Ontario Securities Commission
Commission des valeurs mobilières de l'Ontario
22nd Floor
20 Queen Street West
Toronto ON M5H 3S8
22e étage
20, rue queen ouest
Toronto ON M5H 3S8

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

- AND -

IN THE MATTER OF
NORTH AMERICAN FINANCIAL GROUP INC., NORTH AMERICAN CAPITAL INC., ALEXANDER FLAVIO ARCONTI AND LUIGINO ARCONTI

REASONS AND DECISION
(Section 127 of the *Securities Act*)

Hearing:	April 29 and 30, 2013 May 1-3, 6, 8-10, 22 and 23, 2013 September 11, 2013	
Decision:	December 11, 2013	
Panel:	James D. Carnwath, Q.C.	- Chair of the Panel and Commissioner
Appearances:	Michelle Vaillancourt	- For Staff of the Commission
	Ian Smith	- For North American Financial Group Inc., North American Capital Inc., Alexander Flavio Arconti and Luigino Arconti

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PART 1 – INTRODUCTION

A. Nature of the Hearing

[1] This was a hearing on the merits (the "**Hearing**") before the Ontario Securities Commission (the "**Commission**" or the "**OSC**") pursuant to sections 127 and 127.1 of the Ontario *Securities Act,* R.S.O. 1990, c. S.5, as amended (the "***Act***") to consider whether North American Financial Group Inc. ("**NAFG**"), North American Capital Inc. ("**NAC**"), Alexander Flavio Arconti ("**Flavio Arconti**") and Luigino Arconti ("**Gino Arconti**") (together, the "**Respondents**") contravened Ontario securities law and acted contrary to the public interest. Flavio and Gino Arconti will be collectively referred to as the "**Arcontis**" in these Reasons and Decision. The Hearing was held on April 29 and 30, May 1-3, 6, 8-10, 22 and 23 and September 11, 2013.

[2] On December 28, 2011, a Notice of Hearing was issued by the Commission in connection with the Statement of Allegations filed by Staff of the Commission ("**Staff**"), also dated December 28, 2011.

[3] On November 10, 2010, the Commission issued a temporary cease trade order against the Respondents (the "**Temporary Order**"). The Temporary Order was amended and extended from time to time and, pursuant to an order of the Commission dated July 5, 2012, the Temporary Order was extended, as amended, against the Respondents until the final disposition of this matter, including, if appropriate, any final determination with respect to sanctions and costs.

B. OVERVIEW

[4] This hearing on the merits began with the filing of Exhibit 1 ("**Ex. 1**"), a document entitled "Admissions of the Respondents". The document outlines the Respondents' position in respect of each paragraph of Staff's Statement of Allegations. Provided below is an overview of the facts in this matter based on the Admissions of the Respondents.

[5] During the period July 2005 to September 2010, NAFG raised funds by issuing non-prospectus qualified securities to investors. As at November 30, 2010, over $5.7 million was invested in NAFG.

[6] During the period July 2009 to April 2010, NAC issued shares to approximately 11 investors. The total proceeds of approximately $1,042,000 from the sale of NAC securities were transferred to NAFG.

[7] NAFG is a finance company in the business of the acquisition and servicing of subprime car leases in respect of cars that were acquired through 970910 Ontario Inc. (operating as Prestige Motors) ("**Prestige Motors**"), a used car dealership. NAC was organized to finance car leases, of which leasing was conducted through NAFG.

[8] From at least September 2007 to September 2010, NAFG and/or NAC securities were sold by Carter Securities Inc. ("**Carter**"), a company incorporated in Ontario in February 2007.

Carter's registration as an Exempt Market Dealer ("**EMD**") was suspended on September 22, 2010 by a decision of the Director, following an opportunity to be heard ("**OTBH**") held on August 4 and 26, 2010, regarding its registration ("**Carter's Suspension**"). The Director found that Carter was not suitable for registration, that it failed to comply with Ontario securities law and that Carter's ongoing registration was objectionable (the "**Director's Decision**"). The Respondents do not admit that the decision respecting Carter's registration was correct, but the Respondents admit that the Arcontis' registration was automatically suspended as a result of the Director's Decision (Ex. 1, para. 8). Flavio Arconti, Gino Arconti, NAC and NAFG were not named parties in the OTBH or the resulting Director's Decision.

[9] On October 22, 2010, Carter filed a request for a review of a Director's Decision. Since that time, Carter has not taken any steps to proceed with its request for a review.

[10] On October 15, 2010, less than one month after the Director's Decision suspending Carter's registration, NAFG filed a Notice of Intention to make a proposal under the *Bankruptcy and Insolvency Act*, R.S.C. 1985, c B-3 (the "***BIA***") on the basis that it was an insolvent person, pursuant to subsection 50.4(1) of the *BIA*.

C. Staff Allegations

1. The Arcontis' Liability for the Conduct of Carter

[11] Relying on section 129.2 of the *Act*, Staff alleges that the Arcontis, as actual and/or *de facto* officers and/or directors of Carter, authorized, permitted and/or acquiesced in the non-compliance with Ontario securities law by Carter. Staff alleges that during the period from September 2007 to September 2010, while Carter was selling NAFG and NAC securities, Carter did not disclose to investors the existence of an interest free loan of approximately $2 million by NAFG to Prestige Motors or the severe financial difficulties faced by NAFG. As a result, Staff alleges that:

(a) Carter did not take reasonable steps to ensure that the purchase of NAFG securities was suitable to its clients in breach of section 13.3 of National Instrument 31-103 – *Registration Requirements, Exemptions and Ongoing Registration Obligations* ("**NI 31-103**"); and

(b) Carter failed to deal fairly, honestly and in good faith with its clients in breach of subsection 2.1(1) of OSC Rule 31-505 – *Conditions of Registration* ("**OSC Rule 31-505**").

[12] The material time period referred to in the Statement of Allegations in respect of Carter's conduct is September 2007 to September 2010. However, given that section 13.3 of NI 31-103 did not come into force until September 28, 2009, Staff relies on Carter's conduct from September 29, 2009 to September 24, 2010 (the "**Applicable Period**") in support of the allegations that Carter breached section 13.3 of NI 31-103 and that the Arcontis are liable for that breach pursuant to section 129.2 of the *Act*.

[13] Staff acknowledges that the Director's Decision is binding on Carter and the Arcontis to the extent that it resulted in the suspension of Carter's registration, and the resulting suspension

of the Arcontis' registration, pursuant to subsection 29(2) of the *Act*. However, Staff submits that it does not take the position that the findings in the Director's Decision are binding on the Commission in relation to Staff's allegations of the Arcontis' liability for Carter's non-compliance with Ontario securities law under section 129.2 of the *Act*.

[14] I note that at the Hearing, the parties consented to the removal of the copy of the Director's Decision, which was included in Staff's documentary evidence (Tr. Vol. 1, p. 28, ll. 1-25; p. 31, ll. 1-19; p. 112, ll. 22-25). Staff tendered evidence during the Hearing in support of its allegations that Carter breached Ontario securities law and that the Arcontis are liable for such conduct, pursuant to section 129.2 of the *Act*.

2. Fraud

[15] Staff alleges that during the period January 1, 2009 to September 24, 2010, each of the Respondents directly or indirectly engaged or participated in acts, practices or courses of conduct relating to the securities of NAFG and NAC that they knew or reasonably ought to have known perpetrated a fraud on persons, contrary to subsection 126.1(b) of *Act* and contrary to the public interest.

[16] In addition, Staff alleges that the Arcontis, as actual and/or *de facto* officers and/or directors of NAFG and NAC, authorized, permitted or acquiesced in the breach of subsection 126.1(b) of the *Act* by NAFG and NAC and thereby also breached subsection 126.1(b) of the *Act*, pursuant to section 129.2 of the *Act*.

3. Trading Without Registration after September 22, 2010

[17] Staff alleges that on September 24, 2010, Gino Arconti engaged in and/or held himself out as engaging in the business of trading in securities without registration contrary to subsection 25(1) of the *Act*.

4. Conduct Contrary to the Public Interest

[18] Staff alleges that the conduct referred to above in paragraphs 11 to 17 was also contrary to the public interest.

D. The Respondents' Submissions

[19] NAFG was incorporated in Ontario on July 30, 1996. NAFG is not a reporting issuer and is not registered under the *Act*.

[20] NAC was incorporated in Ontario on November 25, 2008. NAC is not a reporting issuer and is not registered under the *Act*.

[21] Flavio Arconti is a resident of Vaughn, Ontario and Gino Arconti is a resident of Richmond Hill, Ontario.

[22] During the time of the conduct referred to herein, Flavio Arconti and Gino Arconti jointly owned NAFG, NAC, Carter and Prestige Motors and were the actual and/or de facto officers and directors of each of NAFG, NAC, Carter and Prestige Motors.

[23] Flavio Arconti and Gino Arconti are brothers and were registrants from September 17, 2007 to September 22, 2010. In particular, beginning on September 17, 2007, when Carter was registered as a Limited Market Dealer, Flavio Arconti was registered as an Officer and Director (Trading Resident), Shareholder and Designated Compliance Officer of Carter and Gino Arconti was registered as an Officer and Director (Trading Resident) and Shareholder of Carter.

[24] Following Carter's change in designation (by operation of law) to an EMD on September 28, 2009 until Carter's Suspension, Flavio Arconti was registered as the Chief Compliance Officer, Ultimate Designated Person and Dealing Representative of Carter and Gino Arconti was registered as a Dealing Representative of Carter.

[25] The Respondents admit that they acted contrary to the public interest (Ex. 1, para. 6). They admit that the Director made findings against Carter, which led to its suspension (Ex. 1, para. 4). They admit that there was a loan from NAFG to Prestige Motors that eventually amounted to approximately $2 million, although they note that this figure started out as a much smaller amount (Ex. 1, para. 22). The Respondents admit that NAFG was not profitable, but it is not admitted that its financial difficulties were "severe", as characterized in the Director's Decision (Ex. 1, para. 22). The Respondents admit that the loan was not disclosed to NAFG investors initially, but later disclosure better described the uses of investor funds and many investors were advised that NAFG experienced financial difficulties (Ex. 1, para. 22).

[26] In their submissions, the Respondents stress the following themes:

(a) NAFG's typical experience as a young company and the fact that the Respondents developed plans to address the losses of NAFG, which were similar to many start-up companies;

(b) NAFG's representations to investors that they would not receive financial information about the company, since NAFG was not a reporting issuer, nor was NAC for that matter, and that some of the marketing material may have painted a better picture than it should have and that much of the information is properly described as puffery;

(c) the Respondents' real effort to ensure that investors of NAFG and NAC were in fact accredited investors and that mistakes were made in good faith and in reliance on information provided by the investors themselves, who certified they were in fact accredited;

(d) the Respondents' reliance on qualified professionals to advise the Respondents on compliance, to help them fix problems which made them non-compliant and to assist them in charting NAFG's march to profitability;

(e) the Respondents cooperated with Staff's first compliance review in 2009 in good faith and set about addressing Staff's criticisms immediately;

(f) the Respondents cooperated fully and in good faith in the second compliance review in 2010, while expending considerable time, effort and money in responding to Staff's inquiries. The Respondents were shocked and dismayed that they did not receive a deficiency letter from Staff to which they could respond to before Carter's Suspension;

(g) the Respondents took various steps and initiatives that they submit were realistic and in good faith to address NAFG's losses, and that Carter's Suspension effectively interrupted and doomed all of those efforts to address the losses; and

(h) the Arcontis embarked on the project of growing NAFG's business in good faith and with considerable energy and effort, but they did not have the financial, accounting or legal training to make decisions on matters well-outside their prior experience in the automobile business.

E. Evidence

[27] Staff called a total of eight witnesses in this matter. Three of Staff's witnesses are members of Staff: Maria Carelli, Amy Tse and Marcel Tillie. Staff also called five investor witnesses: J.B., L.F., J.S., R.B. and D.M. Staff submitted documentary evidence totalling 21 exhibits.

[28] In order to protect the privacy of the investor witnesses, their names and personal information have been anonymized and I will refer to them by their initials, rather than using their respective names.

[29] Flavio Arconti and Gino Arconti both testified, along with four other witnesses: Stefano Picone, an accountant hired to review the accounts of NAFG and Prestige Motors; David Gilkes, the regulatory consultant hired by the Arcontis; and, two investor witnesses, C.S. and N.B. The Respondents submitted documentary evidence totalling seven exhibits.

[30] To assist the reader to follow and understand the evidence, exhibits will be referred to as "Ex. -, Tab -, p. -" and excerpts from transcripts of the evidence will be referred to as "Tr. Vol. -, p. -, l. -".

PART 2 – STAFF WITNESSES

A. Maria Carelli

[31] Staff called Maria Carelli, who works as a senior accountant in the Compliance and Registration Regulation Branch of the Commission. She is both a chartered accountant and a chartered business valuator. She participated in a compliance review of Carter in 2010 (the "**2010 Compliance Review**"), but did not participate in the compliance review of Carter in 2009 (the "**2009 Compliance Review**"). Anita Chung was the lead reviewer of the 2009 Compliance Review and was an accountant in the Compliance and Registrant Regulation Branch of the Commission at the time of the review.

[32] Ms. Carelli's evidence may be found in Tr. Vol. 1, pp. 44-212 and Tr. Vol. 2, pp. 5-86. The exhibits referred to in her testimony may be found in Exs. 2, 3 and 4.

[33] After identifying certain tabs in Ex. 2 relating to Carter's corporate documents, Ms. Carelli identified the policies and procedures manual for Carter dated November 2007 (Ex. 2, Tab 7). The policies and procedures manual at section 5.3 speaks of "Client Suitability and Disclosure" and describes what persons are required to learn about a client prior to solicitation for an investment. The requirements include finding out if the potential investor understands the benefits of the investment, has a net worth sufficient to sustain the risks inherent in the investment and that the investment is otherwise suitable for the client. The manual also states that the company and each salesperson must have reasonable grounds to believe that all material facts of the investment are adequately disclosed in the offering documents.

[34] The document goes on to provide that "salespersons will not make false or misleading statements, or fail to state material facts in connection with a securities transaction" (Ex. 2, Tab 7, p. 34). Ms. Carelli identified a document in Ex. 2, Tab 9, a "New Client Application" form for Carter. The document provides the address, financial information and the past investment experience of the investor. The document had several attachments, including: "Schedule 'A' To Certificate of Accredited Investor"; a Risk Acknowledgement form highlighting the risks of the product; and a Form of Information Statement describing the risks and investment strategies of the product.

[35] At Ex. 2, Tab 11 is the deficiency report of April 24, 2009 that was addressed to Carter from Christina Pazienza, the former assistant manager of compliance for Staff (the "**2009 Deficiency Report**"). Two significant deficiencies were noted: a lack of "Know Your Client" ("**KYC**") and suitability procedures, and a failure to determine if a prospectus exemption was available to Carter. The 2009 Deficiency Report says the following about the KYC requirements:

> Your KYC form does not include questions to obtain information about an investor's investment time horizon or level of risk tolerance. Also, forms are not always filled out completely or properly (see appendix A). From our review of a sample of your completed KYC forms of clients, we noted instances where the suitability criteria may not have been met. In addition, there were instances where you did not meet directly with your client.
>
> (Ex. 2, Tab 11, p. 210)

[36] The 2009 Deficiency Report stresses Carter's lack of a process to determine if prospectus exemptions were available:

> You do not have a process in place to determine if investors you engage with in your capital raising activities are able to rely on a valid prospectus exemption, such as the accredited investor or minimum amount exemption. For example, in some instances such as [Company X] (see appendix A), the information in the KYC form did not match with the criteria indicated on the accredited investor form.

(Ex. 2, Tab 11, p. 210)

[37] Ms. Carelli's evidence then dealt with Flavio Arconti's response to the 2009 Deficiency Report and a response from Ms. Pazienza requesting further clarification on certain responses from Carter. That in turn prompted a response from Flavio Arconti on November 17, 2009, saying his advisors, Cassels Brock & Blackwell LLP ("**Cassels Brock**") and David Gilkes, a regulatory consultant, were working on providing an update to their efforts to comply. In this response, reference was made to J.B., an investor, and M.G., a cousin of the Arcontis who was shown to be an accredited investor.

[38] Following Staff's receipt of Flavio Arconti's response, Staff decided to complete another compliance review of Carter by way of a designation order dated January 18, 2010 (the "2010 Compliance Review", as defined above). Ms. Carelli was named as a designated person to conduct the compliance review for the Commission.

[39] On January 25, 2010, a meeting was held at Carters' office where Flavio Arconti was asked a series of questions about a number of topics, including: Carter's corporate structure, organizational structure and the roles played by Prestige Motors and NAC. Flavio Arconti answered those questions.

[40] Ms. Carelli also commented on the trial balance of NAFG, as at December 31, 2009. Ms. Carelli stated that this document indicated that the loan from NAFG to Prestige Motors was $1,987,084.74 (Ex. 2, Tab 28, p. 450). In terms of retained earnings, as at December 31, 2008, this document showed accumulated losses of $861,131.73 for NAFG.

[41] Staff referred Ms. Carelli to Ex. 3 containing the client files of 62 investors that Staff obtained during the 2010 Compliance Review. This exhibit also provides documents that are related to the investment of M.G., referred to earlier. M.G. agreed to lend NAFG $100,000 at the rate of 15% by a loan agreement dated November 1, 2009. M.G. certified that she, either alone or with a spouse, had net financial assets in excess of $1 million. NAFG was to repay the loan in 60 consecutive monthly instalments of $2,355.52 commencing on December 4, 2009. The loan would mature on November 4, 2014.

[42] Staff then referred Ms. Carelli to Ex. 4, Tab 1, which contains Staff's notes regarding the additional information received and provided to the Arcontis during the 2010 Compliance Review. The notes range from May 25, 2010 to June 14, 2010, detailing Staff's perceived deficiencies in the responses given by the Arcontis to requests for further information. Tabs 2 to 5 of Ex. 4 contain the email exchanges between Staff and NAFG personnel regarding Staff's reception of NAFG's financial statements for the year ending December 31, 2009, which are found at Tabs 7 to 18 of Ex. 4.

[43] On March 15, 2010, Staff requested a telephone conference with the Arcontis to clarify a number of items noted during its review. The telephone conference took place on March 23, 2010. Following the telephone conference, Staff required additional information from the Arcontis. In an email dated April 12, 2010, Staff listed several documents that were to be provided by the Arcontis no later than April 30, 2010. Additional questions and responses continued between Staff, Margaretha Widjojo and the Arcontis to supply further information.

Ms. Carelli stated that Ms. Widjojo was the bookkeeper of NAFG and Carter at the time. As late as June 8, 2010, Ms. Widjojo was forwarding material to Staff, while thanking Staff for its patience.

[44] By a letter dated June 23, 2010, Flavio Arconti was notified by Staff that it recommended to the Director that Carter's registration as a dealer in the exempt market be suspended (the "**June 2010 Letter**"). Staff identified several violations of Ontario securities law by Carter that called into question whether Carter's operations were being conducted with the requisite integrity of securities professionals. The specific areas of concern were: the inappropriate use of investors' proceeds; the failure to adequately explain product risks to investors; and, misleading and inaccurate marketing materials (Ex. 4, Tab 39, pp. 195-196).

[45] Mr. Gilkes responded to Staff's recommendation to the Director by asking for an opportunity to be heard by way of an appearance before the Director (the "**OTBH**").

[46] Staff's evidence provides for the documents that were relevant to the OTBH of Carter, along with the transcripts of the OTBH (Ex. 4, Tabs 41-43). The OTBH was held on August 4 and 26, 2010. The Director ordered Carter's suspension. On consent of the parties, the copy of the Director's Decision included in Staff's documentary evidence was removed. In a letter dated October 22, 2010, Alexander Gillespie, Carter's legal counsel at the time, wrote to the Secretary of the Commission that Carter requested that the OSC review the Director's Decision (Ex. 4, Tab 49). Ms. Carelli testified that, to her knowledge, no such hearing or review of the Director's Decision took place.

[47] The evidence identified by Ms. Carelli also includes the Commission's news release, dated September 27, 2010, regarding the suspension of Carter's registration. Also filed was a letter dated October 22, 2010 from Farber Financial Group ("**Farber**"), NAFG's trustee in bankruptcy, informing creditors of NAFG that NAFG filed a Notice of Intention to Make a Proposal, pursuant to section 50 of the *BIA*, on October 15, 2010 (Ex. 4, Tabs 48 and 50).

[48] At the beginning of Ms. Carelli's cross-examination, counsel for the Respondents, Mr. Smith, began by obtaining her agreement that Carter and NAFG were run by a small group of people with some outside help with legal and accounting advice. Ms. Carelli agreed that the NAFG group of companies was a small operation and was challenged by Staff's demands for information during the reviews; however, she added that Staff have a number of registrants that are similar in size to the companies, and the expectation is that the information Staff was seeking would have been readily available and ready for review. Ms. Carelli had decided that the books and records were not in good order and were not produced to the Commission with the efficiency expected of registrants.

[49] Ms. Carelli then confirmed that Flavio Arconti had little experience with compliance matters.

[50] During the 2009 Compliance Review, Ms. Carelli confirmed that the areas of greatest concern were the lack of KYC and suitability procedures and the determination if a prospectus exemption was available. She pointed out that the review was a "focus review", which she described as one that is very different from a "complete review", the latter of which was

conducted for the 2010 Compliance Review. She explained that it was quite possible that the reason why the marketing materials were not reviewed for deficiency purposes in the 2009 Compliance Review was that it was beyond the scope of the focus review.

[51] Carter responded to the 2009 Deficiency Report and set out in detail the proposed changes in its approach to investments. Ms. Carelli agreed that the proposed changes would be regarded as an improvement on what had been used before by Carter.

[52] Ms. Carelli was questioned about the trial balance provided by Carter in response to the 2009 Deficiency Report. She acknowledged that retained earnings of $861,131.73 were accumulated losses over a number of years. She confirmed that the delinquent accounts of $496,588.05 would have also accumulated over more than one financial year.

[53] On the question of Carter's marketing materials, Ms. Carelli confirmed her understanding that all investors received some version of Carter's marketing brochure, various examples of which were introduced by Staff in Exs. 3 to 5.

[54] Mr. Smith then directed Ms. Carelli to the letter sent by Staff following the 2010 Compliance Review, informing Flavio Arconti that Staff recommended to the Director that Carter's registration be suspended (Ex. 4, Tab 39). She confirmed that the letter was different from the 2009 Compliance Review, when Staff identified problems and gave Carter an opportunity to correct any deficiencies. No detailed report on Carter's deficiencies was sent to Carter in relation to the 2010 Compliance Review. She further confirmed that she understood that the view of Mr. Gilkes was that, once Staff's concerns were identified, he would be able to work with Carter in the same way as was done during the 2009 Compliance Review.

[55] Mr. Smith's cross-examination of Ms. Carelli ended with questions that were designed to show possible unfairness of the Director's Decision and the manner in which it was communicated at the OTBH by Ellen Bessner, who was counsel for the Respondents at the time. His line of questioning does not assist me inasmuch as the Director's Decision was not appealed.

[56] In re-examination by Staff, Ms. Carelli's attention was directed to a number of documents prepared by Carter for the intention of investors. Ms. Carelli responded that she was unable to tell by looking at the forms if any of them were used by investors, explained orally to investors or were actually read by investors. That concluded the evidence of Ms. Carelli.

B. Amy Tse

[57] Ms. Tse is a chartered accountant and a chartered financial analyst. She has worked for the Commission since 2002, apart from an absence of one year around July 2005 to July 2006. She was assigned to the matter involving Carter in June 2010. Her evidence may be found in Tr. Vol. 2, pp. 86-148. The documents on which she was referred to by Staff are found in Ex. 5.

[58] Ms. Tse first identified documents in Ex. 5, which includes corporation profile reports of NAFG, NAC, Carter and Prestige Motors, the registration data for the Arconti brothers and website print-outs for NAFG and Prestige Motors.

[59] She was referred to an email dated June 10, 2010 that she sent to her colleague, Nalini Khan, who was investigation counsel with the OSC, and to Don Panchuk, Ms. Tse's manager at the time (Ex. 5, Tab 11). The email represents the notes Ms. Tse took for a telephone conversation that she had with Gino Arconti on June 9, 2010. She posed as an individual named "Amy Thorne", who was responding to an advertisement in the *Toronto Star* that was advertising an investment with an annual rate of return of 10%. Gino Arconti told her that NAFG was under Carter, and that "all the companies involved were related" and dealt with consumer financing. The email indicates that Gino Arconti told Ms. Tse that their competitors were "TD and Scotia" and that "TD and Scotia bought out a couple of firms and they are now entering in the same industry as Carter/NAFG as well" (Ex. 5, Tab 11, p. 63). I find that Gino Arconti's description of the activities of NAFG and Carter to have been fairly straight-forward, apart from the glowing terms about competing with TD Bank and Scotia Bank.

[60] Ms. Tse testified that the advertisement in the *Toronto Star* stated that the investment was for accredited investors only. When Ms. Tse, acting as "Amy Thorne", asked what an "accredited investor" meant, Gino Arconti told her that an accredited investor had net financial assets of over $1 million. When asked to repeat the definition, he said "assets over $1 million" without specifying the word "financial". Gino Arconti also told Ms. Tse that if she decided to invest, he would ask a lot of questions to ensure suitability. Gino Arconti did not say anything about the financial circumstances of the company, nor did he mention that NAFG would be loaning money to a car dealership owned by the Arcontis, being Prestige Motors.

[61] Ms. Tse subsequently received a package of documents sent by NAFG, which contained a description of the activities and business of NAFG, described in positive terms.

[62] On June 18, 2010, Ms. Tse and Ms. Khan sent a Direction To Produce Documents made pursuant to subsection 19(3) of the *Act* to Carter. The Direction set out in considerable detail the documents required, and asked for details of the relationship Carter had with its related parties.

[63] On June 18, 2010, Staff also sent three separate letters to NAFG, NAC and North American Mortgage Investment Corporation ("**NAMIC**"), seeking documents and information regarding their activities. On July 12, 2010, Mr. Gilkes, on behalf of Carter, NAFG, NAC and NAMIC, sent a letter to Ms. Khan and Ms. Tse, enclosing responses and supporting documents requested in Staff's letters of June 18, 2010 and the Direction to Produce Documents (Ex. 5, Tab 17).

[64] At the end of her examination-in-chief, Ms. Tse was referred to an email dated August 23, 2010 that was sent by Ms. Tse to Ms. Khan (Ex. 5, Tab 18). The email documented Ms. Tse's conversation with Flavio Arconti on August 23, 2010 when she posed as a possible investor. Ms. Tse put a call to Carter as an individual named "Amy Peterson", who was responding to a voicemail Flavio Arconti left the previous week. The woman who answered the phone answered as "North American Financial" and Ms. Tse was then transferred to Flavio Arconti. Mr. Arconti described three products being offered, including mortgage investments and auto leasing. When "Amy Peterson" asked if her money was safe, she was told by Mr. Arconti that she could lose all the money she invested and that it was not guaranteed.

[65] In cross-examination, Ms. Tse confirmed to counsel that she had no independent recollection of her conversations with the Arconti brothers, other than as recorded in her notes. She confirmed that in his conversation with "Amy Thorne" on June 9, 2010, Gino Arconti told her that a potential investor's financial assets must be over $1 million to be an accredited investor. It was made clear to her that if she decided to invest in the future, Gino Arconti would ask her a lot of questions before he took her investment.

[66] Ms. Tse confirmed to counsel that in his conversation with "Amy Peterson" on August 23, 2010, Flavio Arconti told her that the money invested was used to lease cars and was also for an affiliated car dealer. She confirmed that Mr. Arconti told her that she could lose all her money in the investment. She agreed that one should not take her conversation with Flavio Arconti as the sum total of what she might have been told if she had decided to go forward with the investment. That concluded Ms. Tse's testimony.

C. Marcel Tillie

[67] Staff called Marcel Tillie, a senior forensic accountant in the Enforcement Branch of the Commission. Mr. Tillie's evidence may be found in Tr. Vol. 2, pp. 148-193, Tr. Vol. 4, pp. 113-156 and Tr. Vol. 5, pp. 5-108. Exhibits entered through Mr. Tillie include Exs. 6-11 and Exs. 17-20.

[68] Mr. Tillie obtained his designation as a chartered accountant in 1989 and has worked in the Enforcement Branch of the Commission since March 2007. He was assigned to the NAFG file in mid-April 2011. His assignment was to prepare a source and application of funds in relation to this matter.

[69] Mr. Tillie attended the compelled examination of Flavio Arconti and the voluntary examination of Gino Arconti. Before and after the examination of Flavio Arconti, Mr. Tillie received a binder of documents from counsel for the Arcontis. He also received two bankers' boxes of information from TD Bank, BMO, CIBC and NAFG. Mr. Tillie stated that the only banking documents relevant to this proceeding were those of TD Bank, since the primary banking of NAFG was done solely with TD Bank. Shortly put, the exhibits entered through Mr. Tillie gave him the information he needed to prepare an accurate source and application of funds for the two TD bank accounts operated by NAFG. There was also a third bank account, an account ending in 653 ("**Account 653**'), which was NAC's bank account. Transfers were made from Account 653 to NAFG's bank account (Tr. Vol. 5, p. 36, ll. 2-5).

[70] Found at Ex. 7 are the banking documents with respect to the TD bank account ending in 896 ("**Account 896**"). Found in Ex. 8 are the deposit account histories and some back-up documentation for the TD bank account ending 652 ("**Account 652**"). Found in Ex. 9 is a continuation of supporting documentation for Account 652 for the period July 17, 2009 to December 31, 2009. Ex. 10 contains a number of documents, including the continuing documentation for Account 652 for the period January 4, 2010 to October 4, 2010. The signing officers for the two accounts were Flavio Arconti and Gino Arconti.

[71] Mr. Tillie identified Ex. 11 as containing the transcript of Flavio Arconti's compelled examination held on June 28, 2011, together with documents provided to Mr. Tillie as a result of

the compelled examination. Included at Tab 2 at the back of Ex. 11, starting at page 456, are answers to undertakings obtained during the examination of Mr. Arconti.

[72] Mr. Tillie was referred to Tab C1, an income statement for NAFG from January 1, 2010 to September 30, 2010. Lease finance income for the period was $179,327.89, which represented interest paid by the lessees of cars. Items identified as leasing financing income and "NSF income" were amounts that could have been collected or amounts that might appear in accounts receivable. Ms. Carelli testified that "**NSF**" stood for "Not Sufficient Funds" (Tr. Vol. 1, p. 147, l. 25). Mr. Tillie said that "**NSF income**" represented the fee that was charged to a lessee when a lessee defaulted on their payments or when one of the lessee's payments did not go through the bank account of NAFG. Mr. Tillie said that, based on the income statement, the revenues of NAFG at the time were less than the interest paid to investors. Net income was a loss of $866,346.66 for the nine month period ending September 30, 2010. The total loan payables of NAFG as at September 30, 2010 was $3,391,746.42 (Ex. 11, Tab C2, p. 171). Mr. Tillie stated that to calculate the total loans payable, the total loans payable would have to be added to the loans receivable from Prestige Motors ($2,503,608.43) and deduct the accrued liabilities and accrued NSF income (approximately $80,000), making a total loans payable to investors of approximately $5.8 million (Tr. Vol. 2, p. 178, ll. 7-25; p. 179, ll. 1-11; Ex. 11, Tab C2, pp. 170-171).

[73] Mr. Tillie was then referred to the financial statements of NAFG as at November 30, 2010 (Ex. 11, Tabs C7 and C8). The total revenue of NAFG was significantly less than the investment interest paid to investors for the same period. For the 11 months ending November 30, 2010, there was a net loss of $1,318,646.89.

[74] Continuing with Ex. 11, Mr. Tillie was referred to a list of transactions in Account 652 that listed both debits and credits through the account for the period January 31, 2009 to October 4, 2010 (Ex. 11, Tab D10). The entries reference the TD bank records obtained by Staff. At Tab D11 is a similar document listing all the transactions going through Account 896 for the period January 2, 2009 through October 4, 2010. The significance of Account 896 was its use by NAFG as an arrears account to collect payments returned as "NSF" by lessees. Writers of NSF cheques were required to go to the bank and make a deposit into Account 896, rather than making an electronic fund transfer ("**EFT**") to make lease payments (Tr. Vol. 4, p. 117, ll. 4-20).

[75] I inquired of Staff counsel if the witness was somehow laying the ground work for his preparation of the source and application of funds. Counsel confirmed that this was so.

[76] There then followed a series of questions put by Staff to Mr. Tillie to identify the various types of payments going in and out of Account 652 and Account 896, along with Flavio Arconti's comments on those types of payments as recorded in his compelled testimony. Areas of concentration included attempts to identify the use of the credit cards that both the Arcontis held and payments to the Arcontis of management fees or salaries.

[77] Mr. Tillie was referred to a source and application of funds, which is found in Ex. 18, Tab A, along with supporting documents found behind Tabs B to J. Mr. Tillie confirmed that he was involved in the preparation and review of these documents.

[78] Mr. Tillie described the contents of "Schedule 'A'" in Ex. 18, Tab A, as a schedule identifying the source and application of funds of NAFG for the period of January 1, 2009 to October 4, 2010 for both Account 652 and Account 896. The two primary sources of funds were receipts from investors of NAFG and NAC, and lease payments and other deposits. The schedule organizes the application of NAFG's funds into six main categories, being:

(a) interest paid to investors;

(b) the amounts paid to Prestige Motors on a net basis;

(c) net payments to or for the Arcontis;

(d) operating expenses;

(e) repayments made towards NAFG's bank loan with TD Bank; and

(f) net payments to brokerage firms.

[79] Staff submitted "Schedule 'A' Revised" as Ex. 20 for the period January 1, 2009 to September 24, 2010 ("**Schedule A Revised**"). Staff made changes to the original schedule (found in Ex. 18, Tab A). Staff also went through each of the backup schedules in Ex. 18, Tabs B to J. Staff removed transactions that occurred after September 24, 2010 and revised the balances shown in the previous version of Schedule 'A', which can be found at Ex. 18, Tab A. In the revised schedule, Mr. Tillie included a "Reconciling item", which he submitted was an immaterial amount and therefore chose not pursue. Mr. Tillie confirmed that the total source of funds of NAFG equals the total application of funds for the period of January 1, 2009 to September 24, 2010.

[80] The figures discussed below at paragraphs 81 to 92, regarding Mr. Tillie's analysis of the source and application of NAFG's funds, will refer to the updated values that correspond to Schedule A Revised, which covers the period from January 1, 2009 to September 24, 2010.

[81] The total source of funds for NAFG was calculated by including the net "Receipts from Investors" (Schedule 'B'), the "Lease Payments and Other Deposits" (Schedule 'C') and the opening bank balances of NAFG's two bank accounts, as at January 1, 2009 (Ex. 18, Tabs B and C).

[82] The opening bank balances for Account 652 and Account 896 totalled $830.70 as of January 1, 2009 and the closing bank balances for both accounts as at September 24, 2010 totalled $98,021.66. Mr. Tillie testified that Schedule 'B' contains the details of the receipts from investors (net of repayments). Matters, such as the date of the transaction, description, the account that the transaction relates to and the debits or payments out of the account, all came from the banking information supplied to Mr. Tillie. With four exceptions, all of the receipts and repayments went into Account 652.

[83] In terms of the receipts from investors, found at Schedule 'B', a total of $2,908,170 was received from investors of NAFG, a total of $126,000 was received from investors of NAC and a total of $466,777.58 was repaid to investors. Mr. Tillie took these figures from Schedule 'B' and

entered them into Schedule A Revised under "Receipts from Investors". For the period from January 1, 2009 through September 24, 2010, the net receipts from investors of NAFG and NAC amounted to $2,567,392.42.

[84] Mr. Tillie identified Schedule 'C' as showing lease payment and other deposits into the account of NAFG. This category included the following: lease payments, recovery from automobile sales and "unknown" amounts. Mr. Tillie testified that he analyzed the lease payments that were received by the company through EFTs. Mr. Tillie estimated that at least half of these payments were related to principal repayments by the lessees; nevertheless, he included the entire amount into Schedule A Revised for lease payments. Lease payments collected through Account 896, the arrears account, totalled $228,238.66. Lease payments, net of NSF returns of $339,631.65, amounted to $1,147,154.72. Amounts recovered from the disposal of vehicles or vehicle recovery totalled $86,696.27. "Unknown" amounts were figures that lacked specific details in their bank information, but appeared to be lease payments, and the total amount of which was $99,483.54. The total amount for "Lease Payments and Other Deposits" amounted to $1,333.334.53.

[85] The total application of funds for NAFG was calculated by including the net amounts of the "Interest Paid to Investors" (Schedule 'D'), payments to Prestige Motors (Schedule 'E'), payments to/for the Arcontis (Schedule 'F'), "Apparent Operating Expenses" (Schedule 'G'), NAFG's bank loan with TD Bank (Schedule 'H') and payments made to brokerage firms (Schedule 'I') (Ex. 18, Tabs D to I).

[86] Mr. Tillie described Schedule 'D' as a listing of debits, or payments, made out of the main operating account of NAFG, Account 652. These funds were identified as interest payments that were made to investors and totalled $1,642,413.28. This sum was added to Schedule A Revised as "Interest Paid to Investors".

[87] Mr. Tillie identified Schedule 'E' as a listing of transactions with payments to or receipts from Prestige Motors. The total amounts received by Prestige Motors was $703,407.98. The amounts paid to Prestige Motors were $1,580,907.53. These sums were reported on Schedule A Revised and showed a net payment to Prestige Motors of $877,499.55.

[88] Mr. Tillie reported that Schedule 'F' listed the payments to or for the Arcontis and related parties, along with monies received from the Arcontis and related parties. It lists the various advances from the Arconti brothers, which were all under shareholder advances and totalled $226,000. Amounts received or advanced through various credit cards totalled $53,036.12. Payments were also made directly to Flavio Arconti and/or Gino Arconti under the "Shareholder Withdrawals", which amounted to of $85,614.08. Payments made to various credit cards held by the brothers totalled $502,318.27. The totals from Schedule 'F' are captured on Schedule A Revised under the heading "Payments to/for Arconti", and the net total for such payments was $308,183.37. This value represented the money that went out of Account 652 for the Arcontis' benefit, less any payments made to the account by the Arcontis.

[89] Mr. Tillie described Schedule 'G' as apparent operating expenses. These included expenses related to accounting, auto recovery, bank charges, collections, and legal and regulatory

services. The total of Apparent Operating Expenses came up to $953,127.59, as it appears in Schedule A Revised.

[90] Schedule 'H' lists bank loan repayments made throughout the period of January 1, 2009 to September 24, 2010. These repayments relate to the loan that NAFG had with TD Bank. NAFG was repaying that loan in monthly payments of $500.00. The total sum repaid to TD Bank during the period was $10,500, which was entered into Schedule A Revised.

[91] Schedule 'I' is entitled "Brokerage Firms", which includes a direct payment to TD Waterhouse of $150,000, followed by wire transfers in and out of NAFG's Account 652. These transfers were identified by Mr. Tillie as transactions with interactive brokers. Payments to interactive brokers were $480,000 in total receipts and the amounts received from the brokers were $468,000. After subtracting the funds received from the brokerage firms from the payments made to these firms, the net amount paid to the brokerage accounts was $12,000.

[92] Counsel asked Mr. Tillie a series of questions to demonstrate what conclusions could be drawn from his analysis of the source and application of funds for NAFG. For the period from January 1, 2009 to September 24, 2010, the total lease payments received by NAFG was $1,333,334.53. Mr. Tillie was asked to compare these payments with the interest paid to investors. The total interest paid to investors during the period was $1,642,413.28. Mr. Tillie stated that the conclusion to be drawn from these two figures was that the receipts from lease payments were not sufficient to pay the interest paid to investors during the period (Tr. Vol. 5, p. 58, ll. 14-16). Mr. Tillie said there were only two primary sources of funds for the company: one was the lease payments and the other was the receipts from the investors (Tr. Vol. 5, p. 58, ll. 20-24). In other words, the only other source of funds to make those interest payments was from new investors.

[93] Mr. Tillie identified three deposits listed in Schedule 'B' that were made after the Director's Decision was issued on September 22, 2010. A deposit of $39,270 on September 23, 2010 was made up of deposits from four investors. A deposit of $50,000 from D.M.'s company was made on September 24, 2010, and a deposit of $22,000 from L.F. was made on September 27, 2010. When he was asked if any payments were made to investors during that period, Mr. Tillie identified a draft for $116,853.41 that was made out to M.G on September 28, 2010.

[94] On September 22, 2010, the balance in the main account, Account 652, was $32,692.89. On September 22, 2010, Account 896 had a balance of $112.05. Mr. Tillie was asked by Staff if he could determine whether the payment to M.G. in the amount of $116,853.41 included any part of the investor funds that were deposited on or after September 22, 2010. He replied that if the investor funds had not been deposited on September 23, 24 and 27, 2010, there would have been insufficient funds in the account to pay the draft to M.G.

[95] Counsel then took Mr. Tillie to Ex. 8, where he identified the investor deposit records by way of deposit slips and copies of cheques. Mr. Tillie confirmed that at the end of September 28, 2010 there was an overdraft balance of $9,842.80 in the main account operated by NAFG, being Account 652.

[96] Counsel asked Mr. Tillie to turn to Ex. 18, Tab J, which contains two pages. The first page shows balance sheets for each of the years 2007, 2008, 2009 and 2010 that was prepared by Mr. Tillie from the balance sheets provided to satisfy the undertakings Flavio Arconti made at his compelled examination. The entry "Lease Receivable" is found in the balance sheets under "Current & Long Term" assets. At the end of 2007, that figure was $4,374,488. By the end of 2010, it was reduced to $1,224,708. Lien and promissory notes payable at the end of 2007 totalled $3,035,453. By the end of 2010, that figure had ballooned to $5,920,947.

[97] The second page of Ex. 18, Tab J shows income statements for the same years and was prepared from the income statements provided in response to Flavio Arconti's undertakings. Mr. Tillie confirmed that leasing interest in 2007 was $495,843. It increased slightly in 2008, but by 2010 it had dropped to $232,509. In the same four-year period, interest paid to investors started at $374,816 and grew to $537,499 by the end of 2008. By the end of 2010, investors had been paid $805,815. Mr. Tillie concluded that for the period 2007 to 2010, there was no net income for any of the years presented, rather there was a net loss for each of these years. The cumulative effect of the losses resulted in a deficit at the end of 2010 of $2,596,002.

[98] At the end of July 2011, Mr. Tillie noted that NAFG had closed its TD bank accounts. He asked NAFG's counsel at the time for the name of the financial institution where NAFG was doing business, along with account numbers and copies of the bank statements of NAFG for these accounts (other than any TD accounts) from inception to its most recent statement. Mr. Tillie also prepared an income statement for the period November 1, 2010 to June 30, 2011. The total expenses for the period were $350,000.11, of which $39,000 was paid to the Arcontis.

[99] At Tab 6 of Ex. 19 is a document called the "Trustee's Report to the Creditors" of NAFG, dated January 7, 2011. Staff asked Mr. Tillie to read several lengthy excerpts from the trustee's report which, among other things, identified a range of values for "Noteholders – Unsecured", the high value of which was $5.523 million and the low value was $5.520 million.

[100] Mr. Smith had no questions in cross-examination.

[101] Mr. Tillie was an impressive witness. I have no reason to doubt the accuracy of his calculations or his analysis of the source and application of funds, as described by him in his evidence.

D. J.B.

[102] Staff called J.B., a man in his mid-fifties with a college degree. For the last fifteen years, he has worked for a courier company driving a small cargo van. His evidence may be found in Tr. Vol. 3, pp. 5-93. The documents filed during his examination may be found in Ex. 12.

[103] J.B. saw a small ad in the *Toronto Star* seeking investments in NAFG, which would pay an annual interest rate at 15%. He responded to the ad and met with Flavio Arconti in early February 2008. J.B. filled out an application form, which was in his handwriting, showing his annual income to be $60,000. H indicated in the form that he had other investments of $60,000, and he testified that the only other assets he had was his condo and his van. He estimated his total assets to be $300,000 at the time he filled out the application form.

[104] The form required J.B. to estimate his net worth, and he filled in an amount of $1,050,000. His explanation for doing so was that Flavio Arconti told him that the only way he could proceed with the investment was to show that he had a net worth of $1 million or more. In addition, he initialed paragraph (d) on page two of the application form that indicated he had financial assets exceeding $1,000,000. He gave the same explanation as before, that is, he was told it was a formality and he could only continue by indicating that he had financial assets in excess of $1,000,000.

[105] Flavio Arconti told J.B. that NAFG was borrowing money for auto leasing to people who had little or no credit. They were offering 15% and in turn were lending money to people of poor credit at 30%. Prestige Motors was mentioned during his first meeting, which J.B. understood to be the company associated with the lending arrangements.

[106] The loan agreement that was signed by J.B. was for an investment of $60,000 at an annual interest rate of 15%, in which interest would be payable monthly (Ex. 12, Tab B).

[107] J.B. approached NAFG, seeking to invest further sums in NAFG:

(a) on January 1, 2009, he invested $20,000;

(b) in June to July 2009, he invested a total of $17,000;

(c) on November 23, 2009, he invested $15,000; and

(d) on August 1, 2010, he invested $20,000.

[108] All of the above loans, including the original amount of $60,000, totalled $132,000 at an annual interest rate of 15%.

[109] J.B. testified that on all his loans, either Flavio Arconti or Gino Arconti told him he could not make the investment unless he acknowledged that he was an "accredited investor", that is, someone with financial assets of more than $1,000,000. He acknowledged that in each of the applications he made, he was warned of the risks of investing and that he understood the difference between a low-risk loan and a high-risk loan. He continued to sign and describe himself as an accredited investor.

[110] When asked about how his interaction with NAFG impacted his life, J.B. stated that the destructive effect on his life has been severe. He remains depressed.

[111] In cross-examination, Mr. Smith obtained J.B.'s agreement that every time he was ready to make an investment, he called the Arcontis. He told the Arcontis that he had good investment knowledge and that he had invested in Nelson Financial Group ("**Nelson**"), a company that was essentially in the same business as NAFG. To make that investment with Nelson, he had described himself as an accredited investor. J.B. confirmed to counsel that at the beginning of his relationship with the Arcontis, he would have paid more attention to the documents he was signing and rather less attention as further investments were made. He knew on the basis of the documents that he was taking a risk by making the investment. He acknowledged that he voluntarily signed the investment contracts, but continued to insist that the only way he could

proceed, according to the Arcontis, was to acknowledge that he was an accredited investor. He understood the role that Carter played in his investment with NAFG.

E. L.F.

[112] L.F. is a self-employed man living in Sudbury, Ontario. In 2010, he was engaged in mortgages and loans. His evidence may be found in Tr. Vol. 3, pp. 94-140. Documents relating to his evidence may be found in Ex. 13.

[113] L.F. found out about NAFG from someone who had invested in Nelson. He called NAFG and spoke to Gino Arconti. They discussed the terms of his investment in NAFG over the telephone and L.F. subsequently received an application in the mail (Ex. 13, Tab A). He filled the application in and indicated that he was an accredited investor with over $1,100,000 in net liquid assets.

[114] L.F. was unclear on how many times documents were exchanged between him and Gino Arconti. He said he received a loan agreement in the mail, which had been previously completed, apparently by Gino Arconti, which he signed on September 21, 2010. The agreement called for L.F. to lend $22,000 to NAFG for which he would receive monthly instalments of interest at a rate of 12% per annum. He initialled the second page of the loan agreement at paragraph (j), indicating that he had net financial assets exceeding $1,000,000 (Ex. 13, Tab B).

[115] L.F. was referred to Ex. 13, Tab D, which contains a copy of a cheque for $22,000, signed by L.F. and dated September 1, 2010. He sent the cheque to NAFG by Purolator from Sudbury to Toronto. He was asked if he had been told that NAFG was in financial difficulty and whether he would have made the investment if he was told that the company was experiencing financial difficulties, to which he replied, “I’m not that stupid, I don’t think that I would invest with them” (Tr. Vol. 3, p. 121, ll. 10-25; p. 122, ll. 1-8). L.F. was also referred to a copy of his bank statement, showing a cheque for $22,000 that went through the account on September 28, 2010 (Ex. 13, Tab E).

[116] In cross-examination, L.F. confirmed the facts recorded on his loan application were correct. He described his interaction with Gino Arconti as sending papers back and forth. Apparently he signed some papers, forwarded them to Gino Arconti and asked that they be sent back completed by NAFG. All he could remember is that documents were sent back and forth. L.F. confirmed that he knew he was making a high-risk investment and that the proceeds would be used to finance the daily operations of NAFG and its affiliates. His understanding of Prestige Motors confirmed to him that NAFG was a going concern in dealing with the kind of cars he was interested in.

F. J.S.

[117] J.S. is a retired gentleman in his early eighties living in Toronto, Ontario. He worked as an environmental scientist until 1996. His evidence may be found in Tr. Vol. 3, pp. 141-202. Documents referred to in his evidence may be found in Ex. 14.

[118] J.S. learned about NAFG through an ad in a newspaper. He telephoned to make an appointment and went to NAFG’s office and met with one of the Arconti brothers. He thought

most of his dealings were with Gino Arconti. J.S. understood that NAFG would purchase used automobiles and then lease them to people over shorter periods of time at rates that would almost pay off the cost of the vehicle. He was not told anything about the financial condition of NAFG. Rather, NAFG appeared to be a viable operation that was following a business plan of a company named Carfinco, which seemed to be a successful operation. The Arcontis asked him if he was an accredited investor and he confirmed that he was. In making the calculation of his assets, he included the value of his home. He said he was never aware that you had to exclude real property. The combined income of J.S. and his wife was approximately $90,000.

[119] J.S.'s attention was drawn to Ex. 14, Tab A, which contains a loan agreement. The agreement confirms that he loaned $30,000 to NAFG and was to receive annual interest at 15%. He agreed that he and his wife signed the loan agreement, as well as an acknowledgement that they were accredited investors. J.S. confirmed that if he took his house out of his calculations, he would not qualify as an accredited investor.

[120] J.S. was referred to Tab C in Ex. 14, a document described as a "New client application form" on the letterhead of Carter. J.S. said that he knew very little about Carter, but confirmed that he and his wife signed the form. The handwriting on the form under the "Financial information" and "Investing information" headings was not that of J.S. It appears to have been the handwriting of Gino Arconti. Although the form indicated that J.S. was an accredited investor, J.S. told Staff counsel that his net financial assets at the time were less than $600,000. The form described his investment knowledge as good and J.S. agreed that that was so at the time he signed the form in January 2010. He disagreed with the box on the form that indicated he was seeking a "high-risk/high return" investment. He would have indicated that he was seeking "medium-risk/medium return" investment. Although the form indicated that the value of his investments was $1,500,000, this was denied by J.S.

[121] On September 1, 2010, J.S. invested in a convertible debenture for $40,000 (Ex. 14, Tab F). J.S. was referred to Ex. 14, Tab H, a document entitled "Notice of Conversion", also dated September 1, 2010. The document indicates that J.S. and his wife converted their original investment of $40,000 into units of NAFG. Apart from the signatures, the handwriting on the document appears to be that of Gino Arconti. The Private Placement Subscription Agreement for the debenture is found at Ex. 14, Tab F. The document appears to have been completed by handwriting similar to that of Gino Arconti. The debenture is in the amount of $40,000, being the original amount invested by J.S. and his wife, and is completed to show that J.S. was an accredited investor. In his testimony, J.S. continued to affirm that he was not an accredited investor on September 1, 2010. His understanding of the debenture was that NAFG no longer could pay an annual interest rate of 15% to investors and that "they were doing some footwork to lower it, but still keep the investors in place" (Tr. Vol. 3, p. 173, ll. 13-19). He confirmed that neither of the Arcontis told him that NAFG was experiencing financial difficulties.

[122] In cross-examination, Mr. Smith pointed out to J.S. that he had represented that he had assets in excess of $1,000,000 at the time J.S. signed the documents. J.S. repeated that he did not understand that he had to exclude his house. He acknowledged that the term "accredited investor" was a term with which he was familiar. He confirmed that he told Gino Arconti that he was an accredited investor. He confirmed that he sought out NAFG rather than the reverse.

[123] Mr. Smith suggested to J.S. that the information in the "New client application form", found at Ex. 14, Tab C, was provided by J.S. to the Arcontis. In other words, the Arcontis filled out the form, and J.S. then reviewed and signed it. J.S. disagreed with this suggestion.

[124] Counsel referred J.S. to Ex. 14, Tab F, which is the Private Placement Subscription Agreement dated September 1, 2010, signed by J.S. and his wife. J.S. confirmed that the Arcontis approached them about the possibility of converting their prior investment of $40,000 into a convertible debenture. The Arcontis said they could no longer afford to pay 15% and that they wanted to reduce the interest payable to 5%. Counsel pointed out a paragraph in the agreement that the proceeds of the offering would be used to finance the daily operations of NAFG and its affiliates. J.S. acknowledged that he had read that paragraph when he signed the document, but he had no discussion about those companies with the Arcontis.

G. R.B.

[125] R.B. is a man in his late forties, living with his wife just east of Toronto, Ontario. He is a teaching assistant and he is working towards a PhD. His evidence may be found in Tr. Vol. 4, pp. 7-48. The documents referred to in his evidence may be found in Ex. 15.

[126] R.B. first invested in NAFG in March 2010. At the time, his salary was $16,000 a year and his wife's salary was approximately $50,000 a year. He estimated he had financial assets of $600,000 to $700,000, excluding his house. Including his house, he estimated his total net worth to be approximately $1,200,000. In March 2010, he thought an accredited investor was someone who had good credit. Staff drew his attention to Ex. 15, Tab C, a document entitled "Schedule 'A' Certificate of Accredited Investor". R.B. and his wife had put their initials beside paragraph (j), which indicated that their financial assets were worth more than $1,000,000, but R.B. understood this paragraph to mean that they would be accredited investors if their entire worth was more than $1,000,000. He explained by saying that, including his house, his net worth was approximately $1,200,000. He was unaware that he could not include his house in calculating the total value of his net financial assets.

[127] R.B. learned of NAFG through someone who invested in Nelson. He was given a number to call and spoke with Gino Arconti. Shortly thereafter, he received a package of information from NAFG found in Ex. 15, Tab A.

[128] R.B. said he read the information received from NAFG with care and was struck by the reference to the 20-year history of the company, as well as its business plan, which he recognized to be similar to that of Nelson. He was also encouraged by the GPS locator put in the cars that NAFG sold to persons of poor credit. Summing up his reaction to the information received from NAFG, R.B. said that it appeared to be a "pretty solid company and, you know, a place you would want to invest" (Tr. Vol. 4, p. 22, ll. 1-3).

[129] He next had a conversation with Gino Arconti, where he indicated his willingness to invest. There was no discussion about the accredited investor requirement. He attempted to set up a date to meet Gino Arconti at the office, which proved difficult since they could not get their schedules to meet. Gino Arconti suggested that he would send him the documents in the mail, which R.B. was to sign and return.

[130] In Tab C of Ex. 15 is a loan agreement signed by R.B. and his wife in the amount of $70,000 with an annual interest rate at 15%. Someone signed for NAFG, but R.B. and his wife were not present when that was done. He confirmed his and his wife's signatures on the Schedule 'A' Certificate of Accredited Investor form.

[131] R.B. confirmed that no one told him about the financial condition of NAFG nor was he told that the money he was investing would be loaned to a car dealership owned the Arcontis. He also confirmed that he entered into a second loan agreement with NAFG in March 2010, advancing $14,500 with an annual interest rate at 12%.

[132] In August or September 2010, R.B. was contacted by Flavio Arconti, who informed R.B. that the Arcontis wanted to come and see him, and arranged to meet at R.B.'s house. R.B. learned at the meeting that NAFG was having difficulty paying its high interest rates to investors and it needed to lower those rates. R.B. asked the Arconti brothers if NAFG was insolvent and they responded it was not. R.B. asked if the Commission was involved with them and they responded it was not. R.B. did not enter into a new loan agreement.

[133] Subsequently R.B. learned of NAFG's receivership with Farber. His investment was reduced by 50% and he received some paperwork stating that he would receive a 1% monthly payment on his 50% remainder. He confirmed that if he had known that NAFG was in financial difficulty before he invested in March 2010, he would never have considered doing so. When asked about how his involvement with NAFG affected him, R.B. stated that it has had a very negative effect and it was a horrible experience for him and his wife.

[134] In cross-examination, R.B. confirmed that he told Gino Arconti that he had invested in Nelson before his investment in NAFG. He acknowledged that after he read paragraph (j) of "Schedule 'A' Certificate of Accredited Investor" (Ex. 15, Tab C), he then knew that an accredited investor was something more than someone with good credit. However, what he did understand was that "financial assets" included his home as well. He denied that in a subsequent conversation with one of the Arcontis that they discussed R.B.'s financial circumstances. There was no discussion of whether R.B. was a low-risk, medium-risk or high-risk investor. Regarding his meeting with the Arcontis in August or September 2010, counsel suggested that R.B. did not ask his questions regarding the solvency of NAFG at the meeting, but that those questions were asked much later. This was denied by R.B.

H. D.M.

[135] D.M. is a man in his early forties with a degree in Engineering. He is self-employed and works for a communications company as an IT professional. His evidence may be found in Tr. Vol. 4, pp. 49-112. The documents filed during his examination may be found in Ex. 16.

[136] D.M.'s accountant recommended that he consider investing in NAFG. After meeting with Gino Arconti in September 2010, he received a Confidential Term Sheet in relation to the "Convertible Debenture Offering" (Ex. 16, Tab E), which he looked over before deciding to invest. He met with the Arcontis on September 18, 2010 and was told that there would be an announcement that NAFG would be going public. He examined a brochure (Ex. 16, Tab A), which contained a lot of information that made him confident that NAFG was a worthwhile

investment. He was asked to review a number of documents found at Tabs B to E in Ex. 16, including a Joint Client Application Form, a Private Placement Subscription Agreement, a Notice of Conversion and a Confidential Term Sheet. All of these documents were filled out by either Flavio Arconti or Gino Arconti and signed by D.M. The documents indicate that D.M. had a net worth exceeding $1 million in financial assets. For example, the Joint Client Application form indicated that D.M.'s net worth was $2 million at the time he signed the form on September 20, 2010 (Ex. 16, Tab B). However, D.M. testified that he and his wife did not have financial assets in excess of $1 million, but he was told he had to show that he did or he could not participate in the investment.

[137] D.M. wrote a cheque to NAFG from the account of his company for $50,000 dated September 1, 2010 (Ex. 16, Tab H). D.M. sent an email to the Arcontis confirming their discussion, whereby NAFG would hold off cashing the cheque until D.M. rounded up the funds, which he expected to do so by the following Friday (Ex. 16, Tab I). On Friday, September 24, 2010, Gino Arconti emailed D.M. asking if he could put the cheque through. D.M. responded almost immediately that day, confirming that the cheque could go through (Ex. 16, Tab F). The cheque was deposited into NAFG's main bank account, Account 652, on September 24, 2010.

[138] At no time did the Arcontis tell D.M. that NAFG was in financial difficulty. According to D.M., what they did tell him was that they were planning to "take the company public" (Tr. Vol. 4, p 73, ll. 5-10). His investment would be converted into shares in the public company and thereby have the potential of a significant increase in value.

[139] In cross-examination, D.M. confirmed that one of the Arcontis told him the security could not legally be sold to him if he did not have a net worth above $1,000,000. D.M. confirmed that when the figure of $2 million was written in on the Joint Client Application, D.M. was aware that the information was false. D.M. further confirmed that he was looking for a high-risk, high-return investment, as indicated in the documents he signed. He knew he could lose his total investment. Counsel pointed out to D.M. that the documents made it clear that the possibility of the company going public was completely contingent. D.M. agreed, but continued to insist he was told by the Arcontis that the company was going public in January 2011. He conceded that the documents revealed the investment he was making could be used for a number of purposes, including the operation of a group of companies, such as Prestige Motors.

PART 3 – RESPONDENTS' WITNESSES

A. Flavio Arconti

[140] Mr. Arconti's evidence is found in Tr. Vol. 6, pp. 33-167, Tr. Vol. 7, pp. 4-180 and Tr. Vol. 8, pp. 8-177. Documents introduced during his testimony were entered as Exs. 21 and 22.

[141] Mr. Arconti is 42 years old. He completed one semester at York University and then left to start an automotive dealership business with his brother, Gino Arconti. He began by buying and selling mainly used cars. He moved several times over the last few years. The last location for Prestige Motors was in the Highway 400 and Finch Avenue area, which is north of Toronto, Ontario. That facility comprised of a 30,000 square foot building and three acres of space that could accommodate about 600 cars.

[142] Flavio Arconti was responsible for purchasing used vehicles through various dealer networks, as well as attending wholesale auctions. He hired salespersons, trained them and assisted with sales on the floor. He also interviewed business managers at the dealership and hired them as required. He described Gino Arconti's role as closer to an operations manager. He oversaw the re-conditioning of the vehicles that came into inventory, managed the mechanics and the re-conditioners, assisted with sales management and also hired salespersons and other employees. The Arcontis were, for all intents and purposes, 50-50 partners.

[143] The majority of the purchases from Prestige Motors were financed and many potential customers were unable to obtain bank approvals for their car loans. In 2003 and 2004, there was an expansion of sub-prime lending to such persons, which caught the attention of the Arcontis. NAFG was created to hold motor vehicle leases and the Arcontis began issuing securities by way of loan agreements with accredited investors. They were assisted by Cassels Brock in putting the loan agreement together. In late 2005, they raised approximately $170,000 of equity financing from friends and family members. They attempted to obtain the services of as HDL Capital Corporation ("**HDL**") to see if they could assist with their financing, but were told to come back when the company was a larger size.

[144] Carter was formed in early 2007. NAFG had been advertising as an issuer of exempt market securities and received an inquiry from the OSC. They immediately contacted Cassels Brock for advice, who recommended that they apply as a limited market dealer if they wished to engage in the business of raising securities. Ultimately, they obtained approval for Carter as an Exempt Market Dealer in September 2007. Flavio and Gino Arconti became registrants, with Flavio Arconti as the designated compliance person. Their advertisements in the *Toronto Star* generated many responses, 95% of which were people who did not meet the definition of an accredited investor.

[145] Mr. Arconti then described the difficulties with the automotive industry in 2008 and the collapse in the financial markets. In late 2008 or early 2009, the Arcontis were informed that they were to be the subject of a compliance review, the 2009 Compliance Review. Cassels Brock referred the brothers to David Gilkes, a former manager of registration at the Commission, who subsequently left and went into private practice. Mr. Gilkes assisted the Arcontis with meeting the compliance review requirements.

[146] Following a visit from Staff, the Arcontis received requests for documents and information, which they provided with the help of Mr. Gilkes. Four or five months later, the Commission issued a deficiency report.

[147] One concern expressed by the OSC was the form and content of NAFG's marketing brochures, which were prepared by Flavio Arconti and for which he accepts responsibility.

[148] Counsel took Flavio Arconti through a series of different brochures that were issued by NAFG to prospective investors over several years. One could not characterize the content of the early brochures as modest. Indeed, the material conveyed a picture of a thriving company with a successful business in competition with large players in the sub-prime lending business. Based on Mr. Tillie's evidence I find nothing could be further from the truth.

[149] By letter dated April 24, 2009, the OSC sent a deficiency notice to the Arcontis, the 2009 Deficiency Report. The two significant deficiencies were the lack of procedures designed to satisfy the requirements of KYC, and the lack procedures to determine if prospectus exemptions were available to persons who invested in NAFG. The Arcontis immediately spoke with Cassels Brock and David Gilkes. Mr. Gilkes drafted a response to the Commission, which was dated May 25, 2009, signed by Flavio Arconti and addressed to the Commission (the "**May 2009 Letter**"). Mr. Arconti testified that the effort to comply with the Commission's demands was of the highest high priority for NAFG. Mr. Gilkes assisted in preparing a new version of the New Client Application Form that would be used going forward. A Certificate of Accredited Investor was also prepared. The compliance review continued almost until the end of 2009, with correspondence going back and forth between NAFG and the Commission. Mr. Arconti thought at the time that he had the best advisors money could buy and from whom he was obtaining advice on what to do and how to comply with the requests of the OSC. In late 2009, the Arcontis learned that the OSC was starting a second compliance review in early January 2010, the 2010 Compliance Review.

[150] The Arcontis immediately called Mr. Gilkes, who did not understand why there was to be a second compliance review. The OSC requested "a lot of documents" (Tr. Vol. 6, p. 86, ll. 11-14). At a meeting on January 5, 2010, Flavio Arconti told the OSC that the default rate on the leases was historically 15% every year. He explained that what he meant was that in year one of the lease, there was a 15% default ratio and that in the second year it would accumulate and continue to do so for each year that followed. The probability of default went higher and higher in each year of the lease. Flavio Arconti confirmed at the meeting that he had little experience with compliance matters.

[151] Mr. Smith then asked Flavio Arconti about NAC. Mr. Arconti confirmed that the money invested in NAC went to NAFG. NAC was not licensed to lease vehicles to consumers and therefore NAFG was the conduit for the lease transactions. Mr. Arconti said that people who invested in NAC understood that they were investing in a group of companies, primarily in NAFG.

[152] Counsel then turned to the matter of an accredited investor and asked a series of questions about how seriously Mr. Arconti took his obligations to be satisfied that investors were truly accredited investors. Mr. Arconti confirmed that if an investor included their principal residence in the calculation of financial assets, Mr. Arconti would have told them that was not permitted.

[153] Mr. Arconti was also asked a number of questions about claims contained in the various marketing brochures sent to investors. He admitted that the wording in some of the statements could be construed differently than he interpreted it to mean. He acknowledged that some of the statements in the brochures could have been reworded slightly. This led Mr. Smith to submit a brief of new documents entered as Ex. 22, containing the revised brochures prepared by David Gilkes sometime after July 22, 2009. Mr. Arconti estimated that the new brochures would have been distributed to investors in August and part of September 2010, since the Director's Decision was released in the latter half of September 2010.

[154] Staff had questioned the existence of the loan to Prestige Motors and Mr. Arconti was asked if anything was done to address that criticism. Mr. Arconti described this issue as an oversight and that there was every intention to pay back the loan.

[155] Mr. Arconti was then asked a series of questions, and the answers to which stressed the difficulty the Arcontis faced when responding to the 2010 Compliance Review. He described the time spent in preparing statements and documents for Staff and the difficulties this activity presented. All the while, Mr. Arconti said they were attempting to deal with decreased commercial activity caused by the 2008 financial crisis and the decreased activity in vehicle sales. Nevertheless, the Arcontis anticipated that, following the compliance review, Staff would issue a deficiency report that could be satisfied by the Arcontis, who were working in conjunction with their professional advisors. Mr. Arconti told his counsel:

> We were going to sit down with our advisors and clearly address any deficiencies on anything that the staff had -- would request for changes. We would make sure that we would comply hundred percent.
>
> (Tr. Vol. 6, p. 143, ll. 3-7)

[156] When the Arcontis learned from the June 2010 Letter that Staff would recommend to the Director that Carter's registration as an Exempt Market Dealer be revoked, Flavio Arconti was shocked. There then followed a full review by the Enforcement Branch of the OSC.

[157] Counsel then turned Mr. Arconti's attention to the testimony of Staff's investor witnesses. Mr. Arconti remembered meeting J.B. J.B. told Mr. Arconti that he had net financial assets that exceeded $1 million and that he was an accredited investor. Mr. Arconti asked no further questions of J.B. as to his status as an accredited investor and acknowledged that he "should have dug a little deeper to identify the sources of these financial assets" (Tr. Vol. 6, p. 159, ll. 12-17). He denied ever telling J.B. that signing and initialling statements to the effect that he was an accredited investor was a mere formality. He did not force J.B. to sign any of the documents he signed. He confirmed that J.B. was invited to a meeting where he was asked to voluntarily convert from a higher-yield paying instrument into a convertible debenture with a lower yielding 5% coupon. J.B. was not interested.

[158] Mr. Arconti denied having any contact with the investor L.F.

[159] Mr. Arconti's attention was drawn to Ex. 14, containing the documents pertaining to investor J.S. Mr. Arconti said he would have discussed the issue of an accredited investor with J.S. He denied telling him that it was not important whether or not it was true that he had financial assets that exceeded $1 million. It was J.S. that supplied the number for his estimated net financial assets at $1.5 million. J.S. was one of the investors who was asked to convert his investments to a lower-yield paying instrument.

[160] Counsel then asked questions regarding the investor R.B. and his wife. Flavio Arconti stated that he had no involvement with R.B. in March 2010 when his initial investment was made. Mr. Arconti got in touch with R.B. in August or September 2010 to schedule a face-to-face meeting, when both Arcontis visited R.B. at his home. The brothers explained that NAFG could no longer pay the high rates of interest and that they needed to get their cost of capital

down. However, R.B. was unwilling to change the terms of his investment. Flavio Arconti did not remember having any conversations with respect to NAFG's insolvency. He added that R.B. never asked them if there were OSC proceedings against NAFG. In his testimony, R.B. stated that he had received a marketing brochure from NAFG that described the investment as an "an attractive safe high yield income-generating investment for the investor" (Ex. 15, Tab A). Mr. Arconti explained that the version of the brochure that was sent to R.B. was never approved for distribution and that the word "safe" was a drafting error.

[161] Finally, Mr. Arconti was asked about D.M.'s investment and the documents in Ex. 16. Mr. Arconti testified that since D.M.'s accountant was an investor with NAFG and an accredited investor, his accountant would have clearly known if D.M. was an accredited investor. Mr. Arconti denied telling D.M. that it was unimportant or irrelevant whether his estimated net worth in liquid assets were accurate. He denied changing the number that appears on the form in Tab B of Ex. 16 from $1 million to $2 million. D.M. invested in a convertible debenture with NAFG and Mr. Arconti denied promising D.M. that the company was going to be publicly traded as of January 1, 2011.

[162] Counsel then directed Mr. Arconti's attention to Ex. 18, which includes documents related to Mr. Tillie's source and application of funds, receipts from investors, monies received and paid to Prestige Motors and payments to or for the Arcontis and related parties, as well as other pertinent analyses. Mr. Arconti was asked how often he looked at the company's financial statements and his reply was that he reviewed them on a yearly basis. When the financial statements were compiled for a fiscal year, he and his brother would then review the operations of the company. This usually happened probably a month or two after the fiscal year end. I find this evidence difficult to accept. My ordinary life experience and common sense tells me that persons in the sale of used cars and the financing of high interest loans would be extremely interested in how the business was doing, if not on a daily basis, then certainly weekly and monthly.

[163] Mr. Arconti said that by the time of the OTBH and the Director's Decision, he had not seen the financial numbers for 2010. He said that he had no idea how large the losses were. He pointed out that the ongoing regulatory issues they were trying to correct took a lot of time and resources away from operations of the companies, and that, unfortunately, significantly impacted the revenues for that current year. I take from what Mr. Arconti said that the reason revenues were so poor in 2010 was due, at least partially, to the regulatory activities of the OSC. I contrast this with Mr. Arconti's earlier evidence that all the financial information provided to the OSC flowed from Ms. Widjojo (Tr. Vol. 6, p. 137, ll. 9-10).

[164] During the course of his evidence, Mr. Arconti went into some detail about the efforts of the Arconti brothers to obtain financing through a third-party, HDL. There was considerable evidence about HDL's willingness and belief that it could raise $2.5 million for NAFG and the meetings that took place to develop a suitable course of action. A letter of engagement was signed. Mr. Arconti obviously felt the principals responsible for HDL were of high calibre and capable of carrying through with a suitable financing. HDL cancelled the letter of engagement when it learned of Carter's Suspension with the OSC. Mr. Arconti described the cancellation as extremely devastating for NAFG. He felt NAFG had a real plan of action to grow the company, to make it a successful company, to move the company forward and everything was taken away

from them. Once again, there was a suggestion in Mr. Arconti's evidence that it was the fault of OSC that caused HDL to terminate its relationship with NAFG.

[165] Mr. Arconti concluded his examination-in-chief by repeating his shock at the suspension of Carter's registration from the Director's Decision. Shortly thereafter, NAFG filed a proposal under the *BIA*.

[166] Staff counsel began Mr. Arconti's cross-examination by asking if either he or his brother attended the OTBH. Mr. Arconti confirmed that they did, but neither of them testified. There followed a series of questions concerning NAFG's business that were neither confusing nor complex. Nevertheless Mr. Arconti did his best to avoid giving direct answers, either claiming he could not remember or giving answers unresponsive to the question. This led counsel to observe:

> Q. Mr. Arconti, it's going to be a lot smoother … I just had a very specific question. I'm not trying to trick you. My question is simply: Was NAFG deriving revenue from lease payments from lessees?
>
> A. That was one component of our business.
>
> (Tr. Vol. 7, p. 70, ll. 14-20)

[167] Mr. Arconti confirmed his evidence given in examination-in-chief that after he looked at the financial statements for the fiscal year 2008 at the beginning of 2009, he did not monitor the monies coming in from lessees until a year later. He added that he would not have looked at them until January or February 2010.

[168] Mr. Arconti was referred to Ex. 2, Tab 16, which contain notes taken by Staff at a meeting on January 25, 2010. Counsel sought confirmation about the answers given by Mr. Arconti at that meeting with respect to the policies and procedures manual of Carter. Mr. Arconti's answers to questions put to him during this portion of his cross-examination were not responsive. Immediately before the lunch recess the following exchange took place between Mr. Arconti and myself:

> Chair: Before we break – just remain standing, Mr. Arconti, if you would, please – part of my task in this hearing sometimes requires me to make findings of credibility, and in making findings of credibility one of the things that I take into account are the responses that witnesses make to questions.
>
> What I have observed in the responses that you've made during the course of your testimony both to your counsel and to Staff counsel, are not necessarily as responsive as I think they could be. Now, you're entitled to know this, you see, --
>
> The Witness: Okay.
>
> Chair: -- and the reason you're entitled to know this is if there is a permanent, continual attempt to avoid answering a question directly, then at a certain point

that may require me to make a finding of credibility that isn't very useful for your purposes.

So what I want you to do is listen carefully to the questions. If the question is answered by a "yes" or a "no" and you're comfortable with that, then I want you to consider whether you should answer "yes" or "no".

Now, let me repeat. You're entitled to know this. It's not fair to you for me to sit here for the entire hearing and then in my findings make my findings based on my observations. You're entitled to know that now before we go any further.

The Witness: Okay.

Chair: Do you understand that?

The Witness: Yes, I do.

(Tr. Vol. 7, p. 94, ll. 10-25; p. 95, ll. 1-16)

[169] Staff counsel then drew Mr. Arconti's attention to the two compliance reviews initiated by Staff. Mr. Arconti acknowledged that as a result of the compliance reviews, the practices and procedures of Carter and the NAFG group of companies were amended to demonstrate the importance that investors were accredited. During the course of this cross-examination, Mr. Arconti testified that every single letter that was drafted and sent to the OSC was prepared by David Gilkes and signed by Mr. Arconti on Carter's letterhead. Counsel then put to Mr. Arconti certain financial statements submitted to Staff as a result of undertakings given under his compelled examination. Mr. Arconti confirmed that he was aware as of March 2009 that Prestige Motors owed NAFG approximately $1.2 million as of the 2008 financial year-end. He also confirmed that the deficit for NAFG as of December 2008 was $861,131.73, and that in March 2009 he knew this to be so (Ex. 18, Tab J, p. 36).

[170] Counsel then drew Mr. Arconti's attention to the trial balance for December 31, 2009 for NAFG. Mr. Arconti confirmed that the document showed NAFG's loan to Prestige Motors at $1,987,084.74. He also confirmed that he was aware on January 25, 2010 that the loan had reached almost $2 million. Staff counsel referred Mr. Arconti to the trial balance item entitled "Customer Age Summary" as at December 31, 2009. Mr. Arconti confirmed that he knew that approximately 80% of the current receivables were in the "91+" day default category, but pointed out that he did not prepare the report. Ms. Widjojo was responsible for the preparation of that information. When asked if he reviewed the Customer Age receivables, he said he did glance at them occasionally, but left it up to the accountant and "receivables" people.

[171] Staff referred Mr. Arconti to documents prepared by Ms. Widjojo for the year ending December 31, 2009. Mr. Arconti acknowledged that the loan to Prestige Motors was over $2 million and that the accumulated deficit for NAFG was over $1.1 million.

[172] Mr. Arconti denied that he knew there were problems with the marketing materials for which he was responsible. He denied recalling that Staff raised issues about the marketing materials during the 2010 Compliance Review. He said that the first time he knew of any

problems with the marketing materials was when he received the June 2010 Letter. He denied that compliance deficiencies with the marketing material were discussed with him prior to his receipt of the letter.

[173] Finally, Staff attempted to obtain Mr. Arconti's agreement that as of April 29, 2010, NAFG was not in a good financial situation. Mr. Arconti responded:

> I do admit that there were losses. We were attempting to repair those. We had addressed those. We understood where we were currently. We had retained financial advisors to assist us.
>
> So I understand what you're saying, and I do agree with you, but there were definite major steps towards bringing this company to profitability.
>
> (Tr. Vol. 7, p. 161, ll. 10-16)

[174] In Mr. Arconti's examination-in-chief and cross-examination, he never wavered in asserting that although NAFG and its associated companies were losing money, they were working to return the companies to profitability and were confident that they could do so.

[175] It was put to Mr. Arconti that he transferred ownership of his family home, which had previously been jointly owned by him and his wife, into his wife's name alone. He confirmed this to be so. He said he made a transfer with proper consideration and there was a personal reason. He was going to start flying again with his private pilot's license and was also buying a motorcycle. His wife thought he was being very risky with his actions and she therefore asked for the transfer of his interest in the matrimonial home. He was asked to explain why Gino Arconti did the same thing with his residence, and Flavio Arconti replied that it had nothing to do with him. He denied that he was putting the interest in the matrimonial home beyond the reach of the OSC or potential creditors.

[176] Mr. Arconti stated that the regulatory burden created by the OSC was making things difficult for him. The Arcontis had hired professionals and the professionals were telling them that NAFG had a viable plan and that it was going to work.

[177] On May 9, 2013, the cross-examination of Flavio Arconti continued all day. Much of the day was spent revisiting areas previously covered in the preceding day on May 8, 2013, particularly regarding questions designed to obtain responses from Mr. Arconti which he was not prepared to give. On more than one occasion, I was compelled to invite Staff to move on when a particular line of questioning was either unclear or unhelpful. Three major lines of inquiry were prominent during the day's cross-examination.

[178] The first line of inquiry centered on counsel's efforts to get Mr. Arconti's agreement that NAFG was not a financial success in March 2009:

> Q. And did you view NAFG as at March 2009, a company that had losses year over year and continued to have losses from the end of 2008, did you view NAFG as a successful company?

A. The -- financially it was losing money, but we believed with this deployment of this technology, it was assisting us bringing in higher numbers than if we weren't.

Q. So did you believe that NAFG was a successful company in March 2009?

A. I believed it was going to be a successful company at some point. We did have some losses. We were working with advisors. And I believed at some point we would be profiting.

Q. All right. So you understood as at March 2009, it was not a successful company?

A. I believe it was successful. There were some losses. You don't measure success by just simply a snapshot of a financial statement in a specific time. There's intrinsic value and enterprise value that this company had.

(Tr. Vol. 8, p. 48, ll. 21-25; p. 49, ll. 1-16)

[179] The second line of inquiry was an effort by counsel to obtain Mr. Arconti's agreement that the various marketing brochures he created were designed to give a false impression of NAFG's financial health:

Q. And I put it to you that in preparing this brochure, you were trying to convey an image of NAFG as a large successful company.

A. No.

Q. And, in fact, you knew that NAFG was a small, unsuccessful company when you prepared this brochure?

A. No.

Q. And you were concerned that if you gave the true information about the company in this brochure, no one would want to invest in this company?

A. No.

(Tr. Vol. 8, p. 53, ll. 2-13)

[180] The third line of inquiry was focused on the alleged failure of NAFG to give investors an accurate picture of the financial condition of NAFG:

Q. By June 2010, you are being told by the Ontario Securities Commission staff that it's their view that you are in breach of securities law by selling your product to investors without telling them about the severe financial condition of your company. Correct?

A. Could you repeat that question one more time? Sorry.

Q. On June 23, 2010, the Ontario Securities Commission staff are providing you their view that they -- they are of the view you are in breach of Ontario securities law because you are not telling your investors in NAFG about the severe financial condition being faced by that company?

A. Again, we're going back to the private issuer. We consulted with David Gilkes. He says there's no requirement to provide financials. And we were working it internally, restructuring, reorganizing our company to profitability.

So we -- I didn't know.

Q. And instead of providing information to investors about the financial circumstances of NAFG, you attach even more financial information about successful other companies that aren't at all comparable to NAFG, correct?

A. We were trying to demonstrate that we have engaged [an] investment bank, and we were moving to a similar model of the Carfinco. And that's where we were moving to. We had an investment bank. We made explanations about that. We were trying to educate people about the industry, how it -- the industry is currently performing, and providing research reports that were pulled off the Carfinco website.

We would print them out and say, look, if you want to read -- I didn't have a research report on my company. I had independent research reports available through the Internet. We submitted that to investors. We were just trying to educate them, and we were trying to move into that area.

(Tr. Vol. 8, p. 95, ll. 4-25; Tr. Vol. 8, p. 96, ll. 1-17)

[181] The cross-examination of Flavio Arconti concluded with questions directed to various credit card expenses analyzed in Mr. Tillie's evidence. Neither the questions nor the answers are of much help to me.

B. Luigino (Gino) Arconti

[182] Gino Arconti is 46 years old and completed grade 12. After working in construction and real estate, he and his brother started Prestige Motors together on a part-time basis which became full-time in 1994. They were simply buying and selling cars, primarily used cars.

[183] Mr. Arconti's evidence is found in Tr. Vol. 10, pp. 5-198 and Tr. Vol. 11, pp. 1-126. Documents introduced during his testimony were entered as Exs. 26, 27 and 28.

[184] Mr. Arconti had an operational role preparing and cleaning cars, and overseeing sales staff and mechanics. Prestige Motors grew gradually as it moved from location to location, until their final move to a site north of Toronto just off of Highway 400. The property spanned three acres with a large building, including an indoor show room. They had an eight-bay facility and a complete body shop. The facility was designed as a full-service dealership for reconditioning and sales, as well as servicing customers' cars. The property could house 600 vehicles.

[185] NAFG was formed in 1996, as there was a need to provide financing for potential customers of Prestige Motors. Mr. Arconti testified that people with poor credit were willing to pay a much higher rate of interest, if they could get approved for a loan to buy cars from Prestige Motors.

[186] While searching for ways to grow their business, the Arcontis came across Nelson in an advertisement in a paper. It was raising capital from accredited investors and Nelson's business model appealed to the Arcontis. The model required the Arcontis to form Carter and obtain its registration as an exempt market dealer. It was Gino Arconti's understanding that it would allow the company to raise funds from accredited investors. Their solicitors, Cassels Brock, provided the risk acknowledgement forms to NAFG and stated that they would need to be completed and signed by every investor. They advertised in the *Toronto Star*, which generated a lot of calls, which Gino Arconti calculated to be over 3,000 calls over a five-year period.

[187] Gino Arconti was a licensed sales representative for Carter and Flavio Arconti was the Chief Compliance Officer and a licensed representative. Gino Arconti dealt with most of the investors. He described the state of the automotive and financial industries in 2008 as experiencing a severe recession. The year 2009 was also a very tough year for Prestige Motors.

[188] In the fall of 2009, Carter learned that the OSC was going to conduct a compliance review. The Arcontis notified Cassels Brock who came to the office to prepare responses to the list of items that Staff asked for. Staff interviewed Flavio Arconti, and from Gino Arconti's point of view, the Arcontis provided the Commission with all the requested documents.

[189] Mr. Arconti's attention was drawn to Ex. 2, Tab 6, a version of NAFG's marketing brochure that was provided to Staff during the 2009 Compliance Review. Gino Arconti said he accepted Staff's criticism that the document tended to leave the impression that NAFG was a bigger player than it really was in the automotive and financing industry. Gino Arconti confirmed that this version of the document was more widely distributed than any of the other versions of the brochure. They sought David Gilkes' help to improve the shortcoming of this brochure. Mr. Arconti was then referred to the May 2009 Letter, which was signed by Flavio Arconti, but drafted by Mr. Gilkes. Counsel took Gino Arconti through the new forms created by David Gilkes that were attached to the May 2009 Letter and sent to Staff. Gino Arconti felt that NAFG responded to Staff's list of deficiencies. There followed a lot of back and forth communications between David Gilkes and Staff, which lasted seven months.

[190] Gino Arconti then learned of the 2010 Compliance Review that was to take place in January 2010 from Flavio Arconti, who received a call from Anita Chung. Flavio Arconti took the lead role in responding to Staff's requirements. Mr. Gilkes was again hired to help out with the second compliance review; he was involved in ensuring that everything that Staff was asking for was provided.

[191] In reviewing various documents prepared and submitted to Staff, Gino Arconti confirmed that he understood that: they did not have to provide a prospectus to investors, since Carter was in the exempt market; they were not required to provide financial information to investors; investors were told that the investments were high-risk investments; and, when soliciting

investments with potential investors, he always discussed the Certificate of Accredited Investor with them.

[192] Counsel referred Gino Arconti to a conference call that was held with himself, Flavio Arconti, Margaretha Widjojo and various members of Staff on March 23, 2010. Staff raised the propriety of identifying collectability of outstanding accounts. Gino Arconti disclaimed any understanding of how a proper "Allowance for Doubtful Accounts" should be set up, and stated that Ms. Widjojo, who was NAFG and Carter's accountant at the time, was responsible for that.

[193] Gino Arconti confirmed that there was never any effort to hide NAFG's relationship with Prestige Motors. He said there was nothing wrong with the loans made by NAFG to Prestige Motors.

[194] Gino Arconti's attention was drawn to Ex. 18, Tab J, p. 37, an income statement showing a net loss of $524,727 for 2008. Mr. Arconti testified that the loss for the year 2008 was severe, but that it was manageable. The larger net loss for the year 2010 of over $1.3 million was ascribed to "the regulatory issues that we were dealing with and we weren't really focused so much with the business" (Tr. Vol. 10, p. 57, ll. 9-17). It was about this time that the Arcontis hired Stefano Picone, a chartered accountant who analyzed the accounts of both NAFG and Prestige Motors in order to make them profitable.

[195] Counsel turned Mr. Arconti to consider the telephone call made by Amy Tse, posing as an investor named "Amy Thorne", on June 9, 2010. Gino Arconti stated that he had no recollection of the telephone call. I would give Gino Arconti a passing mark for the responses he made to the questions asked by Ms. Tse, save for the claim that NAFG was competing with TD Bank and Scotia. His answers to questions about Ms. Tse's call employed the use of the words "I would have", indicating that he did not recall specifically what was said, but rather described what he said in his usual discussions with investors.

[196] Gino Arconti was asked about the investor J.B., whose documents are found in Ex. 12. Mr. Arconti denied telling J.B. that the issue of whether or not he was an accredited investor was just a formality. He also denied ever telling any investor that. At Tab D of Ex. 12 is a Carter KYC form, which was completed by Gino Arconti, save for the first line of the form and J.B.'s signatures and initials. Gino Arconti said that he asked J.B. the questions in the form. J.B. provided his answers, which were then recorded by Gino Arconti into the form. He had no doubt that J.B. understood what was required to be an accredited investor. Mr. Arconti could not recall what J.B. said specifically but "we would have had a discussion" about whether or not he was an accredited investor (Tr. Vol. 10, p. 78, ll. 12-20). Then followed a series of questions that were answered by Mr. Arconti with "I would have". Once again, Mr. Arconti denied telling J.B. that signing as an accredited investor was just a formality.

[197] Mr. Arconti then recounted the efforts he made to persuade J.B. to change his investment to the NAFG convertible debenture, which had an annual interest rate of 5%. J.B. refused to accept anything less than 15%. Gino Arconti was then asked how successful the effort was by NAFG to get investors to change from the higher to the lower interest rate. At the time the Arcontis were working with investors to convert their investments, $5 million of investor funds were tied to investments with the higher interest rate. In September 2010, $2 million of those

funds were converted to investments with the lower inter payments at 5% (Tr. Vol. 10, p. 91, l. 25; p. 92, ll. 1-7).

[198] Counsel then turned to the investor L.F., whose documents are found in Ex. 13. Gino Arconti identified the writing in the document to be his own, except for the signature of L.F. (Ex. 13, Tab A). Nevertheless, Mr. Arconti confirmed that L.F. supplied the answers to the questions asked in the document. Mr. Arconti filled out the form in a telephone conversation with L.F., who was in Sudbury, Ontario at the time. He recalls speaking to L.F. Although he tried to persuade L.F. to invest in the convertible debenture at an annual interest rate of 5%, L.F. entered into the loan agreement at an annual interest rate of 12%. Gino Arconti explained this by saying that if an investor wanted the higher interest rate, NAFG would provide it. The document discloses that the proceeds of the offering would be primarily used to provide financing for the daily operations of NAFG and its affiliates, including Prestige Motors. When asked if this was discussed with L.F., Mr. Arconti replied "he actually knew that we were involved with Prestige Motors. We had some discussions about that" (Tr. Vol. 10, p. 98, ll. 3-16).

[199] Mr. Arconti was then asked about investor J.S., whose documents are found in Ex. 14. Mr. Arconti was referred to the New Client Application Form, which was filled out by J.S. and Flavio Arconti (Ex. 14, Tab C). Gino Arconti signed the document on behalf of Carter after it was completed. At the time J.S. signed the New Client Application Form on January 23, 2010, J.S. had already entered into a loan agreement on April 1, 2008 (Ex. 14, Tab A). J.S. signed the form as a result of the 2009 Compliance Review to update the Carter's KYC forms, as well as an effort to respond to Staff's list of deficiencies by contacting all investors. He denied NAFG targeted elderly investors.

[200] Counsel also questioned Gino Arconti about investor R.B., whose documents are found in Ex. 15. R.B.'s documents do not include a New Client Application form or a KYC form. Mr. Arconti had looked for those documents, but was unable to find them. However, he was confident that a KYC was prepared "because that is what I do" (Tr. Vol. 10, p. 106, ll. 13-17). R.B. received a marketing brochure, which contained information describing the investment as "an attractive safe high yield income-generating investment for the investor" (Ex. 15, Tab A). Gino Arconti testified this is the first time he had seen this actual page and said the brochure was not widely distributed. The language in this brochure was not approved by NAFG. In fact, Mr. Arconti told R.B., as he did all investors, that the investment was a high-risk investment, and that, if NAFG were to go bankrupt, all the money of the investment would be lost.

[201] Subsequent to the distribution of the brochure, a meeting was held at R.B.'s residence to see if he would agree to lower the interest rate of his investment to 5%. R.B. refused to do so. Gino Arconti denied that R.B. asked if NAFG was insolvent or whether there were OSC proceedings against it.

[202] Counsel then referred Gino Arconti to investor D.M., whose documents made be found in Ex. 16. D.M. was referred to NAFG by his accountant, who had invested with NAFG for some time. The accountant was an accredited investor. In the Joint Client Application Form, D.M. indicated that he had liquid assets of $1 million and an estimated net worth of $2 million (Ex. 16, Tab B). The $2 million figure looks as though it was altered from a previous number. Mr. Arconti denied that he or his brother altered the number and that it would have been D.M. who

did so. Gino Arconti denied telling D.M. that it was unimportant what the numbers were or that he be an accredited investor. Mr. Arconti also denied telling D.M. that NAFG would be going public.

[203] Counsel then asked Gino Arconti which individuals were responsible for depositing cheques that came into NAFG. Mr. Arconti identified himself, his brother, Ms. Widjojo and Julia, the office administrator. He was also referred to the deposit account history for Account 652 (Ex. 10, Tab 1, pp. 706-707). Three deposits were singled out and brought to Mr. Arconti's attention: $39,720, $50,000 and $22,000.

[204] The first deposit of $39,720 was made at 1:08 p.m. on September 23, 2010 (Ex. 10, Tab 1, p. 706). The Director's Decision suspending Carter's registration was issued on September 22, 2010. The Director's Decision was delivered to the Respondents by mail, and a waybill establishes notice on Carter and Flavio Arconti at about 3:39 p.m. on September 23, 2010 (Ex. 4, Tab 46). Gino Arconti denied knowing of the Director's Decision at 1:08 p.m. on September 23, 2010, which is when the $39,720 was deposited. Independent evidence, found at Ex. 4, Tabs 45 and 46, confirms this to be so.

[205] Counsel next referred to the deposit for $50,000, which were funds provided by D.M. Gino Arconti deposited the funds, and he acknowledged that he knew of Carter's Suspension at the time he made the deposit. Staff also referred to an email chain dated September 24, 2010, where Gino Arconti asked D.M. if he can put D.M.'s cheque through and D.M. provided an affirmative response (Ex. 16, Tab F). Gino Arconti explained the making of the deposit by saying he understood that Carter's Suspension had no legal impact on NAFG. He thought that NAFG was able to continue operating and that depositing D.M.'s cheque was something that was "all right" to do (Tr. Vol. 10, p. 135, ll. 13-16). Mr. Arconti noted that D.M.'s investment was negotiated before the suspension, and confirmed that after the Director's Decision he did not solicit any new investment through Carter.

[206] The third deposit for $22,000 was a sum related to L.F.'s investment. In the account history of Account 652 (Ex. 10, Tab 1, p. 705), the deposit was entered on Monday, September 27, 2010, but Gino Arconti suggested it could have been deposited at any time over the weekend at a bank machine. In any event, Mr. Arconti regarded L.F.'s deposit as similar to that of D.M.'s cheque, in that the deposit was made to finalize an agreement that was negotiated and signed before Carter's Suspension.

[207] Gino Arconti was directed to Ex. 10, Tab 1, p. 720, showing a bank draft drawn in the name of M.G. for $116,853.41, which was dated and cashed in on September 28, 2010. Exhibits 27 and 28 show agreements between NAFG and M.G. that were effective as of July 1, 2010 and replaced earlier loan agreements between the two parties. M.G. had called Gino Arconti and asked for the return of her investment, because she wanted to buy a cottage. The last payment was to be made on September 4, 2010, but it was not paid out at that time since NAFG was "extremely busy" during the month of September (Tr. Vol. 10, p. 144, ll. 1-10). The Arcontis were dealing with the convertible debentures, the OSC proceedings, HDL and the death of Flavio Arconti's father-in-law. M.G. reminded Gino Arconti that she wanted her investment back at the funeral of Flavio Arconti's father-in-law, which took place in mid or late September 2010. Gino Arconti directed the draft be prepared, signed and delivered to M.G.

[208] The effect of the two agreements was that the principal amounts originally to be repaid on December 4, 2014 were paid on September 4, 2010 (Ex. 3, Tab 43). M.G. escaped the 50% loss of principal experienced by other, less fortunate, investors who approved the bankruptcy proposal under the *BIA*.

[209] Counsel asked why it was necessary to file a notice of proposal under the *BIA* for NAFG. Gino Arconti explained that they had lost Carter by way of suspension, HDL had terminated their agreement to look for capital investments and the damage to their reputation made it impossible to continue to raise funds. That concluded the examination-in-chief.

[210] Counsel began the cross-examination of Gino Arconti by referring him to Ex. 11, Tab 2, containing the financial statements for NAFG as at September 30, 2010. In referring to years 2007, 2008 and 2009, Mr. Arconti confirmed that he was aware of the accumulating deficits of NAFG. Counsel had less success with obtaining Mr. Arconti's views on the long-term portion of lease receivables and it was apparent to me that he did not have a complete understanding of what the figures meant. Gino Arconti did agree that Prestige Motors kept the money from the sale of repossessed cars instead of transferring it to NAFG, thus increasing the amount of the "loan" during the fiscal years 2007, 2008 and 2009. Mr. Arconti confirmed that no interest was paid on the loan.

[211] Counsel then read long excerpts from the policies and procedures manual of Carter dated November 2007 (Ex. 2, Tab 7). Counsel asked Gino Arconti if he understood his obligations under the various sections of the manual and he agreed that he did.

[212] Counsel then referred Mr. Arconti to the 2009 Deficiency Report (Ex. 2, Tab 11). Mr. Arconti agreed with the response to the May 2009 Letter, which was prepared by David Gilkes (Ex. 2, Tab 12). There then followed a cross-examination on matters of little assistance to me culminating in Mr. Arconti's agreement that the trial balance as of December 31, 2009 showed an owing balance to Prestige Motors from NAFG of almost $2 million, and that the total for long-term receivables at December 31, 2009 was $1,780,226.14 (Ex. 2, Tab 28, pp. 450-453). I found that Mr. Arconti's answers to the straightforward questions asked by Staff during this period were unresponsive and evasive.

[213] The cross-examination of Gino Arconti continued the next day on May 23, 2013. Counsel obtained agreement from him that he would have known by early March 2010 that the total revenue generated by NAFG was not enough to pay the interest owed to its investors. It was put to him that NAFG needed new investor money in order to pay interest to existing investors. Mr. Arconti replied that he would not say they had to rely solely on new investor money. Counsel put it to Mr. Arconti that he knew very well what the financial situation of the company was in March 2010. Mr. Arconti responded with an answer that was repeated more than once during the cross-examination of Staff that day:

> Q. I put it to you, sir, that you knew very well what your financial situation was at the time. You are the co-owner of the company?
>
> A. Correct. There were losses, but I believe 2009 was less than 2008. And in this period of time, it was a major recession. We suffered. We knew that we were

> going to be putting a plan in place to repair all of this. It was repairable. We didn't believe it was severe like the OSC staff has suggested. We believed that it was manageable. We believed that this could have been corrected and there were a lot of companies that suffered at the time far worse than what we did and they were able to recover and get back to business.
>
> (Tr. Vol. 11, p. 11, ll. 9-24)

[214] From this point on, Gino Arconti's answers to questions became less and less responsive. Examples can be found in Tr. Vol. 11 at p. 23, ll. 15-25; p. 24, ll. 1-8, 15-25; and p. 25, ll. 1-3, 14-23.

[215] Gino Arconti confirmed to counsel that he transferred ownership of his house, which was in his name and his wife's name, into his wife's name alone on May 5, 2010. He explained that he did this because NAFG was sued as a result of an accident involving a lease customer, who was a third party. NAFG was named because of its ownership of the vehicle. Mr. Arconti said that when the action came about, he and his wife started to learn about what their liabilities were, and his wife learned of another settlement for $13 million. After his wife spoke to a friend, who was a lawyer, she asked Mr. Arconti to have the house transferred to her name alone. The house had no equity and was completely mortgaged right up to the purchase price. He denied he did the transfer because he was worried about the financial situation of NAFG and the possibility of being sued in relation to NAFG.

[216] At this point, Staff counsel, no doubt frustrated by Mr. Arconti's evasive answers, started to interrupt the witness while he attempted to respond to questions. Examples include Tr. Vol. 11, p. 29, ll. 7-11; p. 37, ll. 20-24; p. 49, ll. 1-25; and p. 62, ll. 14-20.

[217] At the morning recess following another long response from Gino Arconti, I made the following comment:

> Commissioner Carnwath: I think we will take 15 minutes. This will give you an opportunity to speak to your counsel. Counsel, you will have an opportunity to explain to the witness what I think I explained to his brother in terms of sticking to the question and trying to give the answer. That will give you that chance. I don't think it is necessary for me to give my speech again. I think you are quite capable of doing it. 15 minutes.
>
> (Tr. Vol. 11, p. 63, ll. 19-25; p. 64, ll. 1-3)

[218] Counsel then took Gino Arconti through the June 2010 Letter, regarding Staff's recommendation to the Director that Carter's registration be suspended (Ex. 4, Tab 39). Staff then read a series of excerpts from the letter and asked if Mr. Arconti understood the excerpts. He qualified his answer by saying he understood that was Staff's view at the time. Gino Arconti did not agree that NAFG was in serious financial difficulty. He and Flavio Arconti believed that the difficulties were manageable and repairable.

[219] Staff then asked questions about J.S.'s investment and Gino Arconti confirmed that he did not tell J.S. that NAFG had a cumulative deficit of $1.2 million at the time or that over 90%

of its receivables were in the "91+" day default category. Mr. Arconti also confirmed that he did not tell J.S. that Prestige Motors owed NAFG $2 million. However, he said J.S. understood that funds of the companies could be used for all of the companies related to NAFG. The Arcontis did not believe that the $2 million owed by Prestige Motors was a true loan, but rather thought that it was a receivable balance that was going to be repaid.

[220] The same questions were asked of Mr. Arconti's meetings with D.M. Similar to J.S., Gino Arconti did not tell D.M. that NAFG had an accumulative operating deficit of $1.2 million when they met or did he tell him that over 90% of NAFG's receivables were in the "91+" day default category.

[221] Gino Arconti agreed with counsel's suggestion that HDL was not told about the issues that NAFG had with the Commission until after Carter's Suspension. It was put to him that if HDL had been told about the suspension, the Arconti brothers were concerned that HDL would not want to deal with them. Gino Arconti did not agree with that statement. It was further put to him that investors like L.F. and J.S. would not have invested if they had known of NAFG's financial circumstances in the fall of 2010. Again, Mr. Arconti disagreed.

[222] Gino Arconti confirmed that it was his signature on the cheque that was made out to M.G., dated September 28, 2010 (Ex. 10, Tab 1, p. 719). He also confirmed that it was his signature on the deposit slip for $50,000 for the cheque, which was written from the account of D.M.'s company (Ex. 10, Tab 1, p. 714).

[223] It was put to Mr. Arconti that his cousin M.G. was being paid approximately $116,000, which was, in part, D.M. and L.F.'s money. Gino Arconti replied "if we look at this way and you want to interpret it that way, yes" (Tr. Vol. 11, p. 100, ll. 9-14).

[224] It was put to Gino Arconti that on September 28, 2010 when he obtained the bank draft to be paid to his cousin, he would have known that NAFG was insolvent as of that date. Gino Arconti disagreed. Mr. Arconti explained that at that point, HDL was still in the picture and that they had not received any calls from investors yet. Those calls started coming in after the Commission sent letters notifying investors about the Director's Decision (Tr. Vol. 11, p. 104, ll. 15-25; p. 105, ll. 1-8). Those letters, to Mr. Arconti's understanding, made the investors panic and, in order to get some sort of orderly control, they went to see Farber, NAFG's trustee in bankruptcy. Gino Arconti was also referred to the unaudited balance sheet of NAFG as of December 31, 2010 (Ex. 11, Tab 2-2, p. 463). After comparing the financial statements of 2007 and 2008 with the financial statements for 2009 and 2010, Mr. Arconti agreed that loans to the shareholders of NAFG (i.e. the Arcontis and their companies) began in 2009 and continued in 2010.

[225] Gino Arconti was referred to a document prepared by Mr. Tillie at Ex. 18, Tab F. Mr. Arconti confirmed that he and his brother were receiving payments on their use of credit cards for business expenses. From January 2, 2009 until September 28, 2010 the credit card usage totalled $502,318.27. Mr. Arconti thought that a lot of that sum had to do with business expenses, but stated that it was up to Ms. Widjojo to allocate how to account for business and personal expenses.

[226] It was put to Gino Arconti that Prestige Motors would not have been in a position to repay the $2.3 million as of November 30, 2010 to NAFG. Mr. Arconti said there was no cash in the bank to do that, but they would be able to pay the loan if they sought financing, which they felt was attainable. There then followed a string of long responses to further questions from Staff that repeated a theme often visited during Mr. Arconti's evidence: "Prestige Motors was in a good position to continue its business. We were forced to close it" (Tr. Vol. 11, p. 117, ll. 5-7). This response was expanded on Mr. Arconti's answers found at Tr. Vol. 11, p. 118, ll. 1-25; p. 119, ll. 1-25; and p. 120, ll. 1-5.

[227] Gino Arconti agreed that NAFG's proposal in bankruptcy enabled the Arconti brothers to continue to run NAFG and to receive management salaries. In re-examination by Mr. Smith, Mr. Arconti confirmed that the payments through Ceridian were not all going to the Arconti brothers, but to other staff members of NAFG as well. That concluded Gino Arconti's evidence.

C. Stefano Picone

[228] Mr. Picone has a Bachelor of Commerce degree from the University of Toronto, which he received in 2004. He became a chartered accountant in the fall of 2009 and in May 2010 he started doing work for NAFG. His evidence may be found in Tr. Vol. 9, pp. 7-60.

[229] The Arcontis told Mr. Picone that they needed someone with financial expertise to assist with modeling and financial planning. The Arcontis wanted to restructure and grow their businesses. The businesses were not profitable at the time, but there was, according to Mr. Picone, "nothing beyond remediation" (Tr. Vol. 9, p. 10, ll. 18-20).

[230] Mr. Picone started on a part-time consulting basis between 25 and 30 hours per week. At first, he was heavily engaged in examining the operations of Prestige Motors and NAFG to examine the cause of the financial difficulties. He referred to the difficult economic times that existed in the spring of 2009, both in the credit and automotive sectors. A plan was created to switch Prestige Motors to a consignment sales model, to reduce its overhead and to put Gino Arconti in charge of the service department on a full-time basis. For NAFG, the plan was to reduce its cost of capital by having existing noteholders convert their investments to low-interest convertible debt instruments. The plan also contemplated getting access to more capital by going public in order to get access to an institutional debt line. Mr. Picone confirmed that he was not involved in any effort to persuade existing investors to convert their high-yield notes to a lower interest rate model.

[231] Mr. Picone described his interaction with HDL who, he said, was "very enthusiastic about bringing this company public" (Tr. Vol. 9, p. 22, ll. 11-14). Mr. Picone produced a number of financial models for HDL.

[232] Mr. Picone confirmed that the various plans for reviving NAFG and Prestige Motors failed when the OSC suspended Carter's registration. Nevertheless, he felt NAFG's issues could still be resolved. His primary responsibility was to liaise with NAFG's trustee in bankruptcy, Farber, and provide it with the necessary accounting information. At this point in his evidence, I formed the opinion that Mr. Picone had drunk from the same well of optimism as the Arcontis.

[233] In cross-examination, Mr. Picone confirmed that he had no interaction with the investors until the bankruptcy proposal period, when he advised them of their options. Mr. Picone was asked about a cash-flow projection he prepared with Farber for the Trustee's Report to the Creditors, dated January 7, 2011. The Report indicates that over three years, a surplus cash flow of $322,000 was projected (Ex. 19, Tab 6, pp. 84-85). Mr. Picone's attention was also drawn to the unaudited operating losses of the two companies over the years 2008, 2009 and for the eleven-month period to November 30, 2010, which was $2.239 million for NAFG and $2.991 million for Prestige Motors (Ex. 19, Tab 6, p. 78). Mr. Picone also confirmed that as at the date of Carter's Suspension, Prestige Motors was not in a position to pay the money borrowed from NAFG but "going forward we had identified a plan to do so" (Tr. Vol. 9, p. 32, ll.5-9). The plan was for Prestige Motors to be self-sufficient, but neither of the Arcontis were able to spend the necessary time to run the business. He repeated his earlier testimony that problems of NAFG and Prestige Motors were not beyond remediation.

[234] Mr. Picone was asked a series of questions and the answers to which established that when arriving at a projected cash flow model, he did not take into account his fees, the fees of the trustee in bankruptcy, Farber, or the management fees paid to the Arcontis. This answer does not inspire confidence in his evidence.

[235] I do not accept Mr. Picone's evidence that NAFG and Prestige Motors could be rescued. Whether through lack of experience, his wish to encourage the Arcontis or through a refusal to recognize that the two companies had operating losses of over $2.5 million, his optimism was not supported by the facts. This compels me to reject his evidence on this point.

D. David Gilkes

[236] David Gilkes has a Bachelor of Arts in Economics from McMaster University and a Master's degree from Carleton University. His evidence may be found in Tr. Vol. 9, pp. 102-161.

[237] Mr. Gilkes is a certified fraud examiner. Since May 2011, he has been the president of North Star Compliance & Regulatory Solutions Inc., a firm that helps investment companies that are in the investment industry. Before that time, he was employed with Sutton, Boyce, Gilkes Regulatory Consulting Group, which was also engaged in helping companies in the investment industry, for two years. From January 2002 until December 2008, he was the manager of Registrant Regulation with the Commission. During that time, he led the team for the OSC that drafted NI 31-103.

[238] Cassels Brock referred the Arcontis to Mr. Gilkes for his help in dealing with the 2009 Compliance Review. Staff had identified issues and the Arcontis wanted help to become compliant, resolve the issues and continue to operate their companies in a compliant manner. The two significant deficiencies identified by Staff were lack of KYC and suitability procedures, that is, the determination if prospectus exemptions were available.

[239] Counsel referred Mr. Gilkes to the May 2009 Letter, which was drafted by Mr. Gilkes and sent by Flavio Arconti to Staff (Ex. 2, Tab 12). The letter lays out the proposed actions to be taken by Carter and NAFG, which included contacting investors to collect more KYC

information than had previously been collected by the companies. The letter also referred to new forms that were created to determine whether or not a person was an accredited investor. Mr. Gilkes continued to work with Carter and with the Arcontis to help them implement new policies, new procedures and to address what issues needed to be corrected. Between May and November 2009, this entailed many discussions with the Arcontis and with the OSC. He described the relationship with the OSC as a good one, where both sides were working well together.

[240] Between December 25, 2008 and January 1, 2009, Carter received a letter requiring a full compliance review by the OSC, the 2010 Compliance Review. Mr. Gilkes continued to work with the Arcontis to revise their policies and procedures and to inform them how to cooperate fully with the OSC. The OSC visited Carter's premises and were there for approximately four weeks. This had a demonstrable effect on the Arcontis' ability to carry on their businesses.

[241] Mr. Gilkes believed that following its full compliance review in 2010, Staff would issue a Compliance Field Review Report that would identify deficiencies that needed correction. He believed there was a tacit understanding with Staff that this would be the course of action. However, no deficiency report was supplied to Carter. Instead, Mr. Gilkes learned that the Arcontis received a letter saying that Staff was recommending Carter's suspension to the Director. Mr. Gilkes prepared a letter to the Commission, the June 2010 Letter, requesting an OTBH. He was deeply involved in preparing for the hearing before the Director. Mr. Gilkes confirmed that up until that time, all he knew about the state of NAFG and Carter was that their business was a going concern. He said that he first knew of the level of difficulty that NAFG was in, in terms of its financial situation, from the June 2010 Letter.

[242] Mr. Smith then reviewed with Mr. Gilkes a number of documents, which he prepared for NAFG and which were designed to improve the disclosure provided to investors, regarding the type of product that they would be investing in the period leading up to the Director's Decision. He described this as a work in progress in attempting to meet Staff's concerns.

[243] Mr. Gilkes was involved in the preparation of and attending the OTBH. He was hoping that the Arcontis were going to be able to convince the Director that a more appropriate solution would have been imposing terms and conditions, rather than a suspension. He was surprised to learn that the Director imposed the suspension of Carter's registration.

[244] In cross-examination, Mr. Gilkes was referred to the letter of engagement between HDL and the Arcontis dated September 2, 2010. Mr. Gilkes was not providing NAFG with advice on raising capital.

[245] Staff referred Mr. Gilkes once again to the May 2009 Letter that Carter sent to the OSC. Mr. Gilkes reviewed Carter's policies and procedures manual, which was updated in May 2009, with the Arcontis. Mr. Gilkes said that in his dealings with the Arcontis, he never formed the impression that they did not understand what their obligations were under the manual. He further understood that the Arcontis were going to treat their communications with the public on the basis of truthfulness and fair dealing. He then confirmed that he was never present during the Arcontis' meetings with investors. That concluded the significant portions of the cross-examination of Mr. Gilkes. There was no re-examination by Mr. Smith.

E. C.S.

[246] C.S. is 69 years old and a retired professor of mathematics. He read an ad in the *Toronto Star* and invested in the NAFG group of companies. He arranged a meeting with the Arcontis and had a tour of the operation. His evidence may be found in Tr. Vol. 9, pp. 60-86 and the documents introduced during his testimony may be found in Ex. 23.

[247] C.S. first invested $20,000 and subsequently made a series of investments culminating in a total sum of $130,000. On September 1, 2010 C.S. applied the principal from his loan agreements towards subscription proceeds for convertible debentures of NAFG in the principal amount of $130,000 (Ex. 23, Tab 14). C.S. and his wife signed a "Direction", and this Direction attached loan agreements under "Schedule '1" (Ex. 23, Tab 14, p. 260). I note that there is no Schedule '1' found anywhere in Ex. 23, Tab 14.

[248] C.S. made it clear that he knew the risk involved in his investments with NAFG, that he received interest payments on his loans and that he was an accredited investor. He confirmed that he and his wife signed the documents in Ex. 23, Tab 14, following a conversation with the Arcontis, who wished to reduce their interest expenses. He acknowledged that the information contained in the documents he received over the years expanded on the documents at the beginning of his relationship.

[249] My difficulty with the evidence of C.S. is that neither Staff nor Mr. Smith asked him whether he received all his money back or whether he formed part of the investors in NAFG's bankruptcy proposal for creditors that lost 50% of their principal. He certainly displayed none of the disappointment of Staff's investor witnesses, who suffered the 50% reduction in their principal. By not knowing the result of his investment in NAFG, his evidence is of little assistance to me.

F. N.B.

[250] N.B. is 66 years old and farms near Oshawa, Ontario. His evidence may be found in Tr. Vol. 9, pp. 86-101. Documents connected with his evidence were entered as Ex. 24.

[251] N.B. purchased a convertible debenture from NAFG for $40,000 on September 1, 2010 (Ex. 24, Tab 3). A "Notice of Conversion" was also entered into on September 1, 2010, which, at the option of N.B., converted his units in NAFG on the basis of one unit for each $0.25 of the $40,000 invested. As with C.S., I can find no evidence that deals with the question of whether his investment has been reduced by 50%, according to the terms of the bankruptcy arrangement with creditors. His evidence is of little assistance to me.

PART 4 – THE APPLICABLE LAW AND ANALYSIS

A. The Standard of Proof

[252] The standard of proof which must be met by Staff in a section 127 proceeding under the *Act* is the civil standard of the balance of probabilities (*Re Sunwide Finance Inc.* (2009), 32 O.S.C.B. 4671 ("***Sunwide***") at para. 28).

[253] The Supreme Court of Canada has made it clear that there is only one civil standard of proof for all allegations regardless of the seriousness of the allegations or consequences at issue. That standard requires a proof on a balance of probabilities. On this standard, a trier of fact must decide "whether it is more likely than not" (*F.H. v. MacDougall*, [2008] 3 S.C.R. 41 at paras. 26-40 ("***MacDougall***")).

[254] The Supreme Court of Canada's decision in *MacDougall* has been applied by the Commission in considering the standard of proof applicable to administrative proceedings (*Sunwide*, above at paras. 26-28).

B. The Admissibility of Hearsay Evidence

[255] Some of the evidence introduced at the Hearing was in the nature of hearsay evidence. Subsection 15(1) of the *Statutory Powers Procedure Act*, R.S.O. 1990, c. S.22, as amended (the "***SPPA***") governs the use of hearsay evidence in Commission proceedings:

> **15(1)** Subject to subsections (2) and (3), a tribunal may admit as evidence at a hearing, whether or not given or proven under oath or affirmation or admissible as evidence in court,
>
> (a) any oral testimony; and
>
> (b) any document or other thing,
>
> relevant to the subject-matter of the proceeding and may act on such evidence, but the tribunal may exclude anything unduly repetitious.

[256] Although hearsay evidence is admissible under the *SPPA*, the Commission must determine the appropriate weight to be given to that evidence. In making an assessment as to appropriate weight, the Commission can consider whether documentary evidence adduced by Staff is corroborated or consistent with other documentary evidence (*Sunwide*, above at para. 22).

[257] The documentary evidence that was introduced by the parties at the Hearing corroborated and was consistent with the hearsay evidence in this matter. I therefore am of the view that admitting the hearsay evidence does not undermine the requirement for procedural fairness to the Respondents (*Sunwide*, above at para. 25).

C. Assessment of Credibility Principles and Analysis

[258] An assessment of a witness' credibility refers to the process undertaken by the trier of fact to assess the trustworthiness or believability of the witness' testimony. This process will involve:

(a) as assessment of the general integrity, powers of observation, capacity to remember and accuracy of statements of the witness;

(b) the extent to which the witness' evidence is internally consistent;

(c) the extent to which the witness' evidence is consistent with other proven or undisputed facts; and

(d) in the rarest of cases, the demeanour of the witness.

(CED, (Ont 4th), Vol. 31, Title 82 at § 126)

[259] Investor witnesses described their interactions with the Arconti brothers leading up to, and after, their investment with NAFG. The Arcontis flatly denied several statements made by the investor witnesses. The situation requires me to engage in an assessment of the relative credibility of the two sides, while always remembering that both the investors and the Arcontis may be found not to be credible.

[260] Investor J.B. testified that Flavio Arconti told him that, in order to invest, he had to sign papers showing that he had net assets of over $1 million, which he did not have. Mr. Arconti told him that it was a "formality" (Tr. Vol. 3, p. 15, ll. 21-23). He repeated this evidence in cross-examination (Tr. Vol. 3, p. 78, ll. 11-13).

[261] Investor J.S. signed documents indicating he was an accredited investor. He did not know that he had to exclude his real estate; if he had, his net worth was less than $1 million (Tr. Vol. 3, p. 149, ll. 10-12; p. 161, ll. 20-23). There is no evidence that Gino Arconti made any inquiry into the financial situation of J.S.

[262] R.B. testified that when he first invested with NAFG, he thought an accredited investor was someone who had good credit. The documents for his first investment were prepared by NAFG, sent to him for signature and signed. At no time did Flavio Arconti discuss R.B.'s financial circumstances regarding the accredited investor requirements. In his first conversation with Flavio Arconti, R.B. asked if NAFG was insolvent and if it was under investigation by the OSC. When he was asked to convert to a debenture, he asked the same questions. R.B. said that on both occasions, the Arcontis denied NAFG was insolvent or under investigation.

[263] D.M. testified that he signed his debenture application on September 18, 2010, although it is dated September 20, 2010. His total assets came to approximately $700,000. He indicated on his Joint Client Application form that his net worth was $2 million and explained that Gino or Flavio Arconti told him "that's the profile I had to put in order to be -- in order to participate in the offering" (Tr. Vol. 4, p. 75, ll. 5-16).

[264] Investor witnesses called by Staff did not display any *animus* towards the Arcontis that caused me to suspect they were fabricating their evidence. On the contrary, they seemed to be trying as best they could to recall the events of almost three years ago.

[265] As indicated earlier, I found the evidence of both Arcontis to be evasive and unresponsive. Questions that called for a simple, direct answer were deflected and used as a platform to extol their confidence in their business plans of Carter and NAFG. In doing so, their refusal to acknowledge their lamentable financial circumstances indicated a tenuous, if not non-existent, grasp on commercial reality.

[266] In several instances, both Arcontis describe what they "would have" done. This indicates a lack of specific memory coupled with an intention to justify their failures to inform or inquire about their companies' financial situations. Having dealt with numerous investors, they had less reason to recall their interaction with individual investors. The latter are more likely to have a better recollection of events, given their financial loss.

[267] Independent evidence of Mr. Tillie confirms the financial disarray of NAFG, thus putting considerable pressure on the Arcontis to obtain new and further investments at all costs. In many instances, documents were prepared by NAFG and submitted to investors for signature with no apparent attempt to be satisfied that the investors met, or continued to meet, the definition of an accredited investor.

[268] The Arcontis have admitted that the existence of the Prestige Motor's loan and NAFG's financial position were not disclosed to NAFG investors initially. They allege that "later" many investors were advised that NAFG was experiencing financial difficulty. However, the investors who were told of NAFG's financial difficulty were those who had already invested and who were asked to convert to a debenture at a lower interest rate.

[269] The foregoing state of affairs compels me to conclude that where the evidence of the Arcontis is in direct conflict with investor witnesses, I prefer the evidence of the latter. I am satisfied on the balance of probabilities that the evidence of the investor witnesses is reliable.

D. The Law of Suitability Obligations and Analysis

[270] Staff submit during the Applicable Period, Carter did not take reasonable steps to ensure that the purchase of NAFG securities was suitable for its clients, contrary to section 13.3 of NI 31-103.

[271] The Respondents concede that there were failures to identify certain investors who were not properly accredited, and, in this limited way, Carter violated its requirements under section 13.3 of NI 31-103. The Respondents also concede that Carter did not disclose to investors all negative information about NAFG that could or ought to have been disclosed.

[272] The relevant parts of section 13.3 of NI 31-103 state:

> **13.3 Suitability –** (1) A registrant must take reasonable steps to ensure that, before it makes a recommendation to or accepts an instruction from a client to buy or sell a security, or makes a purchase or sale of a security for a client's managed account, the purchase or sale is suitable for the client.
>
> (2) If a client instructs a registrant to buy, sell or hold a security and in the registrant's reasonable opinion following the instruction would not be suitable for the client, the registrant must inform the client of the registrant's opinion and must not buy or sell the security unless the client instructs the registrant to proceed nonetheless.
>
> (3) This section does not apply if the client is a registered firm, a Canadian financial institution or a Schedule III bank.

(4) This section does not apply to a registrant in respect of a permitted client if

(a) the permitted client has waived, in writing, the requirements under this section, and

(b) the registrant does not act as an adviser in respect of a managed account of the permitted client.

[273] The Commission has recognized that the KYC and suitability requirements "are an essential component of the consumer protection scheme of the *Act* and a basic obligation of a registrant, and a course of conduct by a registrant involving a failure to comply with them is an extremely serious matter" (*Re Daubney* (2008), 31 O.S.C.B. 4817 ("***Daubney***") at para. 15, citing *Re E.A. Manning Ltd.* (1995), 18 O.S.C.B. 5317).

[274] Canadian securities authorities have adopted a three-stage analysis of suitability, according to which a registrant is obliged to:

(a) use due diligence to know the product and know the client;

(b) apply sound professional judgement in establishing the suitability of the product for the client; and

(c) disclose the negative as well as the positive aspects of the proposed investment.

(*Daubney*, above at para. 17, citing *Re Foresight Capital Corp.*, 2007 BCSECCOM 101 (B.C. Securities Comm.))

[275] The Companion Policy to NI 31-103 also addresses the suitability rule, and states in part:

Subsection 13.3(1) requires registrants to take reasonable steps to ensure that a proposed trade is suitable for a client before making a recommendation or accepting instructions from the client. To meet this suitability obligation, registrants should have in-depth knowledge of all securities that they buy and sell for, or recommend to, their clients. This is often referred to as the "know your product" or KYP obligation.

Registrants should know each security well enough to understand and explain to their clients the security's risks, key features, and initial and ongoing costs and fees. Having the registered firm's approval for representatives to sell a product does not mean that the product will be suitable for all clients. Individual registrants must still determine the suitability of each transaction for every client.

Registrants should also be aware of, and act in compliance with, the terms of any exemption being relied on for the trade or distribution of the security.

In all cases, we expect registrants to be able to demonstrate a process for making suitability determinations that are appropriate in the circumstances.

(Companion Policy 31-103 CP - Registration Requirements, Exemptions and Ongoing Registrant Obligations, s. 13.3)

[276] CSA Staff Notice 33-315 provides a list of some factors that registrants should consider when assessing investment products for their clients, which include the issuers' financial position and history (*CSA Staff Notice 33-315 – Suitability Obligation and Know Your Product* (2009), 32 O.S.C.B. 6890).

[277] Investor witness J.B. made two investments in the Applicable Period, on December 1 and August 1, 2010 (Ex. 12, Tabs J and L). He testified that on all the loans he made to NAFG, one or the other of the Arcontis told him he could not make the investment unless he acknowledged that he was an accredited investor. I note that J.B. also signed a $40,000 debenture on September 1, 2010 (Ex. 12, Tab F).

[278] Investor J.S. made an investment of $10,000 during the Applicable Period, on September 22, 2010 (Ex. 14, Tab D). J.S. was the investor who told Gino Arconti that he was an accredited investor. He did so mistakenly believing he could include his real estate in making the calculation.

[279] Investor R.B. invested $84,500 in NAFG in March 2010 (Ex. 15, Tabs C and H). He indicated that he was an accredited investor on the form he signed, also mistakenly believing that he could include the value of his real estate in making the calculation. There was no discussion about the accredited investor requirement with Gino Arconti. The documents were sent to him in the mail, which he signed and returned.

[280] Investor D.M. invested in NAFG in September 2010. D.M. was told by one of the Arcontis that he had to have financial assets in excess of $1 million or he could not participate in the investment.

[281] The evidence of the above investors persuades me that the Arcontis made no attempt to investigate their investors' financial circumstances. In each instance, the question was asked by the Arcontis about their qualification as accredited investors. In each case, they received an affirmative answer and made no further inquiries about the actual circumstances of each individual investor. This in and of itself I find to be a breach of section 13.3 of NI 31-103. In addition, the analysis of the law on NI 31-103 outlined above makes it clear that the Arcontis were obliged to tell investors about NAFG's financial circumstances (*Daubney*, above, at para. 17).

[282] In addition, the Arcontis acknowledged in the Admissions of the Respondents that there was a loan from NAFG to Prestige Motors ultimately for $2 million (Ex. 1, para. 22). The Respondents also admit that NAFG was not profitable (Ex. 1, para. 22). It is also admitted that the existence of the loan in NAFG's financial position were not disclosed to NAFG investors initially. The Respondents submit that later disclosure better described the uses to which the investors' money was to be put. This is true. It was disclosed that the investment could be used by NAFG and its affiliates. That does not constitute disclosure of the difficulties in which NAFG found itself. The Respondents further submit that "many investors" were advised that NAFG was experiencing financial difficulties (Ex. 1, para. 22). My review of the evidence

persuades me that the only time investors were so advised was when they were being asked to convert their original investment to a lower paying debenture, because of NAFG's financial difficulties. That does not constitute disclosure at the time of the original investment made by investors. I find this failure to disclose NAFG's financial difficulties and its loan to Prestige Motors constitutes a breach of section 13.3 of NI 31-103.

[283] Moreover, the Respondents submit that they did not purposefully mislead investors. They submit that although they took serious efforts to obtain professional advice, the Arcontis did not understand their obligations to disclose to investors the negative financial information of NAFG or the loan to Prestige Motors. The Respondents also submit that this failure was due to either inadequate advice or that the Arcontis misunderstood the advice that was given to them. I agree with Staff's submission that it is not credible that the Arcontis did not understand their obligation to disclose significant investment risks to their investors. The evidence has shown that:

(a) Carter's own policies and procedures manual includes a "Client Suitability and Disclosure" section that requires that the company and each salesperson to disclose all material facts of the investment (Ex. 2, Tabs 7 and 26);

(b) during the 2009 Compliance Review, Staff sent a letter to Flavio Arconti on September 3, 2009 that referred to Carter's suitability obligations and directed Mr. Arconti to refer to CSA Staff Notice 33-315 (Ex. 2, Tab 14, p. 280);

(c) Flavio Arconti testified that he read Staff's letter when he received it (Tr. Vol. 7, p. 108, ll. 5-25; p. 109, l. 1);

(d) David Gilkes testified that he went through Carter's policies and procedures with the Arcontis and explained the documents to them, and he also testified that he always thought that the Arcontis understood their obligations (Tr. Vol. 9, p. 153, ll. 2-14; p. 154, ll. 3-8); and

(e) the Respondents concede that Carter did not disclose to investors all negative information about NAFG (particularly regarding the loan between NAFG and Prestige Motors and that the lease income of NAFG could not cover interest payments to investors), and that such information resulted in risks that should have been shared with prospective investors.

[284] I therefore find that during the period September 29, 2009 to September 24, 2010, Carter failed to take necessary steps to ensure that the purchase of NAFG securities was suitable for its clients, contrary to section 13.3 of NI 31-103 and contrary to the public interest.

E. The Duty to Act Fairly, Honestly and in Good Faith and Analysis

[285] Staff submit that from the time Carter was registered on September 17, 2007 to September 24, 2010, Carter failed to deal fairly, honestly and in good faith with its clients, contrary to subsection 2.1(1) of OSC Rule 31-505.

[286] The Respondents deny that Carter failed to act fairly, honestly or in good faith. However, in the Admissions of the Respondents, the Respondents admit that the disclosure made to investors was inadequate. They also admit that the Director made the findings that Carter failed to disclose the $2 million loan by NAFG to Prestige Motors, and that Carter failed to disclose the severe financial difficulties being faced by NAFG. Although they admit that the existence of the loan and NAFG's financial position were not disclosed to NAFG investors initially, later disclosure better described the uses to which the investors' money was to be put and many investors were advised that NAFG was experiencing financial difficulties. The Respondents also submit that the loan started out as a much smaller amount. They admit that NAFG was not profitable, but they do not admit that its financial difficulties were "severe", as characterized in the Director's Decision.

[287] Subsection 2.1(1) of OSC Rule 31-505 states: "A registered dealer or adviser shall deal fairly, honestly and in good faith with its clients"; and subsection 2.1(2) of OSC Rule 31-505 provides: "A representative of a registered dealer or a registered adviser shall deal fairly, honestly and in good faith with his or her clients".

[288] In *Re Norshield Asset Management (Canada) Ltd.* (2010), 33 O.S.C.B. 7171 at para. 79, the Commission said that: "The duty to deal fairly, honestly and in good faith goes to the heart of what securities regulation is about and a breach of this obligation is especially serious".

[289] Carter failed to disclose to its clients the interest-free loans granted to Prestige Motors by NAFG. The Respondents submit that the losses suffered by NAFG were "not severe" (Ex. 1, para. 22). I disagree. The losses were "severe", as submitted by Staff, or catastrophic, as I would describe them. In any event, the Arcontis were obliged to inform investors of the financial state of NAFG. In failing to do so, they failed to deal fairly, honestly and in good faith with its clients, contrary to subsection 2.1(1) of OSC Rule 31-505 by failing to disclose to its clients the interest-free loans it was granting to Prestige Motors and the severe financial difficulties being faced by NAFG from September 17, 2007 to September 24, 2010.

F. Director and Officer Liability – Carter

[290] Staff submit that Flavio Arconti and Gino Arconti, as actual and/or *de facto* officers and directors of Carter, authorized, permitted and/or acquiesced in the non-compliance with Ontario securities law by Carter and thereby were also not in compliance with section 13.3 of NI 31-103 and subsection 2.1(1) of OSC Rule 31-505, pursuant to section 129.2 of the *Act*.

[291] In their submissions, the Respondents concede that, to the extent Carter is found to have violated Ontario securities law, the Arcontis will also be found to have violated Ontario securities law. They admit that as actual and/or *de facto* officers and directors of Carter, the Arcontis are deemed to be liable for Carter's non-compliance with section 13.3 of NI 31-103, pursuant to section 129.2 of the *Act*. In relation to section 2.1 of OSC Rule 31-505, the Respondents deny that they acted contrary to this section, but they admit that the disclosure made to investors was inadequate (Ex. 1, para. 25).

[292] Section 129.2 of the *Act* provides:

> **129.2 Directors and officers –** 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.

[293] The threshold for a finding of liability against a director or officer under section 129.2 of the *Act* is low. Indeed, merely acquiescing in the conduct or activity in question will attract liability. As stated by the Commission in *Re Momentas Corp.* (2006), 29 O.S.C.B. 7407 ("***Momentas***"):

> Although these terms have been interpreted to include some form of knowledge or intention, the threshold for liability under section 122 and 129.2 is a low one, as merely acquiescing the conduct or activity in question will satisfy the requirement of liability. The degree of knowledge of intention found in each of the terms "authorize", "permit", and "acquiesce" varies significantly. "Acquiesce" means to agree or consent quietly without protest. "Permit" means to allow, consent, tolerate, give permission, particularly in writing. "Authorize" means to give official approval or permission, to give power or authority or to give justification.
>
> (*Momentas*, above at para. 118)

[294] A "director" is defined in subsection 1(1) of the *Act* as "a director of a company or an individual performing a similar function or occupying a similar position for any person". The term "officer" is also defined in subsection 1(1) of the *Act*, which provides:

> **"officer"**, with respect to an issuer or registrant, means,
>
> (a) a chair or vice-chair of the board of directors, a chief executive officer, a chief operating officer, a chief financial officer, a president, a vice-president, a secretary, an assistant secretary, a treasurer, an assistant treasurer and a general manager,
>
> (b) every individual who is designated as an officer under a by-law or similar authority of the registrant or issuer, and
>
> (c) every individual who performs functions similar to those normally performed by an individual referred to in clause (a) or (b)

[295] Therefore, a respondent who performs similar functions to an officer or director is considered a *de facto* officer or director and may be captured by the language of section 129.2 of the *Act* as a person who authorized, permitted or acquiesced to the non-compliance of Ontario securities law by the relevant person or company.

[296] Relevant factors, which have been identified for the determination of whether a representative was a *de facto* director or officer, include an individual who was:

(a) responsible for the supervision, direction, control and operation of the company;

(b) ran the company from their office;

(c) negotiated on behalf of the company;

(d) substantially reorganized and managed the company;

(e) selected the name of the company;

(f) made all significant business decisions; and

(g) formed part of the management of the company.

(*Momentas*, above at paras. 102, 103 and 106)

[297] Flavio Arconti and Gino Arconti were both directors, officers and shareholders of Carter. The Arcontis were also the co-owners of Carter (Ex. 2, Tabs 2, 3 and 5; Ex. 5, Tabs 3, 4, 6 and 7).

[298] The Arcontis were active participants in Carter's investment activities and authorized Carter's conduct. I find that Flavio Arconti and Gino Arconti, as actual and *de facto* directors and officers of Carter, are deemed to be liable for Carter's breaches of section 13.3 of NI 31-103 and subsection 2.1(1) of OSC Rule 31-505, pursuant to section 129.2 of the *Act*.

G. Securities Fraud and Analysis

[299] Staff submit that each of the Respondents directly or indirectly engaged or participated in acts, practices or courses of conduct relating to the securities of NAFG and NAC that they knew or reasonably ought to have known perpetrated a fraud on persons contrary to subsection 126.1(b) of the *Act* and contrary to the public interest.

[300] Staff alleges that the Respondents sold securities to investors promising interest, in the case of NAFG, and dividends, in the case of NAC, ranging from 10 to 15% and that they represented to investors that NAFG was a profitable and/or successful business when in fact, unbeknownst to investors, the Respondents used new NAFG and/or NAC investor money either in whole or in part to pay interest, dividends or principal to other NAC or NAFG investors.

[301] The Respondents deny that they acted contrary to subsection 126.1(b) of the *Act*. The Respondents offered and sold securities to investors promising interest rates of 12% to 15%, in the case of NAFG, and a 10% to 12% dividend rate, in the case of NAC. The Respondents note that some securities of NAFG also carried a 5% interest rate. The Respondents admit that some disclosure provided to investors may have had the effect of implying that NAFG was a profitable business, and that the returns to investors were funded, in part, by new investments made in NAFG and/or NAC (Ex. 1, paras. 28 and 29). The Respondents confirm that on October 15, 2010, less than one month after the Director's Decision suspending Carter's registration was

issued, NAFG filed a Notice of Intention to make a proposal under the *BIA* on the basis that it was an insolvent person, pursuant to subsection 50.4(1) of the *BIA*.

[302] Subsection 126.1(b) of the *Act* prohibits conduct relating to securities that a person or company knows or reasonably ought to know would perpetrate a fraud. Subsection 126.1(b) of the *Act* states:

> **126.1 Fraud and market manipulation –** A person or company shall not, directly or indirectly, engage or participate in any act, practice or course of conduct relating to securities…that the person or company knows or reasonably ought to know,
>
> …
>
> (b) perpetrates a fraud on any person or company.

[303] In previous decisions, this Commission has adopted the interpretation of the fraud provision in provincial securities legislation as set out by the British Columbia Court of Appeal in *Anderson v. British Columbia (Securities Commission)* (2004 B.C.C.A. 7 ("***Anderson***"); leave to appeal to the Supreme Court of Canada denied [2004], S.C.C.A. No. 81 (S.C.C.)). In *Anderson*, the British Columbia Court of Appeal held that the fraud provision in the British Columbia *Securities Act*, which is similar to the Ontario fraud provision, requires proof of the same elements of fraud as in a prosecution under the *Criminal Code*, R.S.C., 1985, c. C-46. The fraud provision in the *Act* merely broadens the ambit of liability to those who knew or reasonably ought to have known that a person or company engaged in conduct that perpetrated a fraud. The words "knows or reasonably ought to know" do not diminish the requirement of Staff to prove subjective knowledge of the facts concerning the dishonest act by someone accused of fraud *(Anderson*, above at para. 26).

[304] In previous decisions, this Commission has also referred to the legal test for fraud set out in the leading case of *R v. Théroux*, [1993] 2 S.C.R. 5 (S.C.C.) ("***Théroux***"). In *Théroux*, McLachlin J. (as she then was) summarized the elements of fraud:

> …the *actus reus* of the offence of fraud will be established by proof of:
>
> 1. the prohibited act, be it an act of deceit, a falsehood or some other fraudulent means; and
>
> 2. deprivation caused by the prohibited act, which may consist in actual loss or the placing of the victim's pecuniary interests at risk.
>
> Correspondingly, the *mens rea* of fraud is established by proof of:
>
> 1. subjective knowledge of the prohibited act; and
>
> 2. subjective knowledge that the prohibited act could have as a consequence the deprivation of another (which deprivation may consist of knowledge that the victim's pecuniary interest are put at risk).

(*Théroux*, above at para. 27)

[305] The act of fraud is established by two elements: a dishonest act and deprivation. The dishonest act is established by proof of deceit, falsehood or other fraudulent means. A dishonest act may be established by proof of "other fraudulent means". The phrase "other fraudulent means" encompasses all other means other than deceit or falsehood, which can properly be characterized as dishonest and is "determined objectively, by reference to what a reasonable person would consider to be a dishonest act" (*Théroux*, above at para. 17). The courts have included within the meaning of "other fraudulent means" the "use of corporate funds for personal purposes, non-disclosure of important facts, exploiting the weakness of another, unauthorized diversion of funds, and unauthorized arrogation of funds or property" (*Théroux*, above at para. 18). The use of investors' funds in an unauthorized manner has been determined to be "other fraudulent means" (*R. v. Currie*, [1984] O.J. No. 147 (Ont. CA) at paras. 14-17).

[306] The second element of the *actus reus* of fraud, deprivation, is established by proof of detriment, prejudice or risk of prejudice to the economic interests of the victims caused by the dishonest act. Actual economic loss suffered by the victim may establish deprivation, but it is not required. Prejudice or risk of prejudice to an economic interest is sufficient (*Théroux*, above at paras. 16-17; *R. v. Olan*, [1978] 2 S.C.R. 1175).

[307] A person who deprives another person of what the latter has should not escape criminal responsibility merely because, according to his moral or her personal code, he or she was doing nothing wrong or because of a sanguine belief that all will come out right in the end. Many frauds are perpetrated by people who think there is nothing wrong in what they are doing or who sincerely believe that their act of placing other people's property at risk will not ultimately result in actual loss to those persons. If the offence of fraud is to catch those who actually practise fraud, its *mens rea* cannot be cast so narrowly as this (*Théroux*, above, p. 27).

[308] With regards to NAC, Mr. Tillie testified that some deposits found in NAFG's bank accounts appeared to have been transferred directly from the bank account of NAC (Tr. Vol. 5, p. 27, ll. 20-24; p. 36, ll. 2-9). The source and application of fund analysis completed by Mr. Tillie indicate that all deposits made by NAC investors were deposited into Account 652, which was the main account of NAFG (Ex. 18, Tab B). The Respondents also admit that during the period July 2009 to April 2010, NAC issued shares to approximately 11 investors. The Respondents also admit that the total proceeds of approximately $1,042,000 from the sale of NAC securities were transferred to NAFG (Ex. 1, para. 2). I note, however, that Mr. Tillie's analysis shows that a total of $126,000 was received from NAC investors from the period of January 1, 2009 to September 24, 2010 (Ex. 20).

[309] With regards to NAFG, I accept Mr. Tillie's analysis of NAFG's income statement for the years 2007 to 2010 (Ex. 18, Tab J, p. 37). The income statement indicates that in 2007, NAFG lost $68,047 and the losses continued to the end of 2010. The cumulative effect of the losses resulted in a deficit by December 31, 2010 of $2,596,002. I therefore disagree with the Respondents' description of the effect of the marketing brochures distributed to investors. I find that considerable disclosures were made that implied that NAFG was a profitable business when it was not. This constitutes an act of deceit, falsehood or some other fraudulent means.

[310] I note that the Respondents admit that at no time did they advise investors in NAFG or NAC that their funds would be used either in whole or in part to pay interest, dividends or principal to other NAFG or NAC investors (Ex. 1, para. 30). Mr. Tillie's source and application of funds analysis (Ex. 20) established that the receipts from the lease payments were not sufficient to pay the interest paid to investors from January 1, 2009 to September 24, 2010. As Mr. Tillie said, there were only two primary sources of funds for the company, the lease payments and receipts from the investors. The only source of funds to make the interest payments to investors was funds received from new investors. This activity is often referred to as a "Ponzi" scheme. I find these payments of "new" investor money to "old" investors to be an act of deceit, falsehood or some other fraudulent means.

[311] There is incontrovertible evidence that investors were deprived by the prohibited acts identified in the preceding paragraph. Most of the investors of NAFG and NAC, who were unsecured investors, lost at least half of their investment pursuant to the terms of the arrangement agreed upon in the bankruptcy proceedings of NAFG. The interest rate applied to the remainder of their funds was reduced to 1%.

[312] I find that the prohibited acts coupled with the resulting losses establish the *actus reus* of the offensive fraud committed by the Respondents.

[313] The mental element of fraud is established by proof of subjective knowledge of the prohibited act and subjective knowledge that the prohibited act would have caused the deprivation of another as a consequence. The Alberta Court of Appeal has confirmed that it is appropriate to draw an inference as to the requisite subjective mental element from the totality of the evidence (*Alberta (Securities Commission) v. Brost*, 2008 ABCA 326 at paras. 42 and 43).

[314] Previous decisions issued by the Commission have also found that for a finding of fraud against a corporate respondent, it is sufficient to show that its directing minds knew or reasonably ought to have known that the corporation perpetrated a fraud to prove a breach of subsection 126.(1)(b) of the *Act* (*Re Richvale Resource Corp.* (2012), 35 O.S.C.B. 4286 at para. 104, citing *Re Al-Tar Energy Corp.* (2010), 33 O.S.C.B. 5535 at para. 221 and *Re Global Partners* (2010), 33 O.S.C.B. 7783 at para. 245).

[315] I find that each of the Arcontis were aware that NAFG never made a profit in the years 2007, 2008, 2009 or 2010 (Ex. 18, Tab J, p. 37). Each of them knew that the unsecured interest-free loan to Prestige Motors reached over $2 million. As of September 30, 2010, the loan amounted to a substantial $2,503,608.43 (Ex.1, para. 22; Ex. 11, Tab C2, p. 170).

[316] Each of the Arcontis transferred their interest in their residence to their spouses in May 2010. Each had an explanation for why they did so, which I do not accept. The transfers were made within days of each other and the timing of the transfers coincided with the increasing losses of the NAFG group of companies. This persuades me that the reason for the transfers was to place whatever value there might be in the residences out of the reach of potential creditors.

[317] The Respondents admit that the Arcontis were the directing minds of NAFG, NAC, Carter and Prestige Motors and that "returns to investors were funded in part by new investment in NAFG and/or NAC" (Ex. 1, paras. 4 and 29). I therefore find that the Arcontis each had the

requisite *mens rea* for fraud as alleged by Staff. Accordingly, I also find that NAFG and NAC knew that the representations to investors regarding NAFG's financial situation and the use of investor funds were false and misleading and would cause deprivation to investors by exposing them to risks not contemplated by them

[318] I find that on a balance of probabilities, the Respondents' conduct constituted a breach of subsection 126.1(b) of the *Act* and was contrary to the public interest.

H. Director and Officer Liability – NAFG and NAC

[319] Staff submits that the Arcontis, as actual and/or *de facto* officers and/or directors of NAFG and NAC, are liable for the breaches of subsection 126.1(b) of the *Act* by NAFG and NAC, pursuant to section 129.2 of the *Act*.

[320] The Respondents submit that to the extent that NAFG and NAC are found to have violated Ontario securities law, it is conceded that the Arcontis will also be found to have violated Ontario securities law. However, the Respondents deny Staff's allegation that the Respondents breached subsection 126.1(b) of the *Act*.

[321] Section 129.2 of the *Act* applies to directors or officers of a company that fail to comply with Ontario securities law. I note that the Respondents admit that the Arcontis were co-owners, the directing minds and actual and/or *de facto* officers and directors of NAFG and NAC (Ex. 1, paras. 5 and 12). I agree with Staff's submission that the Arcontis were active members in the fraud committed by NAFG and NAC. The evidence has shown that:

(a) Flavio Arconti prepared the marketing brochures of NAFG, which contained statements that conveyed NAFG as a successful business, when it was not;

(b) Gino Arconti distributed NAFG's marketing brochures to investors;

(c) the Arcontis were two of the four people that were responsible for depositing cheques that came into NAFG;

(d) the Arcontis reviewed the financial statements of NAFG on an annual basis and were aware of NAFG's growing cumulative losses and the growing unsecured, interest-free loan to Prestige Motors; and

(e) the Arcontis were both engaged in discussions with investors.

[322] I find that the Arcontis authorized, permitted or acquiesced in the non-compliance with Ontario securities law by NAFG and NAC, and the Arcontis are therefore are deemed to have failed to comply with Ontario securities law under section 129.2 of the *Act*.

I. Trading without Registration and Analysis

[323] Staff alleges that Gino Arconti, having become aware of his suspension as a registrant on September 23, 2010, did trade in securities contrary to subsection 25(1) of the *Act*.

[324] The Respondents deny Staff's allegation that Gino Arconti continued to engage in and/or hold himself out as engaging in the business of trading in securities.

[325] Subsection 25(1) of the *Act* provides that:

> **25 Registration – (1) Dealers** – Unless a person or company is exempt under Ontario securities law from the requirement to comply with this subsection, the person or company shall not engage in or hold himself, herself or itself out as engaging in the business of trading in securities unless the person or company,
>
> (a) is registered in accordance with Ontario securities law as a dealer; or
>
> (b) is a representative registered in accordance with Ontario securities law as a dealing representative of a registered dealer and is acting on behalf of the registered dealer.

[326] The definition of "security" provided for in subsection 1(1) of the *Act* includes "a bond, debenture, note or other evidence of indebtedness or a share, stock, unit, unit certificate, participation certificate, certificate of share or interest".

[327] The definition of "trade" or "trading" under subsection 1(1) of the *Act* provides for a broad definition, which includes "any sale or disposition of a security for valuable consideration" and "any act, advertisement, solicitation, conduct or negotiation directly or indirectly in furtherance" of such a sale or disposition.

[328] The Commission has adopted a contextual approach to determining whether nonregistered individuals or companies have engaged in acts in furtherance of a trade. The contextual approach examines "the totality of the conduct and the setting in which the acts have occurred" and has as a primary consideration of which is "the effect the acts had on those to whom they were directed" (*Momentas*, above at para. 77).

[329] A variety of conduct has been found by the Commission to constitute acts in furtherance of trade, including:

(a) providing potential investors with subscription agreements to execute;

(b) distributing promotional materials concerning potential investments;

(c) issuing and signing share certificates;

(d) preparing and disseminating materials describing investment programs;

(e) preparing and disseminating forms of agreements for signature by investors;

(f) conducting information sessions with groups of investors;

(g) meeting with individual investors;

(h) accepting investor funds for the purpose of an investment; and

(i) offering securities to investors on the Internet.

(*Momentas*, above at para. 80; *Re Lett* (2004), 27 O.S.C.B. 3215 ("***Lett***") at paras. 50-51 and 64; *Re Allen* (2005), 28 O.S.C.B. 8541 ("***Allen***") at para. 85; *Re Limelight Entertainment Inc.* (2008), 31 O.S.C.B. 1727 ("***Limelight***") at para. 133; *Re First Federal Capital (Canada) Corp.* (2003), 27 O.S.C.B. 1603 ("***First Federal***") at para. 45)

[330] Therefore, taking steps to facilitate the mechanical, or logistical, aspects of trading has been found by the Commission to be an act in furtherance of a trade. In *Lett*, investors transferred, deposited, or caused to be deposited, funds into the accounts of the corporate respondents, which had been opened by an individual respondent. The Commission found that the investors' funds were deposited into the accounts and accepted by the respondents for the purpose of selling securities and held that the respondents had carried out acts in furtherance of trades (*Lett*, above at paras. 60 and 64).

[331] A respondent does not have to have direct contact or make a direct solicitation of an investor for an act to constitute an act in furtherance of a trade (*Lett*, above at paras. 48-51 and 64). An act in furtherance of a trade does not require that an investment contract be completed or that an actual trade otherwise occur (*Allen*, above at para. 85). Any claim that an actual trade must occur for there to be an act in furtherance of a trade would necessarily limit the effectiveness and negate the purpose of the *Act*, which is to regulate those who trade, or who purport to trade, in securities (*First Federal*, above at paras. 46, 47, 50 and 51).

[332] In *Lett*, above, the Commission found that the investors' funds were deposited into the accounts and accepted by the respondents for the purpose of selling securities. The Commission held that the respondents had carried out acts in furtherance of trades (*Lett*, above, at para. 60 and 64).

[333] Once Staff has established that a respondent has engaged in an activity for which registration or a prospectus is required, the onus is on the respondent to prove facts establishing the availability of an exemption.

[334] Gino Arconti's registration as a Dealing Representative of Carter ended on September 22, 2010 when it was automatically suspended by the Director's Decision. This was admitted by the Respondents (Ex. 1, para. 15). It is also admitted that the Arcontis' registration was automatically suspended as a result of the Director's Decision (Ex. 1, para. 8). At the Hearing, Staff introduced certified statements, pursuant to section 139 of the *Act*, with respect to the registration statuses of the Respondents and Carter. Based on the certificates, Gino Arconti was not registered in any capacity with the Commission after September 22, 2010 (Ex. 19, Tab 9). There was also no evidence that a registration exemption was available to Gino Arconti at any time he traded the securities of NAFG or NAC.

[335] It will be recalled that D.M. wrote a cheque to NAFG for $50,000 dated September 1, 2010. D.M. instructed Gino Arconti not to cash the cheque until Friday, September 24, 2010.

Following D.M.'s consent, Gino Arconti deposited the cheque into Account 652, NAFG's main bank account, on September 24, 2010.

[336] I find that the debenture transaction of D.M. constituted a "security" under the *Act*. I also find that the sale of the debenture to D.M. constituted a "trade" under the *Act*, and that Gino Arconti's active steps to complete this transaction constituted an "act in furtherance of a trade".

[337] I therefore find that on September 24, 2010, Gino Arconti engaged in or held himself out as engaging in the business of trading in securities without registration, contrary to subsection 25(1) of the *Act* and contrary to the public interest.

PART 5 - CONCLUSION

[338] For the reasons set out above, I find that:

(a) during the period September 29, 2009 to September 24, 2010, Carter's actions constituted a breach of section 13.3 of NI 31-103 and was contrary to the public interest;

(b) during the period September 17, 2007 to September 24, 2010, Carter's actions constituted a breach of subsection 2.1(1) of OSC Rule 31-505 and was contrary to the public interest;

(c) Flavio Arconti and Gino Arconti, as actual and *de facto* officers and directors of Carter, authorized, permitted or acquiesced in the non-compliance with Ontario securities law by Carter, and are therefore deemed to also have not complied with Ontario securities law, pursuant to section 129.2 of the *Act*;

(d) during the period January 1, 2009 to September 24, 2010, the Respondents directly or indirectly engaged or participated in acts, practices or courses of conduct relating to the securities of NAFG and NAC that they knew or reasonably ought to have known perpetrated a fraud on persons contrary to subsection 126.1(b) of the *Act* and contrary to the public interest;

(e) Flavio Arconti and Gino Arconti, as actual and *de facto* officers and directors of NAFG and NAC, authorized, permitted or acquiesced in the non-compliance with Ontario securities law by NAFG and NAC, and are therefore deemed to also have not complied with Ontario securities law, pursuant to section 129.2 of the *Act*; and

(f) on September 24, 2010, Gino Arconti engaged in or held himself out as engaging in the business of trading in securities without being registered to do so in circumstances in which no exemption was available, contrary to subsection 25(1) of the *Act* and contrary to the public interest.

[339] For the reasons outlined above, I will also issue an order dated December 11, 2013 which sets down the date for the hearing with respect to sanctions and costs in this matter and the schedule for the serving and filing of written submissions on sanctions and costs from the parties.

Dated at Toronto this 11th day of December, 2013.

"James D. Carnwath"

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James D. Carnwath, Q.C.