



Ontario
Securities
Commission

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valeurs mobilières
de l'Ontario

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

- AND -

**NORSHIELD ASSET MANAGEMENT (CANADA) LTD.,
OLYMPUS UNITED GROUP INC., JOHN XANTHOUDAKIS,
DALE SMITH AND PETER KEFALAS**

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

Hearing: October 27, 28, 29, 30, 31, 2008
November 3, 4, 5, 6, 10, 11, 12, 13, 17, 2008
December 8, 11, 2008
May 5, 6, 2009

Decision: March 8, 2010

Panel: Wendell S. Wigle, Q.C. - Commissioner (Chair of the Panel)
David L. Knight, F.C.A. - Commissioner
Margot C. Howard, CFA - Commissioner

Counsel: Melissa MacKewn - for Staff of the Ontario Securities
Pamela Foy Commission

Alistair Crawley - for John Xanthoudakis and
Dale Smith

Éric Cadi - for Peter Kefalas

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REASONS AND DECISION

I. OVERVIEW

A. Introduction

[1] This was a hearing on the merits before the Ontario Securities Commission (the “Commission”) pursuant to section 127 of the *Securities Act*, R.S.O. 1990, c. S.5, as amended (the “Act”) to consider whether Norshield Asset Management (Canada) Ltd. (“NAM”), Olympus United Group Inc. (“Olympus United Group”), John Xanthoudakis (“Xanthoudakis”), Dale Smith (“Smith”) and Peter Kefalas (“Kefalas”) (collectively, the “Respondents”) breached Ontario securities laws and acted contrary to the public interest.

[2] This matter (the “Proceeding”) arose out of a Notice of Hearing issued by the Commission on October 11, 2006 in relation to a Statement of Allegations issued by Staff of the Commission (“Staff”) on the same day. On October 20, 2006, the then existing Temporary Cease Trade Order was extended until the completion of the Proceeding. After a series of adjournments due to issues concerning disclosure, the hearing on the merits began on October 27, 2008.

[3] Staff submit that Xanthoudakis and Smith operated an investment structure that resulted in the loss of most of the \$159 million invested by 1,900 Canadian retail investors.

[4] Staff allege that the Respondents breached Ontario securities laws by failing to communicate the true nature of the investment structure and to account for the funds invested.

[5] The Respondents acknowledge that investors lost money as a result of the failure of the investment structure. However, they claim that this failure is not the result of any intentional and/or wrongful conduct on their part.

[6] Staff submit that the funds under the direction of NAM, Olympus United Group, Xanthoudakis and Smith were managed improperly. They submit that proper records were not kept, that independent and reliable valuations were not made, and that investors were not informed of the nature of their investments. The allegations are set out in paragraph 37 of these Reasons and Decision.

[7] It is the position of Xanthoudakis and Smith that the investment platform they managed operated in a manner consistent with what was represented to investors and to the public. Xanthoudakis and Smith submit that the records of NAM, Olympus United Group and the other entities that they were responsible for were properly maintained, and that the evidentiary record is incomplete with respect to the state of record-keeping below the levels they were responsible for in the investment structure.

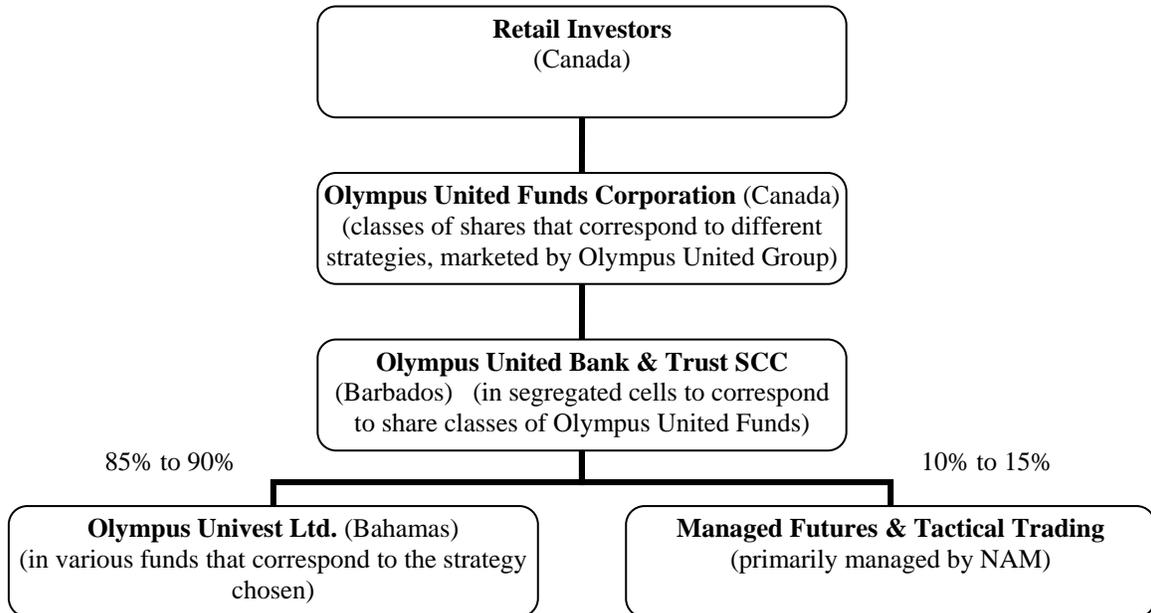
[8] We find that the Respondents were in breach of Ontario securities laws and acted contrary to the public interest, as discussed below.

B. Background

1. The Norshield Investment Structure

[9] The Norshield Investment Structure is a complex corporate structure that stretches across multiple jurisdictions. It was designed to raise and manage retail and institutional funds (the “Norshield Investment Structure”). Retail investors were generally issued shares at the Olympus United Funds Corporation (“Olympus United Funds”) level and institutional investments came in at the Olympus Uninvest Ltd. (“Olympus Uninvest”) level of the structure. Retail investors were issued shares in Olympus United Funds pursuant to a series of offering memoranda. Shares of Olympus United Funds were marketed by Olympus United Group. NAM provided portfolio management services to Olympus United Funds. For a somewhat more detailed description of the companies involved in the Norshield Investment Structure, see Appendix A attached to these Reasons and Decision.

[10] Throughout the hearing, we heard from Staff that the nature of the investment that retail investors thought they were getting when they purchased shares of Olympus United Funds was dramatically different from what they actually received. At its simplest, retail investors thought that they were investing in funds which provided them with access to a portfolio of hedge fund managers which they would have had difficulty accessing on their own due to the minimum investment requirement with each hedge fund manager. While a straightforward concept, the execution of this strategy was to be achieved through a number of different corporate entities in various jurisdictions, as follows:



[11] Retail investor funds were to flow from Olympus United Funds into “segregated asset cells” of Olympus United Bank and Trust SCC (“Olympus Bank”), a licensed offshore bank based in the Barbados. Under Barbados company law, segregated asset cells are used to protect assets from creditors with respect to obligations arising from

transactions involving other segregated assets and non-cellular assets. Investing through Olympus Bank was meant to provide tax advantages to Canadian retail investors.

[12] According to the evidence presented at the hearing, 10 to 15 percent of the funds held by Olympus Bank were invested in an “in-house overlay program”, which was involved in “managed futures” and “tactical trading”. The Olympus United Funds offering memorandum dated June 21, 2004 described “tactical trading” as a “market timing system that invests in futures and commodity contracts, equities, exchange-traded funds, fixed-income instruments, swaps and other derivatives with the objective of achieving high risk-adjusted returns that have a low correlation with traditional market indices”. The remaining 85 to 90 percent of retail investor funds went to share classes of Olympus Uninvest.

[13] At the Olympus Uninvest level, additional funds entered the Norshield Investment Structure from institutional and individual investors who received non-voting preference shares in Olympus Uninvest. At the Olympus Uninvest level, investments from retail and institutional investors were to be directed into various investment funds, corresponding to investors’ chosen strategies.

[14] It is Staff’s submission that what actually occurred was that funds raised from retail investors were not substantially, directly or indirectly, invested in a portfolio of hedge fund managers. Instead, funds from Olympus Uninvest were invested in Mosaic Composite (U.S.) Inc. (“Mosaic Composite”), a corporation with share classes that corresponded to each of the nine Olympus Uninvest investment funds. Mosaic Composite was originally incorporated and domiciled in the Bahamas and subsequently domiciled in the United States.

[15] According to a document prepared by Smith and given to RSM Richter Inc. (appointed as Receiver of NAM in June 2005), Olympus Uninvest and Mosaic Composite had an investment agreement. Pursuant to this agreement, there was apparently a notional separation of Mosaic Composite assets into two categories, “hedged assets”, for the exclusive benefit of Olympus Uninvest shareholders, and “non-hedged assets”, for the exclusive benefit of Mosaic Composite.

[16] The hedged assets included an option from the Royal Bank of Canada (“RBC”) that increased or decreased in value based on the performance of the underlying hedge fund portfolios (the “SOHO Option”).

[17] The SOHO Option was a derivative purchased from RBC with a portion of investors’ funds to provide the returns that would otherwise have been achieved if the funds were directly invested in a portfolio of different hedge fund managers (the “reference portfolio”).

[18] RSM Richter Inc. (“RSM Richter” or the “Receiver”) described the SOHO Option as follows:

The RBC SOHO Option is a financial instrument by which [Mosaic Composite] could gain access to a basket of portfolio investments upon

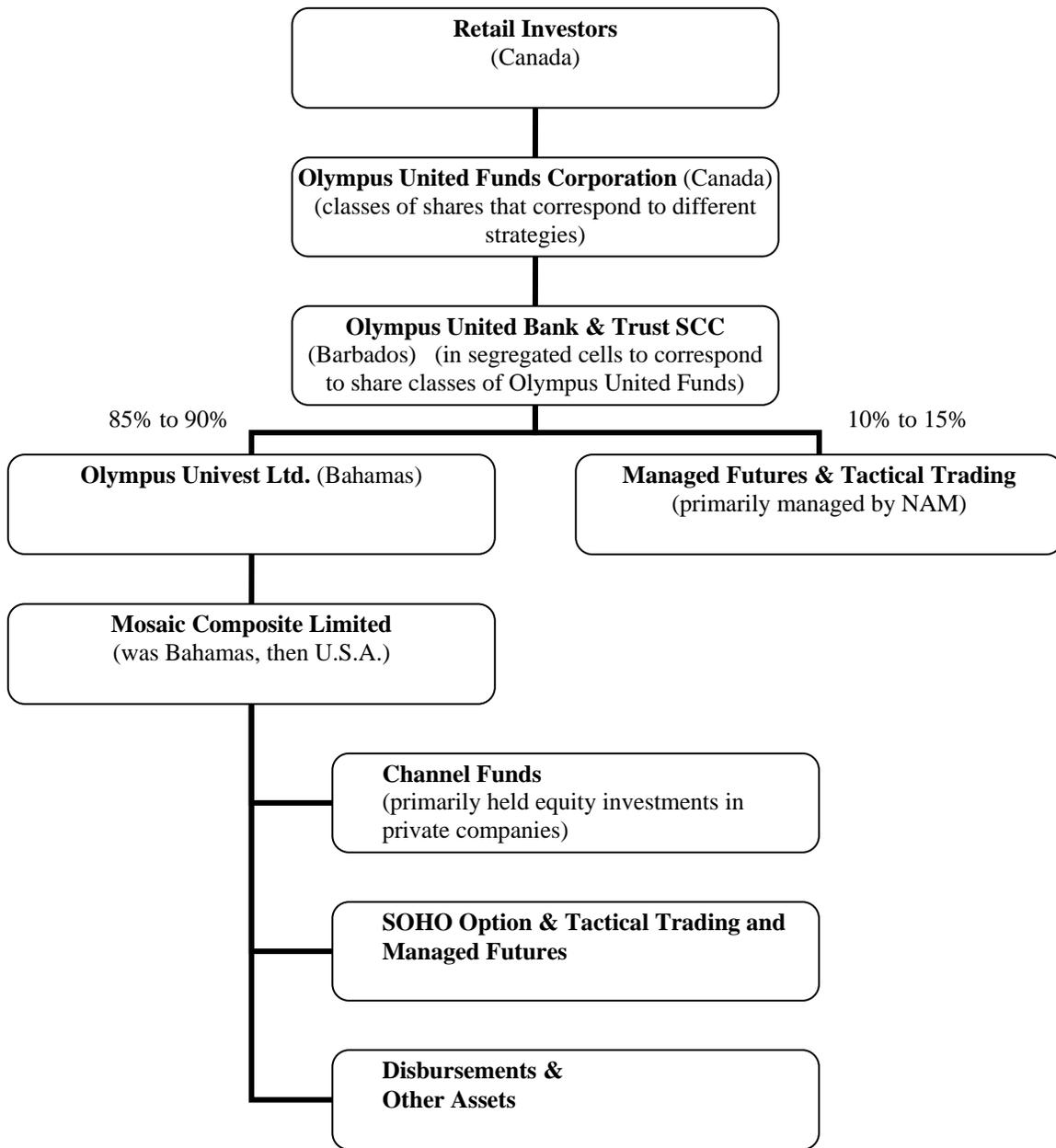
payment to the Royal Bank of Canada of [a Premium] which was equal to a percentage (between 15% and 25%) of a total value of said basket of portfolio investments ([Exposure]). The difference between the Premium and the Exposure represented the leverage that was inherent in the RBC SOHO Option ...

Exhibit 9 – Report of RSM Richter Inc. in its Capacity as the Court-Appointed Receiver of the Norshield Companies, September 16, 2008 at para. 138.

[19] The bulk of the remainder of the funds were invested in a portfolio of equity investments through four Bahamian funds (collectively, the “Channel Funds”). The Channel Funds consisted of Channel Fixed Income Fund Ltd., Channel F.S. Fund Ltd., Channel Technology Fund Ltd. and Channel Diversified Private Equity Fund Ltd. Any remaining funds were either disbursed or invested in other assets.

[20] Some evidence presented indicates that 10 to 15 percent of the funds at the Olympus Uninvest level were placed in in-house tactical trading and managed futures accounts, which were managed by entities owned by Xanthoudakis. However, as noted earlier, we also heard evidence that the in-house accounts were funded at the Olympus Bank level. Consequently, it appears that investor funds were placed into the in-house accounts at both the Olympus Bank and Olympus Uninvest levels.

[21] A simplified organization chart on the next page provides the highlights of Staff’s assertions concerning the flow of funds.



[22] Ultimately, the value of the investments in the Channel Funds and the other assets fell far short of the funds invested in them and there is little residual value remaining for retail and institutional investors. The task of surfacing value has been complicated by missing or incomplete records, multiple jurisdictions, competing claims and intercorporate transfers. While Staff have brought several allegations against the Respondents, a number of them revolve around whether Xanthoudakis and Smith were the directing minds and management of the investment structure and whether the net asset values (“NAV”s) used to sell and redeem fund units, including those to Ontario retail investors, were calculated properly.

2. History of Appointment of Monitor and Receiver

[23] On May 13, 2005, the Commission suspended NAM's registration pursuant to subsection 127(1) of the Act because it was operating without a registered advising and compliance officer. The Commission revoked its May 13, 2005 Order on May 16, 2005 when an advising and compliance officer for NAM was registered with the Commission.

[24] On May 20, 2005, NAM's registration was temporarily suspended (the "Temporary Order") pursuant to section 127(1) of the Act, and the Commission ordered that NAM retain a monitor selected by the Commission.

[25] On June 1, 2005, RSM Richter was appointed Monitor. On June 29, 2005, RSM Richter was appointed Receiver of NAM and a number of related entities by the Ontario Superior Court, upon a motion by Staff. The Commission consequently revoked RSM Richter's retainer as Monitor.

[26] RSM Richter also obtained court appointments in other jurisdictions. There were additional liquidators, receivers and monitors appointed in different jurisdictions for recovery of the assets of other companies in the Norshield Investment Structure. In its reports, the Receiver used information obtained from these sources.

3. Procedural History

[27] The hearing on the merits began on October 27, 2008, and ran until May 6, 2009. Fourteen days of evidence were concluded on November 17, 2008, with oral submissions scheduled for December 8, 2009.

[28] On November 23, 2008, the Chair of the Commission made comments aired on the television program "CBC News: Sunday Night" which became the subject of further proceedings before the Commission and the Divisional Court of the Ontario Superior Court of Justice ("Divisional Court").

[29] On November 28, 2008, Xanthoudakis and Smith filed an application for judicial review with the Divisional Court for an order staying the Proceeding. Staff brought a cross-motion to quash this application on the grounds that it was premature.

[30] The Court found that the motion to quash the application was a discretionary remedy which should properly be heard before a full Divisional Court panel. The Divisional Court found that the application for a stay was premature; that it should be heard on the basis of a full record, including a decision. The Divisional Court did not quash the application and did not grant an interim stay of the Proceeding. (*Dale Smith v. Ontario Securities Commission* (5 December 2008), Toronto DC-08-00000589-00JR (Ont. Div. Ct.)).

[31] On December 11, 2008, the Commission heard a motion for an order staying the Proceeding against Xanthoudakis and Smith. The Panel considered whether the Commission lacked jurisdiction because there was a reasonable apprehension of bias on three grounds: systemic or structural bias, institutional impartiality and corporate taint.

[32] In a separate decision released February 3, 2009 (*Re Norshield Asset Management (Canada) Ltd.* (2009), 32 O.S.C.B. 1249) (the “Stay Decision”), the Panel determined that there was no reasonable apprehension of bias on the part of the Commission. Therefore, the motion requesting a stay was dismissed.

[33] Xanthoudakis and Smith appealed the Stay Decision to the Divisional Court. They brought a motion to stay the Proceeding pending the disposition of the appeal. The Court found that the record was now complete with respect to the issue of bias, but found that the balance of convenience did not favour a stay. The Divisional Court determined that it could address the issues in this appeal, along with any others, once the Proceeding is completed before the Commission (*Xanthoudakis et al. v. Ontario Securities Commission* (27 April 2009), Toronto DC-09-00000071-0000 (Ont. Div. Ct.)).

4. Witnesses

[34] During the hearing, we heard evidence from the following witnesses called by Staff:

- (i) Adam Patterson (“Patterson”) was hired by Xanthoudakis in mid-2001 to work out of the NAM Toronto office in a marketing capacity with institutional clients. In late 2002, Patterson also assumed a compliance role, overseeing wholesalers who were selling Olympus United Funds to the brokerage and retail advisor network.
- (ii) Jeffrey Allan Young (“Young”) was hired as NAM’s Director of Research at the Toronto office in April 2004. His role was to act as a technical resource to Olympus United Funds wholesalers. This involved researching alternative investment strategies, explaining the investment product geared towards retail investors and providing technical support to the wholesalers. He became NAM’s Compliance Officer in August 2004.
- (iii) Sihai Tran (“Tran”) was employed with NAM and related companies from January 1995 until May 2005. He was originally employed with a brokerage arm of the structure as an assistant to a broker and then in a marketing capacity. He was later employed with Norshield Capital Management Corporation (“NCMC”), where he evaluated business plans of companies seeking venture capital investment. In 2000, he started work with NAM, where he was responsible for monitoring the managers chosen for the hedge fund portfolio out of the Montreal office.
- (iv) Raymond Massi (“Massi”) is a partner at RSM Richter, the Receiver. He has been the lead partner in this matter since RSM Richter was given its initial monitoring mandate. In some cases, Massi’s testimony as to the Receiver’s work and findings is based on work and findings of other receivers, liquidators and monitors involved with various companies in the Norshield Investment Structure.
- (v) Richard Radu (“Radu”) is a senior investigator in the Commission’s Enforcement branch who participated in Staff’s investigation in this matter.

- (vi) Trevor Walz (“Walz”) is a Senior Accountant in the Compliance and Regulation branch of the Commission who participated in the on-site reviews of NAM and Olympus United Group.

[35] Kefalas also testified at the hearing.

[36] None of the other Respondents testified or called witnesses.

C. The Allegations

[37] Staff make the following allegations against the Respondents:

- (i) NAM, Olympus United Group, Xanthoudakis and Smith failed to deal fairly, honestly and in good faith with clients, contrary to subsections 2.1(1) and 2.1(2) of OSC Rule 31-505 – *Conditions of Registration*;
- (ii) NAM and Olympus United Group failed to keep and/or maintain proper books and records in relation to the Norshield Investment Structure in contravention of section 19 of the Act and section 113 of Ontario Regulation 1015 of the Act;
- (iii) as a consequence of their positions of seniority and responsibility and in their positions as officers and directors of NAM and/or Olympus United Group, Xanthoudakis and Smith authorized, permitted or acquiesced in the violations of the requirements of Ontario securities laws and breaches of duty described in subparagraphs (i) and (ii) above;
- (iv) the Offering Memorandum filed and distributed by Olympus United Group contained misleading or untrue information and/or failed to state facts which were required to be stated, in contravention of clause (b) of subsection 122(1) of the Act;
- (v) as a consequence of their positions of seniority and responsibility and in their positions as officers and directors of Olympus United Group, Xanthoudakis and Smith authorized, permitted or acquiesced in the breach of Ontario securities law described in subparagraph (iv) above;
- (vi) Xanthoudakis and Smith knowingly made statements and provided evidence and information to Staff that was materially misleading or untrue and/or failed to state facts which were required to be stated in an effort to hide the violations of Ontario securities laws and breaches of duty described in subparagraphs (i) to (v) above, in contravention of clause (a) of subsection 122(1) of the Act; and

(vii) the course of conduct engaged in by Xanthoudakis, Smith and Kefalas compromised the integrity of Ontario's capital markets, was abusive to Ontario's capital markets and was contrary to the public interest.

[38] Staff had originally made allegations (i), (iii) and (vii) above against Kefalas in the Statement of Allegations. During the hearing, Staff informed the Commission that they were only proceeding against Kefalas on allegation (vii), alleging that his conduct compromised the integrity of Ontario's capital markets, was abusive to Ontario's capital markets and was contrary to the public interest.

D. The Respondents

[39] There are a number of related entities that formed part of the overall Norshield Investment Structure at issue in this case and through which investor funds flowed, but that are not named as Respondents in this proceeding. The Respondents are as follows.

1. NAM

[40] NAM created investment products, conducted proprietary research, consulted and provided asset and risk management advisory services to fund and institutional clients.

[41] NAM was appointed to provide portfolio management services with respect to Olympus United Funds.

[42] NAM was incorporated on September 25, 1996 as a Canadian federal corporation and had its head office in Montreal. Prior to 1996 NAM carried on business as GIC Commodity Advisors of USA, GIC Asset Management Ltd. and Norshield Asset Management Ltd.

[43] NAM was wholly owned by Norshield Investment Partners Holdings Ltd. ("Norshield Partners"). Evidence was also presented which indicated that NAM was a subsidiary of NCMC. In any case, both Norshield Partners and NCMC were owned by Xanthoudakis.

[44] NAM was registered under Quebec securities laws as an advisor with an unrestricted practice. Its Ontario securities registrations are as follows:

- (i) NAM was registered in the category of extra provincial adviser, investment counsel and portfolio manager from May 31, 2000 to February 20, 2003. On February 20, 2003, NAM changed its registration to investment counsel and portfolio manager. NAM was also registered with the Commission as a commodity trading counsel and commodity trading manager from November 5, 2003; and
- (ii) On May 13, 2005, the Commission suspended all of NAM's registrations because it no longer had a designated compliance officer or a registered advising officer. On May 16, 2005, the Commission granted registration of a

new advising officer at NAM, who was then designated as NAM's compliance officer and the Commission rescinded its previous order, revoking its suspension of NAM's registrations.

[45] On May 20, 2005, the Commission made a Temporary Order suspending NAM's registration. On October 20, 2006, that order was extended until the Proceeding is concluded and a decision of the Commission is rendered.

2. Olympus United Group

[46] Olympus United Group is a federal corporation with its head office in Montreal, Quebec. It was originally incorporated as Norshield Fund Management Ltd. on September 1, 1994, and carried on business under this name until its name was changed on May 16, 2002.

[47] Olympus United Group was registered with the Commission as a mutual fund dealer on April 21, 1998. On November 12, 1998, it also registered as a limited market dealer. It provided marketing services to Olympus United Funds, selling shares in the hedge fund to Canadian investors.

[48] Olympus United Group was granted membership in the Mutual Fund Dealers Association on March 4, 2003. Its membership was terminated as of September 26, 2006.

[49] Olympus United Group is wholly owned by Norshield Financial Holdings Ltd. ("Norshield Financial Holdings"), which in turn is wholly owned by Xanthoudakis.

[50] On May 13, 2005, the Commission made a temporary order suspending Olympus United Group's registration for not having a designated compliance officer or a registered trading officer. In a temporary order dated May 20, 2005, the Commission ordered that Olympus United Group not pay out, redeem or otherwise return any funds or other assets from any existing client accounts. Both orders were extended on October 20, 2006 until the conclusion of the Proceeding in this matter.

3. Xanthoudakis

[51] Xanthoudakis has worked in the financial services industry since 1982. He was President, Chief Executive Officer and a director of NAM.

[52] Xanthoudakis was President and a director of Olympus United Group.

[53] Xanthoudakis held the following Ontario securities registrations:

- (i) with regard to NAM, from May 31, 2000 to May 13, 2005, he was registered as an extra provincial advisor, investment counsel and portfolio manager as a non-advising officer (President and Chief Executive Officer) and Director, and;
- (ii) with regard to Olympus United Group and its predecessor, Norshield Fund Management Ltd., he was:

- (a) a mutual fund dealer and a non-trading officer (President and Chief Executive Officer) from April 21, 1998 to December 1, 2000;
- (b) a mutual fund dealer and a limited market dealer as a Director from December 1, 2000 to May 13, 2005; and
- (c) a commodity trading counsel and a commodity trading manager as a non-advising officer (President and CEO) and Director from November 5, 2003 to May 13, 2005.

[54] According to an investment proposal submitted to TD Bank Financial Group, Xanthoudakis was the Chairman, CEO, a director and the controlling shareholder of the Norshield Financial Group (“NFG”), the trade name used to describe the corporate structure that marketed and managed investments in Olympus United Funds.

[55] He was also involved with other corporations that Staff allege are part of the Norshield Investment Structure. The level of his involvement in the Norshield Investment Structure is at issue in this matter, and is considered in the analysis below.

4. Smith

[56] Smith became a Chartered Accountant in 1972. In 1998, Smith commenced employment with Xanthoudakis as Chief Financial Officer of NFG. In 2000, he became President and Chief Operating Officer of NFG.

[57] Smith was the Secretary-Treasurer of NAM, though it is not clear from the evidence how long he held the position. Smith was also an officer of Olympus United Group.

[58] The Commission approved Smith with regard to NAM as an advisor in the categories of extra provincial adviser, investment counsel and portfolio manager, as a non-advising officer (Secretary and Treasurer) from May 31, 2000 to May 9, 2005. He was also approved with NAM as an advisor in the categories of commodity trading counsel and commodity trading manager, as a non-advising officer (Secretary and Treasurer), from November 5, 2003 to May 9, 2005.

[59] Smith was registered with the Commission as a mutual fund dealer and limited market dealer, as a non-trading officer (Secretary and Treasurer) for Olympus United Group and its predecessor corporation from December 7, 1999 to October 3, 2004.

[60] Smith served as a director of Olympus Bank starting in June 1999, and was Olympus Bank’s Chairman and CEO beginning in January 2003.

[61] According to the Olympus United Funds offering memorandum, Smith was a director of Olympus United Funds starting in September 2001, and the President and CEO starting in February 2003. He was also a director of Olympus Uninvest.

[62] Aside from the above, Smith was also involved with other entities in the Norshield Investment Structure. His level of involvement in the Norshield Investment Structure is at issue in this matter, and is considered in the analysis below.

5. Kefalas

[63] Kefalas was employed with NAM and its predecessor corporations from March 1985 to April 2005. He was the Senior Portfolio Manager and was involved in the development of NAM's technical and tactical trading models.

[64] Kefalas's Ontario registrations with regard to NAM are as follows:

- (i) he was registered as an advising officer and director under the category of extra provincial adviser, investment counsel and portfolio manager from May 31, 2000 to May 19, 2004;
- (ii) he was registered as investment counsel and portfolio manager from November 19, 2004 to April 25, 2005;
- (iii) he was the Compliance Officer from May 31, 2000 to February 19, 2003;
- (iv) he was designated as Ultimate Responsible Person from August 25, 2004 to November 19, 2004;
- (v) he was registered as an advising representative under the categories of investment counsel and portfolio manager from November 19, 2004 to April 25, 2005; and
- (vi) he was registered as an advisor in the categories of commodity trading counsel and commodity trading manager under the *Commodity Futures Act*, R.S.O. 1990, Chapter 20, as amended as an officer (Investment Advisor and Senior Analyst) from November 13, 2003 to November 19, 2004, and then as an advising representative from November 19, 2004 to April 25, 2005.

E. Ownership and Management of the Norshield Investment Structure

[65] The Norshield Investment Structure raised and managed retail and institutional investor funds. For additional information on the entities involved in the Norshield Investment Structure, see Appendix A of these Reasons and Decision.

[66] According to a 2004 document prepared for the Commission by Karine Simoes, NAM's Director, Corporate & Legal Affairs, Xanthoudakis indirectly held ownership over the entire Norshield Investment Structure down to the Olympus Bank level. Xanthoudakis was also a director and the President of Olympus United Group.

[67] Smith was the Secretary-Treasurer of NAM and an officer of Olympus United Group. He held the following positions as of his March 21, 2005 resignations from NFG entities:

- (i) President and Chief Operating Officer of NFG;
- (ii) director and officer of Olympus United Funds;
- (iii) director and officer of Olympus United Funds Holding Corporation;
- (iv) director, officer and Chairman of Olympus Bank;
- (v) director and Acting Administrator of Olympus Uninvest; and
- (vi) director of Olympus International Preferred Fund Ltd.

[68] According to the Receiver, Olympus Uninvest was apparently controlled by BICE International Inc. (“BICE International”), a Bahamian corporation. The Receiver noted that the June 21, 2004 offering memorandum for Olympus United Funds declares that BICE International was not associated with Olympus United Funds or Olympus Bank.

[69] Regardless of the ownership of Olympus Bank, the June 21, 2004 offering memorandum used in the distribution of the Olympus United Funds states:

NAM Canada is responsible for any loss that arises out of the failure by Olympus United Bank or any other investment manager appointed by it to:

- (a) exercise the powers and discharge the duties of its office honestly, in good faith and in the best interests of NAM Canada and Olympus United [Funds]; or
- (b) exercise the degree of care, diligence and skill that a reasonably prudent person would exercise in the circumstances.

NAM Canada has contractually acknowledged that it may not be relieved by Olympus United [Funds] and/or Olympus United Bank from these responsibilities.

Exhibit 3, tab 1 – Olympus United Funds Offering Memorandum, June 21, 2004 at 9.

[70] The identity of the owners of Olympus Uninvest, Mosaic Composite and the Channel Funds was an unsettled issue during this hearing, and is discussed further in the analysis below.

F. The Admissibility of Certain Transcripts

[71] During the hearing, Staff sought to admit transcripts of the testimony of five individuals examined by the Receiver under oath: Smith, Stephen Hancock (“Hancock”), Lowell Holden (“Holden”), Paul Gomez (“Gomez”) and Peter Marini (“Marini”).

[72] Hancock is a chartered accountant and was a director, Chair and CEO of Cardinal International Funds Services Ltd. (“Cardinal”), a Bahamian company, which acted as Mosaic Composite’s and Olympus Uninvest’s administrator. Hancock was a director of Mosaic Composite from October 1, 1997 until September 27, 2004, a director of Olympus Bank for an indeterminate amount of time starting in June 1999, and a director of Olympus Uninvest from January 17, 2001 until January 31, 2005. Hancock was a director and the Secretary-Treasurer of BICE International from November 8, 2002 to March 24, 2005. He was also a director of the Channel Funds.

[73] Holden was President, Chief Executive Officer and sole director of Mendota Capital, formerly Comprehensive Investor Services Ltd. (“CIS”) and was also President of Mosaic Composite once it moved to the United States in July 2005.

[74] Gomez is a chartered accountant with the accounting firm Gomez & Gomez, a correspondent firm of Grant Thornton in the Bahamas, and was the person responsible for that firm’s audits of Mosaic Composite in 2002 and 2003 and of Olympus Uninvest in 2003.

[75] Marini is a chartered accountant and works for the accounting firm Brooks, Di Santo in Montreal. He was the person responsible for the firm’s audits of the Channel Funds in 2002 and 2003.

1. Submissions

Staff

[76] Staff submit that any issues regarding the admissibility of the transcripts should be addressed through the weight the Panel gives to the evidence in its final determination.

[77] Staff note that, with respect to the individuals other than Smith, none of them could have been compelled to testify at the hearing because they reside outside of the Commission’s jurisdiction. When questioned, Staff stated that they did not invite any of the non-Respondents to voluntarily testify because they had already received transcripts from the Receiver and were confident they would be able to make use of them as evidence at the hearing. Smith, who is a Respondent, was free to choose whether to testify at the hearing.

[78] Staff further submit that Xanthoudakis and Smith have long-standing business relationships with Hancock, Holden, Gomez and Marini and could have sought further evidence from them.

Xanthoudakis and Smith

[79] Xanthoudakis and Smith submit that the Panel should use its discretion not to admit these transcripts because doing so would be inappropriate.

[80] They submit that if the transcripts were to be admitted, the Panel would not have an opportunity to evaluate the weight to be given to the evidence or to assess the credibility of the individuals through *viva voce* evidence. They also submit that the procedural protections in place during an examination-in-chief before the Commission were not necessarily present during the Receiver's examination of the individuals. Leading questions are commonly asked in compelled examinations and Hancock's counsel routinely left the room during his examination.

[81] Xanthoudakis and Smith also submit that they would not have an opportunity to cross-examine the individuals, to test the evidence or to obtain additional potentially exculpatory evidence from these individuals, which could result in prejudice to them. They argue that Staff made the decision to introduce evidence through the transcripts of interviews conducted by the Receiver, and hence made insufficient attempts to seek the aid of other regulatory agencies in order to compel the individuals to testify before the Commission. Xanthoudakis and Smith claim that Staff have not shown that the contents of the transcripts are necessary for the purposes of this Proceeding.

[82] Xanthoudakis and Smith claim they are reliant on information obtained through the disclosure process and from third parties, and that the Panel should take this information asymmetry into account in balancing the interests of the parties.

[83] Finally, they submit that Smith has a right not to testify as a Respondent to the Proceeding, and that Staff's request to admit the transcripts of his interview with the Receiver is an attempt to circumvent Smith's procedural rights.

2. The Law

[84] Subsection 15(1) of the *Statutory Powers Procedure Act*, R.S.O. 1990, c. S.22 ("SPPA") states:

What is admissible in evidence at a hearing

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 a 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.

[85] In their submissions, Staff refer to a British Columbia Court of Appeal decision on the admissibility of hearsay transcript evidence in a regulatory securities proceeding. In this case, the court determined that the British Columbia Securities Commission did not err in admitting transcripts of examinations conducted by staff of that Commission, where the individuals in question refused to appear at the hearing and where the commission lacked the jurisdiction to compel the individuals to testify (*Huber v. British Columbia (Securities Commission)* (1994), 3 C.C.L.S. 98 (B.C.C.A) at paras. 25-31).

3. Ruling

[86] Given the complexity of this case, we ruled at the hearing that the transcripts of Hancock, Holden, Gomez and Marini would be admitted, for the reasons below.

[87] The Panel has the discretion under s. 15 of the SPPA to admit hearsay evidence, but in exercising its discretion it must have regard to the matter before it. The more serious and contentious the matter, the more a tribunal must have regard to the rights of the parties. Though the Panel has the discretion to admit hearsay evidence, the rules of evidence are relevant and applicable in Commission proceedings. Natural justice and fairness issues must still be considered by the Panel when ruling on admissibility.

[88] Parties are entitled to a reasonable opportunity to comment on and contradict evidence. However, hearsay evidence need not be tested by cross-examination in all circumstances.

[89] If the Panel admits the evidence, it must be careful not to put too much weight on the evidence when making its final decision. For example, undue weight should not be placed on uncorroborated evidence. It should also be remembered, that while the standard of proof in administrative proceedings is the civil standard of a balance of probabilities, in the interest of a fair hearing, allegations can only be proven by clear and cogent evidence, as stated in *Investment Dealers Association of Canada v. Boulieris* (2004), 27 O.S.C.B. 1597 (O.S.C.) at para. 34, affirmed [2005] O.J. No. 1984 (Div. Ct.).

[90] In view of the fact that Smith is a Respondent in this Proceeding, we determined that the transcript of his interview with the Receiver would not be admitted.

[91] As a matter of fundamental fairness, persuasive collateral evidence is required to make adverse findings where those findings will have serious consequences for a respondent. In this decision, wherever we have relied on transcript evidence, we have only done so where it is consistent with or supported by other evidence.

II. ANALYSIS

A. Were Xanthoudakis and Smith directing minds of the Norshield Investment Structure?

[92] In order to appropriately consider the allegations against Xanthoudakis and Smith, we must first examine their roles and responsibilities within the Norshield Investment Structure.

1. Submissions

Staff

[93] Staff submit that the Norshield Investment Structure was directed at all times by NFG, through Xanthoudakis and Smith.

[94] Staff refer to NFG marketing materials that describe Xanthoudakis as Chairman and CEO and Smith as the President and Chief Operating Officer. Staff note that Xanthoudakis owned, and along with Smith, held positions of authority in many of the entities in the Norshield Investment Structure. Staff submit that Xanthoudakis, directly or indirectly, owned NAM, Norshield Financial Holdings, Norshield Partners, Norshield Investment Corporation (“NI Corporation”), NCMC, Olympus United Funds and Olympus Bank.

[95] Staff contend that the named directors of various entities connected to the Norshield Investment Structure were merely nominees and that ultimate control lay with Xanthoudakis and NAM. Staff submit that Xanthoudakis and Smith’s roles extended beyond the NAM, Olympus United Group and Olympus Bank levels and encompassed communications with end-clients and investment advisors throughout the structure. Staff refer to evidence from compelled examinations that state that instructions on the management of the Channel Funds and Mosaic Composite came from Xanthoudakis and Smith. Staff submit that Xanthoudakis and Smith also directed the Uninvest Multi Strategy II Fund (“MS-II”) transactions (discussed at paragraphs 211 to 228) that resulted in the sale of the SOHO Option, at the bottom of the Norshield Investment Structure.

[96] Staff submit that Xanthoudakis and Smith played an active role in audits of all the Norshield Investment Structure entities, and had the final say in the calculation and reporting of the NAVs.

[97] Staff submit that, as owner of numerous entities within NFG, Xanthoudakis had a role as a directing mind of NFG and thus, of the Norshield Investment Structure. According to a chart prepared by the Receiver, 87 percent of the carrying value of the Channel Funds assets at September 30, 2003 was attributable to companies related to NFG and/or Olympus Uninvest.

[98] According to Staff’s submissions, Xanthoudakis had the final say in decisions regarding investments in the Norshield Investment Structure. Staff claim that employees’ inquiries about the Norshield Investment Structure were directed to him and Smith, as the ultimate decision makers of the structure.

[99] Staff submit that Xanthoudakis was the directing mind of not only the respondent companies, but also many others connected to the Norshield Investment Structure, including BICE International, Liberty Trust and the Orion Trust.

[100] Staff refer to the positions held by Xanthoudakis’s sister-in-law as further evidence of his connection to all parts of the Norshield Investment Structure. Staff state that she served as an officer and/or director of Cardinal (the company notionally in

charge of Mosaic Composite's and the Channel Funds' books and records), BICE International, Mosaic Composite, Liberty Trust and CIS.

[101] Staff submit that Smith's roles as officer and director of entities within the Norshield Investment Structure make him a directing mind in the structure. At different times he was an officer and director of NAM, Olympus United Group, Olympus United Funds and Olympus Bank. He was on the board of directors for Olympus Uninvest and many of the companies that appear on the financial statements of the Channel Funds.

[102] Staff point out that Smith admits that he was representing the interests of NFG by maintaining directorships on the boards of various Channel Funds investee companies. According to Staff, Smith chose the auditors of these companies and participated at every level at the audit process.

[103] Staff note that in his testimony, Massi described what he knew about the relationship between Xanthoudakis and NFG and the recipients of unexplained payments from Olympus Bank and Mosaic Composite that total \$214 million.

Xanthoudakis and Smith

[104] Xanthoudakis and Smith argue that it is not credible to suggest that either of them was a directing mind of all the entities in the Norshield Investment Structure, given the scale of the operations that NAM was providing advisory services to in 2004 or 2005. They submit that after 2003, Xanthoudakis was principally running the entities in Canada that were providing advisory services and Smith was running Olympus Bank, but their responsibilities did not extend to other entities.

[105] Xanthoudakis and Smith claim that Staff are incorrect in their submission that they had a directing role in the Norshield Investment Structure below the Olympus Bank level. They submit that Mosaic Composite and its investee companies were run by other organizations and qualified management personnel. They claim that Mosaic Composite was controlled by Hancock, who was more than just a "rent-a-director".

[106] Xanthoudakis and Smith express serious concern about the reliability of Hancock's statements about their roles with Mosaic Composite and the Channel Funds. They claim that Hancock has personal motivation to distance himself from the events at issue within the Proceeding. They submit that Hancock was well-qualified to sit as a director of many of the Norshield Investment Structure entities, with an admitted special focus in business management, financial engineering, banking and multi-currency treasury management and corporate finance.

[107] Xanthoudakis and Smith claim that NAM was completely separate from Mosaic Composite, that the books and records of Mosaic Composite were not the responsibility of NAM and that Xanthoudakis and Smith could not have accessed them. They claim that Cardinal provided hedge fund administration services to Olympus Uninvest and Mosaic Composite, and was ultimately responsible for problems with the books and records of those entities.

[108] Xanthoudakis and Smith claim that Cardinal was also responsible for providing the NAV calculations until 2004.

[109] Xanthoudakis admits to having had a family relationship with his former sister-in-law, but submits that it is unfair to assume she did not have her own professional background and aspirations, and did not perform her duties independently from Xanthoudakis.

[110] Xanthoudakis and Smith argue that there is a significant break in the chain of control alleged by Staff. They submit that until January 2003, control of Olympus Bank was in the hands of a man by the name of Fred Purvis and his management team, who owned a 50 percent interest in Olympus Bank up to that point in time. Xanthoudakis and Smith allege that decisions to invest in the Olympus Univest structure were made by Olympus Bank's independent management, and that Fred Purvis and his team were the directing minds of that part of the Norshield Investment Structure, which oversaw between \$97 million and \$130 million in investments during their tenure as managers of Olympus Bank.

[111] Xanthoudakis and Smith admit their involvement with many Norshield Investment Structure entities, but make a distinction between co-operation and communication with these entities and having a controlling role within them. Xanthoudakis submits that even if he did not have a completely arm's length commercial relationship with some entities, this would not make him their *de facto* directing mind.

[112] Smith also submits that his role should be distinguished from that of Xanthoudakis. He argues that they each had their own roles and responsibilities, with Xanthoudakis focused on policy advisory work and the selection of managers for the managed portfolio platform, and Smith involved in the running of Olympus Bank from January 2003 onwards.

[113] Smith contends that his involvement in audits of entities within the Norshield Investment Structure was appropriate, given his background as a chartered accountant. He submits that his role extended only so far as to ensure that all entities that needed to report had done so, and that this is not evidence that he was a directing mind of those entities.

2. Analysis

[114] Xanthoudakis and Smith have been held out to be in control of NFG. In a hedge fund management proposal submitted to the TD Bank Financial Group, Xanthoudakis was described as Chairman, founder and controlling shareholder of NFG. In a document presented to the SEI Investments Company, Xanthoudakis is described as Chairman and Chief Investment Officer and Smith is described as President and Chief Operating Officer of NFG.

[115] NFG is a trade name for the overall corporate structure and is not an incorporated entity. According to a chart provided to Staff during an on-site compliance review at NAM's offices in Montreal, NFG included Norshield Financial Holdings, Olympus

United Group, Norshield Partners, NAM, Olympus United Funds Holding Corporation, Olympus United Funds, Olympus Bank and Norshield Investment Partners Inc. (U.S). All of the entities in NFG are listed on the chart as being directly or indirectly owned in their entirety by Xanthoudakis.

[116] As noted above, Xanthoudakis was NAM's President, CEO and a director and was President and a director of Olympus United Group until they went into receivership.

[117] Smith was Secretary-Treasurer of NAM and of Olympus United Group.

[118] According to its June 21, 2004 offering memorandum, Smith served as a director of Olympus United Funds from September 2001, and was President and CEO beginning in February 2003. Smith was a director of Olympus Bank from June 1999, and served as its Chairman and CEO starting in January 2003. He was also a director of Olympus Univest starting in January 2003.

[119] Smith sat on the boards of numerous companies in which the Channel Funds had invested, including Microslate Inc., Oceanwide.com Inc., Vezina Composites Inc., BDP Retirement Homes Inc. and AMT International Mining Corp.

[120] Hancock, who served as an officer and director of BICE International, the Channel Funds and Cardinal, and a director of Olympus Univest and Mosaic Composite, told the Receiver under oath that all instructions in respect of Mosaic Composite and the Channel Funds came from Xanthoudakis through Smith. He stated that he liaised with Smith, but it was his understanding that Xanthoudakis was the decision maker who passed instructions on to Smith. Hancock also stated that he did not make investment decisions for the Channel Funds, but that instructions came from Smith, who he presumed was acting on decisions made by Xanthoudakis to accept investments that were being transferred into the Channel Funds.

[121] While the Respondents submitted that Hancock had his own reasons for distancing himself from events at NAM, his testimony was under oath, uncontradicted by the Respondents and consistent with that of the NFG employees who appeared as witnesses.

[122] We heard evidence from four former employees of NAM and Olympus United Group, Patterson, Young, Tran and Kefalas. All of these individuals testified that Xanthoudakis was the ultimate decision maker as to the investment of funds in the Norshield Investment Structure, including the selection of hedge fund managers. Patterson also stated that Xanthoudakis had final approval over communications with clients and investment advisors and that when Cardinal ceased as administrator for Olympus Univest, Smith would have been the most aware of the state of NAV calculations.

[123] In addition, employees sent email inquiries regarding the Norshield Investment Structure, Olympus United Funds, Olympus Univest, compliance issues and NAV calculations to Xanthoudakis and Smith.

[124] We note that when RBC Capital Markets terminated the SOHO Option in June 2005, they copied Xanthoudakis on the notice. We also note that Xanthoudakis was directly and indirectly involved in the MS-II transactions and a number of option transactions, which are discussed in greater detail below. These transactions were integral to provide liquidity to Mosaic Composite to meet redemption requests and to support valuations used to produce NAVs at the Olympus United Funds level.

3. Conclusion

[125] Xanthoudakis and Smith were clearly the directing minds of the structure down to the Olympus Bank level, and evidence of their involvement in transactions and communications at the levels below indicate they were the directing minds and management of the Norshield Investment Structure as a whole. The evidence consistently showed that Xanthoudakis and Smith were treated as though they were in control of the Norshield Investment Structure.

[126] Taking into account all of the evidence, we find that Xanthoudakis and Smith were the directing minds and management of the Norshield Investment Structure. Xanthoudakis and Smith did not provide any evidence to contradict this conclusion.

B. Did NAM, Olympus United Group, Xanthoudakis and Smith, fail to deal fairly, honestly and in good faith with clients?

[127] Staff allege that NAM, Olympus United Group, Xanthoudakis and Smith failed to deal fairly, honestly and in good faith with their clients, contrary to subsections 2.1(1) and (2) of OSC Rule 31-505 – *Conditions of Registration*.

1. Submissions

Staff

[128] In particular, Staff submit that NAM, Olympus United Group, Xanthoudakis and Smith failed to deal honestly, fairly and in good faith with investors in their management of investor funds, in calculating the NAVs and in their conduct with regard to redemption requests.

Management of Funds

[129] Staff submit that that these respondents have not accounted for the funds invested by Canadian retail investors. Staff further submit that they permitted payments in excess of \$200 million to be made from Olympus Bank and Mosaic Composite without due diligence.

[130] Staff submit that NAM, Olympus United Group, Xanthoudakis and Smith engaged in the commingling of investment funds without proper record-keeping, resulting in competing claims over assets and unsupported valuations of assets.

Various hedge funds under the common management or direction of [NAM], [Olympus United Group], Xanthoudakis and Smith (such as Globe-X, [Mosaic Composite] and Commax) were commingled without record keeping or independent and reliable valuations so that redemptions could be made from new subscription funds in [Olympus United Funds]/[Olympus Uninvest], as required. Investors were never told that the fund that they had invested in was in-fact a combination of legacy funds and assets for which records and valuations did not exist.

Written Submissions of Staff, dated April 30, 2009 at para. 3.

[131] Staff take issue with the actions of these respondents surrounding in-kind investments accepted at the Olympus Uninvest level. They submit that Xanthoudakis and Smith did not provide sufficient information on the investors or valuations of the in-kind investments. Staff claim that it was improper for these respondents to continue to accept subscriptions when the Norshield Investment Structure was in a net redemption mode, and to be involved in the MS-II share sale transactions which amounted to preferential redemptions for some investors.

[132] Staff allege that NAM, Olympus United Group, Xanthoudakis and Smith directed investor funds into entities for which they did not know the identity of the beneficial owners or which they falsely denied were under their control. The breach of securities law, according to Staff, stems from the duty of these respondents as the registered investment adviser and dealer to account for investor funds. Staff also submit that a significant portion of investors' funds were paid by Mosaic Composite and Olympus Bank to third parties with connections to Xanthoudakis.

NAV Calculations

[133] Staff submit that Xanthoudakis and Smith prepared and instructed the preparation of false NAVs that were reported to investors. Staff allege that overvaluations of assets were improperly obtained to perpetuate the creation of false financial reporting, which Xanthoudakis and Smith then relied upon in false NAVs. Staff allege that NAVs were improperly calculated based on the gross value of the portfolio of investments held by Mosaic, without regard to the leveraged component of the assets, and that the non-hedged assets were not included in the NAV calculations.

Redemptions

[134] Staff submit that NAM's, Olympus United Group's, Xanthoudakis's and Smith's response to redemption requests made by investors were similarly contrary to their obligations to deal fairly, honestly and in good faith.

[135] Staff allege that the assets that investors could look to for recovery were improperly encumbered and/or liquidated and disposed of. Staff make specific reference to transactions involving MS-II shares, which they allege amounted to a preference over other investors with outstanding redemption requests in late 2004. Mosaic Composite sold 16,667 of its 29,667 MS-II Class A shares to Uninvest Convertible Arbitrage Fund

Ltd. and Univest High Yield Fund Ltd. (together, the “Univest Purchasers”). Mosaic Composite then essentially transferred its remaining 13,000 Class A shares to the Univest Purchasers. Staff claim the Univest Purchasers were given preference over the other investors with redemption requests in late 2004.

[136] Staff claim that these respondents improperly continued to accept subscriptions and make redemptions while knowing that the Norshield Investment Structure was in net redemption mode, that all liquid assets had been depleted, that valuations were at issue and that financial statements were overdue. Staff submit that by 2003, an increasing amount of newly invested funds were being used to satisfy redemption requests.

[137] While redemption requests were coming in, Staff allege that the Respondents improperly disposed of and liquidated assets in the Norshield Investment Structure, which investors could otherwise have looked to for recovery.

[138] Staff submit that NAM, Olympus United Group, Xanthoudakis and Smith acted improperly after the MS-II transactions resulted in the sale of most of Mosaic Composite’s interest in the SOHO Option by continuing to calculate NAVs based on the gross value of the SOHO Option.

Xanthoudakis and Smith

Management of Funds

[139] Xanthoudakis and Smith refer to audited financial statements for Mosaic Composite and Olympus Univest, and submit that they were justified in relying on these documents to satisfy their obligation to account for investor funds. They submit that their responsibility did not extend to the Mosaic Composite or Channel Funds level of the Norshield Investment Structure.

[140] According to Xanthoudakis and Smith, there is not sufficient information to determine how specific transactions and in-kind subscriptions occurred. They submit that there is a significantly deficient record relating to transactions that could be the key to understanding the reasons for the failure of the Norshield Investment Structure. Xanthoudakis and Smith did not provide details regarding the in-kind investors to the Receiver because they submit there is an evidentiary vacuum with respect to the events surrounding these transactions.

[141] They take the position that there has been a very limited investigation and that interviews and documents from individuals who clearly played a key role within the Norshield Investment Structure are not available. According to Xanthoudakis and Smith, the evidentiary record is incomplete. They submit that Staff have relied on the Receiver, whose objective differs from Staff’s, with a greater focus on the recovery of assets than on conducting a thorough investigation.

[142] Xanthoudakis and Smith further submit that the question concerning payments in excess of \$200 million was not properly at issue in this Proceeding because it is not a clearly articulated allegation in the Statement of Allegations.

NAV Calculations

[143] In response to allegations that they did not adequately disclose the details of the leverage associated with the SOHO Option, Xanthoudakis and Smith submit that the offering documentation given to investors correctly characterized the nature of the investment. They submit that the NAVs reported to investors correlated to the nature of the investment they were subscribing to, being the returns from the reference portfolio. They argue that valuations of assets were done as a going concern, and that once the structure failed, their value declined. In any case, they contend that the evidence suggests that the NAVs were all reported accurately and properly and organizations such as RBC would not have provided such a platform if material facts had been concealed.

[144] They submit that no inference of improper behaviour should be drawn from the fact that certain people working within the Norshield Investment Structure were not aware of how the entire structure worked. They contend that this is a natural situation given the complex nature of the investment structure.

[145] Xanthoudakis and Smith submit that Tran reviewed the RBC Capital Markets reports on the position values of the SOHO Option which identified the notional amount, the strike price and the premium. It is their position that there was no attempt to hide the SOHO Option and that there was nothing unusual about using that kind of structure within a hedge fund.

Redemptions

[146] According to Xanthoudakis and Smith, the redemption requests within the Norshield Investment Structure must be considered in its context. It is their position that the performance of similar funds at the time and the negative and unusual press that inferred fraudulent conduct on the part of Xanthoudakis and the Norshield Investment Structure, resulted in a massive increase in redemption requests. They submit that any fund in a net redemption mode for a sustained period of time, would also be in financial trouble, and that it was a result of the increase in redemption requests that the illiquid unhedged investments could not be monetized in a sufficient time frame.

2. The Law

[147] Section 2.1 of OSC Rule 31-505 states:

2.1 General Duties – (1) A registered dealer or adviser shall deal fairly, honestly and in good faith with its clients.

(2) A registered salesperson, officer or partner of a registered dealer or a registered officer or partner of a registered advisor shall deal fairly, honestly and in good faith with his or her clients.

...

3. Analysis

[148] Both Xanthoudakis and Smith were required to comply with section 2.1 of OSC Rule 31-505 under their Ontario securities registrations.

(a) Management of Investor Funds

i. In-kind Investments

[149] Staff allege that NAM, Olympus United Group, Xanthoudakis and Smith failed to deal fairly, honestly and in good faith with their clients by allowing in-kind investments to be made into the Norshield Investment Structure without providing further details of the nature of the assets or their values.

[150] Canadian retail investor funds were commingled with other investments at the Olympus Uninvest level. Massi testified that the Receiver estimated that approximately \$200 million in cash was invested in Olympus Uninvest, in addition to approximately \$140 million of Canadian retail investor funds flowing from Olympus Bank. Xanthoudakis and Smith told the Receiver that between \$40 and \$100 million of further investments were made at the Olympus Uninvest level in the form of in-kind investments. Accordingly, the evidence is that investments at the Olympus Uninvest level amounted to between approximately \$380 million and \$440 million.

[151] While in-kind subscribers received the same rights as those investors who contributed actual cash into the Norshield Investment Structure, there is no evidence to substantiate the values assigned to the in-kind investments. Xanthoudakis and Smith did not provide the Receiver with any details as to the identities of the in-kind investors, the nature of the assets, the method by which the assets were valued or the number of in-kind shares redeemed. Furthermore, the Receiver stated that subsequent to October 2004, the books and records of Olympus Uninvest were incomplete, and as a consequence the Receiver could not provide any detail on the in-kind subscriptions.

[152] The possibility that in-kind investments might have been accepted on improvident terms, and consequently might have impaired the ability of Canadian retail investors to redeem their shares in Olympus United Funds, is deeply concerning. However, we have not been presented with evidence which would allow us to conclude whether the role of the in-kind investments in the Norshield Investment Structure was improper or whether NAM, Olympus United Group, Xanthoudakis or Smith failed to deal fairly, honestly and in good faith with their clients by allowing these investments.

ii. Commingling of Funds

[153] The Olympus United Funds offering memorandum dated June 21, 2004 clearly states that funds invested would be used to provide capital to the segregated asset cells of Olympus Bank and that such cells “protect assets from creditors with respect to obligations arising out of other segregated asset cells and non-cellular assets of that corporation”.

[154] The offering memorandum also states that proceeds from the issuance of various classes of shares would be invested in other investment funds, consistent with chosen investment objectives. For example, the core investment made with the proceeds from the issuance of the Class I shares, which account for the majority of the Olympus United Funds assets, is Olympus Univest. The offering memorandum is silent as to whether subscriptions generated through alternative channels were received directly by Olympus Univest, but the Receiver testified that institutions made direct investments. This is consistent with the contents of an investment proposal to TD Bank Financial Group made by Patterson on NAM’s behalf, where there is a reference to the Univest Institutional Fund.

[155] We were not provided with any evidence indicating that the funds were commingled at the Olympus Bank level. However, the Olympus United Funds June 21, 2004 offering memorandum indicates that the monies raised from the issuance of shares at the Olympus Bank level would be invested in other funds, and that some of those funds were affiliated funds.

iii. Third Party Payments

[156] Staff also assert that NAM, Olympus United Group, Xanthoudakis and Smith failed to deal fairly, honestly and in good faith with Canadian retail investors by directing or permitting inappropriate payments to third parties. The Receiver has not been able to determine the purpose of these transactions and we were not presented with any evidence as to the nature of, or the reasons for, the various payments (the “Unexplained Payments”).

[157] According to the Receiver, from 2002 to 2004, Mosaic Composite made Unexplained Payments totalling \$154.5 million, and from 2001 to 2005, Olympus Bank made Unexplained Payments totalling \$60.7 million, to certain third parties, for which the Receiver was unable to obtain adequate documentation.

[158] In particular, Mosaic Composite made the following payments:

CIS (subsequently, Mendota Capital, Inc.)	\$38.4 million
BICE International	3.2
Globe-X Management Ltd., Globe-X Canadiana Ltd., Globe-X Enhanced Yield Fund, Globe-X International, and Globe-X Asset Appreciation (collectively the “Globe-X Entities”)	57.6
C-MAX Advantage Fund Ltd.	14.0
Commax Management	18.3
Univest Fixed Return for Emerald Key Management	3.6
Real Vest Investment Ltd.	1.6
Silicon Isle Ltd.	3.7
Olympus Bank for Liberty Trust	14.2
(rounding)	<u>(0.1)</u>
	<u>\$154.5 million</u>

[159] Olympus Bank made the following payments:

CIS (subsequently, Mendota Capital, Inc.)	\$40.9 million
Cardinal	9.6
BICE International	5.1
Norshield Investment Partners Inc.	2.0
Univest Global Funds Ltd.	1.4
Balanced Return Fund	1.0
Sterling Leaf Income Trust	<u>0.7</u>
	<u>\$60.7 million</u>

Exhibit 9 – Report of RSM Richter Inc. in its Capacity as the Court-Appointed Receiver of the Norshield Companies, September 16, 2008 at paras. 177-186.

[160] Many of these third parties were identified during the hearing as entities related to or under the control of Xanthoudakis. We were not provided with any evidence that either Xanthoudakis or Smith received any financial benefit from the Unexplained Payments, nor has such an allegation been made by Staff or such an assertion been made by the Receiver.

[161] The Globe-X Entities were funds located in the Bahamas. Gomez stated in his interview with the Receiver that the Globe-X Entities were related in some way to the Norshield companies. Massi testified that it was his belief that the Globe-X Entities were predecessor funds to the Olympus Univest investment structure. He testified that this portfolio of investments was being managed by Xanthoudakis and his team at NFG.

[162] CIS is the beneficiary of Liberty Trust, which entered into option agreements with Xanthoudakis and companies he directly controlled, Norshield Financial Holdings and NCMC.

[163] Massi testified that the C-MAX Advantage Fund Ltd. was a fund under the direction of Xanthoudakis and NFG that operated in the 1990s. The Channel Funds also held an investment in C-MAX Advantage Fund Ltd. until 2002.

[164] Kefalas testified that it was well known that Xanthoudakis had the controlling interest in Commax Fund.

[165] In an organization chart prepared by the receiver for Mount Real Financial Management Services Corporation (“Mount Real”) and provided to the Receiver, both Real Vest Investment Ltd. and Sterling Leaf Income Trust appear as entities related to Mount Real. Xanthoudakis’s name appears in the same organization chart.

[166] According to a December 18, 2003 letter written by Holden in his capacity as the Managing Director of Silicon Isle Ltd., Smith and Lino Matteo (“Matteo”), who was the President and Chief Executive Officer of Mount Real, acted as representatives of Silicon Isle Ltd. in connection with an escrow agreement. In a separate but related agreement dated November 11, 2004, Smith and Matteo signed as representatives of Silicon Isle Ltd. The escrow agreement related to the monies resulting from the purchase of assets by

Liberty Trust from Silicon Isle. Such funds were to be used in an attempt to settle various legal proceedings, which included, among others, Cinar Corporation, Xanthoudakis, Silicon Isle Ltd. and a number of the Globe-X Entities.

[167] Evidence was also presented which shows that Xanthoudakis previously had a significant holding in Mount Real Corporation, and that Xanthoudakis and Matteo have a longstanding business relationship. Once the Norshield Investment Structure entered a liquidity crisis, Matteo became directly involved in the structure as shown in a series of emails retrieved from NAM's computers by the Receiver. We find that Xanthoudakis and Matteo were in a non-arm's length relationship during the relevant period.

[168] A lack of information with respect to payments exceeding \$215 million to third parties is of considerable interest. However, as already stated, we were not presented with any evidence as to the nature of, or the reasons for, the Unexplained Payments. Absent such evidence, we cannot conclude whether the Unexplained Payments demonstrate that NAM, Olympus United Group, Xanthoudakis and Smith failed to deal fairly, honestly and in good faith with their clients.

[169] We consider NAM and Olympus United Group's alleged failure to maintain adequate books and records with regard to the Unexplained Payments below.

(b) NAV Calculations

[170] Staff allege that, in addition to mismanaging Canadian retail investor funds, NAM, Olympus United Group, Xanthoudakis and Smith failed to deal fairly, honestly and in good faith with these investors in the information provided to them about NAVs.

[171] Communication of correct NAV calculations was critical to the equitable treatment of investors. Subscription prices and redemption values were based on the NAV calculations. The offering memorandum of Olympus United Funds dated June 21, 2004 contains this description:

How the Class Shares are Valued and Sold

...

The Class Shares are offered at the net asset value per Class Share determined by us ... on the first Valuation Date following the date on which the subscription is received ...

...

Redemptions

Subject to all applicable laws, the Class Shares are redeemable both by you and by us under certain circumstances. The Net Asset Value per Class Share to be redeemed is currently determined as of the last Business Day of each week or such other date as determined by us ...

Exhibit 3, tab 1 – Olympus United Funds Offering Memorandum, June 21, 2004 at ii.

[172] The June 21, 2004 offering memorandum also states that NAV was to be calculated by the directors of Olympus Uninvest in accordance with such methods of evaluation as the directors deemed proper, and in accordance with generally accepted accounting principles.

[173] The Receiver reviewed the NAV calculations for certain weeks in 2004 and 2005 and concluded that the NAV calculations for the Norshield Investment Structure were based on the returns of the hedged assets of Mosaic Composite as well as other assets held at the Olympus Bank level, less fees and expenses, without regard to the leverage relating to the SOHO Option. The Receiver also noted that the value of Mosaic Composite's non-hedged assets was not included in the calculation of the NAVs.

[174] According to information Smith provided to the Receiver with respect to an agreement between Olympus Uninvest and Mosaic Composite, Mosaic Composite's non-hedged assets were not included in the NAV calculations because they were solely for the benefit of Mosaic Composite. Massi testified that Smith told the Receiver that through this agreement, Mosaic Composite assumed responsibility with respect to the leverage of the SOHO Option and guaranteed to Olympus Uninvest 100 percent of the underlying NAV of the Olympic Uninvest portfolio. According to the information Smith gave the Receiver about the agreement, Mosaic Composite was responsible for paying indebtedness to third parties and for maintaining cash reserves to meet liquidity needs. The Receiver was unable to obtain a copy of this agreement.

[175] A letter to investors from Xanthoudakis dated May 11, 2006 describes the structure as follows:

There were basically two portfolios operating under one special purpose investment company, Mosaic Composite Limited:

- a) the investor portfolio, consisting of Hedge Funds that invested in low risk investment strategies with world class fund managers, which portfolio Royal Bank of Canada lent to and held security; and
- b) the collateral portfolio, consisting of less liquid securities used to support the investment structure.

Exhibit 5, tab 4 – Letter from John Xanthoudakis dated May 11, 2006.

[176] Since the NAVs were calculated in reliance on the fact that the collateral investments retained their original value or that Mosaic Composite had the ability to make up for any shortfall, their accuracy depended on the ability of Mosaic Composite to fulfill the terms of the investment agreement. However, the evidence indicates that Mosaic Composite's non-hedged assets were artificially inflated in value and were not sufficient to support the terms of the investment agreement. The Receiver concluded that

the asset values on the Channel Funds' audited financial statements for fiscal 2002 and 2003 were overstated by at least US \$200 million and US \$300 million, respectively. The Receiver describes the impact of this in its report to the Commission:

... As a result, the value of the [Channel Funds'] assets was overstated by approximately 88% on their fiscal 2003 financial statements.

Since Mosaic [Composite] did not have sufficient Non-hedged Assets to fulfill its obligations to Olympus Uninvest, the NAVs upon which the subscriptions to and redemptions from Olympus Uninvest and [Olympus United Funds] were made were inflated. ...

The Receiver has concluded that in view of the enormous disparity between the value of the underlying assets within the Norshield investment structure and the NAVs reported to the Retail Investors, as well as the illiquid nature of those assets, the collapse of the Norshield investment structure was inevitable once redemptions exceeded subscriptions.

Exhibit 9 – Report of RSM Richter Inc. in its Capacity as the Court-Appointed Receiver of the Norshield Companies, September 16, 2008 at paras. 162-164.

i. Mosaic's Non-Hedged Assets

[177] According to Mosaic Composite's September 30, 2003 financial statements, there were approximately \$307 million in assets carried on its balance sheet in the form of equity shares and/or debentures in the Channel Funds. These investments constituted the material component of Mosaic Composite's non-hedged assets.

[178] The Channel Funds were incorporated in the Bahamas in the late 1990s as the Tristar Funds. Massi testified that, based on the Receiver's investigation, little of the purported \$307 million held by Mosaic Composite in the Channel Funds can be traced to actual cash investments:

When we were doing our flow of funds analysis, we came to the revelation that there was very little actual funds or disbursements that we saw going through the Mosaic entity into the Channel Fund and any of the Channel Fund entities.

...

So in a flow of cash perspective, we saw investor money coming in at the [Olympus United Funds level], at the Olympus Uninvest level, and flowing out at the [Mosaic Composite] level to outside parties. And yet, we saw very little cash actually going into the Channel Fund.

And we came to the conclusion that there was really a parallel stream whereby the Channel Fund was really – the investments generated which appeared on the balance sheet of [Mosaic Composite] was really generated as a result of paper transactions as opposed to real investments of cash into the Channel Fund.

... we saw very little cash flowing down to the Channel Fund. Minimal. I believe it was 1-million odd dollars ...

Hearing Transcript, November 4, 2009, pp. 141 and 146.

[179] Staff assert that the assets held by the Channel Funds were not purchased with investor funds, but were transferred from other funds or, from October 2000 to September 2002, through non-monetized option transactions in relation to assets held by NCMC, Norshield Financial Holdings and Xanthoudakis. NCMC and Norshield Financial Holdings were entities owned by Xanthoudakis. NCMC was used to make investments in private equity and Norshield Financial Holdings was a holding company for Olympus United Group. Tran, a former employee of NAM, testified that NCMC did not invest funds from Canadian retail investors.

ii. Option Transactions

[180] Assets owned by Xanthoudakis directly and through Norshield Financial Holdings and NCMC were optioned first to Liberty Trust, and then again to the Channel Funds by way of option agreements. While the assets were recorded on the Channel Funds' financial statements, there is no evidence that the premiums or strike prices associated with the various options were ever paid. Furthermore, the Respondents have not provided us with any evidence to support the valuation of the various assets, nor has the Receiver been able to find any such evidence in the course of its investigation.

[181] Liberty Trust was created in July 1999. At the time the option transactions took place, the settlor was Thomas Muir, a former director of Mosaic Composite and the trustee was Longview Associates. The beneficiary of Liberty Trust is CIS, the shareholders of which are unknown to us or to the Receiver. The Channel Funds engaged in a series of option transactions with Liberty Trust in respect of the shares of four separate entities that were previously owned by Xanthoudakis, Norshield Financial Holdings and NCMC.

First Series of Option Transactions:

[182] On October 1, 2000, Liberty Trust entered into an option agreement to purchase 19.6 Class A common shares of First Horizon Holdings Ltd. (now Olympus United Funds) from Norshield Financial Holdings. The option granted Liberty Trust the right to purchase these shares at a price of US \$2 million.

[183] On the same day, one of the Channel Funds companies (then the Tristar Fund Ltd.) entered into an option agreement with Liberty Trust to acquire the same shares at a price of US \$59,100,370.

[184] The Receiver was unable to obtain satisfactory information to explain the increase in value of the shares on the same day of roughly US \$57 million. The Receiver's investigation found no evidence that the option price was ever paid and title to the shares acquired. In addition, while the September 30, 2002 financial statements of one of the Channel Funds carried the interest in First Horizon Holdings Ltd. (now Olympus United Funds) at US \$59,100,370, the September 30, 2003 financial statements carried the interest at US \$92,249,740. We were not presented with any evidence which explains the significant increase in value of the interest in First Horizon Holdings Ltd. over that year.

Second Series of Option Transactions:

[185] On October 1, 2000, June 30, 2001 and June 30, 2002, Liberty Trust, Norshield Financial Holdings and NCMC entered into option agreements under which Liberty Trust was to acquire from Norshield Financial Holdings and NCMC 722, 713, and 287 common shares of Microslate Inc. at prices of US \$5,870,000, US \$5,800,000 and US \$2,330,000, respectively (for a total of US \$14,000,000).

[186] On the same day of each of the option agreements, a further option agreement was entered into by the Channel Funds (then the Tristar Funds) and Liberty Trust regarding the acquisition by the Channel Funds of the same common shares of Microslate Inc., with option prices of US \$12,720,000, US \$12,562,000 and US \$5,056,423, respectively (for a total of US \$30,338,423). Here too, the Receiver was not able to obtain satisfactory information to explain the values at which the Microslate Inc. shares were optioned to the Channel Funds. The Receiver found that the Channel Funds' accounts do not indicate that the option prices were ever paid.

[187] While the shares of Microslate Inc. were carried on the September 30, 2002 financial statements of the Channel Funds at US \$30,338,423, the September 30, 2003 financial statements of the Channel Funds carried the shares at only US \$19,438,423. We were not presented with any evidence to explain the change in value of the Microslate Inc. shares.

Third Series of Option Transactions:

[188] On October 1, 2000, Liberty Trust also entered into an option agreement with NCMC and Norshield Financial Holdings to purchase 148.5 Class A shares and 2,308,017 Class D shares of Vezina Composites Inc., at a price of US \$1,000,000. On the same day, the Channel Funds and Liberty Trust entered into an option agreement with respect to the same shares, at a price of US \$2,881,946. We were not presented with any evidence to explain the increase in value on the same day, and the Channel Funds' accounts do not indicate that the option price was ever paid.

Fourth Series of Option Transactions:

[189] Finally, on March 31, 2002, Liberty Trust and Xanthoudakis and Norshield Financial Holdings entered into an option agreement under which Liberty Trust acquired the right to buy 40 Class D shares of Olympus United Holdings Inc., with a strike price of US \$10 million. The same shares were the subject of a subsequent option agreement

between the Channel Funds and Liberty Trust on September 30, 2002, with a strike price of US \$46,084,776. Again, we were not presented with any evidence to explain the significant increase in price between the two options.

[190] It appears that the option prices in the various agreements were used by the Channel Funds in valuing the assets in their portfolios for the purposes of their financial statements. Consequently, the option transactions discussed above resulted in an aggregate increase in the book value of the Channel Funds of US \$138.4 million. In the Report of RSM Richter Inc. in its Capacity as the Court-Appointed Receiver of the Norshield Companies, the Receiver told Staff at paragraph 171:

The effect of these option transactions was to artificially inflate the value of the Channel Entities, which represented the most significant portion of Mosaic's non-hedged assets, by at least \$129 million (US\$111 million).

[191] We agree with the Receiver's finding that there was an overstatement of the value of the underlying assets held by the Channel Funds. The values of these private equity investments in Mosaic Composite's portfolio were overstated in the transactions described above, and in the Channel Funds' 2002 and 2003 financial statements.

iii. Other Assets

[192] According to the Channel Funds' financial statements, they also held interests in assets other than those which became part of their portfolio by way of option agreements.

[193] A 95% ownership in Emerald Key Management Ltd. was carried at US \$40.2 million on the Channel Funds' September 30, 2002 financial statements. The Receiver was not able to obtain any records to support the value of the asset or explain how it was acquired by the Channel Funds. On July 29, 2003, the asset was sold to BICE International for US \$148 million, payable over six years and secured by the ownership interest itself. Consequently, the Channel Funds reported a gain of US \$107.8 million, and the US \$148 million owed by BICE International appeared on its September 30, 2003 financial statements as a receivable.

[194] We were not presented with any evidence to explain the initial valuation of the ownership interest in Emerald Key Management Ltd. at approximately US \$40 million and its subsequent valuation at US \$148 million. The Receiver did not find that the US \$107.8 million gain reported by the Channel Funds had been satisfactorily explained or justified. According to the Receiver, the effect of these transactions was to inflate the value of Emerald Key Management Ltd. on the Channel Funds financial statements by replacing it with a receivable of significantly higher value from BICE International. The Receiver concluded that this consequently artificially inflated the NAVs for Mosaic Composite, Olympus Uninvest, Olympus Bank and Olympus United Funds.

[195] In addition to the interest held by the Channel Funds through option agreements and the receivable from BICE International, according to the Channel Funds' September 30, 2003 financial statements, they had these investments / assets:

Emerald Key Advisors	US \$ 8.0 million
Oceanwide.com Inc.	14.7
Lonald Holdings N.V. (PRB SA)	3.2
Niocan Inc.	1.5
BDP Retirement Homes Inc.	1.0
AMT International Mining Corp.	1.0
Other	<u>7.4</u>
	US \$ <u>36.8</u> million

[196] According to the Channel Funds' September 30, 2003 financial statements, the total value of their portfolios was US \$343,500,024.

iv. Valuations

[197] The Receiver concluded that the asset values in the audited financial statements of the Channel Funds were overstated by at least US \$200 million for 2002 and US \$300 million for 2003, an overstatement of approximately 88 percent in 2003.

[198] Xanthoudakis and Smith submit they relied on audits done for various entities in the Norshield Investment Structure. While they do not go so far as to claim reliance on the audits as a defence, they contend that the audits are a relevant consideration:

The fact that audits were being undertaken by credible audit firms is relevant information in trying to interpret the facts of this case and in my submission suggests that there must have been some kind of back up, sufficient back up, both from an accounting books and records perspective, from the perspective of analyzing material financial transactions that took place within those corporate entities with respect to the reliability of management representations concerning the business and affairs of those corporations.

In my submission, the fact [that] audit opinions were rendered, audited, and financial statements were produced would suggest that this was not some kind of rolling Ponzi scheme as suggested by Staff ...

Hearing Transcript, May 6, 2009, pp. 84-85.

[199] Xanthoudakis and Smith argue that Staff's and the Receiver's inability to obtain the full audit files from auditors in the Bahamas, Barbados and Canada has made it more difficult for all concerned to put a complete record before the Commission.

[200] Mount Real provided a letter to Gomez & Gomez dated December 30, 2001 confirming the value of the Tristar Ltd. debentures held by Composite Fund, Ltd. as of June 30, 2001. The letter also stated that neither Mount Real nor any of its subsidiaries were related to Tristar Ltd. Matteo signed a further letter from Mount Real Corporation confirming the Mount Real letter on January 9, 2002. (Tristar Ltd. is a predecessor name for a Channel Fund. Composite Fund, Ltd. is a predecessor name for Mosaic Composite.)

[201] In his examination before the Receiver, Gomez stated that he relied upon Mount Real's valuation of the Channel Funds' debenture investments while performing the audit of Mosaic Composite. However, he also stated that he did not believe Mount Real to be an arm's length party. He stated that he thought there was a connection between Mount Real and the Norshield Investment Structure, and that he did not have confidence in Mount Real's valuations.

[202] Gomez & Gomez also received a management representation letter dated January 2, 2002 from Hancock, as a director of Mosaic Composite, which assured them that the valuations of investments in debentures were properly presented.

[203] Gomez stated, during his examination, that he believed Smith to be the driving force behind the audits, and that Gomez & Gomez asked Smith if Grant Thornton could perform an audit of the Channel Funds for 2002. He stated that Smith chose Brooks, Di Santo to perform the audit instead.

[204] In its 2002 audit of the Channel Funds, Brooks, Di Santo relied on valuations done by Mount Real Innovation Centre, which was also an investee of the Channel Funds. Valuations of the following companies were done by Mount Real Innovation Centre as at September 30, 2002: First Horizon Holdings Ltd. (now, Olympus United Funds), Emerald Key Advisors Inc., Investsafe and Olympus United Holdings Ltd. In its 2003 audit, Brooks, Di Santo relied on valuations by Spectrum Financial Services ("Spectrum"). In the Receiver's research on Spectrum, it found Spectrum provided various human resources and accounting services.

[205] We find that the NAVs were artificially inflated, as the NAVs relied on the integrity of the valuations of the Channel Funds assets. This is discussed more fully in our analysis below.

(c) Conduct Surrounding Redemption Requests

[206] Staff submit that NAM, Olympus United Group, Xanthoudakis and Smith improperly dealt with redemption requests from investors, breaching their duty to deal with them fairly, honestly and in good faith.

i. Use of Subscription Funds to pay Redemptions

[207] It is clear from the evidence presented by Staff that retail investors were providing liquidity to the Norshield Investment Structure. From 2001 to 2005, \$264.7 million were raised from retail investors and \$139.3 million were invested at the Olympus Bank and Olympus Uninvest level, with most of the difference apparently having been used for meeting redemptions from other investors.

[208] Investment funds are frequently in a situation where redemptions and new investments are not equal, and where accepting new subscriptions is acceptable. However, the issues regarding the nature of the actual assets in the investment structure and the appropriateness of the calculations used in establishing NAVs are critical in treating investors fairly. These are discussed below.

[209] Staff submit that subscriptions were inappropriately accepted when financial statements were overdue. Olympus United Funds' financial statements for the financial year ending September 30, 2004 were not completed by January 30, 2005. \$5.4 million in retail subscriptions were accepted after this period in 2005 and it is likely that additional retail subscriptions were accepted in late 2004.

[210] The problem of financial statements being overdue is a technical issue. The fundamental problem with accepting further subscriptions at that time was the fact that the Respondents engaged in conduct, including their involvement in the option transactions discussed earlier and in the MS-II transactions, that would have made them aware that subscriptions ought not to have been accepted. Given all the evidence, we find that NAM, Olympus United Group, Xanthoudakis and Smith breached their duty to deal fairly, honestly and in good faith by accepting these subscriptions.

ii. The MS-II Transactions

[211] Through the MS-II transactions, Staff submit that the respondents displayed preferential treatment to shareholders by fulfilling their requests for redemptions over the requests from Canadian retail investors.

[212] Once Olympus United Funds and Olympus Bank were facing significant redemption requests, steps were taken to generate sufficient liquidity to meet them. Mosaic Composite's interest in the SOHO Option was the most valuable asset in the Norshield Investment Structure, and the primary source from which the redemption requests could be satisfied. However, if all or part of the SOHO Option was exercised to access its intrinsic value, they would no longer be able to calculate NAVs as they had been, and the security which provided investors with leveraged exposure to the portfolio of hedge fund managers would be fully or partially liquidated.

[213] Staff submit that in order to gain access to the value in the SOHO Option while maintaining the basis of the inflated NAV calculations, Mosaic Composite assigned its rights and interest in the SOHO Option to MS-II. MS-II is a Cayman Islands entity, of which Xanthoudakis became a director on February 3, 2005. On November 10, 2004, Mosaic Composite assigned its equity interest of approximately US \$52 million held in the SOHO Option to MS-II in exchange for 29,667 Class A shares and 22,949 Class B shares of MS-II. The effective date was October 29, 2004.

[214] The Class A shares were to provide Mosaic Composite with returns on the equity portion of the SOHO Option and the Class B shares were to provide Mosaic Composite with returns on the leveraged component of the SOHO Option, less any inherent costs in the option.

[215] Three sets of transactions occurred regarding the Class A and B shares of MS-II held by Mosaic Composite to generate liquidity.

[216] Effective November 1, 2004, Mosaic Composite sold 16,667 Class A shares of MS-II with a net asset value of US \$16,667,000 to the Uninvest Purchasers for US \$15 million. The proceeds that Mosaic Composite received were directed by Michael

Maloney (“Maloney”), a director of Mosaic Composite, to a Montreal law firm named Hart, Saint-Pierre, in trust. Although the copies of documents relating to this transaction that were entered into evidence are signed by Maloney only, MS-II and Norshield Investment Partners Inc. were also listed as parties to the transaction. In addition, the direction of the US \$15 million from the Univest Purchasers to Hart, Saint-Pierre, in trust for Mosaic Composite was sent on Norshield Investment Partners Inc. letterhead. Norshield Investment Partners Inc. was the Univest Purchasers’ Investment Manager.

[217] In a letter dated November 11, 2004, Maloney instructed Hart, Saint-Pierre to transfer US \$9 million of the US \$15 million to Liberty Trust to satisfy an amount owing by Mosaic Composite to Liberty Trust for assets purchased. On November 12, 2004, pursuant to an escrow agreement between Liberty Trust and Silicon Isle, and on the instruction of four individuals, including Matteo and Smith, the US \$9 million was used to purchase Univest II USD shares of “Olympus United Corporation” in trust for Silicon Isle (the cheque from Hart, Saint-Pierre relating to this transaction was made payable to Olympus United Funds Corporation). The escrow agreement specifically referred to the US \$9 million as being the funds received from Mosaic Composite.

[218] Further, in a letter dated November 11, 2004, Maloney instructed Hart, Saint-Pierre to pay the remaining US \$6 million to NI Corporation as payment for assets purchased by Mosaic from NI Corporation. As a director of NI Corporation, Xanthoudakis signed the direction of payment for this transaction, which instructs the NI Corporation payment to be made to an Olympus Bank account.

[219] A fax with copies of Maloney’s payment directions for the US \$15 million received by Mosaic Composite as a result of the sale of MS-II shares to the Univest Purchasers was sent from NFG in Montreal to Norshield Investment Partners Inc. in Chicago on November 11, 2004.

[220] On or about December 1, 2004, Mosaic Composite submitted 14,725.6 of its Class B shares in MS-II for redemption. MS-II was able to raise US \$15 million to meet the redemption request by reducing its equity in the SOHO Option. On Maloney’s instruction, the US \$15 million was paid to Olympus Univest by way of Cardinal.

[221] Mosaic Composite created a number of separate entities which were strategy specific and called the Mosaic Strategy Funds. In August 2004, the Univest Equity Long Short Fund made a total investment of US \$13 million in the Mosaic Callisto Fund Ltd., the Mosaic Leda Fund Ltd., and the Mosaic Adrastea Fund Ltd. These funds are referred to as feeder funds and are shareholders of Mosaic Composite. At some point in time, their name was changed from Mosaic Strategy Funds to Tessera Funds (the “Tessera Funds”).

[222] The Univest Equity Long Short Fund made a redemption request dated October 5, 2004 for its entire investment in the three Tessera Funds. This request was acknowledged by Cardinal with a trade dated November 5, 2004. The redemption request was not met as of November 5, 2004. Instead, a letter of agreement was entered into between Univest Equity Long Short Fund, Mosaic Composite and the Tessera Funds whereby it was agreed the redemption request could be met by payment of cash or an in-kind payment

through MS-II Class A shares by January 5, 2005. Effectively, Mosaic Composite entered into an agreement to meet its redemption request through the delivery of its MS-II Class A shares. Alternatively stated, the Univest Equity Long Short Fund could receive MS-II Class A shares with a NAV equal to the unpaid redemption amount to discharge its receivable from Mosaic Composite, and a Tessera Funds receivable was created by the redemption request (the “Tessera Funds Receivable”).

[223] According to Massi’s testimony, a series of transactions in January 2005 resulted in Mosaic effectively redeeming the remaining 13,000 of its MS-II Class A shares in exchange for the Tessera Funds Receivable. This was achieved by Univest Equity Long Short Fund transferring the Tessera Funds Receivable to the Univest Purchasers which in turn transferred it to MS-II for 13,148 MS-II Class A shares. At the same time, Mosaic Composite redeemed 13,000 of its MS-II Class A shares and received the Tessera Funds Receivable from MS-II. While Massi noted that the Receiver did not see the documentation for the internal transfers between the Univest Equity Long Short Fund and the Univest Purchasers, the end result is consistent with the documentation provided during the hearing, namely, that a Univest fund received MS-II Class A shares from Mosaic Composite as an in-kind payment for a redemption request.

[224] Staff submit that Mosaic Composite did not act properly in accepting the Tessera Funds Receivable, and that there is no record of their attempt to collect on this receivable. However, as Mosaic Composite would have created a payable related to the Tessera Funds Receivable at the time they or the Tessera Funds could not meet the Univest Equity Long Short Fund redemption request, the receipt of the Tessera Funds Receivable would effectively eliminate this payable on a consolidated basis. However, we find that these transactions gave certain investors priority to the available liquidity in a way that should have been known would disadvantage the remaining investors. It is clear from events, such as the inability of the Tessera Funds to meet the Univest Equity Long Short Fund redemption request, that there were liquidity problems and that the Channel Funds investments could not be readily liquidated to meet certain redemption requests at the Mosaic Composite level. As a result, the SOHO Option was the only liquid asset and was used to meet redemption requests. This increased the exposure of the remaining investors to the illiquid Channel Funds which was further complicated by the overvaluation of the assets in the Channel Funds as described earlier.

[225] We find that Xanthoudakis and Smith were aware of the exchange of MS-II shares for the Tessera Funds Receivable. In an e-mail dated April 26, 2005, the Chief Financial Officer of Norshield Investment Partners Inc. in Chicago asked for clarification from Xanthoudakis and Smith on the confirmation of the conversion of the Tessera Funds Receivable into MS-II shares, so that the Univest Strategy Fund audits could be finalized. The email also asked Xanthoudakis and Smith why Maloney had not provided confirmation to the auditor.

[226] Following the January 2005 transactions, Mosaic Composite’s interest in the SOHO Option consisted of 8,224.4 Class B shares of MS-II with a carrying value of US \$6.5 million. However, Olympus Fund’s NAV continued to be calculated on the basis of the gross value of the SOHO Option.

[227] Xanthoudakis was copied on a June 1, 2005 letter to MS-II from RBC terminating the SOHO Option. This evidence and the evidence provided through the option transactions described earlier do not support a finding that Xanthoudakis was not responsible for activity in the Norshield Investment Structure below the Olympus Bank level.

[228] Xanthoudakis and Smith were clearly involved in transactions that occurred at the Mosaic Composite level of the Norshield Investment Structure. Corporations that were owned, either directly or indirectly by Xanthoudakis, or for which he and Smith were officers and/or directors were directly involved in each step of the MS-II transactions.

[229] Xanthoudakis and Smith's involvement in these transactions was a breach of their duties as directors and officers of NAM and Olympus United Group to deal fairly, honestly and in good faith with clients. The interests of those who benefitted from the Tessera Funds Receivable transaction were favoured to the detriment of other investors with outstanding redemption requests.

[230] We also find that Olympus United Group and NAM failed to deal fairly, honestly and in good faith with clients in the share redemptions that were the result of the Tessera Funds Receivable Transaction.

4. Conclusion

[231] We find that NAV calculations in 2004 and 2005 were artificially inflated and that Xanthoudakis and Smith were fully aware of this. The NAV calculations were based on the investment agreement which, according to Smith's assertion, existed between Olympus Uninvest and Mosaic Composite. The majority of the reported value of Mosaic Composite's non-hedged assets was generated by way of paper transactions, which include a series of option transactions and a receivable of US \$148 million from BICE International. We note that Xanthoudakis and Smith were involved in many of the various paper transactions and were certainly aware of the option transactions, which served to inflate the NAV calculations. The MS-II transactions were an attempt to convey the value in the SOHO Option to the Uninvest Equity Long Short Fund to satisfy redemption requests without actually meeting redemption requests in cash. This resulted in the remaining investors having to rely on the equity investments in the Channel Funds to an even greater extent for NAV support and, as discussed earlier, we find that the value of these assets was overstated.

[232] We were not presented with any evidence to justify the value created by the paper transactions; or any evidence of any actual cash being withdrawn from or deposited to the Channel Funds' bank accounts in connection with the paper transactions.

[233] It is clear that NAM, Olympus United Group, Xanthoudakis and Smith all allowed Mosaic Composite to accept the Tessera Funds Receivable in exchange for its interest of 13,000 Class A shares of MS-II. This constituted a preference over other investors in the Norshield Investment Structure.

[234] While we are concerned that the values of the Channel Funds assets were overstated in 2002 and 2003, we do not have any evidence of any NAV calculations for these years, so we have restricted our finding on NAV calculations to 2004 and 2005.

[235] We note that the Respondents were generally unable to account for investors' funds. We heard evidence that the Receiver put forth considerable efforts to trace the movement of investor funds through the Norshield Investment Structure, but was not able to determine exactly where the funds went. Although we are not making findings on what happened to the investment funds, the Respondents' inability to account for these funds does not support a conclusion that they behaved fairly, honestly and in good faith with investors.

[236] We therefore find that NAM, Olympus United Group, Xanthoudakis and Smith failed to deal fairly, honestly and in good faith with investors. Communicating information to investors based on artificially inflated NAVs and engaging in transactions that amounted to giving preference to particular redemption requests over others are acts in breach of the duties articulated in s. 2.1 of OSC Rule 31-505.

[237] While we have noted our concern with regard to the acceptance of in-kind investments by Olympus Uninvest, as well as the Unexplained Payments which were made by Olympus Bank and Mosaic Composite, Staff did not lead sufficient evidence to conclude whether NAM, Olympus United Funds, Xanthoudakis or Smith acted improperly by allowing them to take place.

C. Did NAM and Olympus United Group fail to keep proper books and records for the entities in the Norshield Investment Structure?

[238] Staff allege that NAM and Olympus United Group failed to maintain proper books and records for the Norshield Investment Structure in contravention of section 19 of the Act and section 113 of Ontario Regulation 1015.

[239] In the Statement of Allegations, Staff claim that no audited financial statements were prepared or filed for any of the entities referred to in the Norshield Investment Structure, other than NAM, for financial periods after September 30, 2003. They state that adequate books and records in relation to the flow of funds through the Norshield Investment Structure during the material time have not been produced, nor has any documentation with respect to transactions occurring after September 30, 2003 been produced.

1. Submissions

Staff

[240] Staff submit that despite repeated requests from Staff and the Receiver, NAM, Olympus United Group, Xanthoudakis and Smith have not produced the required books and records.

[241] Staff assert that financial statements and accounting records of investments in and by the Channel Funds should have been accessible and reasonably up to date at all times. NAM and Olympus United Group ought to have had accurate records of subscriptions and redemptions. Staff submits that Olympus United Group and NAM ought to have known the officers, directors and beneficial owners of the entities involved in the Norshield Investment Structure.

[242] Staff submit that these respondents did not provide the following required materials during or subsequent to Staff's on-site compliance review in May 2005: (i) a copy of the agreement between Mosaic Composite and Olympus Uninvest regarding Mosaic Composite's undertakings with respect to the SOHO Option; (ii) a copy of the agreement between Mosaic Composite and RBC regarding the SOHO Option; (iii) a complete organization chart of the Norshield Investment Structure; (iv) records evidencing the flow of investor funds within the Norshield Investment Structure; (v) documents to support the existence of client assets; and (vi) current financial statements for all entities within the Norshield Investment Structure after September 30, 2003.

[243] Staff submit that there is evidence from the Receiver that additional violations of securities law record-keeping requirements were committed by NAM, Olympus United Group, Xanthoudakis and Smith. Based on evidence from the Receiver, Staff submit that: (i) Olympus Bank records were stale-dated by at least two months at the time the Receiver was appointed; (ii) evidence indicates that computers had been removed and file folders emptied from the NAM Montreal offices once the Receiver was appointed; (iii) relevant records were moved to Minnesota and only preserved through court proceedings initiated by the Receiver; (iv) only limited records of Olympus Uninvest and Mosaic Composite subsequent to September 2003 were available; and (v) Xanthoudakis and Smith failed to fully provide the Receiver with records provided by Cardinal to NAM employees.

[244] According to Staff, over \$200 million went from Mosaic Composite and Olympus Bank to entities that appear to have relationships with NFG and Xanthoudakis, yet proper records of these payments were not provided to the Receiver. Staff submit that these payments were made to the detriment of Canadian retail investors without good reason and in the absence of any documentation. Staff submit this is a breach of Xanthoudakis's and Smith's duties as officers and directors of registrants.

[245] Staff submit that Ontario registrants are not relieved from their duty to account for the use and flow of investor funds because offshore jurisdictions were involved and books and records may have been kept offshore. NAM and Olympus United Group were obliged to keep sufficient records to account for investor funds and make them available at all times.

[246] In addition, Staff allege that NAM and Olympus United Group did not properly keep their own records. They submit that records of subscriptions and redemptions, documents relating to NAM activities, shareholder resolutions, NAM's minute book and other important documentation were missing.

Xanthoudakis and Smith

[247] Xanthoudakis and Smith submit that the documents held by NAM, Olympus United Group and Olympus Bank were kept appropriately, and that any deficiencies in the books and records were due to failures by Mosaic Composite to provide reliable audited financial statements. Xanthoudakis and Smith assert that NAM was not responsible for the books and records of all companies in the Norshield Investment Structure, especially those in other jurisdictions. They argue that it was reasonable for NAM to rely on other entities to maintain their own books and records. They also submit that evidence with respect to the state of the books and records below the Olympus Bank level is lacking because certain records and working papers were not available to the Receiver.

[248] Xanthoudakis and Smith claim that Cardinal was in control of Mosaic Composite and responsible for its records. They associate the delay in financial reporting by Mosaic Composite with the loss of Cardinal's services. They allege that this delayed the completion of financial statements for Olympus Uninvest, which further delayed the completion of financial statements for Olympus United Funds in Canada. According to Xanthoudakis and Smith, the Respondents' responsibilities did not extend to the financial records of Mosaic Composite and the Channel Funds. The delay in Olympus United Funds reporting was directly attributable to delays further down in the investment structure caused by entities for which the Respondents were not responsible.

[249] According to Xanthoudakis and Smith, it was reasonable and appropriate for NAM in its role as advisor within the Norshield Investment Structure to rely on Cardinal, as a credible third party entity, to maintain the books and records of Mosaic Composite and the Channel Funds.

[250] It is the position of Xanthoudakis and Smith that proper audits had been conducted for Olympus United Funds up to September 2003, when the problem of the delayed information from other entities began. They claim that there is nothing covert or mysterious about the financial statements for 2003, and that audits were done at all levels of the Norshield Investment Structure by well-known accounting firms.

[251] As explained during the hearing, the Receiver was involved at that time in litigation in the Bahamas. As a result of this pending litigation, the Receiver was prohibited from providing to Staff some documentation in its possession relating to the auditors' working papers for some of the entities in the Norshield Investment Structure.

[252] Xanthoudakis and Smith submit that the books of Olympus United Group, Olympus Bank, and NAM and its related companies were in good order. The only deficiency was that the financial statements had not been completed for 2004 due to the failure of Mosaic Composite to provide reporting confirmations that held up the audit process for other entities further up in the Norshield Investment Structure.

[253] In response to allegations regarding the removal of documents from NAM's Montreal office, Xanthoudakis and Smith submit that there is no basis for this claim and

that Massi provided no evidence to support any suggestion that records relevant to the Respondent companies having been removed.

[254] Xanthoudakis and Smith submit that on the evidence, it would appear that the records were reasonably up to date and in good order in the circumstances, unless there is an expectation that records of other Norshield Investment Structure entities be kept in Canada.

[255] As stated earlier, Xanthoudakis and Smith submit that the question of unexplained payments was not properly at issue in this Proceeding because it was not a clearly articulated allegation in the Statement of Allegations.

2. The Law

[256] Under section 19 of the Act, registrants are obligated to keep and maintain proper books and records, and to produce those books and records as required by the Commission:

19. (1) Record-keeping – Every market participant shall keep such books, records and other documents as are necessary for the proper recording of its business transactions and financial affairs and the transactions that it executes on behalf of others and shall keep such other books, records and documents as may otherwise be required under Ontario securities law.

...

(3) Provision of Information to Commission – Every market participant shall deliver to the Commission at such time or times as the Commission or any member, employee or agent of the Commission may require,

- (a) any of the books, records and documents that are required to be kept by the market participant under Ontario securities law; and
- (b) except where prohibited by law, any filings, reports or other communications made to any other regulatory agency whether within or outside of Ontario.

[257] Ontario Regulation 1015, subsection 113(1) states the following:

113. (1) Every registrant shall maintain books and records necessary to record properly its business transactions and financial affairs.

3. Analysis

[258] Massi testified that the Receiver had difficulty tracking investor funds below the Olympus Bank level, as a result of incomplete books and records held by NAM and Olympus United Group. In particular, Massi identified the following information as missing when his firm was appointed as Monitor and when it continued as Receiver: (i) up-to-date records of subscriptions and redemptions; (ii) documents relating to the activities of NAM; (iii) supporting documentation for the NAV calculations; (iv) NAM's

minute book; (v) signed shareholder resolutions; and (vi) agreements with brokers, fund managers, administrators, and custodians.

[259] Massi also testified that when the Receiver entered NAM's offices in Montreal on June 2, 2005, it was apparent that computers and documents had been removed.

[260] Cardinal was hired as the administrator for Mosaic Composite and Olympus Uninvest. When Cardinal could no longer provide the services it was hired to perform, those companies had an obligation to ensure that the necessary services were still performed.

[261] Massi testified that the Receiver received an anonymous tip in May 2006 that eighty boxes of documents relating to the Norshield Investment Structure had been transported from Chicago, Illinois to the Minnesota Horse and Hunt Club. The Receiver successfully obtained a court order in Minnesota authorizing the immediate seizure and delivery of documents related to the Norshield Investment Structure located there. Approximately 36 boxes were ultimately recovered, which contained information that proved useful in the Receiver's investigation.

[262] Xanthoudakis and Smith submit that there is no evidence to suggest anyone was trying to do anything improper with the documents transported to the Minnesota Horse and Hunt Club. They submit that there is no record of the Receiver communicating with anyone to obtain these records on a voluntary basis and therefore no evidence that anyone would have resisted providing those records.

4. Conclusion

[263] The Respondents have submitted that they were not responsible for maintaining the books and records of the entities in the Norshield Investment Structure below the Olympus Bank / Olympus Uninvest level. While we do not find the Respondents had direct responsibility under the Act for maintaining the books and records of those entities, we find, however, that Mosaic Composite and the Channel Funds were so integral in the value chain to investors (so fundamental to the investment structure) that better information relating to their activities and assets should have been available. Given the number of transactions that we have discussed earlier relating to option transactions and MS-II, it is clear that Xanthoudakis and Smith were not at arm's length to Mosaic Composite and the Channel Funds. The Respondents should have been able to make this information available to the Receiver and others looking for an explanation of the investment structure.

[264] Further, we find that NAM's and Olympus United Group's failure to maintain adequate records of significant transactions involving the uses of investors' funds and events affecting the value of their investments was contrary to section 19 of the Act and section 113 of Ontario Regulation 1015. In particular, NAM and Olympus United Group did not provide, and therefore presumably did not have, up-to-date records of subscriptions and redemptions, sufficient supporting documents for the NAV calculations, documentation regarding the in-kind investments made at the Olympus Uninvest level, documents regarding the Unexplained Payments made by Olympus Bank

and Mosaic Composite, copies of the investment agreement between Olympus Uninvest and Mosaic Composite, copies of the agreement between Mosaic Composite and RBC in regard to the SOHO Option, and other relevant documents.

[265] We have not been presented with sufficient evidence to come to any conclusions with regard to the documents held at the Minnesota Horse and Hunt Club. The source of these documents is not clear and we have not been able to determine whether they were under the control of any of the Respondents. We note that Staff and the Receiver never attempted to gain access to the documents held by Norshield Investment Partners Inc. (U.S.) in the United States.

D. As a consequence of their positions of seniority and responsibility and in their positions as officers and directors of NAM and/or Olympus United Group, did Xanthoudakis and Smith authorize, permit or acquiesce in the alleged violations of the requirements of Ontario securities laws and breaches of duties discussed in B and C above?

1. The Law

[266] Staff alleged that Xanthoudakis and Smith authorized, permitted or acquiesced in violations of securities law by Olympus United Group and NAM. Director and officer liability for securities law breaches is set out in subsection 122(3) and section 129.2 of the Act. Subsection 122(3) states:

s. 122(3) Directors and officers – Every director or officer of a company or of a person other than an individual who authorizes, permits or acquiesces in the commission of an offence under subsection (1) by the company or person, whether or not a charge has been laid or a finding of guilt has been made against the company or person in respect of the offence under subsection (1), is guilty of an offence and is liable on conviction to a fine of not more than \$5 million or to imprisonment for a term of not more than five years less a day, or to both.

[267] Similarly, section 129.2 states:

s. 129.2 Directors and officers – For the purpose 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,

2. Analysis and Conclusion

[268] Given our determination that Xanthoudakis and Smith were directing minds of the Norshield Investment Structure, and the clear evidence that they were officers and/or directors of NAM and Olympus United Group, it is clear that Xanthoudakis and Smith are liable for the breaches of Ontario securities laws described in B and C above.

[269] We have already concluded that Xanthoudakis and Smith did not deal fairly, honestly and in good faith with investors in B, above. Even had we not concluded that they breached their duties personally, we would still find them liable for NAM's and Olympus United Group's breaches as directing minds and as directors and/or officers of the corporations. Their knowledge of the artificially inflated NAVs and their connections to the MS-II and third party payment transactions are evidence that they, at a minimum, authorized, permitted or acquiesced in these breaches of duties. Their direct involvement in these transactions demonstrates a much closer relationship than they acknowledge.

[270] In their roles as directors and officers, Xanthoudakis and Smith had a responsibility to ensure that NAM and Olympus United Group properly discharged their responsibilities. As directing minds of the Norshield Investment Structure they were in a position to have access to the relevant information that should have been included in NAM's and Olympus United Group's records, including relevant records of subscriptions and redemptions and NAV calculations.

E. Did the Offering Memorandum filed and distributed by Olympus United Group contain misleading information and/or fail to state facts which were required to be stated?

[271] Staff allege that the offering memorandum filed and distributed by Olympus United Group contained misleading or untrue information and/or failed to state facts which were required to be stated, in contravention of clause (b) of subsection 122(1) of the Act.

1. Submissions

Staff

[272] Staff submit that the offering memorandum used by NAM and Olympus United Group to market shares in Olympus United Funds was materially misleading in several respects.

[273] Staff submit that the offering memorandum should have made reference to: investments other than the segregated asset cells of Olympus Bank, the high degree of leverage that would be used, the fact that this leverage would be supported by investments in private companies and the involvement of foreign jurisdictions, in addition to Barbados. According to Staff, only a small percentage of investor funds were allocated in the manner described in section 2.6 of the offering memorandum through investments,

multi-manager alternative investment portfolios, proprietary index trading and futures trading strategies.

[274] Staff submit that the offering memorandum did not disclose that a high degree of leverage would be used or that this leverage would be supported or collateralized by investments in private companies held by the Channel Funds. Staff insist that the risks of these leveraged investments, particularly with respect to liquidity, should have been identified. It is Staff's position that there is no evidence of any intention to inform investors of this higher level of risk. They submit that investors needed to know these risks in order to make sensible investment decisions.

[275] Staff submit that the offering memorandum should have disclosed that investment funds from Olympus United Funds would be commingled with other funds, regardless of the investment strategy selected and should have accurately described the manner in which NAVs would be calculated. They submit that the NAVs reported to investors were based exclusively on Mosaic Composite's hedged assets and assets at the Olympus Bank level less fees and expenses, so that the leverage was not included in the NAV calculations. Staff point out that there is no mention of Mosaic Composite in the offering documents for Olympus United Funds.

Xanthoudakis and Smith

[276] Xanthoudakis and Smith submit that the offering documentation given to investors was accurate and correctly characterized the nature of the investment. They take the position that the offering documents accurately represented the product the way it was intended to work until events transpired to cause the funds to fail, and that is the way it did work.

[277] Xanthoudakis and Smith submit that they, NAM and the other entities within the Norshield Investment Structure intended to provide investors with what they were told they would receive in the offering memorandum: a return based on a reference portfolio that happens to be very complex. They submit that the rate of return passed on to investors was exactly as represented in the offering memorandum.

[278] In response to Staff's allegation that they should have disclosed what was happening to investor funds below the Olympus Bank level, Xanthoudakis and Smith assert that it is not unusual for investors to receive a return based on a reference fund or portfolio without all the assets invested residing in that fund or portfolio. It is their submission that many financial institutions accept investments that are essentially leveraged, while providing a contractual right of return to investors.

[279] Xanthoudakis and Smith contest the allegations regarding a lack of disclosure relating to the significant leverage of the funds and their support by a portfolio of illiquid private equity investment. They submit that it was the intention of the structure to provide returns based on the performance of the managed account portfolio and that until the structure collapsed, this is exactly what investors did receive. They submit that this was also what was reported to investors through the NAV calculations. They contend that there are many structured products on the market which use significant leverage, and

submit that this can be a method of reducing risk. They suggest that a detailed description of the leverage structure was not required in the offering memorandum.

[280] Xanthoudakis and Smith submit that Cardinal was responsible for the NAV calculations for the SOHO Option and the tactical trading accounts up to 2004. They therefore argue they are not responsible for any errors in the calculation.

[281] Xanthoudakis and Smith do not deny that investor funds were used to meet redemption requests, but it is their submission that there is no rule that indicates that this would be improper when the funds had not yet been applied within the investment structure.

2. The Law

[282] Subsection 122(1)(b) of the Act read as follows:

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

...

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

...

is guilty of an offence and on conviction is liable to a fine of not more than \$5 million or to imprisonment for a term of not more than five years less a day, or to both.

[283] Staff allege that the offering memorandum contained misleading statements, and that Olympus United Group was in breach of s. 122(1)(b) when the offering memorandum was delivered pursuant to the accredited investor exemption under OSC Rule 45-501, s. 6.4:

s. 6.4 Delivery of Offering Memorandum – If an offering memorandum is provided to a prospective purchaser, the seller must deliver to the Commission a copy of the offering memorandum or any amendment to a previously delivered offering memorandum within 10 days of the date of the distribution.

3. Analysis – content of the offering memorandum

[284] The investments in Olympus United Funds were sold pursuant to the accredited investor exemption, under OSC Rule 45-501.

[285] The Olympus United Funds offering memorandum dated June 21, 2004 generally described a structure by which Canadian retail investors could gain access to a fund of funds managed by various hedge fund managers and an overlay program representing up to 15% of the assets invested in derivatives based strategies.

[286] The offering memorandum describes the investment objective generally as follows:

Investment Objective

The broad investment objective of each fund is to obtain a positive absolute return that is uncorrelated with traditional investment strategies by allocating investments to multi-manager alternative investment portfolios, proprietary index timing and futures trading strategies. Each Fund described in this offering memorandum has its own specific objectives ...

Exhibit 3, tab 1 – Olympus United Funds Offering Memorandum, June 21, 2004 at 8.

[287] The specific investment objective and strategy differed among the various funds. The offering memorandum provides the following descriptions in respect of the Olympus United Uninvest II Fund represented by the Class I Redeemable Convertible Non-Voting Shares:

Investment Objective

The Funds' investment objective is to provide a superior yield while maintaining a low degree of volatility and correlation relative to major global markets. The Funds attempt to achieve this objective through allocation of assets to both traditional and non-traditional strategies.

Investment Strategy

The portfolio of the Funds at any one time may be comprised of investments in managed accounts, private placements, bond arbitrage, convertible bonds and preference shares, mortgage-backed securities, debentures, foreign exchange contracts, hedge funds, United States and Canadian government treasury bills, commodities, futures, options, equities, money market instruments, and other interest-bearing obligations including interests in other investment companies, funds and pools. Diversification in types of securities, advisors and strategies will seek to normalize returns and minimize risk. Investments will typically be made in established investment funds and advisors with proven performance growth.

...

The Olympus United Hedge Overlay Program

The Olympus United Hedge Overlay Program (the “Overlay Program”) is a proprietary strategy designed to reduce portfolio risk and volatility as well as to enhance the returns of the Portfolio managers. The Overlay Program is an allocation of up to approximately 15% of the assets of the Fund that is further allocated among a team of additional Portfolio Managers specializing in long/short investments in global equity, fixed income and commodity derivative instruments. The current team of such Portfolio Managers consists of Mondiale Asset Management Ltd., TWR Management Corp. and NAM Canada.

Exhibit 3, tab 1 – Olympus United Funds Offering Memorandum, June 21, 2004, Appendix F at 1.

[288] The Class I shares represented approximately 70% of the issued capital of Olympus Uninvest on September 30, 2003.

[289] While the offering memorandum contained references to the potential use of leverage by the various hedge fund managers, it made no reference to the type or extent of the leverage that was inherent in the SOHO Option nor the fact that the leverage would be collateralized by investments in private companies.

[290] Mosaic Composite’s investment strategy was not that of an investment in a portfolio of hedge funds as described in the offering memorandum. Rather, it participated in a leveraged instrument in a portfolio of hedge funds with an indirect investment in a portfolio of private companies. Massi testified that the non-hedged assets of Mosaic Composite represented \$307 million, which were primarily investments in the Channel Funds.

[291] Even if we accept that the leverage inherent in the SOHO Option was contemplated by the offering memorandum, the allocation of funds to investments in private companies as collateral dramatically changed the nature of the investment. If the collateral funds had been invested in less risky assets such as government treasuries or money market funds, the leverage may have impacted returns, but might not have impacted the investment objective.

[292] The fact remains that because of the dissipation of investor funds at various points throughout the Norshield Investment Structure, only a small portion of investor funds made their way to the hedge fund managers. Massi testified that “[in] later years, most of the money never went down to the bank. It stayed at the fund level” (Hearing Transcript, November 4, 2008, p. 144). Consequently, the use of leverage was required in order to provide the hedge fund managers with sufficient funds and to ensure that a diverse set of assets could be achieved.

4. Analysis – issuer of the offering memorandum

[293] Olympus United Group marketed shares of Olympus United Funds to investors, but the offering memorandum was that of Olympus United Funds and it was Olympus United Funds that was required to deliver its offering memorandum to the Commission, not Olympus United Group.

[294] Liability under s. 122(1)(b) attaches to persons or companies that make misleading or untrue statements or fail to state a fact that is required to be stated so as to not make a statement misleading. However, Staff's allegation was against Olympus United Group only. Statements in the offering memorandum were made by Olympus United Funds, and not by Olympus United Group.

[295] Although Olympus United Group was involved in the marketing of securities for which it is alleged that the offering memorandum was misleading, s. 122(1)(b) does not apply to the allegation of misconduct by Olympus United Group in this situation.

5. Conclusion

[296] We find that the offering memorandum issued by Olympus United Funds was materially misleading with respect to the actual investment structure, the type of leverage used and the risks involved in the leverage. Information on the investment structure at the Mosaic Composite level and below should have been disclosed to investors.

[297] As the issuer of the offering memorandum, Olympus United Funds would be the entity to which liability would attach under s. 122(1)(b). However, Olympus United Funds is not a Respondent in this matter.

[298] Staff's allegation regarding the offering memorandum is levelled at Olympus United Group, but the offering memorandum is that of Olympus United Funds. In the circumstances, Staff's allegation against Olympus United Group is not made out.

F. As a consequence of their positions of seniority and responsibility and in their positions as officers and directors of Olympus United Group, did Xanthoudakis and Smith authorize, permit or acquiesce in the alleged violations of the requirements of Ontario securities laws and breaches of duty discussed in E, above?

[299] Staff's allegation against Xanthoudakis and Smith regarding the offering memorandum requires a breach of s. 122(1)(b) of the Act by Olympus United Group. As explained above, although we find that the offering memorandum of Olympus United Funds was misleading, we find that there was no breach of s. 122(1)(b) of the Act by Olympus United Group. Therefore, we cannot find that Xanthoudakis and Smith breached Ontario Securities law in respect of the misleading offering memorandum of Olympus United Funds as a consequence of their positions of seniority and authority or as officers and directors of Olympus United Group.

G. Did Xanthoudakis and Smith knowingly make statements and provide evidence and information to Staff that was materially misleading and/or fail to state facts which were required to be stated in an effort to hide violations of Ontario securities laws?

[300] Staff allege that Xanthoudakis and Smith knowingly made statements and provided evidence and information to Staff that was materially misleading and failed to state facts which were required to be stated in an effort to hide violations of Ontario securities laws, contrary to subsection 122(1)(a) of the Act.

1. Submissions

Staff

[301] Staff submit that Xanthoudakis and Smith materially misled them regarding the movement of funds through the Norshield Investment Structure. According to Staff, Xanthoudakis and Smith completely failed to inform them of the existence of the Channel Funds during their on-site compliance review at NAM's offices. Staff assert that Xanthoudakis and Smith led them to believe that the majority of the funds invested were placed with US hedge fund managers chosen by NAM through RBC, or in in-house tactical trading and managed futures accounts managed by NAM. According to Staff, they made no mention of a collateral portfolio of less liquid securities used to support the structure.

[302] In addition to this failure to inform Staff of the Channel Funds and their role, Staff submit that Smith directed the alleged independent director of Channel Funds to "play dumb" when questioned by Staff.

[303] Staff state that, at a minimum, registrants have an obligation to disclose what is being done with investor money and where it has gone. They submit that Xanthoudakis and Smith misled Staff regarding this information.

[304] According to Staff, the fact that the structure is complex is not an excuse for the failure to disclose required information to the Commission. Staff submit that there is an obligation on people responsible for an investment structure to be able to clearly and concisely explain to the regulator how it works and how client money flows.

[305] Staff submit that Xanthoudakis's and Smith's decision to limit their description of the Norshield Investment Structure to the level of the SOHO Option is materially misleading and contrary to Ontario securities law.

Xanthoudakis and Smith

[306] Xanthoudakis and Smith submit that they did not intend to mislead Staff regarding the Channel Funds or the investee companies at the Mosaic Composite level.

[307] They argue that it would be "absurd" to think that the assets supporting the SOHO Option could be concealed from a regulator in light of the way the structure worked and

the exposure provided by the RBC platform, and that the Receiver (then as the Monitor) became well aware of the Channel Funds shortly after Staff completed its on-site compliance review.

[308] Xanthoudakis and Smith note that it was NAM that first approached the Commission, and not the other way around. They submit that NAM approached the Commission because its management was essentially in a crisis mode dealing with other litigation and they were concerned about the liquidity crisis they were experiencing. Xanthoudakis and Smith further submit that the Norshield Investment Structure is complex, so there was a lot to explain and that NAM was in crisis mode at the time of the on-site compliance review. They submit that Xanthoudakis expected that he would meet with Staff again after the initial on-site interview.

[309] In response to Staff's assertions that Xanthoudakis and Smith have not provided Staff and the Receiver with information on the location of investor funds, they submit that it has become difficult for them to access the necessary information in order to provide an explanation or an accounting since they have been removed from the organization and the Receiver has taken over.

[310] Xanthoudakis and Smith submit that an inference that the Respondents did not cooperate with Staff should not be drawn from the fact that Staff and the Receiver have been unable to complete their inquiry into the flow of investor funds. They provide evidence that Smith offered his services to assist the Receiver on a consulting basis to help track the funds and obtain the cooperation of individuals in control of Mosaic Composite. Xanthoudakis and Smith submit that no adverse inference should be drawn from the fact that Staff and the Receiver rejected Smith's offer of assistance.

2. The Law

[311] Subsection 122(1)(a) of the Act reads as follows:

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

(a) makes a statement in any material, evidence or information submitted to the Commission, a Director, any person acting under the authority of the Commission or the Executive Director or any person appointed to make an investigation or examination under this Act that, in a material respect and at the time and in the light of the circumstances under which it is made, is misleading or untrue or does not state a fact that is required to be stated or that is necessary to make the statement not misleading;

...

is guilty of an offence and on conviction is liable to a fine of not more than \$5 million or to imprisonment for a term of not more than five years less a day, or to both.

3. Analysis

[312] According to Radu's testimony on May 9, 2005, prior to an on-site review by Staff, Smith, Karine Simoes and counsel for NAM voluntarily met with Staff in Toronto to explain the halt in redemptions.

[313] Staff subsequently conducted an unannounced on-site compliance review at NAM's offices in Montreal from May 16, 2005 to May 19, 2005. During this review Staff interviewed Smith two separate times, on May 17, 2005 and May 19, 2005 and interviewed Xanthoudakis once on May 19, 2005.

[314] In total, four Staff investigators participated in the on-site compliance review in Montreal. Their handwritten notes, made at the time of the examinations or soon after, were put into evidence. In addition, two of Staff's investigators who were present at the on-site compliance review testified before us.

[315] Walz testified that neither Xanthoudakis nor Smith informed Staff that Mosaic Composite had any investments in Canadian private equities, nor that the Norshield Investment Structure was supported by anything other than what was in the managed accounts.

[316] Nor were the investigators informed of the role of the Channel Funds. Walz testified that it was his understanding that there was an overlay program whereby up to 15 percent of investors' monies would be invested with a third party or with NAM to reduce the volatility and risk to investments. He testified that he was led to believe that the Olympus United Funds was a fund of funds where investments in each share class of Olympus United Funds would flow to Olympus Bank, which would fulfill the specific investment objective of each share class.

[317] The notes by Staff members that were put into evidence corroborate the above. A flowchart of the Norshield Investment Structure created shortly after the on-site review by a member of Staff makes no reference to the Channel Funds.

4. Conclusion

[318] We accept that NAM was in "crisis mode" at the time of the on-site compliance review, as described by counsel for Xanthoudakis and Smith, and that Xanthoudakis offered to meet with Staff again at the conclusion of his examination on May 19, 2005. However, the role of the Channel Funds in the Norshield Investment Structure was crucial, and yet it was undisclosed to Staff. As discussed above, the Channel Funds supported the significant leverage in the SOHO Option, and sustained the NAV calculations.

[319] Despite the corporate complexity that relates to tax and legal issues, the investment premise is not particularly complex to describe and we do not accept the complexity argument put forth by the Respondents.

[320] This is not a situation where Xanthoudakis and Smith mentioned the Channel Funds, but failed to describe them in full detail, given the circumstances. They did not

mention their existence at all to Staff. We find that this failure to mention the Channel Funds at all during Staff's four day on-site review materially misled Staff, and was thus contrary to subsection 122(1)(a) of the Act.

H. Was the course of conduct engaged in by Xanthoudakis, Smith and Kefalas abusive to the integrity of Ontario's capital markets, did it compromise the integrity of Ontario's capital markets, or was it otherwise contrary to the public interest?

[321] Staff allege that the conduct of Xanthoudakis, Smith and Kefalas was abusive to the integrity of Ontario's capital markets and contrary to the public interest.

1. Submissions

Staff

[322] Staff submit that Xanthoudakis and Smith acted contrary to the public interest in their failure to inform Staff of essential components of the Norshield Investment Structure, their failure to keep compliant books and records, their provision of misleading information in the offering memorandum for Olympus United Funds and in their breach of their duty to deal fairly, honestly and in good faith with investors.

[323] Staff submit that Kefalas's failure to fulfill his responsibilities as the designated Compliance Officer and Ultimate Responsible Person for NAM was contrary to the public interest.

Xanthoudakis and Smith

[324] As outlined above, Xanthoudakis and Smith contend that they acted properly. They submit that their actions with respect to Staff, investors, the preparation of the offering memorandum, and books and records was not contrary to the public interest.

Kefalas

[325] Kefalas submits that his actions were not contrary to the public interest. He contends that he was never aware of having a compliance role in NAM and that he signed the Commission filings at the behest of NAM's legal counsel, who handled all compliance issues. He submits that between May 31, 2000 and February 13, 2003 he was never called upon to fulfill the role of Compliance Officer for NAM.

[326] Kefalas submits that his conduct was at most negligent, and was not designed for his own gain at the expense of investors and the integrity of Ontario's capital markets. Kefalas therefore claims that he poses no potential for future harm to the public.

2. The Law

[327] The Commission has a public interest jurisdiction to prevent likely future harm to Ontario's capital markets (*Committee for the Equal Treatment of Asbestos Minority*

Shareholders v. Her Majesty in Right of Quebec, [2001] 2 S.C.R. 132 at para. 42). The scope of the Commission's discretion in defining the public interest is limited by the general purposes of the Act (*Gordon Capital Corp. v. Ontario (Securities Commission)* (1991), 14 O.S.C.B. 2713 (Ont. Ct. J.) at para. 37).

3. Analysis

[328] As noted earlier, from May 31, 2000 to February 19, 2003, Kefalas was NAM's designated Compliance Officer, and from August 25, 2004 to November 19, 2004 he was the Ultimate Responsible Person.

[329] Kefalas testified before us, and acknowledged that he had signed the documents filed with the Commission making him NAM's designated Compliance Officer and Ultimate Responsible Person for certain periods, but stated that he did not believe himself to be the acting compliance officer at NAM:

I'm not here to contest the signature, my signature on the documents that are present and filed with the OSC, but my belief at the time and still is, or is currently looking back, that Miss Karine Simoes was the acting compliance person for the firm.

In fact, I cannot recall any instances where other personnel of the firm came up to me to ask me to fulfill any kind of compliance issues or to give them any opinions on any compliance related issues.

Hearing Transcript, November 13, 2008, p. 125.

[330] Only a small fraction of the \$159 million invested by Canadian retail investors will be recovered, according to the Receiver. The fact that Xanthoudakis and Smith have not provided any explanation to the Receiver for that deficit deeply concerns us, and is conduct abusive to the integrity of the capital markets. Given their positions of seniority in the Norshield Investment Structure, as well as their positions as officers and directors of NAM and Olympus United Group, they were responsible for accounting for funds invested by Canadian retail investors.

4. Conclusion

[331] The roles of a Compliance Officer and an Ultimate Responsible Person are crucial to the regulation of the capital markets. By registering with the Commission as a Compliance Officer and Ultimate Responsible Person, Kefalas accepted certain responsibilities. Those who accept such roles are required to understand the seriousness of their undertakings. Consequently we find that Kefalas' failure to fulfill his responsibilities as a Compliance Officer and Ultimate Responsible Person constitutes conduct contrary to the public interest.

[332] Mitigating factors, such as his belief that NAM's legal counsel, Karine Simoes, was in practice the person responsible for compliance in the firm, or the fact that he was never asked by NAM to fulfill any compliance function, can be put to a hearing panel considering potential sanctions against Kefalas.

[333] As a result of this failure to account for funds and our findings in relation to the other allegations, discussed above, we find that Xanthoudakis's and Smith's conduct was contrary to the public interest.

III. CONCLUSION

[334] We find that the Respondents were in breach of their obligations under Ontario securities laws, for all the reasons discussed in our analysis above:

- (i) NAM, Olympus United Group, Xanthoudakis and Smith failed to deal fairly, honestly and in good faith with investors, contrary to subsections 2.1(1) and 2.1(2) of OSC Rule 31-505;
- (ii) NAM and Olympus United Group failed to keep and maintain proper books and records in relation to the Norshield Investment Structure, contrary to section 19 of the Act and section 113 of Ontario Regulation 1015 of the Act;
- (iii) as a consequence of their positions of seniority and responsibility and in their positions as officers and directors of NAM and Olympus United Group, Xanthoudakis and Smith authorized, permitted and acquiesced in the breaches of Ontario securities laws in (i) and (ii), above;
- (iv) Xanthoudakis and Smith knowingly made statements and provided evidence and information to Staff that was materially misleading and failed to state facts which were required to be stated in an effort to hide violations of Ontario securities laws, contrary to clause (a) of subsection 122(1) of the Act; and
- (v) Xanthoudakis, Smith and Kefalas engaged in a course of conduct that was abusive to and compromised the integrity of Ontario's capital markets and was contrary to the public interest.

[335] The parties shall contact the Secretary's office within 10 days to schedule a hearing to determine the appropriate sanctions.

DATED at Toronto this 8th day of March, 2010.

"Wendell S. Wigle"

Wendell S. Wigle, Q.C.

"David L. Knight"

David L. Knight, F.C.A.

"Margot C. Howard"

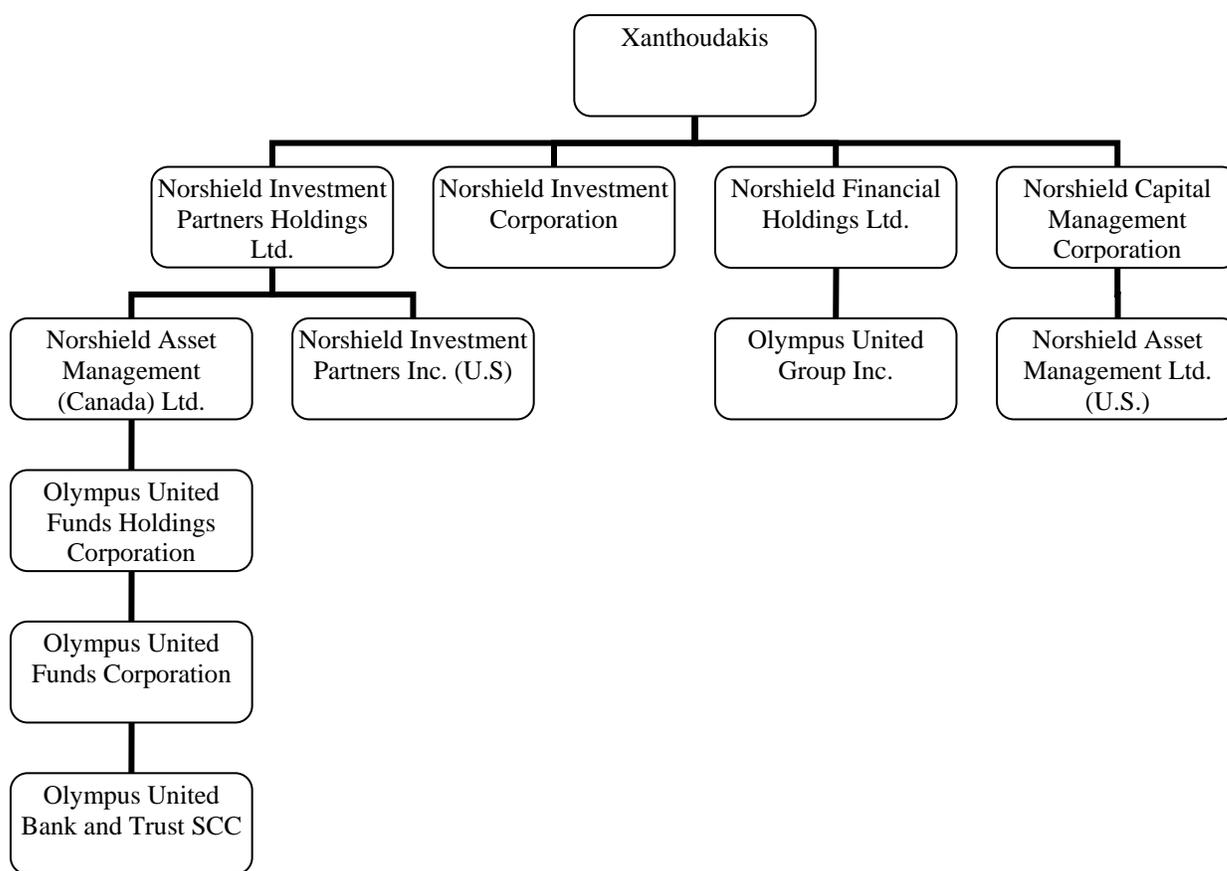
Margot C. Howard, CFA

APPENDIX A
Some Entities Referred to in the Decision

[1] The investment structure considered in this Decision involved a large number of corporate entities and significant transactions with others. To provide some background to our analysis, these entities are briefly described below.

Corporate Entities Fully within the Norshield Investment Structure

[2] Xanthoudakis owned, either directly or indirectly, many of the entities within the Norshield Investment Structure, including the eleven described below.



Norshield Financial Group (“NFG”) is a trade name for the overall corporate structure and does not appear to be an incorporated entity. However, in a June 2004 investment proposal submitted to TD Bank Financial Group, NFG describes itself as a Delaware corporation based in Chicago that is a subsidiary of the Canadian corporation Norshield Investment Partners Holdings Inc. According to a chart provided to Staff during an on-site compliance review at Norshield Asset Management (Canada) Ltd.’s offices in Montreal, NFG included Norshield Financial Holdings Ltd., Olympus United Group Inc., Norshield Investment Partners Holdings Ltd., Norshield Asset Management

(Canada) Ltd., Olympus United Funds Holding Corporation, Olympus United Funds Corporation, Olympus United Bank & Trust SCC and Norshield Investment Partners Inc. (U.S.A.). All of the entities in NFG are listed on the chart as being directly or indirectly owned in their entirety by Xanthoudakis. An earlier document also includes Norshield Capital Management Corporation, Norshield Investment Corporation and Norshield Asset Management Ltd. (U.S.) in the NFG.

Norshield Investment Partners Holdings Ltd. (“Norshield Partners”) is wholly owned by Xanthoudakis. According to an organization chart provided to the Receiver, Norshield Partners is the owner of Norshield Asset Management (Canada) Ltd. and of Norshield Investment Partners Inc.

Norshield Asset Management (Canada) Ltd. (“NAM”) provides portfolio management services to Olympus United Funds Corporation. NAM is a Canadian corporation and it appears that NAM is wholly owned by Norshield Partners or Norshield Capital Management Corporation, both corporations owned by Xanthoudakis. NAM previously carried on business as GIC Commodity Advisors of USA, GIC Asset Management Ltd., and Norshield Asset Management Ltd. NAM’s officers include Xanthoudakis, Smith and Kefalas and its directors include Xanthoudakis and Kefalas.

Olympus United Funds Holdings Corporation owns Olympus United Funds Corporation and is owned by NAM. Smith was President and Chief Executive Officer and a director and officer of this corporation.

Olympus United Funds Corporation (“Olympus United Funds”) offered a hedge fund product that enabled investors to pursue particular investment strategies. It held 100 percent of the voting shares of Olympus United Bank and Trust SCC. Non-voting shares in Olympus United Funds were marketed to Canadian retail investors by Olympus United Group Inc. and the funds invested were managed by NAM. The \$159 million invested in the Norshield Investment Structure by Canadian retail investors was invested through Olympus United Funds. Smith was a director and the President and CEO of Olympus United Funds. Prior to its name change in 2003, Olympus United Funds was incorporated as First Horizon Holdings Ltd.

Olympus United Bank and Trust SCC (“Olympus Bank”) is a licensed offshore bank based in Barbados. It is a subsidiary of Olympus United Funds and a part of NFG. Smith was a director and the chairman and CEO of Olympus Bank. Prior to 2003, Olympus Bank operated as First Horizon Bank (Barbados) Inc. Olympus Bank is also the investment manager to Olympus Uninvest Ltd.

Norshield Investment Partners Inc. is a NFG corporation wholly owned by Xanthoudakis through Norshield Partners. It was incorporated in the United States and maintained an office in Chicago. Xanthoudakis was a director.

Norshield Investment Corporation (“NI Corporation”) is a corporation in the NFG that acts as a nominee to hold equity interests in publicly traded and private equities on behalf of offshore investors. Xanthoudakis is a director and officer as well as the owner of NI Corporation. NI Corporation now operates under the name Honeybee Software Technology Ltd.

Norshield Financial Holdings Ltd. (“Norshield Financial Holdings”) is wholly owned by Xanthoudakis, who is also a director and officer of the corporation. It is a part of the NFG and owns Olympus United Group Inc.

Olympus United Group Inc. (“Olympus United Group”) is a Canadian federal corporation registered as a mutual fund dealer and limited market dealer. It provided marketing services to Olympus United Funds. It is wholly owned by Norshield Financial Holdings, which is owned by Xanthoudakis. Xanthoudakis was the President and CEO and a director of Olympus United Group. Smith is an officer of Olympus United Group. From 1994 until May 2002 Olympus United Group carried on business as Norshield Fund Management Ltd.

Norshield Capital Management Corporation (“NCMC”) is owned by Xanthoudakis. Corporate records, including a July 2001 organization chart and NAM’s OSC registration documents filed in December 1999 indicate that NAM is a subsidiary of NCMC. NCMC was a corporation in the NFG that acted as a nominee to hold equity interests in publicly traded and private equities on behalf of offshore funds.

Norshield Asset Management Ltd. (U.S.) is an American company that provides risk management and asset allocation services. It is owned by NCMC.

Other Entities Associated with the Norshield Investment Structure

[3] Other entities that may not have been owned wholly or in part by the Respondents, but that were involved in the overall Norshield Investment Structure are described below. They include corporations through which investment funds flowed, entities that were involved in transactions related to the Norshield Investment Structure, and entities with an investment management role.

BICE International Inc. (“BICE International”) is a Bahamian corporation and apparently the sole shareholder in Olympus Uninvest Ltd. BICE International bought Emerald Key Management Ltd. from the Channel Funds in July 2003. BICE International is listed as owning management shares in Mosaic Composite (U.S.) Inc., along with Orion Trust.

Olympus Uninvest Ltd. (“Olympus Uninvest”) is a Bahamian hedge fund that received investment funds both directly from investors, and through Olympus Bank. As of 2003, Olympus Uninvest had direct investments in nine strategy-specific funds, which

in turn invested in other funds. Some of these funds are listed below. Smith was a director of Olympus Uninvest. Olympus Uninvest was dissolved in May 2005 as a result of redemption requests that it was unable to satisfy.

Olympus Uninvest Global Fund Ltd. was a European fund that operated out of the Cayman Islands and was listed on the Irish Stock Exchange. NAM was its investment manager and Xanthoudakis was one of its directors.

Olympus Uninvest Convertible Arbitrage Fund Ltd. and **Uninvest High Yield Fund Ltd.** (together, the “Uninvest Purchasers”) are investment entities of Uninvest Global Fund. They are Cayman Islands entities, for which Xanthoudakis is one of the directors and NAM is the investment manager.

Olympus Uninvest Equity Long Short Fund is a Cayman Islands entity for which Xanthoudakis is one of the directors and NAM is the investment manager.

Olympus Uninvest Multi-Strategy II Fund (“MS-II”) is a Cayman Islands entity for which Xanthoudakis is one of the directors and NAM and Norshield Investment Partners Inc. were each listed as the investment manager in different documents.

Olympus Uninvest Fixed Return Fund Ltd. was a Bahamian fund set up in 2000 as a mirror fund for the Balanced Return Fund Limited. It was wound down in 2003 with all shares being exchanged for shares in the Balanced Return Fund Limited. Uninvest Fixed Return Fund Ltd. was an investee of Emerald Key Advisors Ltd.

Olympus Balanced Return Fund Limited was a Bahamian fund that formerly operated as Uninvest Entry Fund Ltd. Shares in this fund were held by Emerald Key Management Ltd. Norshield International was the Business Manager prior to September 2002 when Emerald Key Management became the Fund Manager and Emerald Key Advisors became the Distribution Agent.

Cardinal International Funds Services Ltd. (“Cardinal”) is a Bahamian entity and was the Administrator, Registrar and Transfer Agent for Mosaic Composite (U.S.) Inc. and Olympus Uninvest.

Commax Management is an entity that received payments from Mosaic Composite (U.S.) Inc.

Emerald Key Advisors Inc. is a financial advisor for international alternative funds of funds and is incorporated in the Bahamas.

Comprehensive Investor Services Ltd. (“CIS”), which has operated as Mendota Capital, Inc. since its merger with the company in January 2005, is the beneficiary of

Liberty Trust. CIS received unexplained payments from Olympus Bank and Mosaic Composite totalling over \$79 million.

Liberty Trust, formerly CIS Trust, is a trust with **Longview Associates** as the trustee and Thomas Muir as the settlor. Liberty Trust owns 100 percent of the equity voting shares of Mosaic Composite (U.S.) Inc.

Mosaic Composite (U.S.) Inc. (“Mosaic Composite”) is an entity originally incorporated and domiciled in the Bahamas and subsequently domiciled in the United States. Smith was a director of Mosaic Composite before it became domiciled in the United States in 2003. Mosaic Composite’s assets and liabilities were managed by Norshield Asset Management International Inc. and Cardinal was its Administrator, Registrar and Transfer Agent. Mosaic Composite held portfolios of hedged assets, which consisted of the SOHO Option, and non-hedged assets, which included investments in the Channel Funds.

RBC SOHO Option (the “SOHO Option”) is an option purchased by Mosaic Composite from the Royal Bank of Canada.

Channel Fixed Income Fund Ltd., Channel F.S. Fund Ltd., Channel Diversified Private Equity Fund Ltd., and Channel Technology Fund Ltd. (together, the “Channel Funds”) are Bahamian corporate entities holding investments primarily in Canadian private companies. They were originally incorporated as Tristar Funds.

AMT International Mining Corp. was a Channel Funds investee. Smith was an officer and director of AMT. As of December 1999, Xanthoudakis owned a 31% interest in AMT.

BDP Retirement Homes Inc. was a Channel Funds investee. Smith was on the BDP board of directors.

C-MAX Advantage Fund Ltd. was Bahamian corporation that was a Channel Funds investee. Norshield International Limited owned shares in the corporation.

Emerald Key Management Ltd. was a Channel Funds investee until the Channel Funds sold their interest in it to BICE International in September 2002.

Globe-X Management Ltd., Globe-X Canadiana Ltd., Globe-X Enhanced Yield Fund, Globe-X International, and Globe-X Asset Appreciation (together, the “Globe-X Entities”) were Bahamian corporations in which the Channel Funds invested.

Lonald Holdings N.V. was a Channel Funds investee.

Microslate Inc. was a Channel Funds investee, for which Smith was on the board of directors.

Mount Real Innovation Centre Inc. was a Channel Funds investee.

Niocan Inc. was a Channel Funds investee in which Xanthoudakis had a significant holding (16% in December 1999) and Smith was an officer / director.

Oceanwide.com Inc. was a Channel Funds investee for which Smith was on the board of directors.

Olympus United Holdings Ltd. was a Channel Funds investee.

Veza Composites Inc. was a Channel Funds investee for which Smith was on the board of directors.

Tessera Calisto Fund Ltd., Tessera Leda Fund Ltd., and Tessera Adtrastea Fund Ltd. (together, the “Tessera Funds”) are funds created and run by Mosaic Composite.

Mendota Capital, Inc. is a Minnesota corporation that merged with CIS in January 2005.

Norshield Asset Management International Inc. is the investment manager for Mosaic Composite.

Norshield International Limited owned shares in C-MAX Advantage Fund Ltd.

Orion Trust was established to avoid direct ownership of shares by Olympus Bank, which is the trustee for Orion Trust. Orion Trust owns the management shares in Mosaic Composite, with the beneficiary of these shares being a Mosaic fund.

Mount Real Corporation owns Mount Real Financial Management Services Corporation and is a corporation that Xanthoudakis formerly had a 14% interest in as of December 1999.

Mount Real Financial Management Services Corporation (“Mount Real”) is a wholly owned subsidiary of Mount Real Corporation. It did valuations of the Channel Funds debenture investments. Lino Matteo controls Mount Real, and Xanthoudakis is a former director of the company.

Real Vest Investment Ltd. is an entity related to Mount Real.

Sterling Leaf Income Trust is an entity related to Mount Real.

Silicon Isle entered into an escrow agreement with Hart, Saint-Pierre relating to a MS-II share transaction. Smith signed as a representative of Silicon Isle on a direction of payment relating to this agreement.