure policy as someone responsible for determining materiality. As CFO, Holemans ought to have known about

and was required to make further inquiries with respect to the status of the Leases, rather than simply deferring to Muller's instructions. We find that Holemans acquiesced in Rex's violation of section 75 of the Act and thereby acted contrary to the public interest.

C. Did the Respondents act contrary to the public interest by providing misleading disclosure regarding its operations in Sierra Leone in each of its public filings of February 28, 2003, August 15, 2003 and November 28, 2003?

1. Rex's MD&A Filed February 28, 2003

[242] To summarize, the Outlook section of the MD&A filed February 28, 2003 informed the public that Rex was engaging in operations in Sierra Leone. In particular, a mining camp was being established and mining equipment was being positioned. This was also confirmed by Rex's news release issued on February 28, 2003.

[243] At the time Rex's MD&A was filed on February 28, 2003, Rex was aware that there was some controversy surrounding its Leases. This is evident from the description of the correspondence set out above. In particular, on January 3, 2003, the Government of Sierra Leone sent a warning letter to Rex informing Rex that the Minerals Advisory Board recommended to the Minister of Mineral Resources to terminate the Leases. In response, Rex wrote to the Makpele Chiefdom to secure their support, and Rex also wrote an extensive five page letter to the Director of Mines of Mineral Resources on January 14, 2003 outlining Rex's concerns "to defend [its] contractual rights that have so casually been trampled upon".

[244] While a decision was made on January 14, 2003 to give Rex another chance to meet its legal obligations under the Leases before the Leases would be terminated, the NPAC imposed conditions on Rex and required Rex to file a comprehensive "Work Programme" and comply with it, in addition to paying its financial obligations under the Leases.

[245] Rex's MD&A filed February 28, 2003 made no mention of these issues surrounding the Leases. While the Leases were not terminated at this time, there was still information that should have been communicated to the public, namely Rex had outstanding financial obligations relating to the Leases and Rex was expected to start mining operations on the areas covered by the Leases in order to comply with Sierra Leone's Mines and Minerals Act.

[246] Muller's testimony during the hearing revealed that on or about February 28, 2003, Rex did not have any intention of recommencing mining activities in Sierra Leone. Specifically Muller stated:

We knew we had to do something because as soon as the *force majeure* was lifted we were being told that we should start doing something.

...

We should start doing something, but I was dragging my feet. I didn't really have intention, again, to go and spend serious money in that country because that country was not safe.

[247] The disclosure in the MD&A filed February 28, 2003 was inconsistent with this.

[248] A letter from the Minister of Mines of the Ministry of Mineral Resources dated June 4, 2003 stated that Rex did not commence mining operations as planned, and that the operations in Zimmi were of artisanal nature.

[249] On February 28, 2003, Rex had stated in its MD&A that mining equipment was being moved to Zimmi and that a drilling program was planned to take place. However, the above quoted letter was written to Rex on June 4, 2003 and it seems that the equipment and drilling program discussed in the public filing was not in place at the time the June 4, 2003 letter was sent to Rex.

[250] The evidence also reveals that Rex entered into the Fauvilla MOU to commence operations in Zimmi. However, in his testimony, Muller explained that he entered into this agreement because he was not willing to invest in Sierra Leone at the time and the Fauvilla MOU would therefore discharge his "moral obligation" to the local people and "would alleviate some of the pressure that [Rex] had from the Ministry of Mines".

[251] We find that Rex's MD&A filed February 28, 2003 was inaccurate. Muller's testimony revealed that Rex never had the intention of developing operations on the property covered by the Zimmi Lease, and the correspondence from the Government of Sierra Leone revealed that Rex did not commence operations and drilling with machinery as anticipated.

2. Rex's Annual Information Form for the Year Ended August 15, 2003

[252] The 2003 AIF was filed on August 15, 2003. At this time Rex had received the June 4, 2003 letter from the Minister of Mineral Resources which gave Rex final notice of 90 days that the Leases would be terminated if Rex did not fulfill its obligations under the Leases.

[253] However, Rex's 2003 AIF stated that it held the Leases until February 28, 2019, and there was no mention of the June 4, 2003 warning letter or the possibility that Rex's Leases might be cancelled by the Sierra Leone Government. Instead, the language of the 2003 AIF gave the impression that the commencement of mining operations was imminent and that the future of diamond mining in Sierra Leone was promising.

[254] We find that it was inappropriate on the part of Rex to omit reference to the possibility that Leases were in danger of being terminated. An investor reading Rex's 2003 AIF would be given the impression that Rex's Leases were in good standing and had significant potential value and that mining operations might commence, while, in reality, at the time the 2003 AIF was filed, Rex was warned that the Leases were at risk

of being terminated in the near future. This type of conduct is problematic because all relevant information should be contained in an AIF, not just positive information. It was contrary to the public interest that Rex withheld negative information about the company from the public at this time.

3. Rex's MD&A Filed November 28, 2003

[255] We note that Rex only provided positive information about Sierra Leone in the MD&A filed November 28, 2003.

[256] Like Rex's previous public filings discussed above, the MD&A filed November 28, 2003 did not make any reference to the possibility that the Leases may be cancelled by the Sierra Leone Government. This is a significant omission considering that at this time Rex had received warning letters in January, April and June 2003 and there was ample opportunity for Rex to disclose this information to the public.

4. The Importance of Full Disclosure

[257] Rex's public filings dated February 28, 2003, August 15, 2003 and November 28, 2003 were inaccurate and incomplete because they did not contain balanced information regarding Rex's activities and potential activities in Sierra Leone. Negative information relating to the Leases, which Rex had knowledge of from correspondence from the Government of Sierra Leone was omitted. This omission gave the public a distorted picture of Rex's affairs in Sierra Leone.

[258] Staff submitted that by providing favourable news in its public filings regarding the Leases but withholding negative news, Rex provided the public with an unbalanced and misleading view of its operations in Sierra Leone. We accept this submission and find that Rex's conduct was contrary to the public interest.

[259] Muller also testified that only the shareholders who asked about Sierra Leone and the Notice of Tender were told about the problems with the Leases. Therefore, not all members of the public were given equal access to information.

[260] As Staff pointed out in their submissions, this is problematic because:

As secondary market trading makes up the vast majority of capital market trading in Ontario, investors who purchase in the secondary market rely on the public record of the issuer. In order for investors to be confident in the integrity of the capital markets, it is essential that the public record provide them with accurate information. In the present case, Rex's public record did not provide investors with full disclosure.

[261] Timely disclosure and equal access to information are fundamental to successful operation of the capital markets. The Commission has stated that:

Disclosure is the cornerstone principle of securities regulation. All persons investing in securities should have equal access to information that may affect their investment decisions. The Act's focus on public disclosure of

material facts in order to achieve market integrity would be meaningless without a requirement that such disclosure be accurate and complete and accessible to investors. (*Re Philip Services Corp.* (2006), 29 O.S.C.B. 3941 at para. 7)

[262] The courts have also recognized that investors are protected by disclosure of information enabling them to assess the risks involved in making an investment. For example:

There can be no question but that the filing of a prospectus [and MD&A, AIF, Annual Report...etc.] and its acceptance by the commission [sic] is fundamental to the protection of the investing public who are contemplating purchase of the shares. (*Jones v. F.H. Deacon Hodgson Inc.* (1986), 56 O.R. (2d) 540 at 546 (H.C.)).

[263] We accept Staff's submission that for this principle to have meaning the onus must rest on the company to broadly disseminate information to the public. It should not be necessary for individual shareholders to make specific inquiries to the company's officers in order to find out information which should be made public by the company.

[264] This Commission dealt with the issue of misleading information in a news release and the failure to take appropriate action before approving financial statements in *Re Standard Trustco Ltd. et al* (1992), 15 O.S.C.B. 4322 at 24 and 25. The Commission stated that:

A sound disclosure system is one of the underpinnings of the securities regulatory system. It is therefore generally accepted that the timely provision of reliable financial information by reporting issuers is in the public interest. Where a company provides misleading financial information to the public it is damaging to the capital markets and would be contrary to the public interest. If allowed to go unchecked, such behaviour could in time be very destructive of our capital markets. Accordingly, the Commission has the jurisdiction to sanction those who fail to take the steps that are necessary so that public disclosure is full, fair and balanced.

[265] Cases from the British Columbia Securities Commission ("BCSC") have also emphasized the importance of issuers providing disclosure of details regarding potential mining operations. Staff referred us to *Re Anthian Resources Inc.*, 1999 LNBCSC 132 and *Re Solaia Ventures Inc.*, 1998 LNBCSC 232. In *Re Anthian*, the BCSC expressed concern that a news release which announced the signing of a letter of intent to develop a group of mineral properties in Bolivia failed to disclose material details about the operations. In *Re Solaia*, the BCSC found that there were disclosure deficiencies because the issuer did not file a news release and material change reports concerning the status of the issuer's negotiations for a joint venture exploration. These two cases show that other Canadian regulators have found that it is important for mining companies to disclose detailed and accurate information about their operations to the investing public. Rex should have disclosed the risk that the Leases were in danger of being cancelled, the

actual cancellation of the Leases, and that negotiations were underway to get the Leases reinstated.

[266] Rex's disclosure in its public filings was not full, fair and balanced. Rex's disclosure failed to mention issues relating to the Leases, including the ultimate cancellation in October 2003. We find this conduct to be contrary to the public interest.

[267] In addition, we are concerned by the fact that not only did Rex not make public disclosure about the status of the Leases, it only disclosed information about the Leases to investors who specifically inquired about this. Selective disclosure to only certain investors does not promote truthful and accurate disclosure to the capital markets as a whole.

D. Did the Respondents act contrary to the public interest by misleading RS by providing an incomplete chronology?

1. The Importance of Providing Complete and Accurate Information to Regulators

[268] Pursuant to section 1.1 of the Act, the Commission's mandate is to "(a) provide protection to investors from unfair, improper or fraudulent practices; and (b) to foster fair and efficient capital markets and confidence in capital markets."

[269] Section 2.1 of the Act states that "requirements for timely, accurate and efficient disclosure of information" and "requirements for the maintenance of high standards of fitness and business conduct to ensure honest and responsible conduct by market participants" are some of the primary means to achieve the purposes of the Act.

[270] In order for the Commission and self-regulatory organizations (SROs) like RS to monitor market participants, those involved in the capital markets must co-operate and provide accurate information to the regulators. As explained by the Ontario Court of Appeal in *Wilder v. Ontario (Securities Commission)*, *supra* at para. 21:

The OSC is charged with the statutory obligation to do its best to ensure that those involved in the securities industry provide fair and accurate information so that public confidence in the integrity of capital markets is maintained. *It is difficult to imagine anything that could be more important to protecting the integrity of capital markets than ensuring that those involved in those markets, whether as direct participants or as advisers, provide full and accurate information to the OSC.* [emphasis added]

[271] This principle not only applies to the Commission, but also to all regulators of the capital markets and SROs. We accept Staff's submission that:

RS falls within the framework of securities regulation, and it is therefore equally important that market participants provide full and accurate information to RS in response to inquiries.

[272] Keeping these general principles in mind, we will now examine the evidence and determine in the next section whether Rex cooperated and provided complete and accurate information to RS.

2. Rex did not Provide RS with Complete and Accurate Disclosure

[273] RS requested Rex to provide a chronology of events in order to help RS understand the sequence of events and the cause(s) of the fluctuations in Rex's share price. This information was relied on by Cristello in her analysis and report that was completed for RS; therefore, completeness and accuracy in the information provided to RS was extremely important and expected.

[274] The chronology provided by Rex failed to contain reference to a number of relevant documents and events. Cristello's testimony and the documentary evidence reviewed during the hearing revealed that Rex omitted from its chronology any mention of events or correspondence from the period of January 2003 to August 2003.

[275] For instance, Rex did not disclose to RS that it had received the following correspondence:

- the warning letter dated January 3, 2003 and subsequent correspondence up until January 21, 2003 between Rex and the Makpele Chiefdom and the Sierra Leone Government;
- correspondence in February 2003 from Rex to the Sierra Leone Government with respect to the amounts owed by Rex on the Leases;
- the warning letter dated April 16, 2003;
- the final notice warning letter dated June 4, 2003; and
- the Fauvilla Letter.

[276] With respect to the Fauvilla Letter, Muller testified that it was not included in the chronology provided by Rex to RS because it had not been properly placed in the "Sierra Leone file", instead it was placed in the "Fauvilla file". Muller only produced the Fauvilla Letter later during the Commission's investigation. We find it very troubling that the Fauvilla letter was not provided to RS at the outset because the Fauvilla letter made reference to the fact that termination of the Leases was material information if confirmed to be true.

[277] Moreover, Rex's chronology states that Rex only became aware of the Notice of Tender on January 30, 2004. This is untrue, as the Fauvilla Letter, which was sent by fax to Rex's offices in Antwerp on December 15, 2003, specifically mentioned the Notice of Tender and asked Rex whether its Leases were still in good standing. In addition, on January 23, 2003, Lay sent an e-mail to Holemans alerting him to the fact that there were inquiries that the Sierra Leone Government was re-tendering Rex's Leases.

[278] We note that Holemans was never told about the Fauvilla Letter and did not have knowledge of it; therefore, we do not find that Holemans misled RS with respect to the Fauvilla document.

[279] With respect to the omission of the correspondence in February 2003 relating to the amounts owing on the Leases, we note that in the chronology provided by Rex to RS, Rex took the position that it had pre-paid two years of rents. As pointed out to us in Staff's submissions, this is inconsistent with Rex's request for rent figures in Rex's February 3, 2003 letter to the Sierra Leone Ministry of Mineral Resources.

[280] With respect to the three warning letters that mentioned that the Leases were at risk of being cancelled, Muller testified that he placed these letters in his general filing of papers because he did not take them seriously. Only after receiving an e-mail from Rombouts did he create a "live file" on this issue. We note that these letters were only provided when Muller was asked a second time by the Commission's investigator.

[281] Clearly, Muller's conduct did not fulfill his obligations as a participant in the capital markets to provide true and accurate information to RS. This type of conduct is contrary to the public interest. As discussed above, providing truthful and accurate disclosure to regulators of the capital markets, including SROs is essential to prevent abuse of the capital markets.

[282] As for Holemans, the evidence revealed that he lacked awareness of some of the correspondence that was omitted from the chronology. As a result, his conduct cannot be considered as blameworthy as Muller's. However, we do note that Holemans was the CFO of Rex and he should have ensured in his role as CFO that sufficient processes were in place to ensure that such information was brought to his attention. Holemans should not have deferred to Muller's judgment on all issues. As CFO of Rex, Holemans should have made more enquiries when he suspected that Muller was in possession of information possibly relevant to Rex's operations. Therefore, we also find that Holemans engaged in conduct contrary to the public interest with respect to omitting information from the chronology provided by Rex to RS.

E. Muller and Holemans authorized, permitted or acquiesced in Rex's Breaches of the Act

[283] Section 129.2 of the Act is as follows:

129.2 For the purposes of this Act, if a company or a person other than an individual has not complied with Ontario securities law, a director or officer of the company or person who authorized, permitted or acquiesced in the non-compliance shall be deemed to also have not complied with Ontario securities law, whether or not any proceeding has been commenced against the company or person under Ontario securities law or any order has been made against the company or person under section 127.

[284] We find Muller and Holemans accountable for Rex's failure to provide accurate disclosure in the public filings and to RS.

VI. CONCLUSION

[285] Upon reviewing all the evidence, the applicable law and the submissions made, we have concluded that:

(1) it is likely that there was a material change in the business, operations or capital of Rex when Rex received the following correspondence from the Government of Sierra Leone:

(a) the first warning letter dated January 3, 2003, which advised Rex that the Minerals Advisory Board recommended to the Minister of Mineral Resources that Rex's Leases be cancelled because Rex did not comply with the conditions set out in the Leases; and

(b) the second warning letter dated April 16, 2003, which advised Rex that its Leases were not in good standing and that Rex failed to honour its financial obligations;

(2) material changes did occur in the business, operations or capital of Rex when:

(a) Rex received the final notice warning letter dated June 4, 2003, from the Sierra Leone Government, which advised Rex that it had 90 days to comply with the conditions of the Leases or otherwise the Leases would be revoked;

(b) Rex became aware of the Notice of Tender on December 15, 2003; and

(c) the Government of Sierra Leone issued the Tender Evaluation on March 30, 2004.

(3) Rex should have issued news releases and filed material change reports following the events referred to in paragraphs (a) and (b), and should have filed a material change report as well as issuing a news release following the event described in paragraph (c). By failing to do so, Rex breached section 75 of the Act and acted contrary to the public interest;

(4) Rex acted contrary to the public interest by providing inaccurate and incomplete disclosure regarding its operations in Sierra Leone in each of its public filings of February 28, 2003, August 15, 2003 and November 28, 2003;

(5) Rex acted contrary to the public interest when it provided RS with an inaccurate and incomplete chronology of events; and

(6) Muller, as a director and the CEO of Rex, authorized or permitted, and Holemans, as the CFO of Rex, acquiesced in the conduct described in paragraphs (3) to (5) above, and thereby acted contrary to the public interest.

[286] The parties shall contact the Office of the Secretary within 10 days of this decision to set a date for a sanctions hearing, failing which a date will be fixed by the Office of the Secretary.

Dated at Toronto, this 21st day of August, 2008.

“Wendell Wigle”

Wendell S. Wigle, Q.C

“David Knight”

David L. Knight, FCA

“Kevin Kelly”

Kevin J. Kelly

SCHEDULE “A” – RELEVANT EXCERPTS FROM THE *SECURITIES ACT*

SECURITIES ACT

R.S.O. 1990, c. S.5, as am. S.O. 1992, c. 18, s. 56; 1993, c. 27, Sched.; 1994, c. 11, ss. 349-381; 1994, c. 33; 1997, c. 10, ss. 36-41; 1997, c. 19, s. 23; 1997, c. 31, s.179; 1997, c. 43, Sched. F, s. 13; 1999, c. 6, s. 60; 1999, c. 9, ss. 193-222 [s. 202 not in force at date of publication.]; 2001, c. 23, ss. 209-218.

1. (1) **Definitions** – In this Act,

...

“**material change**”, where 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 any 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; (“changement important”)

...

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.

...

75. (1) **Publication of material change** – 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.

(2) **Report of material change** – Subject to subsection (3), the reporting issuer shall file a report of such material change in accordance with the regulations as soon as practicable and in any event within ten days of the date on which the change occurs.

OSA 75(2)

Regulations: Reg.: 3; Reg.: Form 27; Reg.: Sch. I:35

(3) **Idem** – Where,

(a) in the opinion of the reporting issuer, the disclosure required by subsections (1) and (2) would be unduly detrimental to the interests of the reporting issuer; or

(b) the material change consists of a decision to implement a change made by senior management of the issuer who believe that confirmation of the decision by the board of directors is probably and senior management of the issuer has no reason to believe that persons with knowledge of the material change have made use of such knowledge in purchasing or selling securities of the issuer,

the reporting issuer may, in lieu of compliance with subsection (1), forthwith file with the Commission the report required under subsection (2) marked so as to indicate that it is confidential, together with written reasons for non-disclosure.

OSA 75(3)

Regulations: Reg.: Form 27.

(4) **Idem** – Where a report has been filed with the Commission under subsection (3), the reporting issuer shall advise the Commission in writing where it believes the report should continue to remain confidential within ten days of the date of filing of the initial report and every ten days thereafter until the material change is generally disclosed in the manner referred to in subsection (1) or, if the material change consists of a decision of the type referred to in clause (3)(b), until that decision has been rejected by the board of directors of the issuer

1994, c. 11, s. 349