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

**- AND -**

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

**REASONS AND DECISION ON SANCTIONS AND COSTS  
(Sections 127 and 127.1 of the *Securities Act*)**

**Hearing:** June 23, 2014

**Decision:** September 11, 2014

**Panel:** James D. Carnwath, Q.C. - Chair of the Panel and Commissioner

**Appearances:** Michelle Vaillancourt - For Staff of the Commission

Alexander Gillespie - For North American Financial Group Inc., North American Capital Inc., Alexander Flavio Arconti and Luigino Arconti

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## REASONS AND DECISION ON SANCTIONS AND COSTS

### I. OVERVIEW

#### A. Background

[1] This was a hearing before the Ontario Securities Commission (the “**Commission**”) pursuant to sections 127 and 127.1 of the *Securities Act*, R.S.O. 1990, c. S.5, as amended (the “**Act**”) to determine whether it is in the public interest to order sanctions and costs against North American Financial Group Inc. (“**NAFG**”), North American Capital Inc. (“**NAC**”), Alexander Flavio Arconti (“**Flavio Arconti**”) and Luigino Arconti (“**Gino Arconti**”) (together, the “**Respondents**”). In this decision, I will refer to Flavio Arconti and Gino Arconti collectively as the “**Arcontis**”.

[2] On December 28, 2011, a Notice of Hearing was issued by the Commission in relation to a Statement of Allegations filed by Staff of the Commission (“**Staff**”) on the same day. The hearing on the merits in this matter was held on April 29 and 30, May 1-3, 6, 8-10, 22 and 23 and September 11, 2013 (the “**Merits Hearing**”). The Commission’s Reasons and Decision on the merits were issued on December 11, 2013 (*Re North American Financial Group Inc.* (2013), 36 O.S.C.B. 12095 (the “**Merits Decision**”)).

[3] A separate hearing was held on June 23, 2014 to consider submissions regarding the sanctions and costs to be imposed on the Respondents (the “**Sanctions and Costs Hearing**”). Staff and counsel for the Respondents appeared and made oral submissions. The Arcontis also appeared in person.

#### B. History of the Proceeding

##### 1. The Respondents’ Application under Section 144 of the Act

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

[5] On October 15, 2010, NAFG filed a Notice of Intention to make a proposal under the *Bankruptcy and Insolvency Act*, R.S.C. 1985, c. B-3, as amended (the “**BIA**”) on the basis that it was an insolvent person, pursuant to subsection 50.4(1) of the *BIA*.

[6] On January 6, 2014, Melotel Inc. (“**Melotel**”) applied to the Commission, pursuant to section 144 of the *Act* (the “**Application**”), for a partial revocation of the Temporary Order to allow the holders of NAFG debentures to have an opportunity to vote on a bankruptcy proposal concerning the exchange of NAFG debentures for shares in Melotel (the “**Melotel Proposal**”). Pursuant to the Melotel Proposal, all creditors of NAFG would be issued shares in Melotel in exchange for debts owed to them by NAFG in varying quantities proportionate to the nature and

amount of their debt. The Application provided that NAFG would forward a copy of the Melotel Proposal to the Commission once it was finalized and ready for presentation to the investors of NAFG. Staff opposed the Application and provided written submissions in support of its position, and counsel for Melotel provided further written submissions in response to Staff's submissions. The Respondents did not provide any submissions on the Application.

[7] On February 12, 2014, counsel for Melotel filed a copy of a proposal of NAFG made under subsections 50(2) and 62(1) of the *BIA*. On February 13, 2014, the Commission ordered that the Temporary Order be amended to permit the Melotel Proposal to be put before NAFG's creditors on certain conditions (the "**Melotel Carve-Out**") (*Re North American Financial Group Inc. et al.*, (2014) 37 O.S.C.B. 1920).

[8] A meeting of creditors was held on May 8, 2014, regarding a proposal in bankruptcy of NAFG. The creditors of NAFG refused the proposal, and therefore NAFG was assigned into bankruptcy on that date.

## 2. The Respondents' Adjournment Requests

[9] In the Commission's Order accompanying the Merits Decision dated December 11, 2013, the Commission ordered that the Sanctions and Costs Hearing would be held on March 24, 2014 and set a schedule for the delivery of written submissions of the parties (the "**Schedule**").

[10] On January 31, 2014, after receiving a Notice of Motion from former counsel for the Respondents to withdraw as their representative, the Commission granted leave to counsel to withdraw as counsel of record for the Respondents.

[11] On March 6, 2014, Alexander Gillespie notified the Commission that he had been retained to act for the Respondents. He requested an adjournment of the Sanctions and Costs Hearing from March 24, 2014 to March 28, 2014, and requested a modification to the Schedule. Staff did not oppose the Respondents' requests. On March 10, 2014, the Commission ordered that the Sanctions and Costs Hearing be adjourned to March 28, 2014 and updated the Schedule to provide an extension to the parties for their written submissions.

[12] On March 20, 26 and May 6, 2014, the Respondents requested three additional adjournments, along with corresponding requests to alter the Schedule. Staff did not object to the Respondents' requests made on March 20, 2014, but Staff did object to the requests made on March 26 and May 6, 2014. However, the Commission granted all requests made by the Respondents regarding the three adjournments of the Sanctions and Costs Hearing and the corresponding requests to vary the Schedule.

[13] On May 6, 2014, the Sanctions and Costs Hearing was most recently adjourned to June 23, 2014 and the Commission set an amended Schedule for the Respondents' written submissions (due on June 9, 2014) and Staff's reply submissions (due on June 16, 2014). On June 20, 2014, the Respondents filed their written submissions, the Affidavit of Gino Arconti sworn on June 20, 2014 (the "**Affidavit of Gino Arconti**") and a Sanction and Cost Submissions Brief. Staff did not file any written reply submissions on sanctions and costs.

## II. THE MERITS DECISION

[14] NAFG is a finance company in the business of the acquisition and servicing of subprime car leases in respect of cars that were acquired through 970910 Ontario Inc., operating as Prestige Motors, a used car dealership (“**Prestige Motors**”). NAC was organized to finance car leases that were conducted through NAFG. NAFG and NAC are not reporting issuers and are not registered under the *Act*.

[15] The misconduct of the Respondents involved the sale of non-prospectus qualified securities to investors. From September, 2007 to September, 2010, NAFG and/or NAC securities were sold by Carter Securities Inc. (“**Carter**”), a company that is not a named respondent in this matter. From September 17, 2007 until September 28, 2009, Flavio Arconti and Gino Arconti were registered as Officers and Directors (Trading Residents) and Shareholders of Carter. Flavio Arconti was also registered as the Designated Compliance Officer of Carter. Starting on September 28, 2009, Flavio Arconti was registered as the Chief Compliance Officer, Ultimate Designated Person and Dealing Representative of Carter, and Gino Arconti was registered as a Dealing Representative of Carter.

[16] On September 22, 2010, the Director issued a decision suspending Carter’s registration as an Exempt Market Dealer (the “**Director’s Decision**”). Although the Respondents were not named parties in the Director’s Decision, the Arcontis’ registration was automatically suspended as a result of that decision.

[17] Flavio Arconti and Gino Arconti are brothers and were registrants from September 17, 2007 to September 22, 2010. Flavio Arconti and Gino Arconti jointly owned NAFG, NAC, Carter and Prestige Motors and were the actual and/or *de facto* directors and officers of each of these entities. In a document entitled “Admissions of the Respondents” (Merits Hearing, Exhibit 1), the Respondents admitted that the Arcontis were the directing minds of NAFG, NAC, Carter and Prestige Motors.

[18] In the Merits Decision, I concluded that:

- (a) during the period September 29, 2009 to September 24, 2010, Carter’s actions constituted a breach of section 13.3 of [National Instrument 31-103 – *Registration Requirements, Exemptions and Ongoing Registration Obligations* (“**NI 31-103**”)] and was contrary to the public interest;
- (b) during the period September 17, 2007 to September 24, 2010, Carter’s actions constituted a breach of subsection 2.1(1) of OSC Rule 31-505 and was contrary to the public interest;
- (c) Flavio Arconti and Gino Arconti, as actual and *de facto* officers and directors of Carter, authorized, permitted or acquiesced in the non-compliance with Ontario securities law by Carter, and are therefore deemed to also have not complied with Ontario securities law, pursuant to section 129.2 of the *Act*;

- (d) during the period January 1, 2009 to September 24, 2010, the Respondents directly or indirectly engaged or participated in acts, practices or courses of conduct relating to the securities of NAFG and NAC that they knew or reasonably ought to have known perpetrated a fraud on persons contrary to subsection 126.1(b) of the *Act* and contrary to the public interest;
- (e) Flavio Arconti and Gino Arconti, as actual and *de facto* officers and directors of NAFG and NAC, authorized, permitted or acquiesced in the non-compliance with Ontario securities law by NAFG and NAC, and are therefore deemed to also have not complied with Ontario securities law, pursuant to section 129.2 of the *Act*; and
- (f) on September 24, 2010, Gino Arconti engaged in or held himself out as engaging in the business of trading in securities without being registered to do so in circumstances in which no exemption was available, contrary to subsection 25(1) of the *Act* and contrary to the public interest.

(Merits Decision, above at para. 338)

### **III. THE POSITION OF THE PARTIES**

#### **A. Staff's Submissions**

[19] Prior to the Sanctions and Costs Hearing, Staff filed its written submissions dated February 14, 2014, accompanied by a Brief of Authorities and a Sanction Brief. Staff also filed the Affidavit of Marcel Tillie sworn on March 6, 2014 and the Affidavit of Marcel Tillie sworn on June 16, 2014. The Affidavit of Marcel Tillie sworn on March 6, 2014 was entered as Exhibit 1 at the Sanctions and Costs Hearing, and the Affidavit of Marcel Tillie sworn on June 16, 2014 was entered as Exhibit 2.

[20] In its written submissions, Staff submitted that the following sanctions and costs against the Respondents are appropriate and in the public interest:

- (a) an order pursuant to clause 2 of subsection 127(1) of the *Act* that trading in any securities by NAFG, NAC, Flavio Arconti and Gino Arconti cease permanently;
- (b) an order pursuant to clause 2.1 of subsection 127(1) of the *Act* that the acquisition of any securities by each of NAFG, NAC, Flavio Arconti and Gino Arconti is prohibited permanently;
- (c) an order pursuant to clause 3 of subsection 127(1) of the *Act* that any exemptions contained in Ontario securities law do not apply to NAFG, NAC, Flavio Arconti and Gino Arconti permanently;
- (d) an order pursuant to clause 6 of subsection 127(1) to the *Act* that NAFG, NAC, Flavio Arconti and Gino Arconti be reprimanded;

- (e) an order pursuant to clause 7 of subsection 127(1) of the *Act* that Flavio Arconti and Gino Arconti resign any position that either of them holds as a director or officer of an issuer;
- (f) an order pursuant to clause 8 of subsection 127(1) of the *Act* that Flavio Arconti and Gino Arconti be prohibited permanently from becoming or acting as a director or officer of any issuer;
- (g) an order pursuant to clause 8.2 of subsection 127(1) of the *Act* that Flavio Arconti and Gino Arconti be prohibited permanently from becoming or acting as a director or officer of a registrant;
- (h) an order pursuant to clause 8.4 of subsection 127(1) of the *Act* that Flavio Arconti and Gino Arconti be prohibited permanently from becoming or acting as a director or officer of an investment fund manager;
- (i) an order pursuant to clause 8.5 of subsection 127(1) of the *Act* that NAFG, NAC, Flavio Arconti and Gino Arconti be prohibited permanently from becoming or acting as a registrant, as an investment fund manager or as a promoter;
- (j) an order pursuant to clause 9 of subsection 127(1) of the *Act* that each of NAFG, NAC, Flavio Arconti, Gino Arconti pay an administrative penalty of \$750,000, to be allocated to or for the benefit of third parties in accordance with subsection 3.4(2)(b) of the *Act*;
- (k) an order pursuant to clause 10 of subsection 127(1) of the *Act* that NAFG, Flavio Arconti and Gino Arconti disgorge to the Commission a total of \$2,441,392.42 for which they shall be jointly and severally liable, to be allocated to or for the benefit of third parties in accordance with subsection 3.4(2)(b) of the *Act*;
- (l) an order pursuant to clause 10 of subsection 127(1) of the *Act* that NAC, Flavio Arconti and Gino Arconti disgorge to the Commission a total of \$1,042,000 for which they shall be jointly and severally liable, to be allocated to or for the benefit of third parties in accordance with subsection 3.4(2)(b) of the *Act*; and
- (m) an order pursuant to subsection 127.1 of the *Act* that NAFG, NAC, Flavio Arconti and Gino Arconti pay \$283,843.75 of the costs of the investigation and hearing, for which they shall be jointly and severally liable.

[21] In its written submissions, Staff submitted that given the Commission's Order dated February 13, 2014, wording should be added to the market participating bans on NAFG to include the Melotel Carve-Out. However, on June 19, 2014, Staff sent an email to the Registrar and stated that, in view of NAFG's bankruptcy on May 8, 2014, the Melotel Carve-Out to the permanent market participation bans sought by Staff against NAFG was no longer necessary. In the email, Staff also indicated that it would not be seeking monetary sanctions or costs against NAFG, as described in subparagraphs 20(j), (k) and (m) above.

## B. The Respondents' Submissions

[22] On June 20, 2014, counsel for the Respondents filed their written submissions, the Affidavit of Gino Arconti and a Sanction and Cost Submissions Brief.

[23] The Respondents' written submissions explained the financial difficulties of NAFG and the Arcontis' efforts to overcome these difficulties. The Respondents also submitted that the Commission should consider a number of mitigating factors, including:

- the Respondents' submission that they were held accountable for knowing and understanding their obligations (i.e. in Carter's policies and procedures manual and at law generally) based primarily upon the finding that they understood those obligations as explained to them by David Gilkes ("**Gilkes**"), the regulatory consultant who was hired by the Arcontis. The Respondents submit that if Gilkes did not advise the Respondents that they needed to disclose their financials, then that should be considered as a mitigating factor in addressing their sanctions;
- the Respondents' submission that Gilkes gave uncontradicted testimony that there are no real rules of disclosure when dealing with accredited investors in the exempt market, along with the submission that there was no evidence that Gilkes or the Respondents were able to secure any guidance relating to Staff's concerns before Staff sent its letter on June 23, 2010;
- the Respondents' submission that without the benefit of hindsight or guiding jurisprudence, it was difficult for the Respondents to determine when NAFG's financial difficulties reached sufficient severity to render their current risk-disclosure measures inadequate;
- factors concerning NAFG's marketing brochures, including the following submissions: there was no evidence tendered of an express statement of profitability in the brochures, Staff's failure to raise certain concerns with the brochures at different points in time, and Gilkes' unawareness of any concerns of profitability implications in the brochures when he revised them following Staff's letter dated June 23, 2010;
- factors concerning the misuse of investor funds, including the following submissions: the lack of any shortfall during the period of January 1, 2009 to September 24, 2010 (the "**Fraud Period**") as indicated in NAFG's financial statements, despite exhaustive compliance reviews Staff did not raise any fraudulent concerns until the Respondents were incapable of taking any corrective action, and in 2010 the Respondents took active measures to reduce NAFG's interest payments by advising investors of the financial difficulties of NAFG and by reducing half of its interest expense by a third and working successfully with HDL Financing; and
- certain issues regarding Staff's analysis on the source and application of funds of NAFG, particularly regarding the interest payments and redemption payments made to investors.

[24] I find that the majority of the factors listed above go to the merits of Staff's allegations. The Respondents had the opportunity to fully defend themselves and respond to Staff's case at the Merits Hearing. This is not the appropriate forum to reopen the Merits Hearing or vary any findings that were made in the Merits Decision. The purpose of this hearing is to consider the appropriate sanctions and costs to be imposed on the Respondents. I have accordingly focused my analysis and findings in this decision solely to this purpose.

#### IV. ANALYSIS

##### A. Sanctions

###### 1. The Applicable Law

[25] The Commission's mandate, set out in section 1.1 of the *Act*, is to: (i) provide protection to investors from unfair, improper or fraudulent practices; and (ii) foster fair and efficient capital markets and confidence in capital markets.

[26] In making an Order in the public interest under section 127 of the *Act*, the Commission's jurisdiction should be exercised in a protective and preventative manner. As expressed in the oft-cited decision of *Re Mithras Management Ltd.*:

...the role of this Commission is to protect the public interest by removing from the capital markets -- wholly or partially, permanently or temporarily, as the circumstances may warrant -- those whose conduct in the past leads us to conclude that their conduct in the future may well be detrimental to the integrity of those capital markets. We are not here to punish past conduct; that is the role of the courts...We are here to restrain, as best we can, future conduct that is likely to be prejudicial to the public interest in having capital markets that are both fair and efficient. In so doing we must, of necessity, look to past conduct as a guide to what we believe a person's future conduct might reasonably be expected to be; we are not prescient, after all.

*(Re Mithras Management Ltd. (1990), 13 O.S.C.B. 1600 at 1610-1611)*

[27] This view was endorsed by the Supreme Court of Canada in the following terms:

...the purpose of an order under s. 127 is to restrain future conduct that is likely to be prejudicial to the public interest in fair and efficient capital markets. The role of the [Commission] under s. 127 is to protect the public interest by removing from the capital markets those whose past conduct is so abusive as to warrant apprehension of future conduct detrimental to the integrity of the capital markets.

*(Re Committee for the Equal Treatment of Asbestos Minority Shareholders v. Ontario (Securities Commission), 2001 SCC 37 at para. 43)*

[28] The Supreme Court of Canada has also recognized that general deterrence is an important factor in imposing sanctions by stating that "...it is reasonable to view general deterrence as an

appropriate, and perhaps necessary, consideration in making orders that are both protective and preventative” (*Re Cartaway Resources Corp.*, [2004] 1 S.C.R. 672 at para. 60).

[29] In determining the nature and duration of sanctions, the Commission has considered the following factors:

- (a) the seriousness of the allegations proved;
- (b) the respondents’ experience in the marketplace;
- (c) the level of a respondent’s activity in the marketplace;
- (d) whether or not there has been a recognition of the seriousness of the improprieties;
- (e) whether or not the sanctions imposed may serve to deter not only those involved in the case being considered, but any like-minded people from engaging in similar abuses of the capital markets;
- (f) any mitigating factors;
- (g) whether the violations are isolated or recurrent;
- (h) the size of any profit (or loss) avoided from the illegal conduct;
- (i) the size of any financial sanction or voluntary payment when considering other factors;
- (j) the effect any sanction might have on the livelihood of the respondent;
- (k) the restraint any sanction may have on the ability of a respondent to participate without check in the capital markets;
- (l) the reputation and prestige of the respondent;
- (m) the shame, or financial pain, that any sanction would reasonably cause to the respondent; and
- (n) the remorse of the respondent.

(*Re Belteco Holdings Inc.* (1998), 21 O.S.C.B. 7743 at 7746-7747; *Re M.C.J.C. Holdings Inc.* (2002), 25 O.S.C.B. 1133 (“*M.C.J.C. Holdings*”) at 1136; *Erikson v. Ontario (Securities Commission)*, [2003] O.J. No. 593 (Div. Ct.) (“*Erikson*”))

[30] In determining the appropriate sanctions to be ordered, the Commission will also consider the specific circumstances in each case and ensure that the sanctions are proportionate to those circumstances (*M.C.J.C. Holdings*, above at 1134).

[31] With regards to disgorgement, pursuant to paragraph 10 of subsection 127(1) of the *Act*, the Commission may order a person or company who has not complied with Ontario securities law to disgorge to the Commission “any amounts obtained as a result of the non-compliance”. The Commission has described the purpose of the disgorgement remedy as follows:

[T]he objective of the disgorgement remedy is to deprive a wrongdoer of ill-gotten gains, reflecting the view that it would be inappropriate for those who contravene Ontario securities law to be able to retain any illegally obtained profits...

...

[T]he legal question is not whether a respondent “profited” from the illegal activity but whether the respondent “obtained amounts” as a result of that activity. In our view, this distinction is made in the *Act* to make clear that all money illegally obtained from investors can be ordered to be disgorged, not just the “profit” made as a result of the activity...

(*Re Limelight Entertainment Inc.* (2008), 31 O.S.C.B. 12030 (“*Limelight*”) at paras. 47 and 49)

[32] In *Limelight*, the Commission held that it should consider the following non-exhaustive list of factors when contemplating a disgorgement order, in addition to the general factors for sanctioning:

- (a) whether an amount was obtained by a respondent as a result of non-compliance with the *Act*;
- (b) the seriousness of the misconduct and the breaches of the *Act* and whether investors were seriously harmed;
- (c) whether the amount that a respondent obtained as a result of non-compliance with the *Act* is reasonably ascertainable;
- (d) whether the individuals who suffered losses are likely to be able to obtain redress; and
- (e) the deterrent effect of a disgorgement order on the respondents and other market participants.

(*Limelight*, above at para. 52)

[33] Staff has the onus of proving, on a balance of probabilities, the amounts obtained by a respondent as a result of its non-compliance with the *Act*.

## 2. Relevant Sanctioning Factors

[34] In considering the factors set out in paragraph 29 above, I find the factors below to be relevant to the circumstances of the Respondents.

**(a) Seriousness of the Allegations Proved**

[35] The findings in the Merits Decision established significant contraventions of Ontario securities law and conduct that was found to be contrary to the public interest. In particular, the Commission found that the Respondents breached subsection 126.1(b) of the *Act* during the Fraud Period. The Commission has previously held that fraud is “one of the most egregious securities regulatory violations” and is both an “affront to the individual investors directly targeted” and something that “decreases confidence in the fairness and efficiency of the entire capital market system” (*Re Al-Tar Energy Corp.* (2010), 33 O.S.C.B. 5535 at para. 214, citing *Re Capital Alternatives Inc.* (2007), A.B.A.S.C. 79 at para. 308, citing D. Johnston & K. D. Rockwell, *Canadian Securities Regulation*, 4th ed., Markham: LexisNexis, 2007 at 420).

[36] Moreover, the Divisional Court has held that “[p]articipation in the capital markets is a privilege, not a right” (*Erikson*, above at para. 55).

[37] In this matter, the Arcontis were deemed to have not complied with Ontario securities law through their roles as actual and *de facto* directors and officers of NAFG and NAC, along with their roles as actual and *de facto* directors and officers of Carter, which was found to have breached its suitability obligations under section 13.3 of NI 31-103 and its duty to act fairly, honestly and in good faith under subsection 2.1(1) of OSC Rule 31-505. Additionally, Gino Arconti was found to have illegally traded securities after his registration was automatically suspended as a result of the Director’s Decision, contrary to subsection 25(1) of the *Act*.

**(b) Experience and Level of Activity in the Marketplace**

[38] The Respondents submit that the Arcontis were not experienced in the marketplace. I disagree with this submission. As discussed in paragraph 17 above, the Arcontis were registrants from September 17, 2007 to September 22, 2010. The Commission has previously recognized that registrants are expected to have a higher level of awareness of their duties than non-registrants (*Re Sextant Capital Management Inc.* (2012), 35 O.S.C.B. 5213 at para. 16(b), citing *Re Rowan* (2009), 33 O.S.C.B. 91 at para. 145 and *Re Norshield Asset Management (Canada)* (2010), 33 O.S.C.B. 7171 at paras. 84 and 85).

[39] I find that the Arcontis failed to meet the high standard of conduct that was expected of them as registrants. In the Merits Decision, the Commission found that the Arcontis were active participants in Carter’s investment activities and authorized Carter’s misconduct. The Arcontis were also found to be active members in the fraud committed by NAFG and NAC.

[40] Moreover, the fraudulent scheme spanned more than 20 months and involved the misconduct of all Respondents in this matter. As such, their experience and level of activity in the capital markets is an aggravating factor for each of the Respondents.

**(c) Size of Any Profit or Loss Avoided from Illegal Conduct**

[41] A total of \$2,908,170 was received from investors of NAFG and a total of \$1,042,000 was raised from the sale of NAC securities from 11 investors (Merits Decision, above at paras. 83 and 308). Most of the investors of NAFG and NAC, who were unsecured investors, lost at least half of their investment (Merits Decision, above at para. 311). In my view, while the investor losses in this case fall neither at the most nor the least serious end of the spectrum, they

have the capacity to result in a substantial loss of investor confidence in the integrity of the capital markets.

***(d) Mitigating Factors and Remorse***

[42] The Arcontis both testified at the Merits Hearing, and all the Respondents admitted to certain facts at the commencement of the Merits Hearing. However, I note that the Respondents did not admit to the following allegations: the conduct by Carter amounted to a failure by the company to deal fairly, honestly and in good faith with its clients; the Respondents' conduct amounted to fraud; and Gino Arconti engaged in and/or held himself out as engaging in the business of trading in securities without registration and contrary to the public interest. I therefore consider the Respondents' admissions and the Arcontis' testimonies at the Merits Hearing to be neutral factors when determining the appropriate sanctions to be imposed on the Respondents.

[43] Staff submits that the Arcontis did not take responsibility for their actions, did not express remorse and acted in a way to preserve their best interests, specifically by seeking to obtain releases from investors in relation to the lawsuits against their lawyers and former advisers, including Gilkes. I do not accept these submissions from Staff and therefore do not consider them to be aggravating factors against the Arcontis.

[44] The Respondents submit that the Commission should consider a number of mitigating factors. As discussed in paragraph 24 above, I find that the majority of these factors go to the merits of this case, which were raised in the Merits Hearing and addressed in the Merits Decision. The evidence presented at the Merits Hearing showed that: although Gilkes assisted the Arcontis as a regulatory consultant, he was never present during the Arcontis' meetings with investors; later disclosure made by the Respondents did not constitute disclosure at the time investors initially made their investments; and, it was not credible that the Arcontis did not understand their obligation to disclose significant investment risks to their investors (Merits Decision, above at paras. 245, 282 and 283). I also note that, at the Merits Hearing, counsel for the Respondents did not ask any questions in cross-examination of Staff's forensic accountant, Marcel Tillie ("**Tillie**"), who provided the Panel with the source and application of funds analysis in relation to this matter.

***(e) General and Specific Deterrence***

[45] A message must be sent to the Respondents and like-minded individuals that fraudulent schemes similar to the one involved in this case will result in severe sanctions. Orders removing the Respondents from the capital markets, imposing significant administrative penalties and requiring disgorgement of funds not returned to investors are proportionate to the Respondents' misconduct, and will send a message to like-minded individuals that involvement in this type of misconduct will result in severe sanctions.

**3. Appropriate Sanctions in this Matter**

[46] At the Sanctions and Costs Hearing, Staff provided the Panel with a copy of the Reasons and Decision on Sanctions and Costs in *Re XI Biofuels Inc. et al.* (2010), 33 O.S.C.B. 10963 ("**XI Biofuels**"), and pointed the Panel to paragraph 25, which states:

We accept the submissions of Staff. We are not persuaded that the *BIA* prevents us from exercising our public interest jurisdiction under sections 127 and 127.1 of the *Act* without leave of the Bankruptcy Court. We leave questions of enforcement of our order to another forum. In this case, however, we have determined that the public interest is best served by restricting the monetary orders to the Individual Respondents only, in order to avoid depleting the assets that may be available for compensation or restitution to investors who lost money as a result of the Respondents' non-compliance with the *Act*.

(*XI Biofuels*, above at para. 25)

[47] Relying on paragraph 25 of *XI Biofuels*, I agree with Staff that the Commission has the authority to make public interest orders against NAFG, a bankrupt entity.

[48] I also agree with Staff's submissions that the Commission should not distinguish between the conduct of Flavio Arconti and Gino Arconti, and that the Arcontis therefore deserve the same level of sanctions. During the time of the Respondents' conduct referred to herein, the Arcontis jointly owned NAFG, NAC, Carter and Prestige Motors and were the actual and/or *de facto* directors and officers of each of these entities. Flavio Arconti prepared the marketing brochure of NAFG, which was found to contain misleading statements, while Gino Arconti distributed these brochures to investors. Both Arcontis were the directing minds of NAFG and NAC, they were responsible for depositing cheques that came into NAFG, they reviewed the financial statements of NAFG, and they engaged in discussions with investors. The Arcontis were also active participants in Carter's investment activities and authorized Carter's conduct.

**(a) Trading and Other Market Prohibitions**

[49] Given the seriousness of the misconduct of the Respondents, sanctions in this case should send a strong message to both the Respondents and the public at large. I find that it is in the public interest to make orders removing the Respondents permanently from the capital markets.

[50] I agree with Staff's submission that the Arcontis should be subject to permanent market participation bans with no carve-outs for personal trading. The Commission has ordered permanent cease trade, acquisition and exemption application bans, without exception, in circumstances where respondents were found by the Panel to have engaged in fraud (*Re Al-Tar Energy Corp.* (2011), 34 O.S.C.B. 447 ("*Al-Tar Sanctions*") at para. 35; *Re Lyndz Pharmaceuticals Inc.* (2012), 35 O.S.C.B. 7357 ("*Lyndz*") at para. 80; *Re Goldpoint Resources Corp.* (2013), 36 O.S.C.B. 1464 ("*Goldpoint*") at para. 63). In this matter, the Arcontis engaged in fraudulent conduct, which included providing misleading documents to investors and engaging in unauthorized diversion of investor funds. The Arcontis cannot be trusted to participate in the capital markets in the future and their conduct demonstrates a serious risk to the public.

[51] I therefore find that it is appropriate that the Respondents be subject to permanent trading, acquisition and exemption application bans, and that no carve-outs be afforded to the Arcontis for personal trading. Permanent director or officer bans will also remove the Arcontis from Ontario's capital markets and protect the investing public.

[52] I also find it appropriate to reprimand the Respondents, pursuant to paragraph 6 of subsection 127(1) of the *Act*, in order to reaffirm that the Commission will not tolerate future illegal and fraudulent conduct such as occurred in this case.

**(b) Administrative Penalties**

[53] The Commission's public interest jurisdiction allows it to impose sanctions under section 127 of the *Act*. Under paragraph 9 of subsection 127(1) of the *Act*, I am entitled to impose an administrative penalty of not more than \$1 million in connection with each failure of the Respondents to comply with Ontario securities law. In the Merits Decision, the Commission found that the Respondents were involved with multiple contraventions of Ontario securities law, including fraud, and found that the Respondents acted contrary to the public interest.

[54] As discussed in paragraph 21 above, Staff is no longer seeking monetary sanctions against NAFG, and therefore seeks that each of NAC, Flavio Arconti and Gino Arconti pay an administrative penalty of \$750,000.

[55] I have considered the Commission's prior case-law in determining administrative penalties that are proportionate to the circumstances in this matter. Staff relied on *Al-Tar Sanctions*, which involved unregistered trading, illegal distribution of securities, fraud and director and officer liabilities. The individual respondents were required to pay administrative penalties ranging from \$200,000 to \$750,000. Staff also relied on *Re Maple Leaf Investment Fund Corp.* (2012), 35 O.S.C.B. 3075, *Re New Found Freedom Financial* (2013), 36 O.S.C.B. 6758 ("**New Found Freedom**"), *Re Pogachar* (2012), 35 O.S.C.B. 6479, *Lyndz and Goldpoint*, all of which involved administrative penalties that ranged from \$250,000 to \$750,000 against respondents (I note that one individual respondent in *New Found Freedom Financial* was ordered to pay a \$5,000 administrative penalty). These and other similar Commission decisions provide appropriate precedents for assessing proportionate administrative penalty sanctions.

[56] In this case, the Respondents' actions caused significant harm to investors and the capital markets generally. A total of \$2,908,170 was received from investors of NAFG and \$1,042,000 was raised from the sale of NAC securities. Although there was evidence that the Respondents updated various corporate documents, such as Know Your Client forms and NAFG's marketing brochures, in an effort to be compliant with Ontario securities law, the Commission ultimately found that the Respondents' misconduct resulted in multiple contraventions of Ontario securities law, including a finding of fraud. I note that in his testimony at the Merits Hearing, Flavio Arconti admitted that the wording in some of the statements in the marketing brochures could be construed differently than what he interpreted them to mean, and Gino Arconti, in his testimony, accepted the criticism that the version of the marketing brochure that was most widely distributed to investors could have left the impression that NAFG was a bigger player than it really was in the automotive and financing industry (Merits Decision, above at paras. 153 and 189).

[57] Regarding both Arcontis, they were aware that NAFG never made a profit in the years 2007, 2008, 2009 or 2010, and they knew that the unsecured loan to Prestige Motors reached over \$2 million. Each of the Arcontis transferred their interest in their residence to their spouses in May, 2010; and the reasons for the transfers was to place whatever value there was in the residences out of reach of potential creditors (Merits Decision, above at para. 316). The Arcontis

were also registrants and were the directing minds of NAFG, NAC, Carter and Prestige Motors. There is a need for a reminder that the Commission expects a higher standard of conduct from those provided with the privilege of being involved in the capital markets.

[58] Accordingly, I find that it is appropriate and proportionate to the circumstances in this case to make an order against NAC, Flavio Arconti and Gino Arconti to each pay an administrative penalty of \$600,000.

**(c) Disgorgement**

[59] In the Merits Decision at paragraph 317, the Commission found that through their directing minds (the Arcontis), “NAFG and NAC knew that the representations to investors regarding NAFG’s financial situation and the use of investor funds were false and misleading and would cause deprivation to investors by exposing them to risks not contemplated by them”. It was through the actions and subjective knowledge of the Arcontis that allowed NAFG and NAC to perpetrate the fraudulent Ponzi scheme, in which payments of new investor money were made to previous investors. Investors were substantially harmed, and it does not appear likely that investors will be able to obtain any redress. I find that it is appropriate to impose disgorgement orders against the Respondents for the amounts they obtained through their serious misconduct.

*(i) NAFG, Flavio Arconti and Gino Arconti*

[60] Staff submits that it only seeks disgorgement amounts in relation to the Fraud Period. The evidence showed that a total of \$2,908,170 was received from investors of NAFG, a total of \$126,000 was received from investors of NAC and a total of \$466,777.58 was repaid to investors (Merits Decision, above at para. 83). Staff submits that none of payments totaling \$466,777.58 were made to investors on the NAC investor list. Given that there was no evidence presented to the contrary, I accept Staff’s submission and I will attribute these payments to NAFG’s investors.

[61] In its written submissions, based on the amounts referred in paragraph 60 above, Staff sought an order that NAFG, Flavio Arconti and Gino Arconti disgorge to the Commission a total of \$2,441,392.42 for which they shall be jointly and severally liable, to be allocated to or for the benefit of third parties in accordance with subsection 3.4(2)(b) of the *Act*. However, following its submissions regarding NAFG’s status as a bankrupt, Staff informed the Commission that it would not seek monetary sanctions against NAFG, as discussed in paragraph 21 above.

[62] At the Sanctions and Costs Hearing, Staff revised its disgorgement request of \$2,441,392.42 and submitted that the \$126,000 received from investors of NAC should not be subtracted from the total amount received from investors of NAFG during the Fraud Period. Staff submitted that its revised disgorgement amount should be \$2,567,392.42 (Transcript, Sanctions and Costs Hearing, p. 19, lines 4-11).

[63] The Respondents submit that a reasonable disgorgement order against the Respondents would be \$175,000, which they submit represents the management fees that were paid to the Arcontis (Transcript, Sanctions and Costs Hearing, p. 54, lines 10-12 and p. 59, lines 5-13). The Respondents also submit that the amount of \$1,642,413.28 categorized as “Interest Paid to Investors” in Tillie’s source and application of funds analysis (Merits Decision, Exhibit 20)

includes both interest and redemption payments. The Affidavit of Gino Arconti indicates that a total of \$388,701.26 was received by investors as redemption payments. Staff submits that it does not have any information to refute a finding that these payments were potential principal payments. I therefore accept that \$388,701.26 was repaid to investors as redemption payments.

[64] In calculating the net receipts received from investors of NAFG, I have taken the \$2,908,170 that was received from investors of NAFG and netted out: (a) \$466,777.58 that was repaid to NAFG's investors; and (b) \$388,701.26 that was paid to investors as redemption payments. I have not included the \$126,000 that was received from investors of NAC, which is consistent with Tillie's analysis on the source and application of funds in this matter (Merits Hearing, Exhibit 20). The net receipts from investors of NAFG therefore amount to \$2,052,691.16.

[65] I find that the net receipts from investors of NAFG were obtained as a result of the fraudulent conduct of NAFG and each of the Arcontis. These receipts have been ascertained and a disgorgement order for these receipts would have a significant general and specific deterrent effect. I therefore find that it is appropriate to order Flavio Arconti and Gino Arconti to disgorge, on a joint and several basis, \$2,052,691.16 to the Commission for the amounts they obtained as a result of their non-compliance with Ontario securities law.

(ii) *NAC, Flavio Arconti and Gino Arconti*

[66] Staff seeks an order that NAC, Flavio Arconti and Gino Arconti disgorge to the Commission a total of \$1,042,000 for which they shall be jointly and severally liable, to be allocated to or for the benefit of third parties in accordance with subsection 3.4(2)(b) of the *Act*.

[67] Regarding NAC, Staff submitted in its written submissions that it could only find \$126,000 in funds coming from NAC or NAC investors that were deposited into the bank accounts of NAFG. Staff did not have bank statements for any bank accounts in the name of NAC. However, at the Merits Hearing, the Respondents admitted that during the period July, 2009 to April, 2010, NAC issued shares to approximately 11 investors and the total proceeds from the sale of NAC securities of approximately \$1,042,000 was transferred to NAFG (Merits Decision, above at para. 308). The Respondents, however, submit that the admission regarding the \$1,042,000 from the "sale" of NAC securities was simply an exchange of NAFG securities for NAC securities. I do not accept the Respondents' submission.

[68] As discussed in paragraph 59 above, the Commission made a finding of fraud against NAC based on the subjective knowledge of its directing minds, the Arcontis. The Respondents admitted that approximately \$1,042,000 was raised from the sale of NAC securities. I therefore find that \$1,042,000 was obtained by NAC and the Arcontis through their non-compliance of Ontario securities law, and I order that this amount be disgorged to the Commission on a joint and several basis by NAC, Flavio Arconti and Gino Arconti.

**B. Costs**

## 1. The Applicable Law

[69] Pursuant to section 127.1 of the *Act*, the Commission has authority to order a person or company to pay the costs of an investigation and hearing if the Commission is satisfied that the person or company has not complied with Ontario securities law or has acted contrary to the public interest. Factors to be considered by the Commission when awarding costs are set out in Rule 18.2 of the Commission's *Rules of Procedure* (2014), 37 O.S.C.B. 4168 (the "***Rules of Procedure***").

[70] Staff originally requested in its written submissions that NAFG, NAC, Flavio Arconti and Gino Arconti pay \$283,843.75 of the costs of the investigation and hearing, for which they shall be jointly and severally liable. However, as discussed in paragraph 21 above, in its email sent to the Registrar on June 19, 2014, Staff stated that it would not seek costs against NAFG. Staff therefore currently seeks a costs order against NAC, Flavio Arconti and Gino Arconti.

[71] Staff calculated its costs of the investigation and hearing as set out in the Affidavit of Michelle Spain sworn on February 14, 2014, which includes Staff's Bill of Costs. The Bill of Costs employs the hourly rates approved by the Commission and reflects the time spent by: Staff counsel (Michelle Vaillancourt), a senior investigative counsel (Shaun Flynn) and Staff's forensic accountant (Tillie). The time spent by students-at-law and assistants were excluded. Staff submits that it has employed a conservative approach by applying the following discounts: no time was claimed for the work of a senior litigation counsel who was the litigator on this matter prior to Michelle Vaillancourt's involvement; no time was claimed for the work of law clerks; no time was claimed for the time spent preparing for or attending the Sanctions and Costs Hearing; and no claim was made for any disbursements.

## 2. Analysis

[72] In *Re Ochnik* (2006), 29 O.S.C.B. 5917 ("***Ochnik***"), the Panel identified criteria that was considered by the Commission in past decisions when awarding costs:

- (a) failure by Staff to provide early notice of an intention to seek costs may result in a reduced costs award;
- (b) the seriousness of the charges and the conduct of the parties;
- (c) abuse of process by a respondent may be a factor in increasing the amount of costs;
- (d) the greater investigative/hearing costs that the specific conduct of a respondent tends to require in the case; and
- (e) the reasonableness of the costs requested by Staff.

(*Ochnik*, above at para. 29)

[73] Applying the factors from *Ochnik* and the factors listed in Rule 18.2 of the *Rules of Procedure*, I find the following factors to be relevant in imposing a costs order against NAC, Flavio Arconti and Gino Arconti:

- (a) a Notice of Hearing was issued by the Commission on December 28, 2011 to notify the Respondents in this matter that Staff would be seeking investigation and hearing costs against them;
- (b) Staff has proven serious allegations against the Respondents involving a substantial amount of investor funds and misconduct that led to multiple contraventions of Ontario securities law, including fraud, and conduct contrary to the public interest;
- (c) the Merits Hearing in this matter spanned 12 days;
- (d) the Respondents filed a document entitled “Admissions of the Respondents” at the beginning of the Merits Hearing (Merits Hearing, Exhibit 1);
- (e) the Respondents cooperated with Staff during the investigation of this matter;
- (f) Staff’s request for costs pertains to the period spanning from October 4, 2010 to December 13, 2013, and consequently does not include any costs associated with the Melotel Proposal or the four adjournment requests made by the Respondents that were granted by the Commission, as discussed in paragraphs 4 to 13 above;
- (g) the Commission granted four requests from the Respondents to modify the deadline for their written submissions on sanctions and costs. The Commission’s most recent Order dated May 6, 2014 allowed the Respondents to file and serve their already late written submissions by June 9, 2014. The Respondents provided their written submissions and related materials on sanctions and costs on June 20, 2014; and
- (h) Staff has taken a conservative approach in assessing the amount of costs.

[74] Having considered the foregoing, and in particular, the complexity of the matter and the conduct of both the Respondents and Staff during the Merits Hearing, I find that it is appropriate to award costs in the amount of \$200,000 on a joint and several basis against NAC, Flavio Arconti and Gino Arconti.

## V. CONCLUSION

[75] For the reasons set out above, I conclude that it is in the public interest to make the orders set out below. In my view, the sanctions imposed will deter the Respondents and other like-minded individuals from engaging in similar misconduct in the capital markets in the future and the sanctions are proportionate to the circumstances and conduct of each Respondent.

[76] I will issue a separate order giving effect to my decision on sanctions and costs as follows:

- (a) pursuant to paragraph 2 of subsection 127(1) of the *Act*, trading in any securities by the Respondents shall cease permanently;
- (b) pursuant to paragraph 2.1 of subsection 127(1) of the *Act*, the acquisition of any

securities by the Respondents shall be prohibited permanently;

- (c) pursuant to paragraph 3 of subsection 127(1) of the *Act*, any exemptions contained in Ontario securities law shall not apply to the Respondents permanently;
- (d) pursuant to paragraph 6 of subsection 127(1) of the *Act*, the Respondents are reprimanded;
- (e) pursuant to paragraph 7 of subsection 127(1) of the *Act*, Flavio Arconti and Gino Arconti shall resign any position that they hold as a director or officer of an issuer;
- (f) pursuant to paragraph 8 of subsection 127(1) of the *Act*, Flavio Arconti and Gino Arconti shall be prohibited permanently from becoming or acting as a director or officer of any issuer;
- (g) pursuant to paragraph 8.2 of subsection 127(1) of the *Act*, Flavio Arconti and Gino Arconti shall be prohibited permanently from becoming or acting as a director or officer of a registrant;
- (h) pursuant to paragraph 8.4 of subsection 127(1) of the *Act*, Flavio Arconti and Gino Arconti shall be prohibited permanently from becoming or acting as a director or officer of an investment fund manager;
- (i) pursuant to paragraph 8.5 of subsection 127(1) of the *Act*, the Respondents shall be prohibited permanently from becoming or acting as a registrant, as an investment fund manager or as a promoter;
- (j) pursuant to paragraph 9 of subsection 127(1) of the *Act*, NAC, Flavio Arconti and Gino Arconti shall each pay an administrative penalty of \$600,000 for their non-compliance with Ontario securities law, to be designated for allocation or use by the Commission, pursuant to subsection 3.4(2)(b) of the *Act*;
- (k) pursuant to paragraph 10 of subsection 127(1) of the *Act*, Flavio Arconti and Gino Arconti shall, on a joint and several basis, disgorge to the Commission a total of \$2,052,691.16 obtained as a result of their non-compliance with Ontario securities law, to be designated for allocation or use by the Commission, pursuant to subsection 3.4(2)(b) of the *Act*;
- (l) pursuant to paragraph 10 of subsection 127(1) of the *Act*, NAC, Flavio Arconti and Gino Arconti shall, on a joint and several basis, disgorge to the Commission a total of \$1,042,000 obtained as a result of their non-compliance with Ontario securities law, to be designated for allocation or use by the Commission, pursuant to subsection 3.4(2)(b) of the *Act*;
- (m) pursuant to subsection 127.1 of the *Act*, NAC, Flavio Arconti and Gino Arconti shall jointly and severally pay \$200,000 for the costs incurred in the investigation

and hearing of this matter.

**DATED** at Toronto this 11<sup>th</sup> day of September, 2014.

*“James D. Carnwath”*

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James D. Carnwath, Q.C.