Court File No. CV-14-1051800CL

ONTARIO
SUPERIOR COURT OF JUSTICE
COMMERCIAL LIST
IN THE MATTER OF THE COMPANIES' CREDITORS
ARRANGEMENT ACT, R.S.C. 1985, c. C-36, AS AMENDED

AND IN THE MATTER OF A PLAN OF COMPROMISE OR
ARRANGEMENT OF THE CASH STORE FINANCIAL SERVICES INC., THE CASH
STORE INC., TCS CASH STORE INC., INTSALOANS INC., 7252331 CANADA INC.,
5515433 MANITOBA INC., 1693926 ALBERTA LTD DOING BUSINESS AS "THE TITLE
STORE"

FACTUM OF THE RESPONDENT,
0678786 B.C. LTD. (FORMERLY THE MCCANN FAMILY HOLDING CORPORATION)

Dated: April 25, 2014

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TO: THE SERVICE LIST

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I. OVERVIEW

1. The Applicant, The Cash Store Inc., entered into broker agreements with third party lenders in which it agreed to broker loans between its customers and the third party lenders for a commission fee. The third party lenders advanced approximately $42 million pursuant to the broker agreements.

2. The broker agreements clearly provided that The Cash Store Inc. was not to use the third party lenders' funds for any purpose other than to lend the monies through third party brokered lending agreements. Further, the broker agreements provided that the third party lenders could request that the moneys they provided to The Cash Store Inc. be segregated in a separate

account. 0678786 B.C. Ltd. requested that its monies be segregated and The Cash Store Inc. represented that its monies were safe, segregated and protected.

3. In breach of the broker agreements and the representations made to the third party lenders, the Applicants misappropriated in excess of $20 million of the third party lenders' funds, and then used the misappropriated funds to pay their own operational expenditures and professional fees leading up to this CCAA filing. The Applicants had breached the broker agreements at the time of filing.

4. Rather than propose to return the third party lenders' misappropriated funds, the Applicants applied for and obtained an Amended and Restated Initial Order that forces the third party lenders to allow their remaining funds to be lent out, so that the Applicants can continue to collect their upfront broker commissions on new advances.

5. While acknowledging that loans made now are subject to increased risk of default, the Applicants propose that the third party lenders incur the significant risk of losing further monies to finance the restructuring of the very entities that misappropriated their funds. The Amended and Restated Initial Order is grossly prejudicial to the third party lenders.

6. The Applicants and the Applicants' affiant were not forthright with the court in the materials they filed in support of the Initial Order and in support of the Amended and Restated Initial Order:

(a) in seeking to have the Ontario court assume jurisdiction, the Applicants falsely represented that their principal place of business was Ontario; and

(b) in seeking the court's approval to continue lending funds advanced by third party lenders, the Applicants failed to tell the court that they had already misappropriated half of the funds advanced by third party lenders, using those funds for operations in breach of the broker agreements between the Applicants and the third party lenders.

II. FACTS

A. RELEVANT PARTIES

7. The Respondent 0678786 B.C. Ltd., formerly known as The McCann Family Holding Corporation ("0678786"), is a British Columbia corporation extra-provincially registered in Alberta.

> Affidavit of Sharon Fawcett, sworn April 11, 2014 (the "April 11 Fawcett Affidavit") at para. 2, Exhibit 1 to the Affidavit of Sharon Fawcett, sworn April 22, 2014 (the "April 22 Fawcett Affidavit"), Application Record of 0678786 (the "0678786 Application Record"), Tab 2, p. 11.

8. The Applicant The Cash Store Financial Services Inc. ("Cash Store Financial") is an Ontario corporation that is publicly listed on the Toronto Stock Exchange. The Cash Store Inc. ("Cash Store") is an Alberta corporation and a subsidiary of Cash Store Financial. Both corporations were initially established in Edmonton, Alberta and continue to have their head offices there.

> April 11 Fawcett Affidavit at para. 3, Exhibit 1 to the April 22 Fawcett Affidavit, 0678786 Application Record, Tab 2, p. 12.
>
> Transcript of the Cross-examination of Steven Carlstrom dated April 22, 2014 (the "Carlstrom Cross") at Qs 31-32, Brief of Transcripts of the Respondent 0678786 B.C. Ltd. (the "Brief of Transcripts"), Tab 1, p. 10.

9. All of the Applicants are either direct or indirect subsidiaries of Cash Store Financial.

Affidavit of Steven Carlstrom sworn April 14, 2014 (the "Carlstrom Affidavit") at para 11, Application Record, p. 55.

B. CASH STORE'S CHIEF PLACE OF BUSINESS IS ALBERTA

10. Mr. Carlstrom asserted in the Carlstrom Affidavit that the Cash Store Financial's registered head office is in Toronto, without providing any further details about the office or about the business carried on at that address.

Carlstom Affidavit at para. 24, Application Record, p.61

11. He admitted on cross-examination that the Toronto registered office is the Toronto office of Cassels Brock & Blackwell LLP, outside legal counsel to Cash Store Financial, and that the address was simply used as a mailing address for registered filings. Cash Store Financial carries on no business at that location.

The Carlstrom Cross at Qs 37-41, Brief of Transcripts, Tab 1, pp. 11-12.

12. As Mr. Carlstrom admitted on cross-examination, Cash Store Financial's head office is located in Edmonton, Alberta and Cash Store Financial's public disclosure documents identify the Edmonton office as its head office and Alberta as its "Principal Regulator".

The Carlstrom Cross at Qs 31-32 and Exhibit 1, Brief of Transcripts, Tab 1, p. 10 and Tab 1(A).

13. With the exception of one officer who is involved with a United Kingdom subsidiary, all of the officers of Cash Store Financial are residents of Edmonton, Alberta.

The Carlstrom Cross at Qs 46-47, Brief of Transcripts, Tab 1, pp. 12-13.

14. Despite Mr. Carlstom's assertion in the Carlstrom Affidavit that Cash Store Financial's chief place of business is Ontario, on cross-examination, Mr. Carlstrom admitted that due to a February 12, 2014 court decision, Cash Store Financial ceased carrying on its principal business activities in Ontario prior to the filing, and there is no reasonable prospect of those activities resuming anytime soon.

The Carlstrom Cross at Qs 87-92, Brief of Transcripts, Tab 1, pp. 21-22.

C. BROKER AGREEMENT

15. Pursuant to a Broker Agreement dated June 19, 2012, between 0678786 and Cash Store (the "Broker Agreement"), 0678786 placed over time an aggregate of $13,350,000 (the "0678786 Restricted Cash"), as Financier, with the Cash Store, as Broker, for the sole purpose of those funds being loaned to customers. Extensive loan selection criteria must be met or specific approval of 0678786 must be obtained, before any 0678786 Restricted Cash is loaned. Furthermore, the 0678786 Restricted Cash is to be used for no other purpose, as set out in paragraph 2.10 of the Broker Agreement:

> 2.10 USAGE OF LOAN ADVANCES
>
> For greater certainty, funds from time to time advanced to Broker from Financier are solely intended to be utilized for the purposes of making advances to Broker Customers on Financier's behalf as contemplated hereunder. Broker agrees that any funds not otherwise being held by the Broker as a "float" in anticipation of Loan approvals shall not, without the consent of Financier, be advanced or utilized for any other purpose.

April 11 Fawcett Affidavit at para. 6, Exhibit 1 to the April 22 Fawcett Affidavit, 0678786 Application Record, Tab 2, p. 12.

Broker Agreement, s. 2.10, Exhibit "H" of the Carlstrom Affidavit, Application Record, p. 508.

16. The Broker Agreement contains the following governing law clause (as do all the broker agreements with the other financiers (collectively with 0678786, the "TPLs") further demonstrating that Cash Store's chief place of business is Alberta:

> 8.3 Governing Law
>
> Financier recognizes that while Loans and their associated agreements may be made in, be entered into, or be governed by the laws of other jurisdictions, the majority of Broker Services and other services provided by Broker to Financier will necessarily be performed at or from Broker's offices in the Province of Alberta and that accordingly the appropriate law most appropriate to this Agreement shall be the law of the Province of Alberta. This Agreement shall in all respects, be subject to, interpreted, construed and enforced in accordance with and under the laws of the Province of Alberta and the laws of Canada applicable therein and shall be treated as a contract made in the Province of Alberta. The Parties irrevocably attorn and submit to the jurisdiction of the courts of the Province of Alberta and courts of appeal therefrom in respect of all matters arising out of this Agreement.
>
> Broker Agreement, s. 8.3, Exhibit "H" of the Carlstrom Affidavit, Application Record, p. 515.

17. In discussions leading up to the execution of the Broker Agreement and throughout administering the funds on behalf of 0678786, it was expressed to be important to 0678786 that its funds were kept separate and apart from the general operating funds of Cash Store Financial in accordance with the Broker Agreement. The segregation of funds from general operating funds was at all times assured.

> April 11 Fawcett Affidavit at para. 7, Exhibit 1 to the April 22 Fawcett Affidavit, 0678786 Application Record, Tab 2, p. 13.

18. In fact, it was represented to 0678786 at the time the Broker Agreement was entered into, and it is a term of the Broker Agreement, that all Restricted Cash would be placed in a

"Designated Broker Bank Account", which would be separate and apart from Cash Store Financial's general operating account.

> April 22 Fawcett Affidavit at para. 3 and Exhibit 2, 0678786 Application Record, Tab 2, pp. 7 & 18.

19. At all material times, the understanding was that the Cash Store would act as a broker to lend 0678786's monies to third parties, and that 0678786 would own the loans or the cash it had advanced in trust to its broker and that its accounts would be administered on a segregated basis from the Cash Store's funds and be pooled safely with other "broker only" monies.

> Affidavit of Murray McCann sworn April 22, 2014 (the "McCann Affidavit") at para. 4, 0678786 Application Record, Tab 1, p. 1.

20. Mr. Reykdal, Cash Store's CEO, confirmed in discussions with Mr. Murray McCann, 0678786's former president, that Cash Store was acting as a trustee of 0678786's monies, that the funds would always be administered as such, and that Cash Store would not co-mingle 0678786's funds with Cash Store's operations. None of this was disclosed in the Carlstrom Affidavit.

> McCann Affidavit at para. 5, 0678786 Application Record, Tab 1, p. 2.

21. The funding excess / deficiency which 0678786 received from Cash Store over time provided a summary of the loans which were owned by 0678786. 0678786's monies in excess of the loans were described as "the funding excess deficiency" which was assumed to be segregated in accordance with the Broker Agreement and 0678786's instructions. 0678786's cash was always described as "restricted cash" in Cash Store Financial's public financial statements.

> McCann Affidavit at para. 7, 0678786 Application Record, Tab 1, p. 2.

22. In February 2014, upon learning of the difficulties of the Cash Store operation in Ontario, 0678786 requested an updated listing of its loan portfolio and advised Mr. Carlstrom that given the suspension of the line of credit product in Ontario, 0678786 would prefer to reduce its loan portfolio balance as at February 12, 2014, and that as amounts were collected by the Cash Store, funds would be returned to 0678786 along with the unexpended capital balance of 0678786's funds. The Cash Store would not be obligated to pay 17.5% interest on the returned funds from the date of return. This was the arrangement which had been struck by Mr. McCann and Mr. Reykdal. 0678786 confirmed these arrangements in writing on February 26, 2014, however, funds were not repaid to 0678786.

> April 11 Fawcett Affidavit at para. 9, Exhibit 1 to the April 22 Fawcett Affidavit, 0678786 Application Record, Tab 2, p. 13.

23. As recently as mid-March 2014, Mr. Carlstrom assured 0678786 about the security of undeployed cash and that the money remained available and was being administered in accordance with the Broker Agreement. During this period, Mr. Reykdal continued to assure Mr. McCann that 0678786's monies were segregated and safe, and should be secured by way of loans. This representation was reiterated by Mr. Reykdal to Mr. McCann on March 24, 2014, and in addition to assuring Mr. McCann of the safety and properly segregated nature of 0678786's monies, Mr. Reykdal represented that the only reason that 0678786 was not being repaid was because of instructions from the Special Committee. None of this was disclosed in the Carlstrom Affidavit.

> April 11 Fawcett Affidavit at paras. 12-13, Exhibit 1 to the April 22 Fawcett Affidavit, 0678786 Application Record, Tab 2, p. 14.
>
> McCann Affidavit at paras. 9-10, 0678786 Application Record, Tab 1, pp. 2-3.

24. Based on all of the above, Mr. Carlstrom's assertion that 0678786 only belatedly sought segregation of its funds is simply incorrect. In fact, 0678786 sought and received assurances that the funds would be segregated, and it has always understood and been advised that its funds were trust monies provided to Cash Store as broker to be used only for the purpose of, and in the manner stipulated in, the Broker Agreement.

McCann Affidavit at para. 18, 0678786 Application Record, Tab 1, p. 4.

D. APPLICANTS MISAPPROPRIATED 0678786'S MONIES – AND FAILED TO DISCLOSE MISAPPROPRIATION IN OBTAINING INITIAL ORDER

25. Until March 2014, 0678786 received monthly statements indicating the cash available and the amount deployed. The statement from February 2014 shows that as of February 28, 2014, the sum of $6,449,420 in deployed cash remained available to 0678786. Subsequent to that statement, 0678786 was advised that a further $831,000 had been collected on its third party loan portfolio during the period from March 1, 2014 to March 16, 2014, increasing its undeployed cash balance to $7,280,420. Further collection would have occurred from March 17, 2014 to date, increasing 0678786's undeployed cash balance accordingly.

April 11 Fawcett Affidavit at para. 10, Exhibit 1 to the April 22 Fawcett Affidavit, 0678786 Application Record, Tab 2, p. 14.

26. In the Carlstrom Affidavit, Mr. Carlstrom acknowledged that Restricted Cash, that is cash belong to the TPLs, totaled $12,961,000 as of February 28, 2014, but that as of close of business on April 11, 2014, the total cash in Cash Store's bank account was approximately $2.9 million.

Carlstrom Affidavit at paras. 48 & 156, Application Record, pp. 69 & 106.

27. Mr. Carlstrom did not disclose in his affidavit that, in breach of the Broker Agreement and without the knowledge or consent of 0678786 and contrary to the multiple representations made to 0678786, Cash Store had misappropriated the TPLs' monies and spent them on the Applicants' operating and professional costs leading up to the CCAA filing. This misappropriation was not disclosed to the Court in the evidence filed in support of the Initial Order and in support of the Amended and Restated Initial Order.

28. When the Applicants sought the Initial Order and the Amended and Restated Initial Order, the Applicants did not disclose to the court that The Cash Store Inc. was in breach of the broker agreements when the Applicants sought permission to continue to make advances using funds provided by third party lenders.

Carlstrom Affidavit at paras. 76-86, Application Record, pp.78-83.

29. On cross-examination, Mr. Carlstrom admitted that, as at the end of March 2014 and up to the CCAA filing, the TPLs' monies, that had been advanced only to be used for the purpose of brokering customer borrowings, were in fact used by Cash Store Financial for purposes not authorized by the TPLs. These purposes included the payment of salaries, outside lawyers, consultants, advisors and rent, among other things. Remarkably, Mr. Carlstron estimated that approximately $10 million of TPLs' monies had been used for these unauthorized purposes. This fact was not disclosed to this Court when it issued the Initial Order or the Amended and Restated Order in this proceeding.

Carlstrom Cross at Qs 258-273, Brief of Transcripts, Tab 1, pp. 61-63.

30. Moreover, and again undisclosed in the Carlstrom Affidavit, the Special Committee must have made the decision to use the Restricted Cash knowing that Cash Store and Cash Store

Financial were in breach of the Broker Agreement and that the company had misrepresented that it had segregated 0678786's monies.

April 22 Fawcett Affidavit at para. 5, 0678786 Application Record, Tab 2, p. 8.

31. The Special Committee took steps to ensure that the owners of the Restricted Cash were not apprised of the misrepresentations to enable Cash Store and Cash Store Financial to spend most of the Restricted Cash that belonged to the TPLs. On or about March 31, 2014, the Special Committee instructed management not to speak with Ms. Fawcett or Mr. McCann. Although a request was made on April 4, 2014 to allow PWC to inspect the records of Cash Store on behalf of 0678786 pursuant to its rights under the Broker Agreement, PWC was not allowed access for inspection until after the Initial Order was obtained.

April 22 Fawcett Affidavit at para. 6, 0678786 Application Record, Tab 2, p. 8.

McCann Affidavit at para. 11, 0678786 Application Record, Tab 1, p. 3.

32. Digging into the numbers in the Carlstrom Affidavit and the Monitor's Pre-Filing Report exposes the depth of the problem and the extent to which Cash Store Financial and Cash Store have misappropriated TPLs' funds. It is undisputed that Cash Store received approximately $42 million of TPL monies to broker. Nevertheless, in the Pre-Filing Monitor's Report, the Monitor reports that only $18.66 million of brokered loans are outstanding and that Cash Store only has $2.94 million cash on hand. $18.66 million and $2.94 million equals $21.6 million. All or part of the remaining $20.4 million was misappropriated.

Carlstrom Affidavit at paras. 78 & 84(2), Application Record, pp. 79 & 82.

Monitor's Pre-Filing Report at para 28.

33. Paragraph 22 of the Monitor's Pre-Filing Report estimates that Restricted Cash was approximately $14.7 million as at March 31, 2014. Given that actual cash on hand was only $2.94 million, this means that Cash Store Financial and Cash Store misappropriated at least $11.76 million (more than the $10 million approximated by Mr. Carlstrom during his cross-examination) of TPL monies to fund their operations and pay professional and other expenses not authorized by the TPLs, in breach of the broker agreements and their numerous representations that the TPLs' funds were safe, segregated and protected.

Monitor's Pre-Filing Report at para. 22

34. The remaining shortfall in TPL funds is explained at paragraph 22 of the Monitor Pre-Filing Report in which the Monitor explains that there are amounts totaling approximately $8.5 million in loans to customers pursuant to the broker agreements that the company considers "bad loans" that the Monitor indicates have been outstanding since at least 2012 and are unlikely to be recovered, although they have not yet been written off. The fact that these losses were booked to the third party lenders is a fact evidencing Cash Store's view that the loans are property of the third party lenders.

Monitor's Pre-Filing Report at para. 22.

35. As referenced in the Carlstrom Affidavit, Cash Store had a consistent pre-filing practice of inducing the TPLs to continue to advance capital by protecting the TPLs' capital through either an expensing or purchasing mechanism that ultimately insulated the TPLs from "any losses arising from brokered loans that remain unpaid after 90 days." On cross-examination, Carlstrom admitted that these two mechanisms were consistently applied to protect the capital of third party lenders and had been applied since he had been at the company. In other words, the

receivables and losses belonged to and were booked to the third party lenders, but subject to safeguards designed to protect the capital of the third party lenders.

Carlstrom Affidavit at para. 84(2), Application Record, p. 32.

Carlstrom Cross at Qs. 145-152, , Brief of Transcripts, Tab 1, pp. 35-37.

36. Given that Cash Store admittedly always made the TPLs whole from losses on bad loans that had remain unpaid after 90 days, they must have made the TPLs whole for the $8.5 million in "bad loans". Accordingly, this money ought to equally be added to the amount of Restricted Cash set out in paragraph 22 of the Monitor's Pre-Filing Report providing a true Restricted Cash Amount of $23.2 million (calculated by adding the $14.7 million reported by the Monitor to the $8.5 million in bad loans that would have been protected by Cash Store in accordance with its own evidence). Given that there is only $2.94 million in cash on hand, that means that Cash Store Financial and Cash Store actually misappropriated at least $20.26 of TPLs' monies

37. Had 0678786 been notified earlier that its monies were being spent on Cash Store Financial's general operations or to fund other unauthorized expenses, it would have immediately attended at Court to protect its money (as it ultimately did in the application it commenced in Alberta on April 11, 2014 to restrain the use of its funds). In fact, 0678786 engaged counsel and brought the application in Alberta (as required by its broker agreement) within three days of learning that Cash Store no longer regarded 0678786's monies as trust monies, or as segregated brokerage funds.

April 22 Fawcett Affidavit at paras. 7-8, 0678786 Application Record, Tab 2, pp. 8-9.

McCann Affidavit at para. 13, 0678786 Application Record, Tab 2, p. 3.

E. THE AMENDED AND RESTATED INITIAL ORDER PUTS THE TPLS AT FURTHER RISK

38. Paragraph 32 of the Amended and Restated Initial Order provides that monies for the collection of loans owned by the TPLs (including those owned by 0678786) are eligible to be re-loaned by Cash Store Financial and Cash Store. This is highly prejudicial to 0678786 and the other TPLs. Given Cash Store's well publicized insolvency proceedings, debtors may well be less likely to repay the loans and higher default rates can be anticipated. Moreover, with Cash Store's significantly increased costs and diversion of management's focus in relation to its insolvency proceedings, there is no assurance that Cash Store's collection policies and procedures will be maintained to enforce repayment of loans from customers. The TPLs never agreed to allow their funds to be loaned by an insolvent Cash Store.

April 22 Fawcett Affidavit at para. 10, 0678786 Application Record, Tab 2, p. 9.

39. In fact, on cross-examination, Mr. Carlstrom admitted that a number of Cash Store's customers are repeat customers and that if the Applicants are ultimately unsuccessful in their restructuring and have to go out of business, that it will affect their ability to collect monies that have been lent out. Moreover, Mr. Carlstrom admitted that given that Cash Store gets paid its commission at the time of lending, it has no credit risk in these third party lending broker transactions. This results in a perverse situation under the current Amended and Restated Initial Order in which only the TPLs, who have already had nearly half of their money misappropriated, would incur the increased lending risk of further lending their remaining monies while Cash Store would receive risk-free commission profits.

Carlstrom Cross at Qs 124-125, 137-138, 284-287 & 307, Brief of Transcripts, Tab 1, pp. 30, 33, 65-66 & 70.

40. Furthermore, with recent legislative and policy changes that have negatively affected payday loan businesses and the rates that they can charge (including in Ontario), it is highly doubtful that the Cash Store's operations will be as profitable as they once were or that a viable business is even possible, let alone probable.

41. Not only did the TPLs not agree to allow their monies and receivable to be held and used by an insolvent Cash Store, the Amended and Restated Order obtained by the Applicants puts the TPLs in even greater jeopardy as it purports to create charges against the TPLs' property and treat it as if it is property of the Applicants. Paragraph 53 of the Amended and Restated Initial Order provides that the TPL Charge contemplated by the Order is capped at $2.94 million (the "TPL Charge") and ranks third (*parri passu* with the DIP Lender) after the Administrative Charge and the Directors' Charge (up to a maximum of $1,250,000). This increases the risk that the costs of these proceedings will be paid out of TPLs' monies that simply do not belong to the Applicants.

III. LAW AND ARGUMENT

A. THE APPLICANTS WERE NOT FORTHRIGHT WITH THE COURT

42. When a party seeks *ex parte* relief, that party must abide by the duty to make full and frank disclosure. The party is not entitled to present only its side of the case in the best possible light, as it would if the other side were present. Rather, it is incumbent on the moving party to make a balanced presentation of the facts in law. The duty of full and frank disclosure is required to mitigate the obvious risk of injustice inherent in any situation where a Judge is asked to grant an order without hearing from the other side.

United States v. Friedland, [1996] O.J. No. 4399 (Ont. Ct. J. (Gen. Div.), at paras. 27-30

43. As set out above, despite bringing this application on an *ex parte* basis or in a manner akin to *ex parte*, the Applicants and the Applicants' affiant were not forthright with the court in the materials they filed in support of the Initial Order and in support of the Amended and Restated Initial Order:

(a) in seeking to have the Ontario court assume jurisdiction, the Applicants falsely represented that their principal place of business was Ontario; and

(b) in seeking the court's approval to continue lending funds advanced by third party lenders, the Applicants failed to tell the court that they had already misappropriated half of the funds advanced by third party lenders, using those funds for operations in breach of the broker agreements between the Applicants and the third party lenders.

B. THE AMENDED AND RESTATED INITIAL ORDER IS UNFAIR TO THE TPLS

44. As outlined above, in breach of the brokerage agreements and representations made to 0678786, approximately $20.4 million of TPLs' monies were misappropriated and used to finance the Applicants' operations. Having had nearly half of their monies misappropriated in such a brazen fashion, the TPLs should not now be forced to incur the significant risk of losing further monies to finance the restructuring of the very entities that misappropriated their funds.

45. While, as is briefly described below, 0678786 submits that the TPLs have a proprietary interest that ranks in priority over all creditors of the Applicants regarding the TPLs' monies that were brokered by Cash Store Financial and Cash Store, it acknowledges that such a priority

dispute will be determined by this Court at a future time on a full evidentiary record. In the interim, it seeks relief that will, at a minimum, preserve the TPLs' monies that have not yet been misappropriated by the Applicants to ensure that the TPLs are not further unjustly prejudiced.

46. 0678786 submits that the TPL Charge contemplated at paragraph 30 of the Amended and Restated Initial Order ought not only apply to the Applicants' cash-on-hand as of the effective time of the Initial Order, but should be fixed at $42 million (the amount of TPL funds that were held by Cash Store as broker to lend out on behalf of the TPLs) and apply to all of the Property (since the Property of the Applicants has come from misappropriated TPL funds) and the receivables and cash received in respect of TPL loans, pending further order of the Court. This will at least help ensure that the TPLs' positions will not be unduly prejudiced until this Court has an opportunity to determine whether these funds truly belong to the TPLs (which 0678786 submits that they all do), as opposed to the Applicants, on a full evidentiary record.

47. The priority of the TPL Charge set out in paragraph 53 of the Amended and Restated Initial Order should be elevated to a first priority ranking, until further order of the Court, given that if it is found that the disputed funds are the TPLs' monies, they ought to be returned to the TPLs at once. There is no principled basis upon which the Administration Charge, the Directors' Charge or the DIP Priority Charge should rank above or *pari passu* with the TPL Charge to the extent this Court concludes that the TPL monies are rightfully the property of the TPLs.

48. Furthermore, the Applicants should not be allowed to lend any further monies attributable to TPLs. All monies repaid on currently outstanding third party broker loans should be immediately paid into a segregated trust account, the proceeds of which ought to be held pending the final determination of the priority interest in the TPLs' funds. Furthermore, all of the

available cash on hand ought to be paid into that same segregated trust account as it is clearly the TPLs' money given that even on the Applicants' and Monitor's numbers, Restricted Cash exceeds available cash by $11.4 million.

49. While 0678786 acknowledges that the ultimate priority dispute over the TPL funds will take place at a future date, the below briefly sets out some of the reasons that 0678786 submits that the TPLs have a priority interest over all other creditors regarding their monies that were brokered by the Applicants.

1. The TPLs' Funds are Subject to an Equitable Trust

50. While it is unnecessary to resolve issues of entitlement at this time, at a later date the third party lenders will contend that the TPLs' funds are subject to an equitable trust.

51. The Supreme Court of Canada has set out four conditions which generally should be satisfied when granting a constructive trust for wrongful conduct:

i. The defendant must have been under an equitable obligation, that is, an obligation of the type that courts of equity have enforced, in relation to the activities giving rise to the assets in his hands;

ii. The assets in the hands of the defendant must be shown to have resulted from deemed or actual agency activities of the defendant in breach of his equitable obligation to the plaintiff;

iii. The plaintiff must show a legitimate reason for seeking a proprietary remedy, either personal or related to the need to ensure that others like the defendant remain faithful to their duties and;

iv. There must be no factors which would render imposition of a constructive trust unjust in all the circumstances of the case; e.g. the interests of intervening creditors must be protected.

Soulos v. Korkontzilas, [1997] S.C.J. No. 52 at para. 45.

52. The present facts satisfy the above four criteria. Cash Store was acting as the TPLs' *broker* and owed them a duty to handle their funds in the manner agreed in the broker agreements and as instructed by the TPLs.

53. The Applicants breached that duty by misappropriating the TPLs' funds to pay their operating costs as opposed to lending them out in third party brokered loan agreements.

54. There is a legitimate reason for seeking a proprietary remedy in order to ensure that other brokers on the eve of insolvency don't misappropriate brokered funds to fund their operations.

55. There are no factors that would render the imposition of a proprietary trust unjust. In fact, it would be wholly unjust to deprive the TPLs of their own funds given the misdeeds of Cash Store in failing to treat the TPLs' monies in a manner that fulfilled its duties to the TPLs. None of the Applicants' creditors have any proper claim over the TPLs' monies as they are not creditors of the TPLs.

56. Where a trust in imposed on funds in a mixed account, it is assumed that the trustee spends his own funds before spending those of the beneficiary. Accordingly, on the present facts, the Court is to assume that all remaining funds in the accounts belong to the TPLs.

> *Brookfield Bridge Lending Fund Inc. v. Vanquish Oil & Gas Corp.*, 2009 ABCA 99 at para. 13
>
> *Grant v. Ste. Marie*, 2005 ABQB 35 at para. 29

57. Such an imposition of an equitable trust is consistent with how securities brokerages firms are treated in the insolvency context and the regime set out in Part XII of the *Bankruptcy and Insolvency Act,* R.S.C., 1985, c. B-3 (the "BIA").

2. Analogy to a Securities Brokerage Firm

58. Cash Store was to *broker* the TPLs' monies. Just as an insolvent securities brokerage firm would not be entitled to use its clients' monies to finance its restructuring, nor should the Applicants be permitted to use the TPLs' monies to finance theirs.

59. Parliament has specifically addressed the concern of an insolvent securities brokerage firm in Part XII of the BIA. Part XII of the BIA provides that other than "customer name securities" (those securities that are held for the account of a customer and are registered or recorded in the appropriate manner in the name of the customer or are in the process of being registered or recorded), all other securities and cash held by a bankrupt securities firm are to be pooled in a "customer pool fund" and distributed among all customers of the firm on a pro rata basis. The customer pool fund is paid out before any creditors of the brokerage firm are paid at all.

> BIA, ss. 253 definition of "customer name securities" and ss. 261-262.

60. While 0678786 acknowledges that Part XII of the BIA is not applicable to the current situation, it submits that Part XII of the BIA is instructive in that it reflects a clear intention to prevent brokerage firms from using the monies they are to be brokering to satisfy their debts and to pay their creditors. Instead, if the assets they were to broker are not readily attributable to a particular client, they are to be pooled and distributed to the client pool on a *pro rata* basis. By analogy, 0678786 submits that the Applicants' cash on hand (and any monies received on the outstanding brokered loans) does not belong to the Applicants and ought to be distributed to its rightful owners (the TPLs) on a *pro rata* basis.

3. Under the CCAA, Lenders Have No Obligation to Advance More Funds

61. Subsection 11.01(b) of the CCAA provides that no order made under section 11 or 11.02 can have the effect of requiring the further advance of money or credit. This section appears under the heading "rights of suppliers" and has been held to stand for the proposition that under the CCAA, lenders have no obligation to advance more funds.

Re. Callidus Capital Corporation et al, 2012 ONSC 163 at para. 56

62. On the present facts, the current version of the Amended and Restated Initial Order forces the TPLs to lend their funds to customers of Cash Store through the brokering of new third party brokered loan agreements without their consent. Such an Order breaches subsection 11.01(b) as it purports to force the TPLs to further advance money or credit. It is respectfully submitted that this Honourable Court does not have the jurisdiction to force the TPLs to advance further money or credit, which is precisely the effect of the Amended and Restated Order in relation to the TPLs.

IV. RELIEF SOUGHT

63. Based on all of the above, 0678786 respectfully requests that the Amended and Restated Initial Order be Amended as follows:

(a) The TPL Charge contemplated in paragraph 30 of the Order be amended to be set at $42 million and apply against all of the TPLs' funds and receivables held by the Applicants and all of the Applicants' Property, pending further order of the Court;

(b) The priority of the TPL Charge as set out in paragraph 53 of the Order be elevated to a first priority ranking, in relation to the assets secured, until further order of the Court;

(c) That paragraph 32 of the Order be amended to expressly prohibit the Applicants from brokering new third party brokered loans and instead provide that all monies repaid on currently outstanding third party brokered loans be immediately paid into a segregated account, the proceeds of which are to be held pending the final determination or the proprietary interest in the TPLs' funds;

(d) All of the available cash on hand ought to be paid into that same segregated trust account; and

(e) A declaration by the Court that the Amended and Restated Initial Order and the CCAA Proceedings do not affect or prejudice any rights, remedies, claims or causes of action that any third party lender may have against any directors, officer or employees of the Cash Store or Cash Store Financial or any other person in relation to any insurance policies or proceeds with respect to any acts or

omissions of such directors, officers, employees or person prior to the CCAA filing date.

ALL OF WHICH IS RESPECTFULLY SUBMITTED,

BENNETT JONES LLP
Lawyers for 0678786 B.C. Ltd.

SCHEDULE "A" – AUTHORITIES CITED
Jurisprudence

1. *United States v. Friedland*, [1996] O.J. No. 4399 (Ont. Ct. J. (Gen. Div.))

2. *Soulos v. Korkontzilas*, [1997] S.C.J. No. 52

3. *Brookfield Bridge Lending Fund Inc. v. Vanquish Oil & Gas Corp.*, 2009 ABCA 99

4. *Grant v. Ste. Marie*, 2005 ABQB 35

5. *Re. Callidus Capital Corporation et al*, 2012 ONSC 163

SCHEDULE "B" – STATUTORY REFERENCES

Bankruptcy and Insolvency Act, R.S.C., 1985, c. B-3

PART XII

SECURITIES FIRM BANKRUPTCIES

Interpretation

Definitions

253. In this Part,

...

"customer name securities" means securities that on the date of bankruptcy of a securities firm are held by or on behalf of the securities firm for the account of a customer and are registered or recorded in the appropriate manner in the name of the customer or are in the process of being so registered or recorded, but does not include securities registered or recorded in the appropriate manner in the name of the customer that, by endorsement or otherwise, are negotiable by the securities firm;

...

Distribution of Estate

Vesting of securities, etc., in trustee

- **261.** (1) If a securities firm becomes bankrupt, the following securities and cash vest in the trustee:
  (*a*) securities owned by the securities firm;
  (*b*) securities and cash held by any person for the account of the securities firm; and
  (*c*) securities and cash held by the securities firm for the account of a customer, other than customer name securities.
- **Establishment of a customer pool fund and a general fund**

  (2) Where a securities firm becomes bankrupt and property vests in a trustee under subsection (1) or under other provisions of this Act, the trustee shall establish

  (*a*) a fund, in this Part called the "customer pool fund", including therein
  - (i) securities, including those obtained after the date of the bankruptcy, but excluding customer name securities and excluding eligible financial contracts to which the firm is a party, that are held by or for the account of the firm
  - (A) for a securities account of a customer,

- (B) for an account of a person who has entered into an eligible financial contract with the firm and has deposited the securities with the firm to assure the performance of the person's obligations under the contract, or
- (C) for the firm's own account,
- (ii) cash, including cash obtained after the date of the bankruptcy, and including
- (A) dividends, interest and other income in respect of securities referred to in subparagraph (i),
- (B) proceeds of disposal of securities referred to in subparagraph (i), and
- (C) proceeds of policies of insurance covering claims of customers to securities referred to in subparagraph (i),
- that is held by or for the account of the firm
- (D) for a securities account of a customer,
- (E) for an account of a person who has entered into an eligible financial contract with the firm and has deposited the cash with the firm to assure the performance of the person's obligations under the contract, or
- (F) for the firm's own securities account, and
- (iii) any investments of the securities firm in its subsidiaries that are not referred to in subparagraph (i) or (ii); and

(*b*) a fund, in this Part called the "general fund", including therein all of the remaining vested property.

- 1997, c. 12, s. 118;
- 2004, c. 25, s. 101(F);
- 2005, c. 47, s. 119.

Allocation and distribution of cash and securities in customer pool fund

- **262.** (1) Cash and securities in the customer pool fund shall be allocated in the following priority:

(*a*) for costs of administration referred to in paragraph 136(1)(*b*), to the extent that sufficient funds are not available in the general fund to pay such costs;
(*b*) to customers, other than deferred customers, in proportion to their net equity; and
(*c*) to the general fund.

- **Where property deposited with securities firm under an EFC**

(1.1) Where

(*a*) a person has, under the terms of an eligible financial contract with the securities firm, deposited property with the firm to assure the performance of the person's obligations under the contract, and
(*b*) that property is included in the customer pool fund pursuant to paragraph 261(2)(*a*),

that person shall share in the distribution of the customer pool fund as if the person were a customer of the firm with a claim for net equity equal to the net value of the property deposited that would have been returnable to the person after deducting any amount owing by the person under the contract.

- **Distribution**

(2) To the extent that securities of a particular type are available in the customer pool fund, the trustee shall distribute them to customers with claims to the securities, in proportion to their claims to the securities, up to the appropriate portion of their net equity, unless the

trustee determines that, in the circumstances, it would be more appropriate to sell the securities and distribute the proceeds to the customers with claims to the securities in proportion to their claims to the securities.

- **Compensation in kind**

(2.1) Subject to subsection (2), the trustee may satisfy all or part of a customer's claim to securities of a particular type by delivering to the customer securities of that type to which the customer was entitled at the date of bankruptcy. For greater certainty, the trustee may, for that purpose, exercise the trustee's power to purchase securities in accordance with section 259.

- **Allocation of property in the general fund**

(3) Property in the general fund shall be allocated in the following priority:

(*a*) to preferred creditors in the order set out in subsection 136(1);
(*b*) rateably
- (i) to customers, other than deferred customers, having claims for net equity remaining after distribution of property from the customer pool fund and property provided by a customer compensation body, where applicable, in proportion to claims for net equity remaining,
- (ii) where applicable, to a customer compensation body to the extent that it paid or compensated customers in respect of their net equity, and
- (iii) to creditors in proportion to the values of their claims;

(*c*) rateably to creditors referred to in section 137; and
(*d*) to deferred customers, in proportion to their claims for net equity.

- 1997, c. 12, s. 118;
- 2005, c. 47, s. 120.

Delivery of customer name securities

- **263.** (1) Where a customer is not indebted to a securities firm, the trustee shall deliver to the customer the customer name securities that belong to the customer.
- **Where customer indebted to securities firm**

(2) Where a customer to whom customer name securities belong and who is indebted to the securities firm on account of customer name securities not fully paid for, or on another account, discharges their indebtedness in full, the trustee shall deliver to that customer the customer name securities that belong to the customer.

- **Customer indebted to securities firm**

(3) If a customer to whom customer name securities belong and who is indebted to the securities firm on account of customer name securities not fully paid for, or on another account, does not discharge their indebtedness in full, the trustee may, on notice to the customer, sell sufficient customer name securities to discharge the indebtedness, and those securities are then free of any right, title or interest of the customer. If the trustee so discharges the customer's indebtedness, the trustee shall deliver any remaining customer name securities to the customer.

- 1997, c. 12, s. 118;
- 2005, c. 47, s. 121.

Companies' Creditors Arrangement Act

R.S.C., 1985, c. C-36

11. Despite anything in the *Bankruptcy and Insolvency Act* or the *Winding-up and Restructuring Act*, if an application is made under this Act in respect of a debtor company, the court, on the application of any person interested in the matter, may, subject to the restrictions set out in this Act, on notice to any other person or without notice as it may see fit, make any order that it considers appropriate in the circumstances.

- R.S., 1985, c. C-36, s. 11;
- 1992, c. 27, s. 90;
- 1996, c. 6, s. 167;
- 1997, c. 12, s. 124;
- 2005, c. 47, s. 128.

Rights of suppliers

11.01 No order made under section 11 or 11.02 has the effect of

- (*a*) prohibiting a person from requiring immediate payment for goods, services, use of leased or licensed property or other valuable consideration provided after the order is made; or
- (*b*) requiring the further advance of money or credit.

- 2005, c. 47, s. 128.

Stays, etc. — initial application

- **11.02** (1) A court may, on an initial application in respect of a debtor company, make an order on any terms that it may impose, effective for the period that the court considers necessary, which period may not be more than 30 days,
(*a*) staying, until otherwise ordered by the court, all proceedings taken or that might be taken in respect of the company under the *Bankruptcy and Insolvency Act* or the *Winding-up and Restructuring Act*;
(*b*) restraining, until otherwise ordered by the court, further proceedings in any action, suit or proceeding against the company; and
(*c*) prohibiting, until otherwise ordered by the court, the commencement of any action, suit or proceeding against the company.
- **Stays, etc. — other than initial application**

(2) A court may, on an application in respect of a debtor company other than an initial application, make an order, on any terms that it may impose,

(*a*) staying, until otherwise ordered by the court, for any period that the court considers necessary, all proceedings taken or that might be taken in respect of the company under an Act referred to in paragraph (1)(*a*);
(*b*) restraining, until otherwise ordered by the court, further proceedings in any action, suit or proceeding against the company; and
(*c*) prohibiting, until otherwise ordered by the court, the commencement of any action, suit or proceeding against the company.

- **Burden of proof on application**

(3) The court shall not make the order unless

(*a*) the applicant satisfies the court that circumstances exist that make the order appropriate; and
(*b*) in the case of an order under subsection (2), the applicant also satisfies the court that the applicant has acted, and is acting, in good faith and with due diligence.

- **Restriction**

(4) Orders doing anything referred to in subsection (1) or (2) may only be made under this section.

- 2005, c. 47, s. 128, 2007, c. 36, s. 62(F)

IN THE MATTER OF THE *COMPANIES CREDITORS' ARRANGEMENT ACT*, R.S.C. 1985, c. C-36, AS AMENDED AND IN THE MATTER OF A PLAN OR COMPROMISE OR ARRANGEMENT OF CASH STORE FINANCIAL SERVICES INC. et al

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