Court File No. CV-14-10518-00CL

ONTARIO
SUPERIOR COURT OF JUSTICE - COMMERCIAL LIST

B E T W E E N :

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., INSTALOANS INC., 7252331 CANADA INC., 5515433 MANITOBA INC., 1693926 ALBERTA LTD. DOING BUSINESS AS "THE TITLE STORE"

APPLICANTS

REPLY AND RESPONDING FACTUM OF TRIMOR ANNUITY FOCUS LP #5
(returnable June 11, 2014)

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TO: THE SERVICE LIST

PART I - INTRODUCTION

1. There are two issues on this motion and cross-motion.

2. The issue on the motion is ownership of the outstanding loans ("**TPL Loans**") in the name of Trimor Annuity Focus Limited Partnership #5 ("**Trimor**") and the other third party lenders ("**TPLs**") at the time of the Applicants' CCAA filing, and the proceeds of those TPL Loans.

3. The DIP Lenders to the Applicants (the "**DIP Lenders**") argue that they should benefit from the comingling of funds by the Applicants in breach of their Broker Agreements with the TPLs. The DIP Lenders suggest that as a result of the comingling of funds, the Cash Store converted the TPLs' property, the TPL Loans, into its own property. Despite, having had the benefit of full disclosure of the nature of the Cash Store's business model and its legal relationship with the TPLs at all relevant times, the DIP Lenders now argue opportunistically for the enlargement of the Applicants' estate for their benefit.

4. The issue on the cross-motion is whether the Transactions (as defined below) are preferences under the applicable legislation.

PART II - THE FACTS

5. In determining the issue of ownership, it is important to carefully consider the facts.

6. In reviewing the arguments made by the DIP Lenders, it must be remembered that when they decided to become creditors of Cash Store they were aware of the following facts, all of which were highlighted in a Preliminary TSCI Circular dated January 12, 2012 ("**Preliminary TSCI Circular**"):[1]

(a) Cash Store acts "primarily as a broker of short-term advances between our customers and third-party lender, ***the effect of which is that the loan portfolio we service is not financed on our balance sheet***..."[2]

(b) "... our business will remain dependant on third-party lenders who are willing to make funds available for lending to our customers. ***There are no assurances that the existing or new third-party lenders will continue to make funds available to our customers.*** Any reduction or withdrawal of funds could have a significant material adverse impact on this portion of our business..."[3]

(c) "***The advances provided by the third-party lenders are repayable by the customer to the third-party lenders and represent assets of the lenders; accordingly, they are not included on our balance sheet***..."[4]

(d) "We have made the decision to ***voluntarily make retention payments to the third-party lenders as consideration for continuing to advance funds to our customers.*** The retention payments are made pursuant to a resolution approved

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[1] Second Armstrong Affidavit sworn May 8, 2014 ("**Second Armstrong Affidavit**") at para. 5 and Exhibit "A" - Preliminary TCSI Circular at p. 4 (internal); Motion Record of Trimor, Tab 3.
[2] *Ibid.* at p. 4 (internal).
[3] *Ibid.* at p. 16 (internal).
[4] *Ibid.* at p. 38 (internal).

by our board of directors (the "Board") which authorizes management to pay a maximum amount of retention payments per quarter, and the retention payments are recorded in the period in which a commitment is made to a lender pursuant to the resolution..."[5]

(e) "***While the third-party lenders have not been guaranteed a return, the decision has been made to voluntarily make retention payments to the lenders to lessen the impact of loan losses experienced by the third-party lenders***..."[6]

7. From the above it is clear that the DIP Lenders were aware that the TPL Funds and Receipts were not assets of Cash Store and that the TPLs were receiving retention payments referred to above to the extent authorized from time to time by the Board of Cash Store.

8. Despite this disclosure, the DIP Lenders are now claiming that because Cash Store commingled the proceeds of the TPL Loans, without the knowledge of the TPLs and in clear breach of the Broker Agreement, they have now been converted into an asset of Cash Store.

9. They go on to argue that the receipt of the Retention Payments, which were fully disclosed, supports this argument because these voluntary, discretionary payments transformed a brokerage arrangement into a loan.

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[5] *Ibid.*
[6] *Ibid.*

10. Lastly, they claim that the TPLs did not bear any collection risk, which they say leads to the conclusion that the TPLs are creditors. This is patently false. As described in more detail below, according to Cash Store, almost a third of the Trimor loan portfolio has gone bad and there is little chance of collecting those loans. The risk of loss could not be more clear.

A. Comingling of TPL Loans Proceeds

11. It is uncontested that the Broker Agreements (i) provide for the proceeds of the TPL Loans to be segregated, and (ii) make it very clear that they are only to be used for the purpose of brokering loans to third parties. One of the reasons for this was that it was important from a regulatory perspective that the funds being lent, and the TPL Loans themselves, did not belong to the Applicants.

12. To the extent that the Cash Store comingled funds, it breached the terms of the Broker Agreements. Contrary to the assertions made by the DIP Lenders, there was no reason for the TPLs to believe that the Cash Store would breach the Broker Agreements and applicable regulatory requirements.

13. The DIP Lenders, who are also pre-filing secured creditors of the Applicants, are now opportunistically attempting to use these breaches of the Broker Agreements as justification for confiscating the TPLs' property.

14. The DIP Lenders argue that by comingling the proceeds of the TPL Loans with its own funds, Cash Store converted the TPL Loans into an asset of Cash Store. Their argument suggests that the Cash Store ought to be entitled to rely on its breach of the

Broker Agreements, and if the DIP Lenders are to be believed, potentially applicable law, to convert the TPL Funds to a Cash Store asset.[7]

B. Retention Payments and Collection Risk

15. The DIP Lenders correctly note that Cash Store's legal relationship with the TPLs is not exhaustively defined by the Broker Agreements. The conduct of the parties is also relevant. For example, the payment of voluntary retention payments and capital protection was not provided for in the Broker Agreements. As highlighted above, these payments and transfers were disclosed to all of Cash Stores creditors, including the DIP Lenders/bondholders/secured creditors and were approved by Cash Store's Board of Directors pursuant to resolutions passed from time to time, presumably in accordance with the Board's business judgment. [8] Despite an oblique reference to the contrary in the DIP Lenders' factum, there is not a shred of evidence that suggests that the Cash Store did not at all relevant times operate at arm's length from the TPLs.

16. The reason for these payments is clear. This brokering model was very lucrative for Cash Store, which received a risk free 23% brokering fee upfront each and every time a loan was made. That meant that it made a risk free profit on every transaction, and the TPLs assumed the borrower's credit risk.[9] Without the retention payments, the TPLs

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[7] The *ex turpi causa* doctrine prohibits a party from benefitting from its illegal or immoral conduct: *Randhawa v. 420413 B.C. Ltd.*, 2009 BCCA 602 at para. 66 citing *Canada Cement LaFarge Ltd. v. British Columbia Lightweight Aggregate Ltd*., [1983] 1 S.C.R. 45; Book of Authorities of Trimor, Tab 1. This doctrine has been applied in the context of bankruptcy proceedings. In *Re Bluebird Corp*. [1926] 2 D.L.R. 484, the Court confirmed that "no one can have the assistance of the Court in an attempt to place himself in better legal position by breaking the law." Book of Authorities of Trimor, Tab 2.

[8] Affidavit of Steven Carlstrom sworn April 14, 2014 ("**Carlstrom Affidavit**") at para. 85; Motion Record of the Applicants at Tab 1.

[9] Report of PricewaterhouseCoopers dated May 14, 2014 (the "**PwC Report**") at p. 6 (internal); Motion Record of Trimor, Tab 4.

would have demanded the return of the TPL Loans and proceeds and deprived the Cash Store of an important source of revenue that could be used, among other things, to service its secured loans and bonds. [10]

17. To encourage the TPLs to continue to make the TPL Funds available for brokering, the Cash Store decided from time to time to make Retention Payments. As stated by Mr. Carlstrom in his affidavit, "Under the broker model, Cash Store makes voluntary retention payments to the TPLs to encourage them to continue making funds available to Cash Store".[11]

18. The Retention Payments made by the Cash Store were neither "fixed" nor "guaranteed". The Retention Payments were "voluntary" and could be made in any amount the Cash Store Board of Directors determined appropriate, which is evidenced by the fact that they fluctuated over time.[12] They were entirely at the discretion of the Cash Store and could be terminated unilaterally by the Cash Store at any time, as can be seen by the fact that, as the DIP Lenders state in their factum, "Cash Store elected not to make any ***voluntary*** retention payments to the TPLs" after February 2014.[13]

19. While it is true that, as stated in Mr. Carlstrom's affidavit, the Retention Payments were made to "lessen the impact of loan losses",[14] there is no doubt that the TPLs continue to have collection risk and suffered loan losses. In fact, the Applicants

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[10] Carlstrom Affidavit at para. 85; Motion Record of the Applicants at Tab 1.
[11] Carlstrom Affidavit at para. 85; Motion Record of the Applicants at Tab 1.
[12] Trimor Distribution Summary, March 2014, DIP Lender Cross-Motion Record, Tab 2
[13] DIP Lender Factum, para. 47
[14] Carlstrom Affidavit at para 84; Motion Record of the Applicants at Tab 1.

allege that Trimor experienced more than $8 million in loan losses according to Cash Store's records.[15]

20. The DIP Lenders inaccurately state at paragraph 27 of their factum that the reason that 0% of Trimor's loans were greater than 90 days past due is that Cash Store had "acquired all of Trimor's bad debt, insulating it completely from the credit risk of the payday lending products." This is simply wrong. The reason that 0% of Trimor's loans were more than 90 days overdue is that Cash Store wrote off all loans that were more than 90 days past due. The amount of loans that were more than 90 days past due is included in the "balance forward" shown in the Trimor portfolio summary as at March 31, 2014 contained in the PwC Report.[16]

21. This is clearly stated in the PwC Report, "The current loan portfolio balance represents loans less than 90 days overdue" and "The balance forward [of $8,514,000] presented on the lender statement is comprised primarily of loans more than 90 days overdue". [17] PwC goes on to state that "The Company has acknowledged that loans more than 90 days [overdue] are more difficult to collect and have a low likelihood of being collected".[18] As a result, there is a low likelihood that Trimor will recover approximately 30% of the amounts it has lent to Cash Store customers. This is a significant credit risk.

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[15] PwC Report at pp. 13 and 17, Trimor Motion Record, Vol. 3, Tab 4.
[16] PwC Report at p. 13, Trimor Motion Record, Vol. 3, Tab 4.
[17] PwC Report at p. 17; Trimor Motion Record, Vol. 3, Tab 4.
[18] PwC Report at p. 18; Trimor Motion Record, Vol. 3, Tab 4.

PART III - ISSUES AND THE LAW

22. The sole issue on the cross-motion is whether making payments to the TPLs is a preference under the legislation referred to by the DIP Lenders.

A. The Brokering Business was not a Preference

i. The TPLs are not creditors of the Cash Store

23. The TPLs are not creditors of Cash Store with respect to the TPL Loans or proceeds of the TPL Loans. It is clear from both the Broker Agreements and the conduct of the parties that the TPL funds were made available by the TPLs solely for the purpose of brokering TPL Loans to third parties, and were not lent to Cash Store.

24. The cases relied on by DIP Lenders to assert a debtor-creditor relationship are either distinguishable or support the TPLs argument that there is no such relationship.

25. The DIP Lenders argue that the Retention Payments are "interest" and that this establishes a debtor-creditor relationship. The only "interest" that was required to be paid to the TPLs was to be paid by the Applicants' customers. In Trimor's case, the obligation to pay interest was set out in the loan agreements entered into between Trimor (not Cash Store) and the Applicants' customers.[19] The DIP Lenders have not introduced any evidence that any TPL Loans in the name of Trimor were made pursuant to agreements between Cash Store and its customers. There is no legal obligation for any customer of Cash Store that is a borrower under a TPL Loan in the name of Trimor to pay principal or interest to Cash Store. A customer's legal obligation to Cash Store is to pay a broker commission at the time a loan is made.

26. As between Cash Store and Trimor, the risk of a customer failing to repay its loan remained solely with Trimor. The fact that Cash Store might unilaterally and

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[19] PwC Report p. 10, Motion Record of Trimor, Vol. 3, Tab 4.

voluntarily elect to offset all or a portion of the losses arising from that risk from time to time in order to induce Trimor to leave the TPL Loans with Cash Store does not turn a broker relationship into a debtor creditor relationship.

27. At paragraph 53 of their Factum, the DIP Lenders include a quote from *Oosterhoff on Trusts* which actually supports the TPLs position. It states that:

> [T]he debtor always remains liable to the creditor until the debt is paid. The trustee, however, is not personally obligated to compensate the beneficiaries if the trust property is lost other than through the trustee's own fault.

28. That is exactly the case here. According to the Applicants, Trimor currently holds over $8 million in bad, or written off, loans in its loan portfolio. As provided in the Broker Agreement, Cash Store has no obligation to make Trimor whole unless it was negligent in its duties.[20] When the Broker Agreement terminates, all that the TPLs receive is the cash and loans in existence at the time of the termination, which includes all of the bad loans.[21] Nothing in the Broker Agreements or in the Cash Store's conduct requires the Cash Store to make the TPLs whole for bad loans. The TPLs are at risk, not the broker, Cash Store.

29. At paragraph 55 of their Factum, the DIP Lenders rely on *Salo v. Royal Bank of Canada*, where the Court held that "no direction or control was exercised"[22] over the property at issue. The facts of this case obviously differ from *Salo*. Trimor exercised

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[20] Affidavit of Erin Armstrong sworn April 13, 2014 (the "**Armstrong Affidavit**") – Exhibits "A" and "B", s. 7.1; Motion Record of Trimor, Tab 1.
[21] Armstrong Affidavit – Exhibits "A" and "B, s. 6.4; Motion Record of Trimor, Tab 1.
[22] 1998 BCJ No. 999 (BCCA) at p. 2; Book of Authorities of Trimor, Tab 3.

significant control over the TPL Funds, which included, but was not limited to, the fact that:

(a) The Broker Agreements required the TPL Funds to be segregated from Cash Store's funds; [23]

(b) The TPL Funds could only be used for the purpose of brokering loans to third parties;[24]

(c) The TPLs retained the right to reduce the TPLs Funds available for brokering on 120 days' notice;[25]

(d) Trimor had the legal authority to approve loans and specify the amounts of loans that were made to Customers;[26] and

(e) The TPLs had audit rights, which they exercised.[27]

30. In paragraph 54 of its factum, the DIP Lender relies on *Outset Media Corp. v. Stewart House Publishing Inc.* ("*Outset*").[28] That case is also clearly distinguishable from the facts here. In *Outset*, "the parties entered into a contract that obligated the applicant to pay the respondent 75 percent (a fixed rate) of an amount invoiced to purchasers regardless of the ultimate sale price of the product. In contrast, Cash Store had no obligation under the Broker Agreement, or otherwise, to make the voluntary retention payments at a particular rate, or at all.

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[23] Affidavit of Erin Armstrong sworn April 13, 2014 (the "**Armstrong Affidavit**") – Exhibits "A" and "B", s. 1.1(g) and (h).
[24] Transcript of Cross-Examination of Erin Armstrong on her affidavits sworn April 13 and May 8, 2014 held on May 21, 2014 ("**Armstrong Cross-Examination Transcript**"), questions 97, 98, 168 and Exhibits "1", "2", "3" and"9"; Motion Record of Trimor at Tab 6.
[25] Armstrong Affidavit, Exhibits "A" and "B" at ss. 2.2 and 6.4.
[26] Armstrong April 13 Affidavit, at para. 13, Motion Record of Trimor at Tab 1 and Armstrong Affidavit at para. 13, Exhibits "A" and "B" at s. 2.3, Motion Record of Trimor at Tab 6.
[27] Armstrong Affidavit at para. 13, Exhibits "A" and "B" at s. 5.1, Carlstrom Affidavit at para. 134 and Exhibit "U".
[28] [2003] O.J. No. 2558 (C.A.); Book of Authorities of Trimor, Tab 4.

31. The DIP Lenders have fundamentally mischaracterized what they refer to as the "basic foundation" of the relationship between Cash Store and the TPLs. The TPLs had no legal right to a specified rate of return on their capital and the TPLs assumed the credit risk of Cash Store's customers.

32. The DIP Lenders' claim that Trimor made its funds "generally available to Cash Store in the running of its business" is also simply wrong. In fact, Trimor obtained an express statement from Cash Store that it had "never used [proceeds of Trimor Loans] for any other purpose than loans to customers or maintaining a loan float."[29] Trimor also believed that the Trimor Funds were also separated from Cash Store's funds in a segregated account containing only TPL Funds.[30]

ii. If TPLs were Otherwise Creditors of Cash Store, the Proceeds of TPL Loans are impressed with a Trust

33. To the extent that this Court finds that there is a creditor-debtor relationship between the Cash Store and Trimor, the Trimor Loans and Receipts are the subject of a "Quistclose trust". A "Quistclose trust" arises in the following circumstances:

(a) Where the mutual intent of the parties is that the funds advanced be used exclusively for a particular use, the lender obtains an equitable right to see that the funds are applied for the primary designated purpose;[31] and

(b) If the primary purpose cannot be carried out, the question arises if a secondary purpose (*i.e.*, repayment to the lender) has been agreed expressly or by implication. If so, a secondary resulting "Quistclose trust" arises for the benefit of the lender.[32]

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[29] Transcript of Cross-Examination of Erin Armstrong on her affidavits sworn April 13 and May 8, 2014 held on May 21, 2014 ("**Armstrong Cross-Examination Transcript**"), Exhibit "3" and "9"; Motion Record of Trimor at Tab 6.
[30] Second Armstrong Affidavit at para. 10; Motion Record of Trimor, Tab 3.
[31] *Maple Homes Canada* , 2000 BCSC 1443 at para. 47 citing *Barclays Bank Ltd. v. Quistclose Investments Ltd*. (1968), [1970] A.C. 567 (U.K. H.L.).
[32] *Maple Homes Canada* , 2000 BCSC 1443 at para. 47 citing *Barclays Bank Ltd. v. Quistclose Investments Ltd*. (1968), [1970] A.C. 567 (U.K. H.L.).

34. Cash Store advised Trimor that it would not use Trimor Loans and Receipts for any purpose other than advancing loans in accordance with the Broker Agreements, unless Cash Store first obtained Trimor's written permission.[33] No such permission was ever granted. Cash Store also advised Trimor that it had "never used [Trimor Funds] for any other purpose than loans to customers or maintaining a loan float."[34]

35. The CRO has determined, in consultation with the Monitor, that it is necessary and appropriate to implement a cessation of the brokered loan business and cease brokering new loans in all jurisdictions in which the Cash Store operates.[35] Cash Store's intention to cease all brokered loan operations effectively terminates the Broker Agreements.

36. Trimor and Cash Store expressly agreed that on termination of the Broker Agreements, the Trimor Loans and Receipts would, at the sole option of Trimor, be repaid to Trimor.[36] Accordingly, the Trimor Loans and proceeds of Trimor Loans are the subject of a "Quistclose Trust" for the benefit of Trimor.

B. The Transfer of Loan Receivables to TPLs Was Not a Preference

37. The DIP Lenders seek a declaration that two categories of transactions which occurred between the TPLs and the Cash Store constitute preferences:

(a) Cash Store's designation of advances or loans in the TPLs' names; and

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[33] Armstrong Cross-Examination Transcript, questions 97, 98, 168 and Exhibits "1", "2", "3" and"9".
[34] Armstrong Cross-Examination Transcript, Exhibit "3" and "9".
[35] Affidavit of William Aziz sworn May 9, 2014 (the "**Aziz Affidavit**") at para. 29.
[36] Upon termination of the Broker Agreements, Trimor has the option to allow the Applicants to continue to administer the Trimor Loans, transfer the administration of them to a new service provider, or sell the Trimor Loans to a third party. Armstrong Affidavit, Exhibits "A" and "B" at paras. 6.4.

(b) Any assignment by the Cash Store to the TPLs of non-brokered loans made in Cash Store's name (the "**Transactions**").

38. By way of cross-motion, the DIP Lenders ask for the Court's assistance in reversing the Transactions in order, they say, to ensure that the proceeds of loans made or brokered by the Cash Store are available to all creditors in accordance with their respective priorities. This application has nothing whatsoever to do with "all creditors" of the Cash Store nor is it brought in furtherance of the policies and objectives of the CCAA. This is a blatant attempt by the DIP Lenders to summarily opportunistically scoop the TPL Loans and the proceeds of the TPL Loans to secure repayment of their DIP Loans and nothing more. The DIP Lenders lack both the standing and the legal basis to impugn any Transactions. This backend attack on the substance of the Broker Agreements and the regular course business practices between the TPLs and the Cash Store of which the DIP Lenders ("qua" DIP Lenders, pre-filing lien holders and pre-filing bondholders) were always well aware ought not to be countenanced by this Court.

i. The DIP Lenders Lack Standing to Bring Preference Claim

39. Creditors, such as the DIP Lenders, are not entitled as of right to impugn a payment as a preference in a CCAA proceeding.

40. Under sections 95 and 96 of the BIA, a trustee in bankruptcy has the right to impugn a payment or transaction as a preference or transfer at undervalue. Section 36.1 of the CCAA extends this right to a CCAA Monitor. It does not extend it to individual creditors of the CCAA estate unless the creditor complies with Section 38 and takes an

assignment of the claim. The Monitor has not challenged any transaction involving the TPLs as a preference. The DIP Lenders have not purported to take an assignment of the claim, nor would it be appropriate for them to do so in light of their express or implied consent to the ordinary course Transactions that they now complain of.

ii. The Transactions are not void as Preferences

41. Even if the DIP Lenders' motion was properly before the Court, the Transactions are not preferences or otherwise void under any legal theory advanced by the DIP Lenders in their cross-motion and factum or any other legal theory. The DIP Lenders seek to void or set aside the Transactions as:

(a) preferences under section 95 of the BIA; or

(b) void transactions under section 2 of Ontario's Fraudulent Conveyances Act and section 3 of Alberta's Fraudulent Preferences Act (Alberta).[37]

42. The DIP Lenders must, in order to successfully impeach the Transactions under any of these provisions, prove the following essential elements:

(a) that the Cash Store was insolvent at the time of the Transactions; and

(b) that the Transactions were made with the intention to prefer or that the Transactions were made outside the ordinary course of business of the Cash Store and for inadequate consideration.

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[37] BIA, ss 95, 96; *Fraudulent Conveyances Act*, RSO 1990, c F.29 [***FCA***] s. 2; *Fraudulent Preferences Act*, RSA 2000, c F-24 [***FPA***] ss. 2, 3.

43. The DIP Lenders have not proven any of these elements.

C. DIP Lenders have Failed to Establish the Statutory Requirements for a Preference

44. Under section 95 of the BIA, a trustee in bankruptcy (or a monitor in a CCAA) is empowered to attack certain payments, transfers of property or provision of services before the initial bankruptcy event with the intent of preferring one arms' length creditor (or multiple creditors) over others.

45. A pre-CCAA-filing transaction with an arm's length creditor is void under section 95 if three conditions are met:

(a) The transaction was made within the prescribed period;

(b) The debtor was insolvent on the date of the impugned transaction; and

(c) The debtor intended to prefer one creditor over another.[38]

46. For arm's length creditors, the prescribed period is three months before the date of the initial bankruptcy event. For non-arm's length creditors, the prescribed period is one year before the date of the initial bankruptcy event.

47. The BIA provides that test for determining whether non-related parties are dealing at arm's length is whether the "transaction at arm's length could be considered to

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[38] *Keith G Collins Ltd v Canadian Imperial Bank of Commerce*, 2011 MBCA 41 at para 19, 268 Man R (2d) 30; Book of Authorities of Trimor, Tab 9. *Touche Ross Ltd v Weldwood of Canada Sales Ltd*, 48 CBR (NS) 83 at paras 3- 7, 1983 CarswellOnt 214 (SC) [*Touche Ross*]; Book of Authorities of Trimor, Tab 10.

be a transaction between persons between whom there are no bonds of dependence, control or influence, in the sense that neither of the two co-contracting parties has available any moral or psychological leverage sufficient to diminish or possibly influence the free decision-making of the other".[39]Notwithstanding a vague reservation of rights in their Factum, the DIP Lenders have not seriously suggested, nor have they provided any evidence to establish, that any of the TPLs did not operate at arm's length from the Cash Store.

48. There is no evidence that either the Cash Store or Trimor have any moral or psychological leverage over one another that would diminish or possibly influence the free decision-making of the other. The DIP Lenders have not shown that the Cash Store and Trimor do not deal at arm's length. Therefore that three month period applies.

49. Section 2 of the FCA requires the DIP Lenders to prove intent to "defeat, hinder, delay or defraud" creditors. For conveyances made for good consideration, the DIP Lenders must prove the fraudulent intent of both parties to the transaction. For voluntary conveyances, the DIP Lenders need to prove the fraudulent intent of the maker of the conveyance.[40]

50. In Alberta, the FPA sets out rules which are substantially similar to those in Ontario. Under section 3 of the FPA, a transaction is void if, within one year of the impugned transaction, an action is commenced to set it aside, the debtor company was

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[39] BIA, s. 4(4); *Abou-Rached*, Re 2002 BCSC 1022 at para 46; Book of Authorities of Trimor, Tab 11.
[40] *FCA*, s. 2.

in insolvent circumstances or unable to pay debts in full or was on the eve of insolvency, and the transaction had the effect of giving a creditor a preference. Section 3 provides as follows:

> [3 Subject to sections 6 to 9, every gift, conveyance, assignment, transfer, delivery over or payment of goods, chattels or effects or of bills, bonds, notes or securities or of shares, dividends, premiums or bonus in any bank, company or corporation, or of any other property, real or personal, made
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> (a) by a person at a time when the person is in insolvent circumstances or is unable to pay the person's debts in full or knows that the person is on the eve of insolvency, and
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> (b) to or for a creditor and having the effect of giving that creditor a preference over the other creditors of the debtor or over any one or more of them,
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> is, in and with respect to any action that within one year after the transaction is brought to impeach or set aside the transaction, void as against the creditor or creditors injured, delayed, prejudiced or postponed.

51. While an intention to prefer need not be shown under section 3 of the FPA if the impugned transaction has preferential effect, bona fides transactions are protected from the ambit of the FPA at s. 6, which provides:

> **6** Nothing in sections 1 to 5 applies to
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> (a) a bona fide sale or payment made in the ordinary course of trade or calling to innocent purchasers or parties, or
>
> (b) a payment of money to a creditor, or a bona fide conveyance, assignment, transfer or delivery over of any goods, securities or property, of any kind as above mentioned, that is made in consideration of a present actual bona fide sale or delivery of goods or other property or of a present actual bona fide payment in money, or by way of security for a present actual bona fide advance of money,
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> if the money paid or the goods or other property sold or delivered bear a fair and reasonable relative value to the consideration for it.

52. As described in greater detail below, all of the Transactions were in the ordinary course of business.

ii. No Evidence of Insolvency

53. All of the statutory provisions pursuant to which the DIP Lenders ask the court to set aside the Transactions require the DIP Lender's to prove that the Cash Store was insolvent at the time the Transactions took place.

54. A party seeking to have a transaction set aside on the basis that it constitutes a preference has the burden of proving that the debtor was in fact insolvent at the time of the impugned transaction. The court is not to presume insolvency.[41]

55. Pursuant to s. 2 of the BIA, "insolvent person" means

> a person who is not bankrupt and who resides, carries on business or has property in Canada, whose liabilities to creditors provable as claims under this Act amount to one thousand dollars, and
>
> (a) who is for any reason unable to meet his obligations as they generally become due,
>
> (b) who has ceased paying his current obligations in the ordinary course of business as they generally become due, or
>
> (c) the aggregate of whose property is not, at a fair valuation, sufficient, or, if disposed of at a fairly conducted sale under legal process, would not be sufficient to enable payment of all his obligations, due and accruing due;

56. In a recent decision of the Ontario Superior Court, it was held that despite the fact that the plaintiff was in default of their mortgage (failed to make payments for 13 months), they were not insolvent under the BIA.

57. An application under section 248 must be made by an insolvent person. The onus of proving insolvency is on the applicant, on a balance of probabilities. The definition of

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[41] *Keith G. Collins Ltd. v. Canadian Imperial Bank of Commerce*, 2011 MBCA 41 at para. 20; Book of Authorities of Trimor, Tab 9.

an "insolvent person" is found in section 2 of the BIA. Having regard to that definition, although I am satisfied the Plaintiff is not bankrupt, carries on business in Canada, and has liabilities in excess of $1,000, there has been no evidence led upon which I could find it is unable to meet its obligations in the ordinary course of business, has ceased paying its current obligations in the ordinary course of business as they generally become due, or that the aggregate of its property is not, at a fair valuation, sufficient, if disposed of at a fairly conducted sale under legal process, to enable payment of all its obligations.[42]

58. The DIP Lenders have not produced any evidence to show that the Cash Store was insolvent as of September 2013 or any time prior to April 14, 2014. They have not shown that the Cash Store was unable to meet its obligations generally as they became due or that the Cash Store had ceased meeting its obligations in the ordinary course of business.

59. The DIP Lenders have also not proven that, as at September 2013, the aggregate of the Cash Store's property if disposed of at a fairly conducted sale under legal process, would not be sufficient to enable payment of all his obligations, due and accruing due. Simply referring to the book value of the assets and liabilities as stated on Cash Store's balance sheet is not enough to meet the burden. In *King Petroleum Ltd*., Re, 29 C.B.R. (N.S.) 76, the Ontario Superior Court noted as follows:

> 11 To consider the question of insolvency under cl. (c) I must look to the aggregate property of the company and come to a conclusion as to whether or not

[42] *917488 Ontario Inc. v. Sam Mortgages Ltd*, 2013 ONSC 2212 at para. 38.

> it would be sufficient to enable payment of all obligations due and accruing due. There are two tests to be applied: first, its fair value and, secondly, its value if disposed of at a fairly conducted sale under legal process. The balance sheet is the starting point, but the evidence relating to the fair value of the assets and what they might realize if disposed of at a fairly conducted sale under legal process must be reviewed in interpreting it.[43]

iii. The Transactions occurred in the ordinary course of business of the Cash Store

60. All of the statutory provisions relied on by the DIP Lenders, with the exception of section 3 of the FPA require the DIP Lenders to show that the Cash Store intended to prefer the TPLs. However, section 3 of the FPA presumes a preference has occurred if the impugned transaction has the effect of preferring a creditor but transactions made in the ordinary course of the business of the debtors or payments given by the debtor in exchange for a benefit are exempted from the application of section 3 and the other avoidance provisions in the FPA.

61. The debtor's intention and ordinary course of business are related concepts. If a transaction occurred in the ordinary course of the debtor's business or payment or transfer given in exchange for present consideration the presumption of intention that such transaction, payment or transfer constituted a preference is rebutted.[44]

62. The fact is that the Transactions occurred in the ordinary course of business of the Cash Store in accordance with the Broker Agreements entered into by the Cash Store outside the review periods prescribed by the various statutes with the full knowledge of

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[43] *King Petroleum Ltd*., Re, 29 C.B.R. (N.S.) 76 at para. 11; Trimor Book of Authorities of Trimor, Tab 12.
[44] *St. Anne-Nackawic Pulp Co. (Trustee of) v. Logistec Stevedoring (Atlantic) Inc.*, 2005 NBCA 55 at para 13; Trimor Book of Authorities of Trimor, Tab 17; L.W. Houlden and Geoffrey B. Morawetz, *Houlden and Morawetz Bankruptcy and Insolvency Analysis*, Bankruptcy and Insolvency Act Part IV (ss. 67-101.2), F§210 — Rebutting The Presumption; Trimor Book of Authorities, Tab 18.

the secured creditors and bondholders. Further the transfers of loan receivables were made for valuable consideration to encourage the TPLs to continue to make their funds available to the Cash Store, again with the knowledge of the secured creditors and bondholders.

63. Intention requires an objective assessment of the debtor's intention at the time of the transaction. Justice Bastin furnished the quintessential statement of this test in *Re Holt Motors Ltd.*:[45]

> The test which I consider should be applied is an objective and not a subjective one, that is to say, the intention which should be attributed to the parties will always be that which their conduct bears a reasonably construed and not that which, long after the event, they claim they believe was present in their minds.

64. In the present case, as in the Holt Motors case, the intention which should be attributed to the Cash Store is that which their conduct reasonably bears. The evidentiary record makes clear that the Cash Store did not intend to prefer Trimor through the Transactions. The Transactions were made in accordance with the Broker Agreements and the established practices between the Trimor and the Cash Store, both of which the DIP Lenders (qua DIP Lenders, pre-filing lienholders, and pre-filing bondholders) were well aware of.

65. Payments in the ordinary course of business are usually made so that the debtor company can take advantage of favourable payment terms or to secure a continued supply of goods or services so that the debtor company can continue in business. In such

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[45] *Re Holt Motors Ltd* (1966), 57 DLR (2d) 180 at para 8, 56 WWR 182 (Man QB) [Holt Motors]; Book of Authorities of Trimor, Tab 13. *Thorne Riddell v Fleishman*, 47 CBR (NS) 233 at para 26, 1983 CarswellOnt 201 (Sup Ct); Book of Authorities of Trimor, Tab 14.

circumstances, the debtor company's expectation that the transaction would permit it to remain in business and buy some time to extricate itself from its financial difficulties will strongly militate against finding an intent to prefer.[46]

66. In the present case, the Transactions bear none of the badges of fraud which the courts will often look at in reviewable transaction cases where there is often no direct evidence of intent. The Cash Store's secured creditors had notice of the business arrangements between Cash Store and Trimor, including the fact that Trimor retained ownership of the Trimor Loans and proceeds of the Trimor Loans. The secured creditors did not therefore suffer any prejudice. Rather, they benefitted from the risks of lending into a structure in which these TPL arrangements were in place. The Cash Store received the benefit of the broker fees earned on loans brokered to Customers with TPL monies, which were in turn used to make interest payments to Cash Store's secured creditors. The secured lenders cannot now seek to confiscate the Trimor Loans and the proceeds of the Trimor Loans simply because the inherent risks in their investments materialized into real losses.

67. As set out above, the evidence of the TPLs is that they are, and have always been, the sole legal and beneficial owners of the TPL property. The Cash Store did not transfer their property to the TPLs.

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[46] *Re AR Colquhoun & Son Ltd*, [1937] WWR 222, 18 CBR 124 (SaskKB); Book of Authorities of Trimor, Tab 15. *Re Norris* (1994), 23 Alta LR (3d) 397 at para 7, 28 CBR (3d) 167 (QB), rev'd on other grounds (1996), 45 Alta LR (3d) 1., 193 AR 15 (CA); Book of Authorities of Trimor, Tab 16.

68. In their factum, the DIP Lenders allege that even Transactions entered into after the Initial Order was made constitute preferences under the BIA and/or voidable transactions under the FPA and FCA. In addition to the points made above, those transactions were entered into by the Applicants under the management of the CRO and the supervision of the Monitor and as expressly contemplated in the Initial Order and the Additional TPL Protection Order made in these proceedings. The DIP Lenders had notice of and consented to both of those orders. For the DIP Lenders to now argue that such transactions are improper is telling.

PART IV - ORDER REQUESTED

69. Trimor respectfully requests that the relief sought by the DIP Lender in the cross-motion be dismissed with costs.

ALL OF WHICH IS RESPECTFULLY SUBMITTED this 5th day of June, 2014.

Brett Harrison and Adam Maerov
McMillan LLP

Lawyer for Trimor Annuity Focus Limited Partnership #5

SCHEDULE "A"
LIST OF AUTHORITIES

1 *Randhawa v 420413 BC Ltd*, 2009 BCCA 602, 2009 CarswellBC 3512

2 *Bluebird Corp, Re*, 1926 CarswellOnt 29, [1926] 2 DLR 484

3 *Salo v Royal Bank of Canada*, 1988 CarswellBC 3186, 11 ACWS (3d) 148

4 *Outset Media Corp v Stewart House Publishing Inc*, 2003 CarswellOnt 2460, 34 BLR (3d) 241

5 *Maple Homes Canada Ltd, Re*, 2000 BCSC 1443, 2000 CarswellBC 2017

6 *Tucker v Aero Inventory (UK) Ltd*, 2011 ONSC 4223, 2011 CarswellOnt 8476

7 *Verdellen v Monaghan Mushrooms Ltd*, 2011 ONSC 5820, 2011 CarswellOnt 11612

8 *Dilollo, Re*, 2013 ONSC 578, 2013 CarswellOnt 781

9 *Keith G Collins Ltd v Canadian Imperial Bank of Commerce*, 2011 MBCA 41, 2011 CarswellMan 196

10 *Abou-Rached, Re*, 2002 BCSC 1022, 2002 CarswellBC 1642

11 *917488 Ontario Inc v Sam Mortgages Ltd*, 2013 ONSC 2212, 2013 CarswellOnt 4413

12 *King Petroleum Ltd, Re*, 1978 CarswellOnt 197, 29 CBR (NS) 76

13 *Holt Motors Ltd, Re*, 1966 CarswellMan 3, 56 WWR 182

14 *Thorne Riddell v Fleishman*, 1983 CarswellOnt 201, 47 CBR (NS) 233

15 *AR Colquhoun & Son Ltd, Re*, 1936 CarswellSask 15, [1937] 1 WWR 222

16 *Norris, Re*, 1994 CarswellAlta 353, [1994] AWLD 831

17 *St. Anne Nackawic Pulp Company Ltd.*, 2005 NBCA 55

18 L.W. Houlden and Geoffrey B. Morawetz, *Houlden and Morawetz Bankruptcy and Insolvency Analysis*, Bankruptcy and Insolvency Act Part IV (ss. 67-101.2), F§210 — Rebutting The Presumption; Trimor Book of Authorities, Tab 18

SCHEDULE "B"
RELEVANT STATUTES

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

S.2: "insolvent person"

a person who is not bankrupt and who resides, carries on business or has property in Canada, whose liabilities to creditors provable as claims under this Act amount to one thousand dollars, and

(a) who is for any reason unable to meet his obligations as they generally become due,

(b) who has ceased paying his current obligations in the ordinary course of business as they generally become due, or

(c) the aggregate of whose property is not, at a fair valuation, sufficient, or, if disposed of at a fairly conducted sale under legal process, would not be sufficient to enable payment of all his obligations, due and accruing due;

S. 4(4):

Question of fact

(4) It is a question of fact whether persons not related to one another were at a particular time dealing with each other at arm's length.

Preferences

95. (1) A transfer of property made, a provision of services made, a charge on property made, a payment made, an obligation incurred or a judicial proceeding taken or suffered by an insolvent person

(a) in favour of a creditor who is dealing at arm's length with the insolvent person, or a person in trust for that creditor, with a view to giving that creditor a preference over another creditor is void as against — or, in Quebec, may not be set up against — the trustee if it is made, incurred, taken or suffered, as the case may be, during the period beginning on the day that is three months before the date of the initial bankruptcy event and ending on the date of the bankruptcy; and

(b) in favour of a creditor who is not dealing at arm's length with the insolvent person, or a person in trust for that creditor, that has the effect of giving that creditor a preference over another creditor is void as against — or, in Quebec, may not be set up

against — the trustee if it is made, incurred, taken or suffered, as the case may be, during the period beginning on the day that is 12 months before the date of the initial bankruptcy event and ending on the date of the bankruptcy.

Transfer at undervalue

96. (1) On application by the trustee, a court may declare that a transfer at undervalue is void as against, or, in Quebec, may not be set up against, the trustee — or order that a party to the transfer or any other person who is privy to the transfer, or all of those persons, pay to the estate the difference between the value of the consideration received by the debtor and the value of the consideration given by the debtor — if

a. the party was dealing at arm's length with the debtor and

   i. the transfer occurred during the period that begins on the day that is one year before the date of the initial bankruptcy event and that ends on the date of the bankruptcy,

   ii. the debtor was insolvent at the time of the transfer or was rendered insolvent by it, and

   iii. the debtor intended to defraud, defeat or delay a creditor; or

b. the party was not dealing at arm's length with the debtor and

   i. the transfer occurred during the period that begins on the day that is one year before the date of the initial bankruptcy event and ends on the date of the bankruptcy, or

   ii. the transfer occurred during the period that begins on the day that is five years before the date of the initial bankruptcy event and ends on the day before the day on which the period referred to in subparagraph (i) begins and

      (A) the debtor was insolvent at the time of the transfer or was rendered insolvent by it, or

      (B) the debtor intended to defraud, defeat or delay a creditor.

Fraudulent Conveyances Act, R.S.O. 1990, c. F.29

Where conveyances void as against creditors

2. Every conveyance of real property or personal property and every bond, suit, judgment and execution heretofore or hereafter made with intent to defeat, hinder, delay or defraud creditors or others of their just and lawful actions, suits, debts, accounts,

damages, penalties or forfeitures are void as against such persons and their assigns. R.S.O. 1990, c. F.29, s. 2.

Fraudulent Preferences Act, RSA 2000, c F-24

Preferential effect

3 Subject to sections 6 to 9, every gift, conveyance, assignment, transfer, delivery over or payment of goods, chattels or effects or of bills, bonds, notes or securities or of shares, dividends, premiums or bonus in any bank, company or corporation, or of any other property, real or personal, made

(a)by a person at a time when the person is in insolvent circumstances or is unable to pay the person's debts in full or knows that the person is on the eve of insolvency, and

(b)to or for a creditor and having the effect of giving that creditor a preference over the other creditors of the debtor or over any one or more of them,

is, in and with respect to any action that within one year after the transaction is brought to impeach or set aside the transaction, void as against the creditor or creditors injured, delayed, prejudiced or postponed.

6 Nothing in sections 1 to 5 applies to

(a) a bona fide sale or payment made in the ordinary course of trade or calling to innocent purchasers or parties, or

(b) a payment of money to a creditor, or a bona fide conveyance, assignment, transfer or delivery over of any goods, securities or property, of any kind as above mentioned, that is made in consideration of a present actual bona fide sale or delivery of goods or other property or of a present actual bona fide payment in money, or by way of security for a present actual bona fide advance of money,

if the money paid or the goods or other property sold or delivered bear a fair and reasonable relative value to the consideration for it.

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., INSTALOANS INC., 7252331 CANADA INC., 5515433 MANITOBA INC., 1693926 ALBERTA LTD. DOING BUSINESS AS "THE TITLE STORE"

APPLICANTS

Court File No. CV-14-10518-00CL

ONTARIO
SUPERIOR COURT OF JUSTICE - COMMERCIAL LIST

Proceeding commenced at Toronto

REPLY AND RESPONDING FACTUM OF TRIMOR ANNUITY FOCUS LP #5 (RETURNABLE JUNE 11, 2014)

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