

CITATION: 1511419 Ontario Inc. (formerly known as The Cash Store v.
KPMG LLP, and Canaccord Genuity Corp., and
Cassells Brock & Blackwell LLP; 2025 ONSC 5796

COURT FILE NO.: CV-14-0010771-00CL
CV-14-0010773-00CL
CV-14-0010774-00CL

DATE: 2025/10/14

**SUPERIOR COURT OF JUSTICE – ONTARIO
(COMMERCIAL LIST)**

RE: 1511419 Ontario Inc. (formerly known as THE CASH STORE FINANCIAL
SERVICES INC.)

AND

KPMG LLP

AND

CANACCORD GENUITY CORP.

AND

CASSELLS BROCK & BLACKWELL LLP

BEFORE: W.D. Black J.

COUNSEL: *John Finnigan, James Hardy and Jessica DeFilippis*, for the Plaintiff
Megan Keenberg, for the Plaintiff

Gerald L.R. Ranking, Jesse R. Harper, Pavel Sergeyev and Anita Hojabr,
for the Defendant KPMG LLP

Dan Murdoch, Sinziana Hennig, Maryam Shahid and RJ Reid, for the
Defendant Cassels Brock & Blackwell LLP

HEARD: April 30 – June 13 , 2025 (Closing submissions on June 23-25)

ENDORSEMENT

I. Overview

[1] Commencing in 2002, and continuing until April 14, 2014, when it was granted protection under the *Companies' Creditors Arrangement Act*, R.S.C. 1985, c. C-36 (the "CCAA"), The Cash Store Financial Services Inc. ("Cash Store") operated in the "payday loan" industry.

[2] Cash Store's head office was in Edmonton. At the time of filing under the CCAA, Cash Store operated 509 branches across Canada, operating under the names "Cash Store Financial", "Instaloans" and "The Title Store", and had approximately 1700 hourly and salaried Canadian employees. Cash Store also owned and operated 27 branches in the United Kingdom under the Cash Store Financial name (in this endorsement I will refer to all such entities collectively as "Cash Store" except in any instances where it is necessary to refer to any such entity individually).

[3] Cash Store's primary business was to offer a high volume of relatively small, short-term advances. While there was modest debate in the evidence about this characterization, it appears clear that Cash Store's customers, by and large, were people who were unable to and/or did not access traditional bank products and services from financial institutions, often living paycheck to paycheck and experiencing cash flow problems.

[4] As an illustration of the high-volume, small-loans nature of this business, evidence at trial showed that in 2011 Cash Store made approximately 1.4 million loans for which the average amount was \$492 and for which the average term was 19 days.

[5] From 2002 to 2014, Cash Store was listed on the Toronto Stock Exchange. It was also listed on the New York Stock Exchange from 2010 to 2014.

[6] In general terms, this case (in fact two claims being tried together) concerns Cash Store's deterioration from a growing and profitable business in its first few years of operation to an insolvent entity requiring CCAA protection in 2014. More particularly, the central issues in the case before me relate to the timing, causes and circumstances of Cash Store's insolvency.

[7] Cash Store's estate (which I will refer to as the "CS Estate" in order to distinguish the post-CCAA entity, the CS Estate, from the business that operated until 2014, Cash Store), alleges that the company's insolvency was established and ought to have been evident by a point in late 2011 or early 2012 (around the time that Cash Store acquired a loan portfolio (the "Loan Portfolio") from third-party lenders ("TPLs" and the "Loan Internalization Transaction" or "LIT")).

[8] The CS Estate asserts that the LIT, financed in large part by Cash Store's corresponding note offering in early 2012 (the "Note Offering"), effectively unmasked and laid bare the underlying fact of Cash Store's insolvency, and put into sharp relief that Cash Store was not genuinely a "broker" of loans, as it had uniformly represented throughout its existence, but was in fact itself a lender, without a license to operate as such, and was in reality exposed in that capacity to the credit risks and problems that the LIT revealed and exacerbated.

[9] CS Estate alleges that Cash Store's professional advisors – KPMG LLP ("KPMG") and Cassels Brock & Blackwell LLP ("Cassels") – knew or ought to have known the true nature of Cash Store's business, knew or ought to have known that Cash Store was insolvent by late 2011,

and that Cash Store's continued operation was also under threat from provincial regulators. The CS Estate claims that KPMG and Cassels, in that alleged context of evident insolvency and existential regulatory threat, ought to have prevented Cash Store from making certain representations, allegedly omitting or misstating those realities, to creditors and in the public domain.

[10] Those alleged material misrepresentations, and Cash Store's continued operations from late 2011 until its demise in April of 2014, despite its undetected or unacknowledged insolvency, led, CS Estate claims, to a "deepening" of the insolvency during that period, with significant financial consequences to Cash Store's stakeholders.

[11] In particular, it is alleged that Cash Store's unaudited interim financial statements for the second and third quarters ended March 31, 2012 and June 30, 2012, respectively contained various errors, including significant material overstatements of the value of the recently acquired Loan Portfolio.

[12] Indeed, Cash Store itself determined, later in 2012 – at the time of the audit of its year end statements for September 30, 2012 – to issue restatements of the March 31 and June 30 interim financial statements, and in those restated interim financial statements revised the represented value of the loan portfolio considerably downwards.

[13] Subsequently, after receiving written third-party communications alleging additional concerns and improprieties regarding the Loan Internalization Transaction and other aspects of Cash Store's business, Cash Store conducted an internal investigation and formed a special committee (the "Special Committee") to investigate these further allegations.

[14] In the result, Cash Store ultimately issued amended and restated audited financial statements for the fiscal years ended September 30, 2012 and September 30, 2011.

[15] CS Estate claims, as against KPMG, that Cash Store's original financial statements for the year ended September 30, 2011, for the quarters ended March 31 and June 30, 2012, and for the year ended September 30, 2012 were materially misstated in various respects, and not prepared in accordance with generally accepted accounting principles ("GAAP") or generally accepted auditing standards ("GAAS").

[16] It claims that, owing to a mischaracterization of the true nature and risks of Cash Store's operations – which it alleges is a misrepresentation the ought to have been detected by KPMG and for which additional disclosure ought to have been made – over one hundred million dollars of off-balance sheet debt was incorrectly excluded from the company's reported liabilities, and that loans receivable from Cash Store's customers were improperly excluded from Cash Store's reported assets. The underlying theory is that, despite certain contractual terms in Cash Store's brokerage agreements (the "TPL Agreements", sometimes referred to in various materials as the "Broker Agreements") with the TPLs, in reality Cash Store was a direct lender rather than a broker, and in fact assumed substantially all risks associated with the TPL-funded loans to payday customers.

[17] As against Cassels, the claim is based in allegations of breach of the retainer agreement, solicitor's negligence, and breach of fiduciary duty. In particular, among other concerns, Cash Store Estate alleges that Cassels was in an untenable conflict of interest as a result of Cassels' "relationship partner" for the Cash Store/Cassels relationship, Paul Stein, also being a principal of one of the TPLs, and having allegedly profited from that role with the TPL even as Cash Store's financial health deteriorated. CS Estate also criticizes the advice that Cassels gave concerning the changing regulatory environment within which Cash Store operated. In addition, CS Estate asserts that Cassels' acceptance of Cash Store's ongoing mischaracterization of its business, and of the increasing regulatory threat, delayed the recognition of Cash Store's inevitable debt-laden demise.

[18] Given those allegations, this case raises questions as to the nature and extent of the duty of professional advisors, in this case an auditor and external counsel, respectively, to take a client's representations about the client's operations with a grain of salt, and to perform independent investigations, including investigations beyond the ostensible scope of a professional advisor's formal engagement, to satisfy itself as to whether or not the client's public disclosure precisely and fairly captures the nature and details of the client's business.

[19] CS Estate settled its claim, arising from these same circumstances, against Canaccord Genuity Corp. ("Canaccord") – relative to a valuation exercise and resulting fairness opinion provided by Canaccord for purposes of the LIT – on the eve of trial.

[20] Likewise, CS Estate had previously settled its claim against a number of Cash Store's former directors and officers (the "D & O"(s) and the "D & O Claim").

[21] CS Estate formulates the claim for damages in different ways, depending on the initial date chosen for the calculation and the precise premise for the determination, but it quantifies the claim as ranging from a minimum of \$119,326,332 to a maximum of \$177,926,332. It also claims from Cassels a disgorgement of the full amount of fees Cash Store paid to Cassels between October of 2009 and April of 2014, in the amount of \$6,701,213,58.

[22] On all such amounts, CS Estate claims interest from November 27, 2014, the date of issuance of the original Notice of Action in this proceeding, at the relevant *Courts of Justice Act*, R.S.O. 1990, c. C.43 rate.

II. Overview of Issues to be Determined

[23] Considering the parties' starkly competing views as to critical aspects of the claim, and having regard to the totality of the evidence I heard, I believe that, in order to determine the claims against KPMG and Cassels, I must address the following issues:

- (A) Did Cash Store's financial statements during the period at issue – both audited annual statements and the interim statements assessed by way of review engagement as well as other contemporaneous public disclosures – fairly and reasonably represent that true nature of the Cash Store business, and fairly and reasonably characterize the essence and status of the relationships between and among Cash Store, the payday loan customers, and the TPLs?

- (B) Regardless of the conclusion on those issues set out in subparagraph (a), did KPMG comply, in its audits and reviews of the relevant financial statements with the requirements of GAAS and GAAP as applicable?
- (C) What obligation did KPMG have to undertake audit-like procedures relative to the Loan Internalization Transaction and the related Note Offering, in order to value the loan portfolio acquired and/or to take issue with management/EY's conclusions as to that value?
- (D) Did Cassels, in its work on behalf of Cash Store, assist Cash Store in misrepresenting its true financial state and/or the status of Cash Store's interactions with provincial regulators, and what consequences flow from Mr. Stein's alleged conflict of interest?
- (E) Did the breaches by the defendants, if any, of relevant standards of care and/or fiduciary duties cause damages to Cash Store?
- (F) Whatever the conclusion on the liability issues, what is the appropriate calculation of damages suffered by Cash Store (on the basis of CS Estate's "deepening insolvency" theory)? and
- (G) Are the claims caught by limitations, and statute-barred?

III. Conclusions

[24] I have concluded that these claims against KPMG and Cassels must fail, and I dismiss them for the reasons set out in detail below.

IV. Relevant Background Facts

(A) Origins of Cash Store

[25] Cash Store's history effectively began on February 23, 2001, when it was incorporated in Ontario.

[26] On January 17, 2002, it amalgamated with another entity and was known for the next few years as "Rentcash Inc."

[27] On March 31, 2008, it changed its name to "The Cash Store Financial Services Inc." Over the years Cash Store operated under various banners, but from 2008 through the end of its operations it largely conducted business under the Cash Store and "Instaloan" names.

[28] Cash Store's 2002 Annual Report discloses that, as of June 30, 2002, Gordon Reykdal was Cash Store's President and CEO. Mr. Reykdal remained Cash Store's CEO throughout its existence (up to a point in the CCAA proceedings), and testified before me in this trial. Paul Stein, of Cassels, who also testified and featured prominently in the trial before me, was initially listed as an officer (Corporate Secretary).

[29] In that same 2002 Annual Report, KPMG was identified as Cash Store's auditor and Cassels (of which Mr. Stein was a partner in its Toronto office) was described as Cash Store's solicitors.

[30] In his evidence, mostly gleaned in his capacity as Chief Restructuring Officer ("CRO") for Cash Store in the CCAA proceedings, William Aziz (about whom there is more below), confirmed that to get "up to speed" on important aspects of Cash Store's history, he necessarily reviewed various events and materials. Those events and materials that Mr. Aziz necessarily reviewed in detail as part of his mandate as CRO, all of which are also germane to this trial, include:

- (A) The application record that Cash Store filed in support of its application for CCAA protection;
- (B) The affidavit of Steve Carlstrom, a Cash Store officer, filed within the application for CCAA protection, which in turn attached:
 - 1. The audited financial statements for the fiscal years ended September 30, 2011, 2012 and 2013;
 - 2. Interim consolidated financial statements (prepared on the basis of a review engagement) for the three months ended December 31, 2012, and December 31, 2013;
- (C) A letter dated November 6, 2012, that KPMG received from Clearwater Capital Management Inc. ("Clearwater"), in the nature of a whistleblower communication, raising concerns about Cash Store's interim financial statements and inadequate disclosures about, among other matters, undisclosed related parties;
- (D) A letter sent to Cash Store's board of directors on January 17, 2012, by Michael Woollcombe of VWK Capital Management Inc. ("VWK"), an investment manager with a short position in Cash Store, describing three branch visits in Ontario and alleging that Cash Store's business was being conducted in violation of Ontario payday loan legislation and that Cash Store was in breach of its obligations under applicable securities laws to make timely disclosure;
- (E) A letter dated April 12, 2012, that VWK's counsel Graeme Cameron sent on behalf of VWK to Giles Gherson, Deputy Minister of Consumer Services for the Ontario Ministry of Consumer Services, providing extensive and detailed information regarding alleged "serious and ongoing violations of the *Payday Loan Act*, 2008 and its accompanying Regulation" by Cash Store; and,
- (F) A further letter that VWK sent to Cash Store's board on August 27, 2012, setting out concerns about the value of the Loan Portfolio acquired by way of the Loan Internalization Transaction, and expressing related concerns about the relationships between Cash Store and the TPLs and Cash Store's allegedly deficient disclosures on these items.

(B) Key Aspects of the Operation of Cash Store's Business up to September of 2011

[31] Various aspects of Cash Store's operations featured in the disputes at issue in this trial, and it is important to understand these features, and the parties' respective positions on them. First, there is no dispute that the funds ultimately loaned to Cash Store's payday loan customers were provided by the TPLs.

[32] The TPLs, numbering approximately 10-15 during the timeframe at issue, provided varying amounts to Cash Store from time to time to payday loan customers. These amounts ranged, as at 2013, when the total loan funds available from TPLs were approximately \$130 million, from roughly \$52 million in the case of Cash Store's largest TPL, Assistive Financial Corp. ("Assistive Financial"), to about \$23.5 million from Cash Store's second largest lender 367463 Alberta Ltd. ("367 Alberta"), to considerably smaller amounts in the case of other lenders.

[33] It is important to understand, in order to appreciate the manner of deployment of those funds from the TPLs, the way in which Cash Store's business operated, and the (contested) contractual framework under which these operations ostensibly proceeded.

(1) "Cashless" Broker Model

[34] From its inception, Cash Store operated as a self-described broker, using a "cashless" model. The notion of Cash Store operating as a broker was the subject of an apparently approbating opinion from its Alberta counsel Reynolds Mirth at or about the time of Cash Store's incorporation (and confirmed at certain points in its operational life). While I was advised that the original Reynolds Mirth opinion was never produced in the litigation, it is evident from other aspects of the evidence that Cash Store relied on Reynolds Mirth's views as to the propriety and advantages of the broker model. The key benefit of Cash Store functioning as a broker rather than as a direct lender was that brokering loans to customers using funds from the TPLs ostensibly allowed Cash Store to reduce its capital risk. It also ostensibly allowed Cash Store to charge a brokerage fee apart from the maximum allowed interest rate chargeable on the consumer payday loans.

[35] In the Offering Circular dated January 24, 2012 prepared by Cash Store for the Note Offering in conjunction with the LIT, Cash Store described this broker model, in a fashion with which CS Estate takes issue, as follows:

"When the Company acts as a broker on behalf of income earning consumers seeking short-term advances, the funding of short-term advances is provided by independent third party lenders. 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 the Company's balance sheet."

[36] As discussed in considerable detail below, CS Estate denies that the TPLs were "independent," and denies that the funds advanced by the TPLs were assets of the TPLs and/or properly excluded from Cash Store's balance sheet.

[37] The “cashless” aspect of the business, also discussed in more detail below, meant that, by deploying methods other than handing over cash per se to fund the customers’ loans, Cash Store did not require extensive in-store security like its payday loans competitors did. As will be seen, however, the cashless model eventually ran afoul of various provincial regulators’ views as to how the relevant legislation and regulations required Cash Store to operate.

[38] By way of overarching description of the day-to-day operations, as noted Cash Store’s customers typically borrowed relatively modest amounts for brief periods of time. During most of the relevant timeframe Cash Store provided alternative financial products and services to customers for whom traditional banking services were unavailable or inconvenient. Cash Store’s main product was “payday loans,” typically used by consumers to bridge the gap between their current financial needs and their next pay cheque.

[39] The cashless feature of Cash Store’s model meant that rather than receiving cash, customers had the option, in most provinces up to roughly 2011, of receiving cheques or pre-loaded debit or credit cards. These products too at a certain point attracted regulatory disapproval.

[40] As noted, the average amount of individual loans made by Cash Store – invariably from individual Cash Store branches – was in the range of approximately \$500.00. The terms of these individual loans typically required repayment within approximately two-four weeks.

(2) Process and Documents for Individual Payday Loans

[41] For each such individual loan, the process and relevant documentation was as follows:

- (A) The individual customer would fill out an application, in which he or she would request a loan, and provide information about his or her financial circumstances, including income (the “Loan Application”);
- (B) The loan selection criteria were pre-existing, having been established as between Cash Store and the TPLs, and were assessed and applied at the branch level for purposes of any such individual loan request;
- (C) If approved, the customer would then sign a promissory note (the “Promissory Note” sometimes referred to as the “Loan Agreement”), confirming the customer’s agreement to repay the loan to the particular TPL designated by Cash Store for that particular loan;
- (D) Under the TPL Agreements, Cash Store received funds from the TPLs – in varying amounts as noted – which Cash Store used to fund the individual consumer loans. In the TPL Agreements, Cash Store’s role and function was expressly described as that of a broker;
- (E) It is important to understand that Cash Store did not receive the specific amounts of individual loans from the TPLs in “real time” for purposes of a given individual loan.

In fact Cash Store instead maintained a “float” of pooled funds from the various TPLs, and made the decision in the case of each individual loan as to which TPL’s funds would be deployed for the purpose of that particular loan (and there was evidence that particular individual branches would generally deploy funds from particular TPLs);

- (F) It is also important to note that, contrary to the letter of the TPL Agreements, Cash Store did not physically segregate the funds received from individual TPLs, either on a loan-by-loan or even TPL-by-TPL basis. Rather, while accounting for the funds from individual TPLs in separate and dedicated accounts, Cash Store pooled – and co-mingled – the funds from the various TPLs together, in fact co-mingled those funds with Cash Store’s own operating funds, and may have used those collected funds not only for the payday customer loans, but also for Cash Store’s general corporate purposes (there was some dispute about this in the evidence) and for regular working capital. Cash Store did, however, account for the flow of funds from and to each TPL separately, thus segregating the accounting for the funds if not segregating the physical funds themselves;
- (G) Pursuant to the Promissory Note for the individual consumer loan, the customer would commit to paying interest on the payday loan at the rate of 59% (sometimes stated to be 59.9%) (which rate was evidently chosen having regard to a provision of the *Criminal Code* of Canada declaring interest rates of, at that time, 60% or more to be illegal);
- (H) Cash Store in turn paid the TPLs a regular, agreed-upon rate of return on a monthly basis, equivalent to an interest rate which, over the period at issue, was mostly 17.5% (it had been as high as 25% earlier in the relationships, and had been stepped down to 22%, then 20% and finally to the 17.5% where it stood as of the time of the events in issue) and in addition accrued in its financial statements amounts described as “retention payments” (discussed in detail below);
- (I) Unless and until a TPL exited from its role and discontinued funding Cash Store’s loans to payday loan customers, Cash Store did not at any point in the ongoing relationship with a TPL return the full outstanding amount of funds advanced by a given TPL. Instead, to the knowledge of, and it appears with the encouragement of the TPLs, Cash Store would re-loan, in whole or in part, the amounts repaid by payday loan customers against advanced funds.

(3) Cash Store Disclosure re TPL Relationships

[42] In its financial disclosures, including in its audited year-end financial statements, Cash Store represented that:

- (A) The TPLs were independent lenders;

- (B) Cash Store's customers were responsible for repaying the TPL advances (i.e. the amounts of individual loans) to the relevant TPLs through Cash Store;
- (C) Under the TPL Agreements, Cash Store provided services to the TPLs related to the collection of customer information and documents, as well as loan collection services and earned a fee for doing so;
- (D) Losses suffered on account of uncollectible loans were described by Cash Store as being the responsibility of the TPLs themselves, subject to Cash Store's compliance with its duties as set out in the TPL Agreements. As set out by Cash Store in public disclosures:

“the significant duties under the terms of the agreements generally include ensuring that any proposed loan was applied for through an authorized outlet, ensuring each potential customer meets the loan selection criteria as set forth by the third party lender prior to approval and release of funding, satisfying the documentation requirements in a full and timely manner, providing loan management services throughout the term of the loan and providing collection services on behalf of the third party lender for all loans funded which are not paid in full by the due date, all of which while ensuring information system integrity is maintained.”

[43] As will be evident throughout these reasons, there are a number of instances for which the payday loan practices did not precisely match the contractual provisions described above, in particular in the case of the provisions of the TPL Agreements. The effect of this incongruence is a critical issue in this case.

(4) Differences Between TPL Agreements and Actual Practices

[44] As one example of the difference between the letter of the TPL agreements and Cash Store's practices “on the ground” under the TPL Agreements, the TPLs had the right to determine on a loan-by-loan basis whether or not to advance a particular loan to Cash Store's payday loan customer. In fact, while as noted Cash Store ensured that a particular customer's circumstances met the established loan selection criteria and recorded all relevant documents and information pursuant to specified “Documentation and Funding Requirements”, the approval of a given customer loan appears effectively to have been a decision made by Cash Store at the branch level. Moreover, as noted, Cash Store also identified the TPL to fund a particular loan once a customer was approved, providing the loan documentation after the fact to the selected TPL. Cash Store would proceed to fund the individual loan notionally from within the particular TPL's share of the overall “float” of TPL funds (and did not have to ask for specific funds to be forwarded by a TPL for each such loan). A second example, discussed above and in more detail below, is Cash Store's acknowledged failure to maintain segregated physical accounts, as provided in the TPL Agreements, for the funds from each TPL.

[45] The reasons for these departures from the letter of the various agreements and in particular the TPL Agreements are easy enough to understand. Given the sheer volume and wide geographic distribution of relatively modest loans, a requirement for the TPL to consider each application and forward funds on a loan-by-loan basis would be unwieldy and impractical.

[46] Moreover, it is clear that both Cash Store and all TPLs were specifically aware, at all relevant times, that Cash Store operated in the manner described above, and not entirely in accordance with the provisions of the TPL Agreements. The evidence shows that, notwithstanding the TPLs' knowledge that Cash Store was thus consistently in technical breach of various aspects of the TPL Agreements, no TPL at any point took steps to enforce the rights they had under sections 5 and 7 of the TPL Agreements to audit Cash Store's accounts and/or to demand immediate repayment of outstanding loan balances.

[47] That said, the nature and extent of the departures from the letter of the contracts was a critical theme of the trial, and a major point of contention between the experts. Slightly overstated, the dispute was whether the departures from the letter of the TPL Agreements were merely practical adjustments, known and accepted by the TPLs, to allow the high volume brokerage arrangement to function efficiently, as the defendants and Cash Store's former officers and directors attest, or were instead ill-conceived attempts to conceal Cash Store's true essence as a lender, and the inescapable and deepening insolvency that it faced in that guise, as the plaintiff asserts.

(5) Retention Payments

[48] Central to the debate was Cash Store's development and ongoing use of retention payments ("Retention Payments").

[49] As set out above, Cash Store did not, when it received payment from an individual payday loan customer, forward to the relevant TPL a full loan-specific payment of principal and interest less a brokerage fee and/or a provision for bad loans.

[50] Instead, Cash Store would record the payment in favour of the TPL whose funds were used for the particular loan, and Cash Store's board of directors would, on a quarterly basis, authorize payments to the TPLs (the Retention Payments), described in Cash Store's disclosure as follows:

"The Company's Board of Directors regularly approves a resolution which authorizes management to pay a maximum amount of retention payments per quarter to third party lenders as consideration to those lenders that continue to be willing to fund advances to the Company's customers. 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 third party lenders. Retention payments are recorded in the period in which a commitment is made to a lender pursuant to the resolution approved by the Board of Directors."

[51] These Retention Payments were thus approved quarterly (which the record shows was done invariably and faithfully), and accrued to the credit of each TPL, based on and representing a portion of the outstanding amount of money each TPL had advanced to Cash Store to fund loans.

[52] In addition, on a monthly basis, Cash Store provided reconciliations to each TPL, and a partial payment of the accrued Retention Payment owed. These monthly payments were, during the relevant period, calculated and paid based on the rate of 17.5% discussed above.

[53] While there was frankly some confusion and inconsistency in the evidence at trial about the precise calculation of the Retention Payments, the accrual of Retention Payments comprised the amount of interest payable by payday loan customers to the TPL based on the Promissory Note, with an adjustment and some recompense for bad debts (which by all accounts beset a substantial portion of the overall number of loans made, as one might expect in the pay day loan circumstances), less the amounts actually paid to TPLs monthly based on the rate of 17.5%.

[54] The plaintiff, relying on its accounting liability expert's opinion, argues that the Retention Payments were, and operated as, a guarantee in favour of the TPLs that each TPL would be made whole for all amounts advanced. This notion of a guarantee is at the heart of CS Estate's central allegation that Cash Store, and not the TPLs, bore the risk for the loans.

[55] The defendants, supported in their position by the evidence of the various Cash Store managers and executives who testified at trial, and by KPMG's accounting liability expert, insisted that despite their recurring and ostensibly predictable nature, the Retention Payments were in fact voluntary, and had to be approved by the Cash Store board each quarter, failing which they would not be paid.

[56] To illustrate how the Retention Payments functioned in practice, the plaintiff points out that as of September 30, 2011 (in the year-end financial statements) Cash Store recorded, in its lender reconciliations, write-offs since December 31, 2010, of \$32.3 million, compared to Retention Payments (approved) of \$19.7 million.

[57] CS Estate asserts that this difference between loan write-offs and amounts of Retention Payments ought to have resulted in a depletion of the TPLs' capital and a publicly disclosed recognition and confirmation of that depletion.

[58] Instead, Cash Store continued to pay the TPLs interest – at that point at the rate of 17.5% – and to accrue Retention Payments, on the full amount of funds advanced by each TPL, without any deduction for loan losses. Again, when any TPL exited as a lender – either prior to or as part of the LIT – they received back the full face amount of their advances to Cash Store.

[59] In this way, the plaintiff alleges, Cash Store in effect took on the risk and exposure of the loans to customers, guaranteeing a rate of return to the TPLs and gradually but steadily absorbing the loan losses itself.

(6) Other Aspects of TPL Agreements

[60] The plaintiff's accounting liability expert Mr. Koch also points out, as discussed above, that under the TPL Agreements, the TPLs had the contractual right to audit the state of their accounts with Cash Store, and the right, if Cash Store breached any of its obligations under the TPL Agreements, to claim the entire amount of their outstanding funds.

[61] I should note that there were slight differences between and among the TPL Agreements over the course of the relevant time frame, but that all versions of those agreements contained certain key provisions that were largely identical.

[62] The TPL Agreements define the TPL as the "Financier" and Cash Store as the "Broker".

[63] Consistent with these definitions, the TPL Agreements provide that Cash Store is to perform "Broker Services" including defined "Documentation and Funding Requirements" and "Loan Services", in turn defined as:

"...the services and activities for: (i) collection of principal and interest on Loans from Broker Customers in the normal course (and forwarding same to Financier of repayment of the principal and interest owing on Loans), (ii) the contacting of Broker Customers for reminder and other purposes, and (iii) the delivery, communication and transmission of documents and information to Financier..."

[64] Article 2.2 in the TPL Agreements provides that the TPL "shall not be obligated to continue to re-invest funds from collected Loans in new loans but may agree to do so as part of the loan selection process."

[65] Article 2.3 confirms that the TPL has the right to determine on a loan-by-loan basis whether to advance a loan. Cash Store is to present a loan to a TPL if the potential loan meets the Loan Selection Criteria, and no loans are to be advanced unless approved by the TPL.

[66] Article 2.9 is the provision requiring Cash Store to segregate each of the TPL's funds and to hold them in trust for the TPL.

[67] Article 5.1 gives the TPLs the right to inspect Cash Store's "Authorized Outlets" (i.e. the individual branches).

[68] Article 7.1(a) provides that Cash Store will indemnify the TPL from any losses suffered by the TPL arising from the performance or non-performance of Cash Store's obligations under the TPL Agreement, unless Cash Store complies in full with the Loan Selection Criteria and provides all of the Broker Services in a competent and timely manner.

[69] Finally, in this vein, article 7.1(b) provides that if any loan made to a customer of Cash Store is not repaid in full, and Cash Store does not provide evidence to the TPL that it performed "each and every one" of the Broker Services "in exactly the manner described herein (no matter how minor or inconsequential" the failure to do so) then Cash Store must pay the TPL the full amount of the loan loss. It further provides that, because it would be too difficult to prove that any

particular deficiency caused a loss, Cash Store must indemnify the TPL “even without clear evidence” that Cash Store’s failure caused the loss.”

[70] CS Estate acknowledges that, taken together, the terms of the TPL Agreements describe Cash Store in a manner consistent with the legal form of a broker. That is, under the TPL Agreements, Cash Store was to receive funds from the TPL and hold those funds in a segregated trust account. Cash Store was permitted to advance those funds to payday borrowers, on a loan-by-loan basis at specific store locations in accordance with the established Loan Selection Criteria, and to collect various documents at the time the loan was advanced. Cash Store was then to collect the principal and interest and remit those funds to the TPL (unless there was a specific further agreement to re-invest the funds). The TPLs retained control over their funds and the process by which those funds are advanced (1) through the segregation of funds in trust accounts, (2) by establishing the criteria by which loans are advanced and the documentation that must be collected, (3) through the right to receive principal and interest repayments (at a rate set at 59% with no obligation to re-invest, (4) through the right to audit Cash Store outlets, and (5) through an indemnity against losses if Cash Store fails in (any of) its obligations.

[71] CS Estate argues that, in practice, however, there were significant differences from these various contractual provisions and what happened in fact, and likewise significant differences between the facts and what was reported in Cash Store’s public disclosures

[72] These differences, all of which featured prominently in the evidence of Mr. Koch, include Cash Store’s failure to physically segregate individual TPLs’ funds, the failure by Cash Store to forward to the TPLs interest payments collected at the rate of 59% – as contemplated by the TPL Agreements – on an ongoing basis, the failure by the TPLs to invoke the indemnity process contemplated in section 7 of the TPL Agreements, and Cash Store’s ongoing re-investment of (by re-lending) TPL funds without express and specific loan-by-loan authorization.

[73] Mr. Koch notes that during the relevant timeframe no TPL ever exercised its audit rights, nor made any demand for repayment, despite the fact that, as acknowledged from time to time by Cash Store, and as discussed above, Cash Store was undoubtedly in breach of various provisions of the TPL Agreements.

(C) Overview of Parties Competing Positions on Retention Payments

[74] Mr. Koch opines that the only reason that TPLs did not exercise their contractual rights to audit their accounts and compel payment was because they understood that their capital was not at risk. The Retention Payments functioned as a guarantee and included accruals and credits for loan losses – which in the payday loan industry are predictable and significant – consistent with the de facto existence of this guarantee. The risks of the loans were thus, Mr. Koch asserts, not borne by the TPLs, but were in fact absorbed by Cash Store.

[75] KPMG, supported by its expert Mr. Cameron and by the testimony of a number of former Cash Store executives, counters that the Retention Payments were consistently characterized as, and were in fact, voluntary.

[76] It points out that there was no contractual obligation for Cash Store to make Retention Payments, and that Cash Store did so voluntarily, as it repeatedly disclosed in the public domain, in order to ease the impact of loan losses for the TPLs, and in order to ensure thereby that the TPLs remained incentivized and willing to provide funds for Cash Store to loan to its payday loan customers. KPMG and the former Cash Store employees who testified maintain that the Retention Payments were the product of a discretionary business judgment as opposed to a binding contractual guarantee.

[77] Consistent with this interpretation, KPMG points out, Cash Store's board of directors considered and approved maximum Retention Payments on a quarterly basis, despite having no affirmative contractual or other obligation to do so.

[78] KPMG also emphasizes that, consistent with Cash Store's broker role as described in the TPL Agreements, Cash Store maintained up-to-date and accurate records for each TPL as to the particular TPL's loans to Cash Store customers.

[79] Cash Store's fee for its brokerage services was taken from amounts collected from the customers, and from the collection of overdue debts, which Cash Store itself pursued under the TPL Agreements, and for which credit was provided to the TPLs in the calculation of the Retention Payments.

[80] The nature and function of the Retention Payments is a key consideration in the competing characterizations of the Cash Store business, which in turn drives the competing contentions as to what items ought to have been shown in Cash Store's financial statements.

[81] That is, if Cash Store was itself a lender, as the plaintiff asserts, then it ought to have carried the consumer loan portfolio as an asset in its Balance Sheet, and ought to have carried the corresponding obligations for outstanding loans as a liability.

[82] Had Cash Store done so, the plaintiff maintains, the insolvency of Cash Store, based on the overwhelming extent to which the liabilities progressively outstripped the assets, would have been clear by at least the end of Cash Store's fiscal year as at September 30, 2011.

[83] This evident insolvency, the plaintiff argues, which should have been apparent by that time had the assets and liabilities of Cash Store been properly contained and disclosed in Cash Store's books, became inescapably obvious when Cash Store undertook the LIT closing in early 2012.

(D) Implications of Departures from TPL Agreements

[84] It is evident, and I find, that the way in which Cash Store and the TPLs conducted their business interactions, and the relationship that each of them had in that context with the payday loan customers, was not precisely in keeping with the agreements in place to govern those dealings.

[85] The plaintiff's observations about those discrepancies are therefore factually apt.

[86] The question for me is whether or not the parties' evident departures from the specific details of the relationships contemplated by the agreements (to the knowledge of the TPLs) transformed the nature of Cash Store's business from broker to lender, whether those departures in and of themselves exposed Cash Store to the insolvency it ultimately suffered, and if so, at what point the insolvency was or ought to have been evident. I must also determine whether the departures from the letter of the agreements ought to have been better disclosed in Cash Store's public representations.

[87] Imbedded in these determinations is the question of whether, when parties function in a fashion that is to some extent at odds with what the agreements between them require, but do so consensually and on an ongoing basis, their divergence from the strict letter of their contracts is a basis to find fault. This question must also consider, where one of the parties is a public company, as Cash Store was, what disclosure is necessary and sufficient in the circumstances.

[88] In my view, consistent with extensive authority relative to assessing alleged negligence, the court's assessment of these claims should proceed, to the extent possible, from the circumstances in which the parties found themselves at the relevant time. Courts have repeatedly cautioned against construing these claims with the benefit of hindsight, and against allowing known outcomes to influence the assessment of the parties' actions at the time and in the actual circumstances in which their decisions were made.

[89] That is, much of CS Estate's criticism is premised on Cash Store's established insolvency as of the commencement of CCAA proceedings in April of 2014, and in particular on Morawetz R.S.J. (as he then was)'s findings later in 2014 that Cash Store's business was in the nature of a lender rather than of a broker.

[90] In assessing the conduct of the defendants, however, I must be careful to do so based on the known and knowable facts as of late 2011 and early 2012 rather than allowing the later emergence of insolvency and the later judicial finding as to the true nature of Cash Store's business (in a particular context as of mid-2014) unduly influence my determinations.

[91] In my view, in that regard, it is important and necessary to take into account and consider other factors that may have driven or contributed to Cash Store's eventual insolvency, and which may have impacted Cash Store's ability to function successfully as a broker and its decision to undertake the LIT and Note Offering in early 2012.

(E) The Changing Regulatory Environment

[92] In that regard and in order to understand the impetus for the LIT, it is instructive to consider the regulatory environment within which Cash Store operated, and changes to that framework during the period from 2009 onward. These regulatory changes also impact squarely on the claim against Cassels, part of which is premised on Cassels' alleged failure to ensure that Cash Store made proper disclosure of the tightening regulatory constraints that it faced, and about the increasingly antithetical stance of provincial regulators towards Cash Store's practices.

[93] As a backdrop to that exercise, it is important to note that in May of 2007, the federal government amended the *Criminal Code*, R.S.C. 1985, c. C-46 to permit exemptions from the criminal rate of interest provisions for payday lenders provided the payday lenders were licensed through a designated provincial regulatory regime.

[94] This amendment ushered in an era in which Cash Store went from being effectively unregulated – subject only to the criminal interest rate provisions of the *Criminal Code* – to becoming more closely regulated province by province.

[95] The precise timing for increased regulatory oversight differed from province to province, but the increased regulatory attention took largely the same form, albeit at slightly different intervals, in the various jurisdictions in which Cash Store operated.

[96] In November of 2009, British Columbia’s payday lending regulatory regime came into force, followed by Ontario’s regulatory regime in December of 2009, and Alberta’s regulatory regime in March of 2010. Thus, in the space of five months, Cash Store faced new regulatory strictures in its three largest markets in Canada. To illustrate the extent to which the regulations in these provinces impacted Cash Store’s business, as at the date that Cash Store filed for CCAA protection (in April of 2014), of the 509 branches that Cash Store then operated across Canada, 176 branches were in Ontario, 120 branches were in Alberta, and 97 branches were in British Columbia. So, almost 400 of Cash Store’s 509 branches were in those three provinces.

[97] Within the same timeframe, other provinces likewise enacted similar regulations governing the payday loan industry. In parallel to these regulatory initiatives, various class actions were mounted against Cash Store (and other payday lenders) in various jurisdictions, alleging non-compliance by Cash Store with legislative provisions (in most instances alleging that the interest charged to payday loan customers, when combined with additional amounts charged by Cash Store, exceeded the maximum of 60% allowed under the *Criminal Code*).

[98] In an affidavit sworn April 14, 2014 and filed in the motion seeking CCAA protection for Cash Store, Steven Carlstrom, then Cash Store’s Vice President, Financial Reporting, described the collective effect of regulatory pressures, multiple class actions in Canada and the United States, and resulting cash flow issues. Mr. Carlstrom said:

“Cash Store is facing immediate and multiple challenges to its continued operations, including regulatory issues that affect its core business strategy, multiple class actions requiring defence across Canada and in the U.S., cash flow issues, and the resulting deterioration of its liquidity position. Significantly, on February 13, 2014, the Ontario Registrar of the Ministry of Consumer Services (“Ontario Registrar”) issued a proposal to refuse to issue a lender’s license to Cash Store’s subsidiaries, The Cash Store Inc. and Instalogs Inc. under the *Payday Loans Act*, 2008, S.O. 2008, Ch. 9 (“*Payday Loans Act*”). On March 27, 2014, the Ontario Registrar issued a final notice of its decision not to grant a license under the *Payday Loans Act*. Further, a recent decision of the Ontario Superior Court of Justice determined that Cash Store could not sell its line of products in Ontario. Cash Store is therefore not

currently permitted to sell any payday loan products or line of credit products in Ontario.”

[99] On the regulatory front, as noted, since late 2009 the Canadian payday loan market had been in transition from a largely unregulated market to being subject to varying degrees of provincial regulation.

[100] The regulations initially enacted in B.C., Alberta, Saskatchewan, Manitoba, Ontario and Nova Scotia entailed caps on loan size, duration of loans, and fees allowed to be charged.

[101] These regulations typically limited payday loans to a maximum amount of \$1,500.00, and a maximum duration of 62 days, as well as establishing a rate cap.

(F) Changes in Business Prompted by Changes in Regulatory Environment

[102] These changes to the regulatory framework precipitated substantial changes in Cash Store’s business model. Fundamentally, in the regulated provinces, Cash Store determined to undertake a transition from being a broker of payday loans to a direct lender itself.

[103] It was this determination that led to the LIT, and to the subsequent development of a suite of “line of credit” products that Cash Store offered directly to payday loan customers.

[104] By way of overview of the differences between the two business models, in the remaining unregulated provinces, in which Cash Store purported to continue to act as a broker, the arrangements were as described above. Cash Store would obtain a Loan Application form the customer, would assess the customer’s creditworthiness on the basis of the established loan approval criteria, and if approved, would provide the cash advance to the customer on behalf of the chosen TPL. When the loan became due and payable, the customer would pay the principal and interest owing to the lender through Cash Store, the payments would be recorded in the relevant TPL ledger, and those funds would be retained in Cash Store’s operating account, less amounts paid monthly, until redeployed to new borrowers. If there was a default, Cash Store would pursue collection proceedings, including potentially turning the customer’s account over to an independent collection agency. As part of that arrangement, Cash Store would keep for its own account delinquent funds recovered by internal and third-party collection efforts.

[105] On a monthly basis, Cash Store would pay the TPLs amounts that, when combined with portfolio returns (interest collected, net of losses) would provide an annual return of 17.5% on the total TPL funds (at earlier points, as noted, this rate of return had been as high as 25%, but was reduced over time).

[106] In addition, relative to the amount of losses suffered by a TPL, Cash Store would credit the TPL with a Retention Payment in the form of book entries accrued to offset the losses, recorded as an expense on Cash Store’s balance sheet. This accounting treatment had the effect that the TPL funds were not, from an accounting perspective, eroded by losses.

[107] The line of credit products that Cash Store launched in late 2012 and early 2013 in the regulated provinces, including as at February 1, 2013 in Ontario, consisted of an unsecured, medium term revolving line of credit with regular minimum payment requirements tailored to a customer's needs and profile. The line of credit products were all described as brokered products, with the exception of a small number of "Elite" lines of credit that Cash Store offered until March of 2014. That is, in respect of the line of credit products, as with the brokered payday loan products in unregulated jurisdictions, TPLs would provide the funds for the lines of credit, and Cash Store would earn fees on those transactions.

[108] The regulatory changes described generally above impacted the entire payday loan industry in Canada, but had a particularly severe impact on Cash Store given Cash Store's business model.

[109] The relevant details of Cash Store's operations, and the impact of positions taken by the Registrar in Ontario – the person designated under the provincial payday loan legislation to administer and oversee the regulation of the industry – were described by Timothy Pinos, of Cassels, in his testimony.

[110] Mr. Pinos, the lead lawyer advising Cash Store with respect to litigation and related regulatory matters, explained that, in contrast to other payday loan businesses, and as noted above, Cash Store operated by way of a "cashless" model. That is, Cash Store branches did not have cash per se on hand, as a result of which Cash Store's branches did not require the extensive and stringent security features typifying the operations of its competitors. As such, Mr. Pinos explained, Cash Store's cashless model thus resulted in a relatively safer environment for Cash Store's staff and customers.

[111] In order to fund the loans it brokered, using the advances from the TPLs, Cash Store would offer the payday loan customers different vehicles or mechanisms to receive the authorized loan amounts. Specifically, as of late 2009 and early 2010, customers could elect to receive loan funds by way of a cheque, or by way of a pre-authorized debit or credit card (pre-loaded with funds in the approved amount of the loan).

[112] Up to and then in parallel with the introduction of the new payday loan legislation in Ontario in late 2009, Mr. Pinos and Cassels advised and acted for Cash Store in connection with various class actions. Mr. Pinos was lead counsel in an Ontario class action – in which the representative plaintiff was Thompson McCutcheon – and consulted to varying degrees with and for some of the local counsel acting for Cash Store in other jurisdictions in which class action proceedings were underway.

[113] Cash Store also consulted Cassels and Mr. Pinos (as well as other Cassels lawyers), in addition to consulting with other counsel in other provinces, with respect to features of the new legislation and regulations.

[114] In early 2010, Cash Store began receiving correspondence from the newly appointed Registrar in Ontario (on behalf of the Consumer Protection Branch of the Ontario Ministry of

Consumer Services) (the “Registrar”), about a number of aspects of Cash Store’s operations that were thought by the Registrar to be in violation of the *Payday Loans Act*, 2008, S.O. 2008, c. 9.

[115] The Registrar (initially via a letter from a compliance inspector for the Consumer Protection Branch) expressed concerns that, among other issues, since the debit card and credit card options each entailed an additional charge added to the cost of borrowing, the effect was to bring the cost of borrowing to an amount exceeding the maximum charge permitted under the *Payday Loans Act* of \$21 per \$100. The compliance inspector also asserted that the customers were being offered a “Payday Loan Protection Plan” – a form of insurance - which constituted an additional product offending the prohibition under the *Payday Loans Act* against offering products beyond the loan itself.

[116] There then ensued a series of letters back and forth over many months, with the communications on Cash Store’s side authored either by Michael Thompson, a Cash Store executive whose role entailed a focus on regulatory matters, or by Mr. Pinos (or by a combination of the two of them). In that ongoing exchange, the regulator took issue with various features of Cash Store’s operations at the branch level, alleging that certain aspects of these operations were not in compliance with the legislation and/or the regulations. Cash Store pushed back on some items, agreed to make changes to address other concerns, and generally expressed a willingness to engage in an ongoing dialogue with a view to satisfying the regulator’s concerns.

[117] This same type of exchange occurred in parallel, to varying degrees, in other jurisdictions in which Cash Store operated, and Mr. Pinos and his Cassels colleagues were consulted in some instances and again to varying degrees, for input as to how best to engage with and respond to the respective provincial regulators, and participated to varying degrees in those exchanges as well. It appears evident that the respective provincial regulators were themselves comparing notes, or at least keeping track of one another’s positions, and mounting attacks on Cash Store comprised of consistent allegations from one province to another (albeit with modest differences arising from differences in the legislative/regulatory provisions from jurisdiction to jurisdiction).

(G) The Note Offering and the Loan Internalization Transaction in January of 2012

[118] As touched on above, on January 31, 2012, Cash Store issued, through a private placement in Canada and the U.S., \$132.5 million of 11.5% Senior Secured Notes (as defined above as the Note Offering).

[119] The Notes were to mature on January 31, 2017, and would bear interest on the aggregate principal amount from the date of issue at 11.5% per annum payable on a semi-annual basis in equal instalments on January 31 and July 31 of each year, commencing in July of 2012. The Notes were issued at a discounted price of 94.608%, resulting in an effective interest rate of 13.4%.

[120] Cash Store used the majority of the proceeds of the sale of the Notes to fund the LIT and to settle pre-existing relationships with TPLs.

(H) Confluence of Problems Facing Cash Store in 2012-2014

[121] By early 2013, after the LIT, heralding an evolving intended shift by Cash Store from being a broker to a direct lending model, and after launching its suite of line of credit products on February 1, 2013, Cash Store's ongoing disagreements with provincial regulators, and its ongoing inability to satisfy the regulators that its operations were compliant with the legislation, were coming to a head. The following regulatory developments and litigation arose, reflecting the increasing threats to Cash Store's operations and existence.

[122] In late 2012, Cash Store, to keep its strategic options open (as explained by Mr. Pinos in his testimony), had submitted an application for judicial review in Ontario, seeking a declaration that certain provisions of the regulations under the Ontario *Payday Loans Act* were void and unenforceable.

[123] On February 4, 2013, the Ontario Registrar issued a proposal to revoke the payday lending licenses of Cash Store (and Instalogs Inc.). Cash Store filed an appeal with the License Appeal Tribunal on February 19, 2013.

[124] On June 7, 2013, the Director designated under the Ontario *Ministry of Consumer and Business Services Act*, R.S.O. 1990, c. M.21 filed an application in this court seeking a declaration that Cash Store's basic line of credit ("BLOC") was subject to the *Payday Loans Act*, and that Cash Store must obtain a specific broker license to offer this product.

[125] Cash Store chose to allow its payday license to expire in Ontario effective July 4, 2013, inasmuch as Cash Store was of the view that it could offer lines of credit without such a license. As a result of this choice and belief, Cash Store also withdrew its pending appeal before the License Appeal Tribunal.

[126] On October 2, 2013, Cash Store's application, seeking a declaration that certain provisions of the regulations made under the *Payday Loans Act* were void and unenforceable, was heard. This court dismissed that application on November 5, 2013, and Cash Store did not appeal that decision.

[127] On November 29, 2013, Morgan J. heard the application filed by the Director on June 7, 2013, seeking a declaration that Cash Store's new BLOC product was subject to the *Payday Loans Act*, and that Cash Store had to obtain a broker license under the legislation in order to offer this product legally.

[128] As noted above, on February 12, 2014, Morgan J. released his decision finding that Cash Store's BLOC product was subject to the *Payday Loans Act*, and ordered that Cash Store and Instalogs were prohibited from acting as a loan broker in respect of the BLOC product without a broker's license under the *Payday Loans Act*. It is evident that Morgan J. regarded the decision as a close call. In fact, His Honour colourfully wrote, in concluding that "the BLOC amounts to a 'payday loan' under subsection 1(1) of the Act," that "Although the contest is a close one, it is evident to me that this time the persistent regulatory cat has caught the clever business mouse" (*The Director v. The Cash Store*, 2014 ONSC 980, para. 9).

[129] On March 14, 2014, Cash Store commenced an appeal of Morgan J.'s decision.

[130] In the meantime, in light of Morgan J.'s decision, Cash Store necessarily ceased offering all line of credit products to its customers in Ontario branches and issued a press release reporting Morgan J.'s decision and Cash Store's resulting action to discontinue offering line of credit products in Ontario.

[131] In parallel to the proceeding culminating in Morgan J.'s decision, on December 17, 2013, the Ontario government filed Ontario Regulation 351/13 under the *Payday Loans Act*, earmarking certain categories of credit such that the *Payday Loans Act* would undoubtedly apply to line of credit products offered by Cash Store and Instalogs. Regulation 351/13 specifically required Cash Store to obtain licenses under the *Payday Loans Act* in order to continue providing access to certain line of credit products in the Ontario market after February 15, 2014.

[132] With a view to complying with these new requirements, Cash Store applied for the requisite licenses.

[133] In response to Cash Store's license application, on February 13, 2014, the day after the release of Morgan J.'s decision, the Ontario Registrar issued a proposal to refuse to issue a lender's license to Cash Store and Instalogs under the *Payday Loans Act*.

[134] The *Payday Loans Act* provides that applicants are entitled to a hearing before the License Appeal Tribunal in respect of a proposal by the Ontario Registrar to refuse to issue a license. However, Cash Store (consciously) allowed the time for an appeal of this decision to lapse while it was in continued negotiations with the Ontario Registrar. These negotiations failed to produce an agreement, and on March 27, 2014, the Ontario Registrar issued a final notice of its decision not to grant Cash Store a license under the *Payday Loans Act*.

[135] As a result of that decision, Cash Store was not permitted to sell any payday loan products in Ontario, and was not eligible to re-apply for a license for 12 months from the date of the Registrar's issuance of the final order. This combination of circumstances effectively sounded a death knell for Cash Store's Ontario business by eviscerating a substantial part of Cash Store's overall operations.

[136] It is evident that these circumstances were central to Cash Store's decision to seek protection under the CCAA on April 14, 2014.

(I) Various Whistleblower Allegations

[137] I should discuss as well, although the substance and immediate impact of these assertions on Cash Store's operations are not as obvious to me, the so-called "whistleblower" allegations made against Cash Store during the relevant timeframe by at least two parties.

[138] The first set of such allegations came in a letter from VWK dated January 17, 2012, authored by Mr. Woollcombe, in which he described three visits he made to Cash Store branches in Ontario posing as a payday loan customer. Mr. Woollcombe claimed that Cash Store's business,

at least in those branches, was being conducted in violation of Ontario payday loan legislation, and that Cash Store was in breach of its timely disclosure obligations under applicable securities laws.

[139] Specifically, Mr. Woollcombe, who had (via VWK), and acknowledged in his letter that he had, a short position in Cash Store shares, made three complaints:

- (A) That Cash Store was charging fees to payday borrowers, including for debit and credit cards, that improperly increased the cost of borrowing to more than the statutory cap of \$21 for each \$100 advanced;
- (B) That Cash Store was not giving payday borrowers the ability to receive their payday loans in cash; and
- (C) That Cash Store was unlawfully offering to provide goods or services other than payday loans in connection with payday loan agreements, including bank accounts and insurance.

[140] Cash Store was already aware by this point, based on its interactions with the Ontario Registrar (and regulators from other provinces), that some of these items were of concern and thought by regulators to be offside regulatory parameters.

[141] Moreover, Cash Store was already in the throes, at that stage, of ongoing dialogue with provincial regulators about whether or not the practices on which Mr. Woollcombe focused were in fact offside the regulations, and about potential modifications of the practices to achieve compliance.

[142] As such, Mr. Woollcombe's letter was not revelatory for Cash Store. Cash Store was aware of the concerns that Mr. Woollcombe highlighted, and was in discussions with regulators concerning possible solutions.

[143] Mr. Woollcombe also asserted that Cash Store had not yet, and was required to issue a press release concerning recent amendments to the Ontario regulations, and their impact on Cash Store's business and operations.

[144] Cash Store responded to Mr. Woollcombe's letter in a letter signed by Mr. Reykdal dated January 20, 2012, essentially denying Mr. Woollcombe's allegations and explaining the details of and rationale for the practices impugned in Mr. Woollcombe's letter (which in Cash Store's view complied with the regulatory requirements).

[145] Cash Store also issued a press release on January 24, 2012, disclosing and describing the January 17, 2012 VWK letter, and responding to the concerns raised in the VWK letter as follows:

"The Company also announced that the Board of Directors of the Company recently received a letter from a self-described short seller. The letter alleges that the Company is in violation of payday loan regulations in the Province of Ontario and

that, as a result, the Company's existing public reports are not accurate. After reviewing the allegations, the Company believes that it is in compliance with applicable regulations in the Province of Ontario in all material respects. The Company suspects that the letter is the commencement of an opportunistic attack on the Company by a short seller, designed to disrupt the Company's previously announced private offering of senior secured notes. The Company will vigorously defend itself against the short-seller's self-interested and misleading attacks."

[146] On April 12, 2012, counsel on behalf of VWK, Graeme Camerson, wrote to the Deputy Minister of Consumer Services for Ontario, reiterating the complaints set out in Mr. Woollcombe's letter, and setting out, in 46 pages, additional evidence and a detailed analysis of Cash Store's alleged non-compliance with various relevant provisions of the legislation and regulations.

[147] On August 27, 2012, Mr. Woollcombe wrote to Cash Store again, addressing his letter to various executives and Cash Store's board of directors.

[148] While Mr. Woollcombe referenced his exchange of letters with Mr. Reykdal in January of that year, the focus of Mr. Woollcombe's August 27 letter was the Note Offering and LIT completed on January 31, 2012.

[149] By way of brief summary of Mr. Woollcombe's August 27 letter, which in my view factors into the limitations analysis later in this endorsement, he alleged that the loan portfolio purchased via the LIT was substantially overvalued, and that Cash Store's disclosure concerning the true nature and value of the transaction was substantially deficient.

[150] By the time of this August 27 letter, Cash Store, after initially reporting a value of the loan portfolio of approximately \$80 million (which Mr. Woollcombe alleged was itself an overvaluation and the subject of inadequate disclosure), had in its Q3 2012 interim review statements adjusted the value of the portfolio downward by about \$10 million to approximately \$70 million. Mr. Woollcombe decried a lack of meaningful disclosure concerning this adjustment as well.

[151] Mr. Woollcombe's August 27 letter goes on to complain: "We do not believe there is any rationale [sic] explanation for why Cash Store opted to acquire the Purchased Loans at a significant premium to fair value." Mr. Woollcombe speculates that Cash Store could instead "simply [have] allowed the third-party loan portfolio to run-off, with new loan origination being made by Cash Store," that Cash Store's true intention in acquiring the purchased loans (at a significant premium), must have been to "mask the true extent of the loan losses associated with that portfolio", and to "avoid having to acknowledge commitments to its third-party lenders regarding loan losses and third-party lender returns that were inconsistent with Cash Store's prior public disclosure."

[152] On the topic of loan losses, Mr. Woollcombe's letter expresses a purportedly longstanding concern that Cash Store, by way of the Retention Payments, had been concealing the true extent of the loan losses arising from the payday loans. He asserts that of the Retention Payments recorded as an expense in Cash Store's 2011 year-end audited statement in the amount of \$26.8 million, the amount likely attributed to loan losses (net of the non-guaranteed return of 19%

(later reduced to 17.5%) to Cash Store's TPLs confirmed in those statements), would reflect only \$5.5 million of loan losses, representing less than one percent of loan volume during the fiscal year.

[153] Mr. Woollcombe points in his letter to industry-wide reports of loan losses ranging upward from 2.25%, and Mr. Reykdal's own public statement at an annual shareholders' meeting that Cash Store's loan losses ran at about six percent. He alleges that therefore the loan losses were higher than implied in the Retention Payments expense, and that the purchased Loan Portfolio must have included extensive bad debt that had not been recognized or disclosed.

[154] Around this same time, commencing in or about July of 2012, Craig Warnock replaced Nancy Bland as Cash Store's CFO.

[155] Mr. Warnock, early in his tenure, developed a concern that the extent of loan losses implied in the valuation of the Loan Portfolio – which value was being reduced in Cash Store's public disclosure to approximately \$70 million, as discussed above – remained understated, and that in particular the valuation had used projected loan losses reflecting a better collection outcome than Cash Store's historical track record did.

[156] Mr. Warnock's persistent insistence that the value of the Loan Portfolio, even at \$70 million, was thus overstated, led the company to further reduce its estimate of that value, representing by the time of the year-end 2012 financial statements that the value was in fact approximately \$50 million.

[157] There was no evidence before me as to what extent, if any, Mr. Woollcombe's concerns about the overvaluation of the Loan Portfolio sparked Mr. Warnock's investigation and recommendation. Mr. Warnock testified that it was Michael Zvonkovic of Cash Store who initially raised a concern with him. Suffice to say that there was an emerging concurrence, led internally at Cash Store by Mr. Warnock, that the value of the Loan Portfolio was overstated based on an unrealistic assumption about collection rates, and had to be written down. I note that Cash Store, in this context, had earlier engaged EY in connection with the LIT specifically to undertake an exercise to better determine the value of the Loan Portfolio.

[158] Finally on the topic of "whistleblower" letters, KPMG, in its capacity as Cash Store's auditor, received a letter dated November 6, 2012, from Clearwater Capital Management Inc. ("Clearwater"). Clearwater wrote to KPMG as a holder of Cash Store Senior Secured 11.5% notes issued in the Note Offering.

[159] Clearwater's letter, though not referring to the VWK letter(s), in part echoed and amplified the concerns expressed by VWK regarding the provisions for loan losses, expressing the expectation that KPMG would "diligently assess [Cash Store]'s credit provisioning practices in light of its default and collection experience and compare its policy to other participants in the payday loan business."

[160] In addition, Clearwater raised concerns about Cash Store's possible non-disclosure of related parties in connection with the LIT, citing "rumours that [Cash Store] officers and/or

directors have been participants in the partnerships that previously financed [Cash Store]’s loan originations” (about which more below).

[161] Putting these concerns together, Clearwater said (and note that the figures cited by Clearwater alleged to be in excess of fair market value reflect the purchase price for the LIT less \$80 million, initially, and then less the adjusted figure of \$70 million):

“The \$36 million payment (since adjusted to \$46 million) in excess of estimated fair value for the former LP Payday Loan portfolios brings into question the business reason for such purchase and the potential value of the benefits that may accrue to [Cash Store] from the Supplier and Non-Compete Agreements. The payment in excess of fair value has led to the speculation that the purchased Payday Loan portfolios had experienced significant uncollectable and defaulted loans and that the purchase price effectively included payment for a cumulative deficiency that had not been previously met by a combination of Retention Payments made by [Cash Store] to the LPs [TPLs] and interest earned directly by the LPs on the Payday Loan portfolios. There is speculation that [Cash Store] officers and directors may have been participants in the former LPs and benefitted from the purchase of the short term loan portfolios.”

[162] Clearwater also articulated the expectation that KPMG would diligently investigate and ensure disclosure with respect to the status of potential related party transactions.

(J) Cash Store Establishes Special Committee to Investigate Whistleblower Claims

[163] The Clearwater letter, likely in conjunction with the other factors discussed above, led to a decision by Cash Store’s board of directors to appoint the Special Committee of Cash Store’s independent directors, ultimately with assistance from the Torys LLP law firm and from the accounting firm Deloitte, which was in turn engaged by Torys to investigate and report on the various items of expressed concerns.

[164] Deloitte’s report of its findings, dated May 13, 2013, is instructive in various respects.

[165] As summarized in the report’s executive summary, among other things, Deloitte:

- (A) Did not find any evidence to indicate the existence of “side agreements” between Cash Store and the TPLs (which is an allegation that CS Estate continued to make before me);
- (B) Were repeatedly informed by management and members of Cash Store’s Board that no guarantees were provided to TPLs, and confirmed that Cash Store’s public disclosure was consistent with this proposition;

- (C) Identified seven email communications between Cash Store's management and the TPL Assistive Financial during the relevant timeframe relating to the confirmation of Retention Payments and the rate of return to Assistive Financial; and,
- (D) Noted differences in the terms of the Loan Portfolio Purchase Agreement between Cash Store and Assistive Financial which did not appear to have been communicated to the Board.

[166] Deloitte also reported that it found no discrepancies in matters publicly disclosed in the restated financial statements and the management discussion and analysis document ("MD&A"(s)) with respect to the facts and circumstances surrounding the LIT.

[167] On the topic of the restated financial statements, Deloitte noted that Cash Store's accounting for the LIT had been incorrect in the original interim review financial statements for Q2 and Q3 of the 2012 fiscal year. This led to the restated financial statements based on Cash Store's determination that approximately \$36.8 million of the total consideration paid to acquire the loan portfolio "should have been recognized as an expense to settle pre-existing business relationships with third party lenders." An MD&A from that timeframe was also updated to disclose management's determination that material weaknesses existed regarding the effectiveness of internal controls over financial reporting as at March 31, 2012 and June 30, 2012.

[168] Of note, given the allegations in the Clearwater letter about related parties, Deloitte "did not identify any related parties requiring disclosure that were not previously identified in the investigation conducted by Cash Store's internal audit group and disclosed by Cash Store." (These allegations about related parties will be discussed below).

[169] Deloitte also confirmed that Cash Store had historically operated under a broker model, and that it was as a result of the implementation of provincial regulations in various provinces that Cash Store considered other financing options and decided to "transition its short-term lending business in the regulated Canadian provinces from a broker model to a direct lending model."

[170] Deloitte described the LIT and related Note Offering, noting that Cash Store acquired the Loan Portfolio from TPLs for total consideration of \$116.3 million, with the result that Cash Store's effective cost of capital was reduced and the loan financing business was now, in the regulated provinces, brought onto the balance sheet. Deloitte noted that in unregulated provinces, Cash Store continued to operate using TPLs and the broker model.

[171] Deloitte discussed the allegations in the "whistleblower" letters, described additional relevant details of the LIT, and then outlined the investigation that Deloitte had undertaken at the request of the Special Committee leading to the findings summarized above.

(K) Regulatory and Other Issues as at Early 2014 and Decision to Seek CCAA Protection

[172] Mr. Aziz, once ensconced as CRO, also met with Cash Store's Chief Compliance and Regulatory Officer to understand more about the regulatory issues confronting Cash Store.

Subsequently, accompanied by a representative of the monitor, Mr. Aziz met individually with other senior management of Cash Store, and with its CEO Gordon Reykdal.

[173] On that regulatory front, in Ontario, on February 12, 2014, as noted, Morgan J. of this court ordered that Cash Store and certain of its affiliates were prohibited from acting as a loan broker in respect of Cash Store's recently introduced BLOC product without a broker's license under the *Payday Loans Act*. The next day, February 13, 2014, again as noted above, the Ontario Registrar of Payday Loans (the "Ontario Registrar"), issued a proposal to refuse to issue a lender's license to Cash Store and certain of its affiliates under the *Payday Loans Act*. As a result of these events, Cash Store was effectively precluded from offering any payday loan products in Ontario.

[174] Cash Store issued a news release on March 28, 2014, confirming that the Ontario Registrar had issued a final order refusing to license Cash Store or certain of its affiliates under the *Payday Loans Act*. Cash Store announced that it was not permitted to offer any payday loan products in Ontario, and would not be eligible to re-apply for a license for 12 months from the date of the Ontario Registrar's issuance of the final order.

[175] In the same March 28, 2014 news release, Cash Store announced that it had appealed Morgan J.'s February 12, 2014 decision. However, subsequently, by letter dated May 2, 2014, by which time the initial CCAA Order was in place, Cash Store's counsel advised that Cash Store would not be pursuing this appeal.

[176] In discussions with counsel from the Ontario Attorney General's Office for the Ministry of Consumer Services during that time frame, Mr. Aziz was advised that the Ontario Registrar would not consider re-licensing Cash Store while its then-current management team remained in place.

[177] It is evident that as of the spring of 2014, Cash Store's regulatory status in other Canadian provinces in which it did business was also in flux and at risk.

[178] For example, in Alberta, where Cash Store's headquarters were located, the provincial regulator had revoked a license it had granted to Loans Alberta, a Cash Store subsidiary, and was investigating Cash Store's collection practices. Similar circumstances were unfolding in British Columbia, Saskatchewan, Manitoba and Nova Scotia.

(L) Steps Taken in CCAA Proceedings

[179] Mr. Aziz's evidence was that this precarious and untenable regulatory situation, coupled with concerns expressed by certain stakeholders within the CCAA proceedings, led Mr. Aziz in his capacity as CRO (as defined below) to terminate various members of Cash Store's senior management on May 22, 2014, including its CEO Mr. Reyhdal.

[180] Prior to the commencement of the CCAA proceedings, the Cash Store Special Committee had retained Rothschild Inc. to act as an independent financial advisor and had commenced a process seeking either the sale of Cash Store, or a significant investment into the business. This sale and investment process ("SISP") continued into the CCAA proceedings.

[181] This court granted an order approving the SISP on June 16, 2014. The SISP attracted considerable interest, ultimately yielding 12 non-binding expressions of interest and five final round proposals.

[182] In the result Cash Store completed three court-approved asset sale transactions during the course of the CCAA proceedings, the largest and most significant of which was an asset purchase agreement under which National Money Mart Company (a competitor of Cash Store in the payday loan industry) acquired the bulk of Cash Store's remaining assets, resulting in \$51.1 million for Cash Store (excluding post-closing adjustments).

[183] Together with two smaller court-approved transactions, substantially all of Cash Store's realizable assets were sold, bringing approximately \$54.3 million into the Cash Store estate.

[184] During the course of the CCAA proceedings, Cash Store also settled various ongoing class proceedings against it, and other claims by and against it, including the claims against the Ds & Os mentioned above. Cash Store also settled with two senior secured lenders, paying \$9,150,000 to that end.

[185] Also during the course of the CCAA proceedings, the court approved debtor-in-possession ("DIP") financing for Cash Store, and Cash Store's estate incurred substantial professional fees in connection with the restructuring and sale transactions.

[186] Mr. Aziz's evidence was that, in parallel to these various aspects of the CCAA proceeding, he was developing a concern, based on advice from "a number of parties", that Cash Store's broker business was not legally defensible under criminal interest rate provisions of the *Criminal Code* and that Cash Store's TPLs were no longer prepared to continue funding the business. At least one provincial regulator had also expressed the view that Cash Store's BLOC product did not comply with the law.

[187] As noted, at the same time, Mr. Aziz and others involved in the CCAA proceedings discussed concerns about Cash Store's core management leading, as discussed above, to the termination of Mr. Reykdal and others.

[188] These various considerations ultimately led to the conclusion, spearheaded by Mr. Aziz, that Cash Store's broker business model would have to be discontinued, and the winding up process, including the asset sale transactions discussed above, undertaken in an orderly fashion.

[189] In late May of 2014, Mr. Aziz met with representatives of Cassels, and discussed, among other items, Cassels' billings to Cash Store as its counsel, and the relationship between Mr. Stein and Cash Store.

[190] This meeting led to Cassels sending a letter, later that same day, advising that Cassels was "unable to continue to act for Cash Store in any matter" and was "required to withdraw as counsel pursuant to the Rules of Professional Conduct".

[191] Around that same time, Mr. Aziz had learned of Mr. Stein's role, concurrent with acting as the relationship partner at Cassels for the Cash Store work, as a principal of Abel Financial Inc. ("FSC Abel"), one of Cash Store's TPLs, from which loans had been purchased as part of the Loan Internalization Transaction. There was no direct evidence before me as to the reason for Cassels' withdrawal, but it appears likely that Mr. Stein's alleged conflict, and the potential for a claim against Cassels based on those and other allegations, made Cassels' continued retainer untenable.

(M) Decision of Morawetz R.S.J. (As He Then Was) on Priority Dispute Between TPLS and DIP Lenders

[192] Also in May of 2014, a number of TPLs brought a motion within the CCAA proceeding seeking an order that the TPLs were the sole legal and beneficial owners of funds loaned in their names and purportedly brokered by Cash Store and advanced to Cash Store's payday loan customers. The TPLs sought a priority over the DIP lenders (the "DIP Lenders) relative to those funds.

[193] That motion was heard by Morawetz R.S.J. (as he then was), and resulted in His Honour's decision of August 5, 2014, *Cash Store Financial Services (Re)*, 2014 ONSC 4326, 31 B.L.R. (5th) 313, which looms large in the actions before me.

[194] In that decision, Morawetz R.S.J. concluded that, at least at that stage, the relationship between Cash Store and the TPLs was substantively different in character than as portrayed in Cash Store's financial statements and other public disclosure. Justice Morawetz held that the relationship was properly understood as a "debtor-creditor relationship", rather than a broker relationship as represented by Cash Store.

[195] This decision dovetails with, and presumably precipitated in part the position taken by CS Estate before me.

[196] His Honour held:

"[3] On paper, Cash Store obtains funding from sources which include a number of third party lenders ("TPLs"). On paper, these TPLs provide Cash Store with funds which Cash Store, as broker, then lends to Cash Store customers. On paper, the loans are assigned to the TPLs. On paper, the TPLs "own" all payments received from the customers. These payments are comprised of principal and interest. Interest is charged at the rate of 59% per annum. On paper, Cash Store is required to keep TPL funds segregated. On paper, the operating model leads to a conclusion that the relationships between TPLs and Cash Store is not a debtor-creditor relationship, but is one where Cash Store functions as a broker.

[4] However, the manner in which Cash Store business operations were conducted differed substantially from that set out "on paper". Specifically, interest payments did not flow to the TPLs at the contract rate of 59% - or even at 59% less a bad debt expense, or after an allowance for impaired loans. Rather, Cash Store would make "voluntary payments" or "retention payments" at the rate of 17.5%

(in some cases 20%) to the TPLs as “an inducement” to ensure the continued support of the TPLs.

[5] Payments received from Cash Store customers were used in the operations of Cash Store. Cash Store did not keep payments that it received from its customers in a segregated account for TPLs. The TPLs did not audit the account of Cash Store.

[...]

[126] From the standpoint of the DIP Lenders, this ongoing payment equivalent to 17.5% of outstanding amounts is significant and leads me to a finding that the relationship between the TPLs and Cash Store was a debtor-creditor relationship and that the payments which are equivalent to 17.5% of outstanding funding reflect a payment of interest. A payment of interest is clearly inconsistent with the position being put forth by the TPLs, namely that there was no debtor-creditor relationship.”

[197] Mr. Aziz, in his evidence, says that Morawetz R.S.J.’s decision was “important to my evolving understanding of how the business was run and whether Cash Store should be pursuing claims.”

[198] There is no doubt that Justice Morawetz’s decision is significant in these proceedings, and requires respect and deference. It is also clear, however, that His Honour’s decision did not consider the claims against Cassels and KPMG – which did not yet exist at that time – and that neither of those parties was before Morawetz R.S.J. in the context of his determination of the issues as between the TPLs and the DIP Lenders. As such, in my view, His Honour’s decision does not foreclose arguments as to the defences of Cassels and KPMG before me, which in large part turn on issues other than those decided by His Honour.

[199] I also note that His Honour’s characterization of the payment(s) based on the rate of 17.5% as constituting the “retention payments” is not entirely apt. As stated, and based on the fuller evidentiary record before me, Retention Payments were accrued based on quarterly approvals by Cash Store’s board of directors, and these accruals exceeded the amounts of the payments based on 17.5%. Justice Morawetz’s apparent conclusion that the only payments from Cash Store to the TPLs were at the rate of 17.5% (or as he notes, at 20% in some cases), and that there was no provision for bad debts does not consider, presumably because the parties before him had a narrow evidentiary focus on the priority dispute in which they were engaged, the function of the accrual of Retention Payments beyond the monthly (17.5%) payments, nor the interplay between accrued Retention Payments and bad debts. From an accounting perspective, in particular, in my view the characterization of the Retention Payments is a more subtle and nuanced exercise than the way it was presented before Morawetz R.S.J. (where the fight was between two combatants each asserting a priority claim to limited funds within Cash Store’s estate).

[200] As set out below, while again Morawetz R.S.J. (as he then was)’s decision is entitled to deference insofar as it determined the priority dispute between the TPLs and the DIP lenders, it did not address and is therefore not determinative of the claims against KPMG and Cassels.

(N) Important Aspects of Fact Evidence at Trial

(1) Discussion re Evidence of William Aziz

[201] The first, and main fact witness called by the plaintiff was Mr. Aziz.

[202] Mr. Aziz, and in particular his company Blue Tree Advisors Inc. (“Blue Tree”), was appointed as Chief Restructuring Officer (“CRO”), to 1511419 Ontario Inc. (formerly known as The Cash Store Financial Services) (in this endorsement, included in “Cash Store”, as defined).

[203] The timing and circumstances of Mr. Aziz’s (and that of Blue Tree’s) introduction to the Cash Store saga as CRO has various implications for his evidence.

[204] First, it is fair to observe, as the defendants emphasize, that Mr. Aziz’s information is not based on first-hand contemporaneous knowledge, but rather based on Mr. Aziz’s retrospective investigation – albeit a comprehensive one – as to the circumstances of Cash Store’s demise.

[205] There is also, in my view, a further concern about Mr. Aziz’s evidence. That is, it emerged in a rather matter-of-fact way during Mr. Aziz’s cross-examination that Mr. Aziz has an agreement pursuant to which, if the plaintiff succeeds in this action, he will receive a percentage of the proceeds of any damages awarded. Mr. Aziz confirmed in cross-examination that he is not prepared to disclose the percentage for which he has bargained, and cross-examining counsel did not push for an answer (or ask that I direct Mr. Aziz to answer). Mr. Aziz appears also to have worked, in developing this claim, with Mr. Woollcombe and his company, with whom (and with which) Mr. Aziz acknowledged he has worked in the past, and which had staked a claim as a short seller of Cash Store securities. It also emerged that Mr. Woollcombe’s firm, as discussed below, is itself contractually entitled to a share of proceeds of this lawsuit.

[206] It appears that while Mr. Aziz had originally negotiated for his own direct contingency-like arrangement, his/Blue Tree’s deal was ultimately structured on the basis that he/it will receive a portion of the contingency-based amount to be paid to plaintiff’s counsel in the event of damages being awarded to the plaintiff.

[207] As such, I am left with the somewhat unsettling scenario in which I am aware that Mr. Aziz/Blue Tree will profit personally from a judgment in CS Estate’s favour, to an unknown extent.

[208] To be clear, I am not concerned that plaintiff’s counsel’s potential compensation is structured as a contingency. Plaintiff’s counsel are reputable officers of the court, and conducted themselves with professionalism and integrity throughout the trial. Moreover, such contingency arrangements for counsel are permissible and not uncommon.

[209] However, I did find it troubling to learn that Mr. Aziz, the key fact witness for the plaintiff, had an incentive to ensure that the plaintiff succeeds.

[210] By an agreement among the parties that I confirmed in a trial management conference shortly before the trial, Mr. Aziz's evidence-in-chief was in large part set out in an affidavit-like witness statement, fleshed out by time-limited viva voce evidence at trial. Nowhere in Mr. Aziz's witness statement, nor in his viva voce evidence-in-chief, did he identify or discuss his contingency arrangement.

[211] That is not to say that I found Mr. Aziz to be overtly biased or otherwise generally unfair in his testimony. To the contrary, it is clear that Mr. Aziz is an experienced officer of the court, and for the most part he delivered his evidence in a fair and even-handed way.

[212] However, I observed, during the initial part of Mr. Aziz's cross-examination – before I became aware of his deal to share in any upside – that he pushed back unnecessarily, and in a kind of aggressively defensive knee-jerk fashion at odds with most of his testimony, in response to certain questions about the conduct of KPMG and Cassels. His answers on those issues largely recited, in a somewhat pro forma but emphatic fashion, the plaintiff's key theories as against those defendants.

[213] After learning of Mr. Aziz/Blue Tree's financial incentive, I became concerned about this aspect of Mr. Aziz's testimony, and in particular that his somewhat uncharacteristically aggressive response to certain questions about the role and conduct of the professional advisors, may have been coloured in part by his compensation being tethered to the outcome of the trial.

[214] As noted, it also appears that Mr. Aziz has an ongoing relationship with Mr. Woollcombe of VWK, the entity that had a "short position" in Cash Store during the time period in which Cash Store's operations came under scrutiny and losses became evident. Mr. Woollcombe and VWK, who wrote or caused to be written the series of "whistleblower" letters in 2012, thus had a vested financial interest in Cash Store's demise, an incentive that seems to me to be at odds with the altruistic motives normally associated with "whistleblowing." Evidence emerged during Mr. Aziz's cross-examination confirming that Mr. Woollcombe and his partner Wes Voorheis, and their firm Voorheis & Co. LLP, also have a stake in the outcome of this trial, and a percentage interest in the proceeds of the trial, if any. Neither Mr. Woollcombe nor Mr. Voorheis testified at trial, but the VWK "whistleblower" letters were entered into evidence and referenced by the plaintiff as part of its claim.

[215] These various interests, that is those of Mr. Aziz/Blue Tree, plaintiff's counsel and Voorheis & Co (labelled as co-counsel) (collectively for this purpose the "Contingency Recipients"), are ultimately recorded and subsumed in a "litigation funding agreement" dated September 8, 2021, in which an England-based entity, Augusta Pool 4 Canada Limited, agrees to provide certain funding and in which the Contingency Recipients (and others) share in potential proceeds of this action (in an amount that has been redacted from the agreement and hence remains unknown to me). The litigation funding agreement was also not entered into evidence before or during Mr. Aziz's evidence in chief.

[216] I do not suggest that there is anything illegal or impermissible about these arrangements (which I understand may be necessary in certain circumstances to fund litigation that is thought to

be meritorious). I nonetheless find it concerning that the key fact witness for the plaintiff, who functioned as the CRO in the CCAA proceedings, has an unknown percentage interest in the proceeds of the litigation and, hence, an undeniable incentive to see the plaintiff succeed.

[217] In closing submissions, in response to my questions about this arrangement, plaintiff's counsel suggested that it is no different than any plaintiff who testifies at any trial; the plaintiff inevitably and invariably has an interest in the outcome of the proceeding in which he or she may be a key fact witness. In my view, however, where the witness at issue has been a designated officer of the court, charged with and expected to uphold utmost duties of impartiality, the considerations are somewhat different. Indeed, Mr. Aziz was presented to the court as one with considerable experience as a CRO, and offered as an expert-like witness, cloaked in the mantle of that experience and role as a neutral court officer. When it emerged (only in cross-examination) that Mr. Aziz has "a piece of the action" it tends in my view to undermine that characterization, particularly when Mr. Aziz's deal was not disclosed and explained up front. While this (initially) undisclosed incentive does not disqualify Mr. Aziz from testifying, it does in my view raise concerns about the neutrality of his testimony.

[218] Accordingly, I approach certain aspects of Mr. Aziz's evidence with caution, and in particular put minimal weight on his specific criticisms of the defendants, which are in any event best understood and considered based on the expert evidence I heard.

[219] The substance of Mr. Aziz's evidence was in large part devoted to presenting an overview of Cash Store's business, largely as discussed above, with a particular focus on the last couple of years of its operations, leading to and following the CCAA application, and Mr. Aziz's appointment as CRO. That narrative from Mr. Aziz is largely uncontroversial, and was indeed helpful to the court.

[220] Mr. Aziz's evidence also focused, however, on his purported discovery of the alleged misrepresentation of Cash Store's true business model and operations, and on his purported determination that various Cash Store employees and executives, and Cash Store's professional advisors – including Cassels, KPMG and Canaccord – had turned a blind eye to the ongoing misrepresentations about Cash Store's business, and to the purported fact of Cash Store's insolvency. It is relative to these aspects of Mr. Aziz's testimony that my concerns, and the need for caution, arise.

(2) Evidence of Cash Store Officers and Employees

[221] Various Cash Store officers and employees also testified before me.

[222] These included Mr. Reykal, Ms. Bland, who was Cash Store's Chief Financial Officer during much of the relevant time period, Mr. Warnock, who took over the CFO role from Ms. Bland at a point in 2012, and Albert (Al) Mondor, an independent director of Cash Store, and the chair of Cash Store's Audit Committee. Other former Cash Store employees also testified. In addition, by agreement, excerpts of evidence of still other Cash Store directors and officers were entered into evidence without the attendance of those witnesses.

[223] The various former Cash Store employees and officers who testified were uniformly sophisticated and well-informed, and presented very well as witnesses. Virtually to a person, the former Cash Store employees and officers attested to Cash Store having carried on business as a broker, and as to the development of and ongoing arrangements with the TPLs, including the practice of Retention Payments.

[224] These witnesses confirmed that Cash Store did not operate to any extent as a lender until after the point in 2011-2012 when, as a result of the changing regulatory environment governing payday loans, and impacting Cash Store in particular, it necessarily considered changes to its business model and began a transformation, in the regulated provinces, to a direct lending model (including the newly developed BLOC product).

[225] The Cash Store witnesses each explained the rationale for redeploying the TPLs' funds, during the time that Cash Store functioned as a broker, for the purpose of further loans rather than providing repayment in full each time a consumer paid off a loan, and each had an understanding and testified as to the reasons for the Retention Payments. They each also confirmed that those Retention Payments were voluntary and not guaranteed, and that they had to be approved on a regular basis by Cash Store's board. I note that this testimony appears entirely consistent with the information provided by Cash Store employees and management to Deloitte in the context of the Special Committee investigation.

[226] Cash Store's accounting department, in particular, was relatively large and sophisticated.

[227] Ms. Bland, for example, who oversaw the group as CFO during most of the timeframe at issue, had joined Cash Store, initially as its vice-president of finance, after working as an auditor with the Grant Thornton firm. Mr. Mondor, the chair of Cash Store's audit committee from a point in 2012, was also an experienced accountant/auditor.

[228] Ms. Bland in her evidence confirmed her understanding that Cash Store was responsible for its financial reporting and for the preparation, accuracy and completeness of its interim and annual financial statements, as well as the contents, including financial information, within the MD&As and AIFs.

[229] Ms. Bland explained that all such statements were prepared initially in draft by Cash Store's accounting department under the supervision of the Vice President of Financial Reporting, who would conduct the first review of the statements for completeness and accuracy.

[230] Ms. Bland would then review the statements herself, and once she had done so, the statements were reviewed by Cash Store's audit committee.

[231] Once the audit committee signed off, it would recommend approval by Cash Store's Board. The Board, based on that recommendation and its own review, would then vote a resolution to approve the statements.

[232] The defendants assert, and in my view the evidence shows, that Cash Store had an active and engaged management team and board (with six independent board members) that took

appropriate steps to ensure that Cash Store's financial and other disclosure accurately reflected Cash Store's business operations, its assets and liabilities, and its financial affairs generally.

[233] The consolidated annual financial statements of Cash Store for the year ending September 30, 2011 were stated to be prepared and presented in accordance with Canadian GAAP and reconciled to the U.S. generally accepted accounting principles ("US GAAP"). Likewise, Cash Store's consolidated annual financial statements for the year ending September 30, 2012 were prepared in accordance with US GAAP.

[234] To the knowledge of Ms. Bland and the members of her team at Cash Store (and of course to the knowledge of the Cash Store's Audit Committee and its board), KPMG audited Cash Store's 2011 and 2012 annual financial statements in accordance with both Canadian GAAS and the standards of the Public Company Accounting Oversight Board (the "PCAOB" or "US GAAS").

[235] Cash Store's interim financial statements for the periods ending December 31, 2011 and March 31 and June 30, 2012 were stated to be prepared in accordance with US GAAP. KPMG carried out its review engagements in respect of these interim financial statements in accordance with Canadian generally accepted interim review standards (under CICA 7050).

[236] The evidence of numerous witnesses including Ms. Bland and Natalie Brykman, one of the lead managers for KPMG's audits of Cash Store's 2011 and 2012 annual financial statements, was that the disclosure in those financial statements, consistent with all of Cash Store's other public disclosures and representations, consistently held Cash Store out as a broker that facilitated short-term loans (advanced by TPLs) to customers. These disclosures included Cash Store's financial statements, its Annual Information Forms ("AIFs"), its MD&As and its press releases. Ms. Bland testified that at the time, and still as of the date of her trial testimony, she continued to view the disclosures as accurate.

V. Evidence and Discussion Concerning KPMG's Approach to the Audits and Interim Reviews

[237] A number of documents were put in evidence to demonstrate the contractual arrangements, parameters and specific information exchanged and reviewed for purposes of each of KPMG's mandates for Cash Store. Various KPMG personnel also testified at trial, and discussed the detailed and extensive planning and execution of the audits and reviews.

[238] For example, and importantly, KPMG's engagement letter dated April 26, 2011 sets out, clearly, the respective roles and responsibilities of KPMG and Cash Store (in particular Cash Store's management) relative to the 2011 audit (as well as the 2012 interim statements). The document specifically confirms that Cash Store's management was responsible for the preparation and fair presentation of its financial statements in accordance with the applicable financial reporting framework. KPMG points out, and the Cash Store witnesses each confirmed, that each and every financial statement prepared by Cash Store's management during the relevant timeframe represented and reflected Cash Store as a broker.

[239] KPMG’s function, as Cash Store’s auditor, was to audit or review the financial statements prepared by Cash Store, and to express an opinion (for the annual audits) on whether Cash Store’s financial statements were prepared, in all material respects, in accordance with the applicable financial reporting regimens. KPMG’s engagement letters made clear that it could not obtain or provide absolute assurance that Cash Store’s annual financial statements were free from material misstatements; rather, it would provide “reasonable assurance” about whether the financial statements were free from material misstatements, which is what the audit standards (both Canadian and U.S.) require.

[240] The role for this court, relative to the claim against KPMG, is to determine whether, in the context of its contractual obligations and its obligations at common law, KPMG met the standard of a reasonable accountant carrying out audit and review engagements in 2011 and 2012.

[241] In order to determine the standard of care to be applied, Ontario courts (and other courts in Canada) have consistently referred to and relied on the Canadian Institute of Chartered Accountants Handbook (the “CICA Handbook”) as authoritative evidence of the standards governing the profession.

[242] In that regard, KPMG in its argument cites the decision of the Court of Appeal for Ontario in *Livent Inc. (Receiver of) v. Deloitte & Touche*, 2016 ONCA 11, 128 O.R. (3d) 225, rev’d in part on other grounds 2017 SCC 63, [2017] 2 S.C.R. 855 at paras. 199-200, in which the court undertook a review of guidance from the Supreme Court of Canada confirming the importance of self-governing bodies’ rules when reviewing the trial judge’s reliance on the CICA Handbook and in discussion relevant provisions thereof. The Court of Appeal for Ontario said:

“[198] Deloitte’s role as Livent’s auditor was also subject to the professional standards applicable to auditors as set out in the CICA Handbook and the ICAO Member’s Handbook at the time.

[199] The Supreme Court of Canada has said that rules set by a self-governing professional body are “of guiding importance in determining the nature of duties flowing from a particular professional relationship...” [T]hese rules must be taken as expressing the collective views of the profession as to the appropriate standards to which the profession should adhere... .”

[200] In the auditing context, this court has held that the CICA Handbook “is of great assistance” to courts in determining the requisite standard and “a persuasive guide to the applicable standard of care”; *Bloor Italian Gifts Ltd. v. Dixon* (2000), 48 O.R. (3d) 760, [2000] O.J. No. 1771 (C.A.), at paras. 27, 31; and *Sherman v. Orenstein & Partners*, [2005] O.J. No. 5161, 11 B.L.R. (4th) 233 (C.A.), at para. 33..

[201] The trial judge reviewed the relevant provisions in the CICA Handbook in considerable detail, focusing on those sections dealing with “Audit of Financial Statements” (s. 5000), “Knowledge of the Entity’s Business” (s. 5140) and “Auditor’s Responsibility to Detect and Communicate Misstatements (s. 5135).

[202] Given their significance, I will review the standards from the CICA Handbook in effect at the relevant time in some detail.”

[243] As will be seen, KPMG in its expert evidence and submissions puts particular emphasis on the relevant provisions of the CICA Handbook in place during the relevant timeframe, and its accounting liability expert, Mr. Cameron, in his evidence undertook a painstaking review of the CICA Handbook provisions that in his opinion apply to the matters at issue and confirm the requirements of GAAP and GAAS flowing from these provisions, and testified as to his view that KPMG’s audit work complied with these standards.

[244] The plaintiff, while acknowledging that “there can be little doubt that KPMG was required to conduct its audits in accordance with the applicable GAAS, and to express an opinion as to the compliance of Cash Store’s financial statements to GAAP,” argues that “However, that is not the full extent of KPMG’s common law obligations. Compliance with GAAS and conformity with GAAP are necessary but not sufficient to discharge the duty of care. In addition, KPMG is required to ensure that the financial statements are not materially misleading, even if prepared in accordance with GAAP.”

[245] In support of this proposition, the plaintiff cites and places particular reliance on the decision of the Court of Appeal for British Columbia in *Kripps v. Touche Ross & Co.*, (1997), 33 B.C.L.R. (3d) 254, [1997] 6 W.W.R. 421 (B.C.C.A.), application for leave dismissed, [1997] S.C.C.A. No. 380, in which Finch J., for the majority, wrote:

“In my view, therefore, while professional standards would normally be a persuasive guide as to what constitutes reasonable care, those standards cannot be taken to supplant or to replace the degree of care called for by law [...] It is for this reason that I respectfully disagree with the learned trial judge that it is appropriate for auditors to sign unqualified auditor’s reports if the financial statements are prepared in accordance with GAAP, if the auditors know or ought to know that the financial statements are misleading” (para 73).

[246] In my view the submissions of both sides of this issue have merit and are not mutually exclusive. That is, there can be no doubt that the GAAP and GAAS standards enshrined in the relevant provisions of the CICA Handbook carry considerable weight and are entitled to considerable deference from the court in terms of establishing the standards to which accountants and auditors must adhere.. However, if it can be shown that the auditor – here KPMG – applied the relevant CICA Handbook standards appropriately, but nonetheless countenanced financial statements that were materially misleading, compliance with the CICA Handbook standards would not preclude a potential finding that the auditor fell below the required standard of care.

[247] I would go further to say that, as a general proposition, confirmation of compliance with the relevant CICA Handbook standards provides substantial and compelling evidence of adherence to the standard of care, and it would be a rare circumstance in which compliance with the relevant CICA Handbook standards establishing GAAP and GAAS would nonetheless allow for a finding of a common law breach of the standard of care.

[248] I also note that there was extensive evidence as to the manner in which KPMG staffed its audits (and reviews), the manner in which it planned and executed all aspects of those mandates, the manner in which it deployed numerous professionals in various aspects of the performance of these undertakings, and the manner in which the more senior members of the KPMG team oversaw and reviewed the work done by more junior members.

[249] There was in fact no particular criticism, and certainly no compelling criticism, offered by the plaintiff's expert(s) of the manner in which KPMG approached and staffed its tasks. Rather, the criticism is of certain conclusions and omissions alleged to render KPMG's work substandard.

[250] In my view, while of course KPMG's conclusions, and CS Estate's criticisms thereof, must be considered on their merits, the fact that KPMG approached its mandate in a fashion that appears comprehensive and thoughtful, and relative to which no meaningful criticism is levied, is a factor properly taken into account in assessing allegations of negligence. The fact that the means by which KPMG discharged its mandates do not attract reproach is not determinative, but it is a factor not to be ignored in the analysis.

[251] Having set out at a high level the parties' respective positions on what establishes the standard of care here, I turn now to an analysis of their detailed arguments, in each case largely premised on the opinions of their respective experts.

VI. Overview of Liability Experts and Their Opinions

[252] As noted, Mr. Aziz in his evidence cited Morawetz R.S.J.'s decision as providing a critical revelation and basis for this claim. Justice Morawetz's conclusions are embraced and enlarged upon in the plaintiff's expert reports in support of the claims.

[253] I should note that the plaintiff's primary expert, and its only expert tendered with respect to the alleged negligence of KPMG, Mr. Koch, was challenged by KPMG in terms of his qualifications to give expert evidence in this trial, which challenge was the subject of a day-long voir dire. By way of overview, KPMG argued that Mr. Koch, who is American and whose auditing experience was exclusively in the United States, has no relevant experience in opining on Canadian GAAP and GAAS standards, and that the only relevant experience he has had in the auditing sphere at all is extremely dated (Mr. Koch last performed direct audit work in 1991).

[254] I heard evidence and argument on the voir dire, and concluded that Mr. Koch was sufficiently qualified to testify by virtue of his audit experience, albeit remote and dated, but that I would have to consider, given the identified concerns about his experience, what weight could be accorded to his opinion on certain aspects of the case. I noted in reaching that conclusion the concern that it represented "taking the easy way out" and abdicating my gatekeeping role, but because of Mr. Koch's historical experience as an auditor, albeit long ago, I felt that he was capable of assisting my understanding of the issues.

[255] I discuss those considerations further below, but what follows immediately below is a high-level summary of salient aspects of Mr. Koch's opinion and that of Mr. Cameron on behalf

of KPMG (without any evaluation, at this point of this decision, of the question of weight to attach to those views, which I address later in this decision).

[256] In a summary of Delta Consulting Group (“Delta”)’s opinions vis-à-vis KPMG, Mr. Koch (the co-author of the Delta reports relative to KPMG, and the plaintiff’s witness on these matters at trial), stated that:

- (A) Cash Store’s original financial statements for the timeframe at issue were materially misstated as a result of Cash Store’s failure to present these statements “in a manner that reflected its economic substance as a lender, rather than its legal form as a broker”;
- (B) had Cash Store presented its financial statements in a manner consistent with its actual operating practices, approximately \$129.6 million of off-balance sheet debt would have been included in the company’s reported liabilities. In addition, consumer loan receivables – which would appropriately be valued at their net realizable value under GAAP after making a reasonable provision for doubtful accounts – would have been recorded as part of Cash Store’s reported assets;
- (C) as of September 30, 2011, the net realizable value of the consumer loan portfolio should have been recorded at approximately \$52.7 million, such that Cash Store would have had and reported a much lower net worth than the \$87.3 million stated in its original September 30, 2011 financial statements; and
- (D) if properly presented, Cash Store’s income statement within those September 30, 2011 financial statements would have shown a net loss of approximately \$11.5 million instead of net income of \$10.6 million as in fact reported.

[257] As can be seen, the fundamental premise from which virtually all aspects of Mr. Koch’s opinion flow is the notion that Cash Store’s operations were not fairly characterized as those of a broker. Building from this premise, Mr. Koch opines that KPMG, in its reviews of the interim statements during the period in question, and in its audits of the year-end financial statements for 2011 and 2012, by failing to recognize these purported conclusions, failed to meet the relevant standards under Canadian and U.S. GAAP and Canadian and U.S. GAAS.

[258] I note in passing that, building in turn on Mr. Koch’s opinions, Jimmy Pappas was called by the plaintiff to provide an opinion that Cash Store was insolvent as of September 30, 2011 and/or as of December 31, 2011, and to calculate the damages resulting from Cash Store’s deepening insolvency, quantified commencing from these respective dates as alternative scenarios, by the time of the CCAA order on April 14, 2014. I note as well that the defendants also called responding experts to discuss the quantification of the alleged losses, and that the calculation of losses will be discussed below.

[259] On the accounting liability issues, KPMG called Douglas Cameron, a long-time partner at Ernst & Young Canada (“EY”), and its Professional Practice Director for many years, as its expert on the accounting and auditing issues. Mr. Cameron contends, in response to Mr. Koch’s opinions, that Mr. Koch’s opinions “do not objectively consider relevant accounting and auditing principles having regard to the underlying facts and circumstances when KPMG was auditing Cash Store’s financial statements in 2011 and 2012.”

[260] More particularly, Mr. Cameron:

- (A) Rejects Mr. Koch’s conclusion that, in substance, Cash Store acted as a borrower from the TPLs and a lender to the payday loan customers such that Cash Store’s balance sheet should have included customer loans receivable of \$52.7 million and loans payable to the TPLs of \$129.6 million as of September 30, 2011. Mr. Cameron asserts, contrary to Mr. Koch’s view, that these assets and liabilities did not meet the GAAP definitions of assets and liabilities of Cash Store. He opines that Mr. Koch’s characterization unduly minimizes, if not completely ignores, the underlying legal agreements between the TPLs and their customers, and between Cash Store and the TPLs, and that under GAAP generally substance and form are equivalent, with only rare exceptions. Mr. Cameron opines, contrary to Mr. Koch, that KPMG in fact complied with GAAS (and GAAP) in carrying out its 2011 and 2012 audits and review engagements;
- (B) Disagrees with Mr. Koch’s conclusion that Cash Store did not comply with the terms of the TPL Agreements such that Cash Store became responsible for all loan losses, and that it omitted certain required disclosures regarding that alleged non-compliance with the TPL Agreements. Mr. Cameron does not identify any material breaches or non-compliance with the TPL Agreements. He also maintains that because the retention payments made by Cash Store were voluntary (again contrary to Mr. Koch’s opinion) there is no basis for a conclusion that Cash Store became responsible for all loan losses;
- (C) Does not accept that KPMG should have detected errors in Cash Store’s accounting for the Loan Internalization Transaction in the unaudited interim financial statements for the second and third quarters of fiscal 2012 and says, in effect, that it was reasonable for KPMG to rely, in that context, on valuation work done at that time, including in particular the valuation estimate undertaken by EY, and that KPMG’s review engagement procedures relative to the interim statements complied with relevant standards; and,
- (D) Opines, relative to alleged deficiencies in related party disclosures, that although additional related party disclosures were made in Cash Store’s 2012 annual and restated interim financial statements, these additional disclosures occurred in a “markedly different context” in which there were “investor concerns” and regulatory pressures, and that in any event, KPMG’s audit and review procedures for related

party transactions during the 2011 audit and the second and third quarter review in 2012, complied with GAAS.

VII. Detailed Analysis of the Claim Against KPMG

(A) Did the Financial Statements Fairly Represent the Nature of Cash Store's Business?

[261] Dealing with the first issue, as to whether or not Cash Store's financial statements, both the audited year-end statements and the interim review statements during the period in question fairly portrayed the nature of Cash Store's business and accurately represented Cash Store's financial circumstances, the essence of Mr. Koch's opinion is that Cash Store was not fairly characterized and understood as a "broker" but was instead, in substance, a direct lender. This conclusion, if upheld, has implications for the evaluation of Cash Store's financial condition during the relevant timeframe.

[262] That is, premised on its characterization of itself as a broker, Cash Store did not reflect in its books and financial statements a loan payable to the TPLs in the amount of \$129.6 million as of September 30, 2011, nor a loan receivable from the payday loan customers ultimately valued in the restated financial statements at \$52.7 million as of that date.

[263] Had Cash Store reflected those "off-Balance Sheet" assets and liabilities on its financial statements – as Mr. Koch opines it ought to have done – the reality that Cash Store was already substantially and irretrievably insolvent, again as Mr. Koch (echoed by Mr. Pappas) alleges, would have been abundantly evident and would (and should) have led immediately to a cessation of Cash Store's business and an orderly winding up at or soon after late 2011. This in turn, it is asserted, would have prevented the insolvency from "deepening" as CS Estate alleges it did, and would have saved stakeholders from substantial additional losses incurred from late 2011 onward.

[264] Mr. Koch's conclusion about the true nature of Cash Store's business relies on a number of factors, and on a fundamental disagreement with Cash Store's self-description of its business, including in the financial statements audited and reviewed by KPMG.

[265] As an initial matter, CS Estate and Mr. Koch point out that by 2011 KPMG had been auditing Cash Store for ten years, and had the benefit of ten years of accumulated knowledge (and cumulative audit evidence) about the nature of Cash Store's business and operations.

[266] Consistent with that observation, CS Estate (based on the opinions provided by Mr. Koch) notes in particular the evidence at trial of Natalie Brykman and Brad Owen, both of whom were longstanding members of KPMG's audit team for Cash Store, confirming the importance, from their perspective, of having a strong understanding of Cash Store's business, its accounting policies, significant transactions, relevant underlying records, and the relationship between Cash Store and other relevant entities. Both Ms. Brykman and Mr. Owen testified that the purpose for developing this comprehensive and deep understanding was to identify and assess the risk of material misstatements in Cash Store's financial statements.

[267] As part of that necessary understanding, CS Estate asserts, KPMG was keenly aware that the payday loans advanced by Cash Store were high risk loans for which extensive bad debt provisions were predictable. In his testimony Mr. Owen, a senior KPMG audit expert who assisted with the Cash Store audits in relevant years, colourfully described Cash Store's business as "one step above loan sharks", and confirmed KPMG's understanding that loan losses in that setting were predictably significant.

[268] In this context, CS Estate and Mr. Koch maintain that it is critical that, to the knowledge of KPMG and as set out above, Cash Store was not operating its business in strict compliance with the TPL Agreements, including:

- (A) KPMG knew that Cash Store was commingling the TPLs' funds with the funds of other TPLs, the funds collected from payday borrowers and Cash Store's own operating funds, and knew that Cash Store used those funds for general corporate purposes;
- (B) KPMG knew that the TPLs were not auditing Cash Store branches, and were not making claims under the indemnity provisions of the TPL Agreements;
- (C) KPMG knew that Cash Store was not meeting all of its obligations under the TPL Agreements and the Loan Selection Criteria, including that it was not collecting all documentation it was required to collect under the TPL Agreements;
- (D) KPMG knew that the TPL Agreements were in some cases out of date;
- (E) KPMG knew that Cash Store was retaining interest that it collected on defaulted loans for its own use, instead of repaying or crediting these amounts to the TPLs; and,
- (F) KPMG knew that Cash Store was transferring loans between TPLs at fair value without specific authorization.

[269] CS Estate alleges that the evidence at trial demonstrated that KPMG did not understand how funds in fact flowed between Cash Store and the TPLs, and did not understand the "nature or scope of the economic benefit the TPLs were receiving from Cash Store, or the relative exposure of Cash Store and the TPLs to losses on defaulted loans".

[270] CS Estate argues that, particularly after having served as Cash Store's auditor for so many years, KPMG had all necessary information at hand from which to understand the true nature, and risks, of Cash Store's business.

[271] First, it points out that KPMG knew about the Retention Payments, and that they were not contemplated nor provided for in the TPL Agreements. KPMG also knew that the Retention Payments were paid (or accrued) "routinely and consistently" and in fact there was never a period during the relevant timeframe where a Retention Payment was withheld.

[272] Relatedly, CS Estate argues that the Retention Payments were intended to and did in fact function to make the TPLs whole, thus ensuring that the TPLs' capital was not at risk, and causing Cash Store to assume the risks of the payday loans itself. CS Estate points to evidence in the record which it says confirms that KPMG was aware, and itself acknowledged in writing, that the Retention Payments were intended to make the TPLs whole.

[273] CS Estate says that KPMG knew that the TPLs were not receiving returns of their principal advances in whole, and that Cash Store was instead "re-investing" the TPLs' funds (i.e. re-advancing those funds for further payday loans) without specific authorization.

[274] KPMG also knew, CS Estate asserts, that TPLs were receiving fixed rates of return (for the most part at 17.5% during that period at issue) and was aware that the payments of 17.5% interest were based on the full amount of advances from a TPL outstanding at the point in time at which this calculation was made and amounts paid.

[275] In this regard, KPMG knew or ought to have known, according to CS Estate, that the Retention Payments were not in fact voluntary, as Cash Store portrayed and KPMG accepted, but that the Retention Payments were mandatory and necessary in order for Cash Store to "retain the TPLs" as lenders, and for "Cash Store to continue its loan-making operations."

[276] CS Estate, based on Mr. Koch's opinions, labels KPMG's approach, allegedly blind to the realities of the relationship between Cash Store and the TPLs, as an unthinking devotion to form over substance, a stance that Mr. Koch/CS Estate say is expressly not permitted under the CICA Handbook.

[277] In response to CS Estate's assertion that in reality Cash Store did not operate as a broker, but was instead in a debtor-creditor relationship with the TPLs and exposed to loan losses, KPMG first argues that Mr. Koch is selective in his purported use of the provisions of the CICA Handbook, and selectively ignores fundamental tenets of GAAP and GAAS, as confirmed in the CICA Handbook, that support KPMG's conduct and undermine Mr. Koch's assertions.

1. Application and Relevance of Various CICA Handbook Provisions

[278] To understand this argument requires specific consideration of the "hierarchy" of relevant provisions within the CICA Handbook, the determination of which principles of GAAP and GAAS are to be applied to the circumstances at hand, and the priority of application of potentially competing principles.

[279] Specifically, as noted, Mr. Koch's opinion in large part rests on the notion that GAAP requires a practitioner to ensure that she or it is considering the substance of a matter or transaction as opposed to merely the form of that matter or transaction.

[280] While this proposition has self-evident appeal, it is important to understand its source and standing within the array of potentially applicable provisions from the CICA Handbook.

[281] As a starting point, as the CICA Handbook makes clear, an auditor is first required to consider primary sources of GAAP, and need only reach for general concepts like “substance over form” where the CICA Handbook does not specify applicable accounting principles (for example in an area in which accounting principles are developing).

[282] This proposition is confirmed in Section 1100.11 of the CICA Handbook, which provides that where primary sources of GAAP exist (which themselves are contained within the CICA Handbook) the primary sources of GAAP prevail over other potentially competing principles.

[283] The “substance over form” concept at the heart of Mr. Koch’s opinion is found in Section 1000 of the CICA Handbook.

[284] Section 1000 of the CICA Handbook discusses “Financial Statement Concepts” and includes the unassailable notion that reporting transactions, events and circumstances in accordance with their substance rather than their legal or other form is necessary to achieve financial statements that are “representationally faithful” and therefore reliable for users of financial statements.

[285] It is clear, and Mr. Koch acknowledges, that Section 1000 is not a primary source for GAAP standards, but he argues that it is the “foundation of all GAAP standards that underlie the development and use of GAAP in financial reporting.” He maintains that the “foundational” concepts of Section 1000 “guide, support and strengthen GAAP standards” and “promote overall transparency in financial reporting.” He goes on to say that the Accounting Standards Board – the body responsible for approving part V of the CICA Handbook – “expects Section 1000 to be used by preparers of financial statements...in exercising their professional judgment for the application of GAAP.”

[286] Mr. Cameron, in his evidence, explained that the intention of the CICA Handbook is that, where primary sources of GAAP exist and are set out in Section 1100, the expectation is that those provisions will govern, and will result in financial statements that fairly and appropriately report the financial circumstances of the reporting entity. I note that in his career Mr. Cameron has spent considerable time in the development and application of the principles codified in the CICA Handbook, and is well-qualified to opine on their intended function.

[287] The introductory language of Sections 1000 and 1100, respectively, confirm Mr. Cameron’s view that, where there are sources of GAAP in Section 1100, those sources prevail, whereas Section 1000 sets out concepts that may inform the development of accounting standards for financial reporting and may fill gaps, but do not establish primary standards for financial reporting.

[288] To that end, part .01 of Section 1000 says that “The purpose of this Section is to describe the concepts underlying the development and use of accounting principles in general purpose financial statements....” The section goes on to say, under the heading “GENERALLY ACCEPTED ACCOUNTING PRINCIPLES,” that “Section 1100 establishes standards for financial reporting in accordance with generally accepted accounting principles. It describes what constitutes Canadian generally accepted accounting principles and their sources.”

[289] Consistent with this notion, Section 1100.02 lists the primary sources of GAAP (which do not include Section 1000) and Section 1100.03 confirms that “An entity should apply every primary source of GAAP that deals with the accounting and reporting in financial statements of transactions or events encountered by the entity.”

[290] Part .02 of Section 1000 goes on to explain that Section 1000 is expected to be used by practitioners “in exercising their professional judgment as to the application of generally accepted accounting principles and in establishing accounting principles in areas in which accounting principles are developing.”

[291] Importantly, and in my view effectively settling the matter, part .03 of Section 1000 says that “This Section does not establish standards for particular measurement of disclosure issues. Nothing in this Section overrides any specific Recommendation in another Section of the Handbook or any other accounting principle considered to be generally accepted...”

[292] Moreover, Section 1100.11, addressing the interplay between Section 1000 and primary sources of GAAP, says that “When the concepts in FINANCIAL STATEMENT CONCEPTS, Section 1000, conflict with a primary source of GAAP, the requirements of the primary source of GAAP prevail.”

[293] I conclude from those excerpts that, as Mr. Cameron testified, where there are applicable provisions within Section 1100, those provisions are expected to be applied, will govern and direct the appropriate accounting treatment for the circumstances at hand, are expected to produce financial reporting that is appropriate and fair in the circumstances, and will not lead to any material misstatement(s).

[294] Section 1000, on the other hand, can be helpful in guiding practitioners in exercising their professional judgment, and may be used to help in establishing appropriate accounting principles in areas in which principles are developing.

[295] There was a debate between the experts as to whether Section 1400, which is listed within Section 1100 as a primary source of GAAP, imports into GAAP standards the “substance over form” notion touted by Mr. Koch from within Section 1000.

[296] That is, Section 1400.03 provides that:

“.03 Financial statements should present fairly in accordance with Canadian generally accepted accounting principles the financial position, results of operations and cash flows of an entity (that is, represent faithfully the substance of transactions and other events in accordance with the elements of financial statement, and the recognition and measurement criteria set out in FINANCIAL STATEMENT CONCEPTS, Section 1000).”

[297] KPMG maintains that the next subsection, Section 1400.04, informs the way in which Section 1400.03 is to be interpreted, and confirms that authoritative sources of GAAP nonetheless prevail, saying:

“04 A fair presentation in accordance with generally accepted accounting principles is achieved by:

“(a) applying GENERALLY ACCEPTED ACCOUNTING PRINCIPLES, Section 1100.”

[298] Based on these excerpts, and on the testimony of Mr. Cameron in particular (but taking into account the role of Section 1000 in informing a practitioner’s exercise of professional judgment) I find that as a general proposition, where applicable standards exist in Section 1100, those are the standards to apply, and the application of those standards is expected to produce financial statements that fairly reflect an entity’s financial circumstances.

[299] I would say that, nonetheless, in the unlikely event that the application of provisions from Section 1100 somehow yields financial statements that clearly promote form over substance, and lead to financial reporting that is misleading to the point of material misstatement, it would be appropriate – and in such circumstances the guidance from the B.C. Court of Appeal’s decision in *Kripps* would be apt – to draw upon the conceptual framework set out in Section 1000, and to ensure that form does not overwhelm substance to the point of creating unreliable financial reporting. In that circumstance, as in *Kripps*, a practitioner’s blind adherence to form might constitute a failure to meet the required standard of care.

2. CICA Handbook Definitions of Assets and Liabilities and Application to Cash Store Business

[300] Among the primary sources of GAAP enumerated within Section 1100, Section 3855 of the CICA Handbook establishes the standards for recognizing and measuring, among other things, financial assets and financial liabilities. Section 3855.19 sets out definitions, including:

- “19 (a) A financial instrument is any contract that gives rise to a financial asset of one party and a financial liability....of another party.
- (b) A financial asset is any asset that is:
 - (ii) a contractual right to receive cash or another financial asset from another party
- (c) A financial liability is any liability that is a contractual obligation,
 - (i) to deliver cash or another financial asset to another party.”

[301] Mr. Cameron’s evidence, which I accept, is that the customer loans repayable to the TPLs under the Promissory Notes and the amounts receivable by the TPLs from the payday loan customers were “financial instruments”, “financial assets” and “financial liabilities” of the TPLs, as defined in Section 3855.19 of the CICA Handbook. He testified that, contrary to CS Estate’s position, payday customer loans did not meet the GAAP definition of, and thus could not be

reflected as, assets of Cash Store. Similarly, the advances from the TPLs could not be reflected as Cash Store's liabilities.

[302] In this regard, KPMG points out that Mr. Koch did not in his reports refer to or consider the Loan Applications and Promissory Notes, which Mr. Cameron opines are critical to the proper application of GAAP. Likewise, Mr. Camerson notes that Mr. Koch has not confronted the relevant definitions, from Section 3855, of financial instruments, financial assets and financial liabilities, and has not considered the application of these primary GAAP sources in determining the proper accounting for the consumer loans and advances made by the TPLs.

[303] KPMG argues that it is helpful, in this context, to recall that in describing its brokerage business, in note 1(e) of its 2011 annual financial statements (and consistently elsewhere) Cash Store specifically confirms that as a broker it was using funds advanced by the TPLs to payday loan customers, with the resulting loans being repayable to the TPLs. The payday customer loans, as assets of the TPLs, were properly excluded from Cash Store's balance sheet, an approach which was disclosed by Cash Store as follows:

“When the Company acts as a broker on behalf of income earning customers seeking short-term advances, the funding of short-term advances is provided by independent third-party lenders. The advances provided by the third-party lenders are repayable by the customers to the third-party lenders and represent assets of the lenders: accordingly, they are not included in the Company's balance sheet.”

[304] This representation and treatment of the obligations arising from the loans is consistent with the terms of the Promissory Notes, pursuant to which the TPLs had the contractual right to receive payments of the loans. Conversely (under the Promissory Notes), the payday loan customers, and not Cash Store, had the contractual obligation – the financial liability – to re-pay the TPLs.

[305] As such, and for purposes of Mr. Koch's “substance over form” argument, there can be no doubt that the form of the underlying transactions – expressly confirmed in the relevant documentation involved in every loan – supports the characterization of Cash Store as broker (rather than lender).

[306] In my view, there is persuasive evidence to show that this “form” also reflects the substance of these transactions.

3. Cash Store Did Not Control TPL Assets

[307] Of particular importance in this analysis, I find that there is no basis to conclude that Cash Store had the ability to convert to its own use or control payday customer loans, as would be the case if these loans were financial assets (as defined) of Cash Store.

[308] More particularly, Cash Store could not control access to the benefits of the payday customer loans, such as, by way of instructive and compelling example, having the ability to pledge the loans as security.

[309] In response to Cash Store's evident inability to pledge these loans, which I regard as central and critical to the analysis, Mr. Koch's response was to say that "legal enforceability" is not a prerequisite for a benefit to qualify as an asset "if the entity has the ability to obtain and control the benefit in other ways."

[310] I find that in his evidence, Mr. Koch did not squarely address Cash Store's evident inability to exercise ownership-like control over the loans. CS Estate's closing submissions addressed the issue by suggesting that Cash Store, as custodian of the funds, was able to assert control over collections (for example).

[311] In my view, as argued by KPMG, Cash Store only "controlled" the relevant loans/funds as a broker, and did not and could not control access to the benefits of the payday customer loans, including in particular the ability to pledge those loans as security. Cash Store could not do so because the loans were not, during the relevant timeframe, assets of Cash Store (as defined in the CICA Handbook). Cash Store did not own the loans.

[312] Mr. Cameron, in his report and his testimony, summarized his views on Mr. Koch's "substance over form" opinion as follows:

"I do not consider Delta's approach to "substance over form" to be consistent with the requirements of GAAP, either in theory or practice. I say that because the CICA Handbook contains specific accounting principles that applied to customer loans brokered through Cash Store as well as the advances from TPLs that funded those loans. The application of the specific accounting principles applied by Cash Store appropriately reflected the substance of Cash Store's transactions and balances. For the reasons set out below, I do not agree with Delta's subjective view that Cash Store should have recorded customer loans receivable as its own assets or that its financial statements did not accurately portray the substance of its relationship with the TPLs."

[313] In my view, consistent with the notion that alleged negligence is to be assessed as at the time of the events at issue and not retrospectively, it would have been surprising, and would have prompted immediate opposition from the TPLs, if Cash Store had asserted, for example in the fall of 2011, that it owned the payday customer loans, and had purported to carry those loans as assets on its balance sheet or purported to pledge them as security in another context. The TPLs could and surely would have successfully contested any such characterization; the relevant documentation clearly established that the loans were assets of the TPLs, and as set out above I find that this legal form also reflected the substance of the loan transactions funded by the TPLs and confirmed in the relevant agreements.

[314] I find that, with respect to CS Estates fundamental premise that Cash Store was not operating as a broker but instead assuming the risk of the customer loans, Cash Store's lack of ownership control of the assets means that the premise is not made out, at least up to the time of the LIT, and that the claim as against KPMG and Cassels based on the notion that they knew or ought to have known that Cash Store was misrepresenting the true nature of its business in its public disclosure cannot succeed.

[315] This is not to say that the risks faced by Cash Store did not increase once it undertook the LIT and associated Note Offering. It is also not to say that Cash Store's initial valuation of the Loan Portfolio did not prove to be considerably overstated.

[316] But in my view, up to that point, the suggestion that KMG and/or Cassels ought to have recognized that Cash Store was misrepresenting the true nature and risks of its business is not established on the balance of probabilities and falls short of the mark.

4. Cash Store Remained a Broker During the Relevant Timeframe in 2011-2012

[317] I am also not persuaded by Mr. Koch's related observations and opinions concerning features of Cash Store's operations and practices which he says transform Cash Store's business from broker to lender.

[318] These arguments, KPMG's responses, and my findings on these assertions are set out summarily in the following paragraphs.

[319] First, Mr. Koch urges that a key issue is that Cash Store paid interest to the TPLs on a monthly basis, which Mr. Koch says would be expected with a line of credit (and a debtor-creditor relationship).

[320] There is no question, and it was evident and disclosed in Cash Store's financial reporting, that it provided monthly reconciliations to the TPLs, and made monthly payments to the TPLs calculated at a fixed rate (which, as noted, changed over time, decreasing in steps from 25% to 17.5%, where it stood at the time of relevant events).

[321] As confirmed by various Cash Store witnesses, Cash Store's business practice was to make regular payments to the TPLs and to accrue Retention Payments in order to defray TPL loan losses and to reduce its overall liabilities to the TPLs. These practices were undertaken, as again the evidence clearly and consistently attested, to ensure that the TPLs would continue to lend.

[322] As Mr. Cameron opined, these monthly distributions and accruals were not an "interest expense" under GAAP because the amounts on which they were based were not a corresponding liability, nor a debt, owing to the TPLs by Cash Store. The payday loan customers, not Cash Store, had the obligation to re-pay the advances by the TPLs.

[323] As discussed in detail above, Cash Store, in the ordinary course of its business, collected principal and interest (at 59%) from the payday loan customers and credited each TPL with the applicable collections. Cash Store then made monthly distributions (equivalent, at the relevant time, to a rate of return of 17.5% of total funds advanced by a given TPL) together with such additional amounts, included in accrued Retention Payments, as Cash Store considered appropriate (and its board approved). While it is true that Cash Store did not remit to the TPLs the entirety of the amounts collected from payday loan customers, this is in large measure because, to the knowledge of and with the concurrence of the TPLs, Cash Store redeployed part of the collected funds as further loans from the TPLs to payday loan customers.

[324] From an accounting perspective, Cash Store fully recognized and credited the TPLs for all principal and interest collected and it provided each TPL with a full accounting by way of monthly reconciliations.

5. Cash Store's Public Disclosure of Arrangements with TPLs

[325] The fact that these practices were known to the TPLs, indeed accepted and encouraged by the TPLs, and transparently disclosed in Cash Store's ongoing financial disclosure, is in my view significant. From KPMG's perspective, as auditor, the fact of this ongoing fair and accurate disclosure is all-important. There is no suggestion, other than CS Estate's assertion of the fundamental misrepresentation of the true nature of Cash Store's business, which assertion I have rejected, that Cash Store withheld these various business practices from the public. To the contrary, I find that Cash Store made fulsome and fair disclosure of these details.

[326] To that end, a consistent note to Cash Store's financial statements entitled "Accounts Payable and Accrued Liabilities" advised:

"The amounts due to third-party lenders reflects funds made available by lenders but not yet advanced to customers, and liability under the lending agreement, including any [un]paid retention payments, as well as loan repayment and interest amounts collected from customer. Amounts due to third-party lenders are non-interest bearing, unsecured, and have no specific repayment terms."

6. Concerns re Evidence of Mr. Koch

[327] With respect to other aspects of Mr. Koch's opinions, KPMG asserts, and there is evidence consistent with the notion, that Mr. Koch has been selective and thereby unfairly narrow in premising his criticisms.

[328] For example, Mr. Koch expresses the opinion that:

"...in our opinion the Retention Payments were a necessity to continue Cash Store's operations as a going concern. In other words, the repercussions of discontinuing the Retention Payments would have been catastrophic to Cash Store's business, and as such, the Retention Payments should have been viewed, in our opinion, as being mandatory."

[329] KPMG contends that this represents impermissible purported fact-finding on the part of Mr. Koch. The opinion at issue does not, KPMG points out, reference or rely upon any accounting or auditing principles. While Mr. Koch's opinion that Retention Payments were mandatory, if supported by relevant GAAP principles, may be admissible, his further conclusion that discontinuing Retention Payments "would have been catastrophic to Cash Store's business" is speculative and represents purported fact-finding beyond the realm of Mr. Koch's expertise and role.

[330] This and other selective propositions advanced by Mr. Koch give me concern, as foreshadowed in the reservations I expressed in qualifying Mr. Koch to testify, that his relative lack of experience applying concepts from Canadian GAAP and GAAS and the CICA Handbook, and his very dated experience applying even U.S. GAAP, have caused him to overlook overarching principles, and to seek out propositions out of context or beyond the scope of Mr. Koch's mandate and opinions, that selectively support the plaintiff's positions.

[331] To similar effect, I find that various aspects of the evidence cited by Mr. Koch as further alleged instances of misrepresentations by Cash Store and failures by KPMG to prevent such alleged misrepresentations, do not carry the implications and weight suggested by Mr. Koch.

[332] For example, there was considerable evidence about the uncontested fact that, contrary to the letter of the TPL Agreements, Cash Store failed to physically segregate the funds from TPLs on a loan-by-loan or TPL-by-TPL basis, instead "segregating" the respective TPLs' funds by way of accounting entries. It was suggested by Mr. Koch and CS Estate that this represented a flagrant and ongoing breach of the TPL Agreements, and ought to have prompted TPLs to assert such breach and take steps to trigger the indemnity provisions under section 7 of the TPL Agreements.

[333] However, as noted above, Cash Store did in fact record the funds made available by each TPL in dedicated ledger accounts (TPL-by-TPL). The amounts involved and account activity, including the monthly net balances, were provided to each TPL by way of monthly reconciliations. As part of the annual audit process, each TPL also confirmed its knowledge and acceptance of Cash Store's accounting for TPL funds by way of confirmation letters collected by KPMG. (I should note that Mr. Stein, in his evidence, said that he did not carefully consider, while operating as the principal of a TPL (FSC Abel), the details of the confirmations sought in confirmation letters he received from KPMG, but merely responded affirmatively. This evidence was a little puzzling, inasmuch as the contents of the confirmation letters were clear, and Mr. Stein clearly had the wherewithal to understand them. In my view, because the confirmation letters were clear and straightforward, Mr. Stein's puzzling lack of attention to them does not undermine the legitimacy of the confirmations they contained).

[334] Similarly, in connection with Cash Store's retention of interest on defaulted payday loans, a matter highlighted by Mr. Koch as creating concern, the evidence confirms that KPMG again identified this issue and sent confirmations to the TPLs, each of which acknowledged their understanding and agreement that Cash Store could retain such interest.

[335] Of greater significance, with respect to the Retention Payments, characterized by Mr. Koch as reflecting a guarantee from Cash Store that the TPLs would be made whole, the evidence from the Cash Store employees and executives was uniformly, without exception, that the Retention Payments (both the monthly payments and the parallel accruals) were discretionary and not guaranteed. In keeping with this notion, as Mr. Cameron testified, the Retention Payments did not alter the rights or obligations of the parties. That is, the TPLs continued to retain the contractual right to collect the principal and interest from the payday loan customers, and the customers were contractually obligated to pay these amounts to the TPLs. As Mr. Cameron put it:

“Voluntary retention payments did not cause the customer loans and borrowings to become financial assets and financial liabilities, respectively, of Cash Store. Written agreements and confirmations from Cash Store and the TPLs clearly established both the form and substance of Cash Store’s business as a broker. KPMG’s audit procedures were appropriate and complied with GAAS.”

[336] Moreover, Cash Store’s practices with respect to the Retention Payments were also the subject of ongoing extensive disclosure in Cash Store’s financial statements. For example, note 1(e) to the 2011 and 2012 consolidated financial statements disclosed Cash Store’s policy regarding Retention Payments as follows:

“Cash Store’s Board of Directors regularly approves a resolution which authorizes management to pay a maximum amount of retention payments per quarter to third party lenders as consideration to those lenders that continue to be willing to fund advances to Cash Store’s customers. 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 third party lenders. Retention payments are recorded in the period in which a commitment is made to a lender pursuant to the resolution approved by the Board of Directors.”

[337] Once again, on this issue, the TPLs provided signed confirmations within the context of KPMG’s annual audits attesting to the fact that the Retention Payments were voluntary and not guaranteed.

[338] There was considerable evidence indicating that the voluntariness and appropriate accounting treatment of the Retention Payments was considered and discussed, within the KPMG team and between KPMG and Cash Store on a regular basis. However, in terms of evaluating the role and responsibility of KPMG, the fact that the TPLs confirmed on an annual basis that the Retention Payments were not guaranteed, and the fact that, it appears to a person, the Cash Store personnel all understood and confirmed this proposition, meant, in my view, that KPMG had ample evidence to justify Cash Store’s accounting treatment of the Retention Payments, and ample evidence that Cash Store was regularly and comprehensively disclosing to the public its practices in that regard and the rationale for those practices.

[339] I find, therefore, that these criticisms levied by Mr. Koch are at odds with the preponderance of the evidence.

[340] I also found Mr. Koch, while clearly an adept and articulate witness, to be inflexible and recalcitrant in his insistence on propositions that supported his opinions, and unwilling to consider and apply propositions at odds with his conclusions.

7. I Accept and Prefer the Evidence of Mr. Cameron

[341] Mr. Cameron, in contrast, was fair to acknowledge evidence and points of view potentially attenuating his conclusions, and to consider thoughtfully the impact of those propositions on his opinions.

[342] For these reasons, and also based on Mr. Cameron's much more extensive and contemporaneous experience considering and applying GAAP, GAAS (including US GAAP and GAAS) and the CICA Handbook, where the evidence of Mr. Koch and Mr. Cameron conflict, I generally prefer and accept the evidence of Mr. Cameron.

(B) Discussion/Analysis of Standard of Care for KPMG

[343] This aspect of the claim against KPMG is framed in negligence.

[344] As such, I should relate my findings thus far to the question of standard of care in the negligence analysis.

[345] In moving forward to the issue of standard of care, I should note that I am assuming that there is a duty here owed by KPMG and Cassels, to their former client Cash Store.

[346] It might be suggested that the question of the duty owed is somewhat clouded by the fact that the party to which the duty was owed, Cash Store, no longer exists as a going concern, that its former employees and officers appear uniformly to be of the view that KPMG appropriately discharged its obligations to Cash Store, and that the current party asserting allegations to the contrary is an entity that did not exist at the time of the relevant underlying events. Another set of entities that might assert a duty owing to them by KPMG, the TPLs, most recently argued, in the motion before Morawetz R.S.J., in favour of the conception of Cash Store and its business that the defendants urge as apt in the current proceedings, that Cash Store was a broker, and that the TPLs had a priority interest, as creditors, in the assets remaining in the estate.

[347] In any event, in the absence of argument on the question of the duty owed, and having regard to my other conclusions, I am prepared to assume for purposes of the balance of the analysis that both KPMG and Cassels owed a duty of care to the plaintiff.

[348] My analysis of the claim against Cassels is set out below, and so I focus here on the negligence claim against KPMG.

[349] Based on my findings about the primary sources of GAAP and GAAS that apply to and largely establish the standard of care that KPMG must meet, based as well on my findings about the relevant aspects of the evidence, and based on my findings about the credibility and reliability of the respective accounting liability experts, I find that the evidence before me falls short of establishing a breach of the standard of care by KPMG.

[350] To the contrary, in my view the evidence demonstrates that KPMG was diligent and appropriately thoughtful in its capacity as auditor of Cash Store, both in connection with the annual audits and with respect to the interim statements assessed on the basis of review engagements.

[351] KPMG, in my view, appropriately investigated and considered the evidence informing and impacting upon its audit (and review) opinions, exhibited appropriate professional skepticism with respect to all such matters, and exercised its judgment in that regard in an appropriately honest and intelligent fashion.

[352] I therefore find no breach of the requisite standard of care in KPMG's performance of the 2011 and 2012 audits, or in its performance of the interim review engagements.

[353] Beyond that finding, there are at least four additional areas for my consideration before reaching an overall conclusion on negligence relative to KPMG. My analysis of the claim against Cassels then follows my discussion of those four additional areas (some of which also factors into the claim against Cassels).

[354] As to the four additional areas for discussion, first, I believe I should first consider the impact on my conclusions of the LIT, and of the subsequent revisiting of Cash Store's financial circumstances, both in terms of the write-down of the value of the Loan Portfolio acquired, and by way of the subsequent restatements of certain of the relevant financial statements for which KPMG had given a "clean" opinion.

[355] Second, it remains to consider the "related party" issue.

[356] Third, of course in order to complete the negligence analysis, I must consider the question of causation – an element of the tort.

[357] Fourth, in the unique circumstances of this case, I should specifically consider the impact on my analysis of the 2014 decision rendered by Morawetz R.S.J. (as he then was), in which His Honour found, in the context of a dispute between the TPLs and the DIP Lenders within the CCAA proceedings, that in fact Cash Store's representation of its operation was at odds with the reality of those operations.

1. Impact of the LIT

[358] With respect to the LIT, the evidence shows that at a point in early 2011, Cash Store began to consider a transaction that ultimately became the LIT and Note Offering. The notion motivating this potential transaction was that Cash Store believed it could borrow money at a lower rate than the amounts it was paying and accruing on the funds from the LITs based on its collection of payments from payday loan customers.

[359] Cash Store established a working group to consider and assist with the proposed transaction, including representatives from Cash Store; Cassels; KPMG; as well as Cash Store's U.S. counsel Paul, Weiss; Imperial Capital; Canaccord; and Jones Day (U.S. Underwriter's counsel).

[360] Ultimately members of this group (primarily Mr. Reykdal and Ms. Bland) produced a memorandum on the proposed transaction that was delivered to Cash Store's board of directors in the late spring of 2011 entitled Cash Store "transition to On-Balance-Sheet Lending." Two versions of the memorandum were introduced at trial. The version of the transaction that Cash Store's board ultimately opted to pursue was the so-called "Face Value" option, in which Cash Store would pay the "face value" of the Loan Portfolio, being the full amount of funds that the TPLs had made available and advanced to Cash Store to fund the payday customer loans.

[361] The evidence at trial confirmed that, in this context, KPMG specifically advised Cash Store that it would be prudent for Cash Store to engage KPMG to take a closer look – by way of performing audit procedures – as to the value of the Loan Portfolio.

(i) Reliance on Valuation Work by EY

[362] Cash Store ultimately chose not to do so, and instead engaged EY to undertake a form of valuation of the assets potentially to be acquired, and engaged Canaccord to prepare a fairness opinion relative to the proposed transaction.

[363] The report prepared by EY relative to the valuation exercise it performed, issued as a series of drafts throughout late 2011 and 2012, and ultimately delivered in final form in November of 2012, is notable in a couple of respects.

[364] First, while the report was never in the form of a full-blown or definitive valuation report, it supported Cash Store's determination to value the Loan Portfolio – the most significant and valuable assets being acquired via the LIT – at \$80 million. This valuation, without implying criticism of EY given the limitations of EY's investigation and report, proved to reflect a substantial overstatement of the value of the Loan Portfolio.

[365] There was no claim brought against EY, presumably indicating that given the limits of EY's mandate, there was no suggestion of any shortcomings in EY's performance of the valuation mandate that it undertook.

[366] Second, in Mr. Koch's evidence at trial, he testified that in his opinion, it was incumbent on KPMG to perform an audit (or audit-like procedures) to satisfy itself as to the value of the Loan Portfolio being acquired, notwithstanding that KPMG was specifically not engaged to do so, and notwithstanding that EY was specifically engaged to perform the relevant valuation.

[367] In my view, this suggestion by Mr. Koch was not a reasonable or realistic one, and is again a product of hindsight, knowing that the \$80 million valuation proved to be excessive. Mr. Koch did not reference any existing standards in support of this proposition.

[368] In fact, while it had no obligation in my view to do so, KPMG had specifically recommended to Cash Store that Cash Store engage KPMG to perform audit procedures to test the value of the Loan Portfolio. To expect KPMG to proceed unilaterally to do so, notwithstanding having asked to perform the mandate and that request having been specifically declined by Cash Store, is well beyond any reasonable or realistic expectation for a professional firm. That is particularly so given that KPMG was aware that EY, a firm in the same category of "Big 4" accounting firms as KPMG, had been specifically engaged to undertake a form of valuation of that Loan Portfolio.

[369] As events transpired, based on concerns expressed by Mr. Warnock, and supported by KPMG, a decision was made at around the time of the Q3 2012 interim financial statements to adjust the value of the Loan Portfolio, in Cash Store's balance sheet, downwards by \$10 million (to \$70 million).

[370] Subsequently, again based on Mr. Warnock's continued concerns and investigations, the value of the Loan Portfolio was reduced to \$50 million. Mr. Warnock learned, in his investigations, that the projected collection rates (of the payday customer loans) used in the initial valuation of the Loan Portfolio had been considerably higher than the historical collection rates actually experienced relative to these loans.

[371] On that basis, and frankly through Mr. Warnock's dogged insistence, in late 2012 Cash Store made the further adjustment to value the Loan Portfolio in Cash Store's balance sheet at approximately \$50 million, and issued restated interim Q2 and Q3 2012 financial statements. In May of 2013, Cash Store went on to restate its 2011 and consolidated 2012 annual financial statements.

[372] In each of the Q2 and Q3 Restated Financial Statements, the error in relation to the Loan Portfolio is described as follows:

- "i. The computation of collection rates used as a basis to estimate expected future cash flows of the acquired loans contained errors. the correction of these errors resulted in an acquisition date fair value of the portfolio of loans acquired of \$50,014[,000] as compared to \$80,333[,000] (Q3: 70,334[,000]) as originally reported.
- ii. The previously disclosed fair value of intangible assets acquired of \$39,081[,000] has been amended to \$32,024[,000] as a result of a re-allocation of consideration in excess of the fair value of intangible assets to the premium paid to acquire the portfolio of loans.
- iii. The Company has recognized \$36,820[,000] of the total consideration paid as a premium paid to acquire the portfolio of loans. In accordance with GAAP the Company determined that this portion of the transaction settled pre-existing relationships between the Company and third-party lenders. Accordingly the premium paid to acquire the portfolio of loans was measured at its fair value and recorded as an expense in the consolidated statement of operations as part of the acquisition transaction."

[373] Subparagraphs ii. and iii. above require some additional explanation.

[374] The overall consideration paid by Cash Store in the Loan Portfolio transaction was \$116,344,000. When it was initially determined, as supported by the EY valuation exercise, that the value of the Loan Portfolio itself was about \$80 million, the additional consideration paid – being the delta between \$116 million and \$80 million (\$36 million) – was allocated, in Cash Store's financial statements, to certain specified intangible assets (a non-compete agreement, favourable supplier relationships and proprietary knowledge). It is, and was perhaps at the time evident that these intangible assets likely did not possess the value attributed to them, but Cash Store's initial decision was nonetheless to spread the "excess" consideration among those intangible assets.

[375] When the stated value of the Loan Portfolio was ultimately reduced to \$50 million, a decision was taken to re-allocate a portion of the amounts initially attributed to the intangible assets, and to attribute a large portion of the delta between the overall consideration paid and the (reduced) stated value of the Loan Portfolio, which delta had considerably increased as a result of the restated reduced value of the Loan Portfolio, to a one-time expense characterized as a “premium to acquire the portfolio of assets”, valued at just shy of \$37 million. The evidence showed that KPMG was consulted at that point in respect of the potential reallocation of the overall purchase price, engaged senior KPMG experts in considering the right accounting approach, and ultimately felt the one-time premium to purchase the Loan Portfolio was the appropriate means of accounting for the transaction.

[376] As is evident, the acquisition of the Loan Portfolio, at the price Cash Store paid, was very problematic from a financial point of view. The reductions in the value of the Loan Portfolio, in addition to dramatically devaluing the Cash Store business, also created an immediate and dramatic reduction in the value of the Notes issued to raise funds in conjunction with and for the purposes of the LIT.

[377] It is undoubtedly the case that the necessary and precipitous drop in the stated value of the Loan Portfolio that it had just acquired was devastating for Cash Store.

[378] However, in my view, as discussed in more detail in the sections below analyzing causation and the damages claim, the devaluation of the Loan Portfolio was only one of a number of factors ultimately leading to Cash Store’s insolvency and its resort to the CCAA Proceedings.

[379] Equally crippling to Cash Store’s operations were the regulatory changes, announced and enforced more or less in concert in various provinces across the country commencing in 2009 and continuing throughout the relevant timeframe. These changes in the regulatory environment in which Cash Store operated are discussed above, and in more detail below in the analysis of the claim against Cassels. In brief, these actions by regulators effectively led to Cash Store having to discontinue its Ontario operations altogether, and to Cash Store facing restrictions and similarly existential threats in other Canadian jurisdictions.

[380] I am hard-pressed to attribute fault, as the plaintiff urges, for Cash Store’s pronounced and increasing difficulties, from a point in 2012 through its application for CCAA protection in April of 2014, to KPMG or Cassels. The discussion regarding the claim against Cassels is set out below. In the case of KPMG, there is in my view nothing to suggest that KPMG’s conduct, in any of its work for Cash Store, fell below the standard of care required. Moreover, as discussed more fully in addressing causation, below, there is in my view no link between KPMG’s audits and reviews of Cash Store’s annual and interim financial statements and Cash Store’s ultimate demise.

[381] In my view, the two largest factors, by far, implicated in Cash Store’s insolvency, were the LIT – and in particular the over-valuation of the Loan Portfolio in that setting – and the increasing regulatory antagonism faced by Cash Store, leading to a piecemeal dismantling over time of various critical features of Cash Store’s operations.

[382] I find no credible evidence to suggest that, but for those two factors, Cash Store would have had to cease operations. It was not KPMG's mandate (nor that of Cassels) to make or advise business decisions for Cash Store. Cash Store had a sophisticated and experienced management team to make strategic and other business decisions. As I have already found, in the domain in which its expertise was required and expected, in the audit and review of Cash Store's financial statements, KPMG met the standard required of it.

(ii) Effect of Restatements

[383] CS Estate also argues that, inasmuch as the restatements of Cash Store's financial statements are, or necessarily entail, acknowledgements of mistakes, the fact of the restatements themselves is evidence that KPMG fell below the standard required in its work.

[384] Again, I disagree.

[385] The primary impetus for the restatements was the devaluation of the Loan Portfolio, from about \$80 million to about \$70 million and finally to about \$50 million.

[386] The genesis and the need for those reduced values are as discussed above.

[387] I find no basis to implicate KPMG in the necessary reduction in the carrying value of the Loan Portfolio. Despite advising Cash Store of the need to perform a valuation of that Loan Portfolio during the course of its participation in the working group struck to consider an acquisition of the Loan Portfolio, KPMG was not engaged to undertake that work.

[388] As set out above, I find no reasonable basis from which to conclude that KPMG had an onus in the circumstances to proceed unilaterally and without a formal engagement to nonetheless perform the valuation work, and find that it was entirely reasonable for KPMG to defer to the work done by EY in that context.

[389] Accordingly, while KPMG as auditor agreed, once the over-valuation of the Loan Portfolio became apparent, that a restatement of the financial statements, both interim and annual, to correct the initial over-valuation of the Loan Portfolio was appropriate, the "mistake" that was being corrected was not of KPMG's making, and not something of which KPMG could reasonably be expected to be aware prior to the discovery, prompted by both internal and external forces, that the Loan Portfolio had been substantially overvalued for purposes of the LIT.

2. The Related Parties Issue

[390] There was also a restatement of the financial statements relative to the question of related party transactions, to which I now turn.

[391] At the outset I observe that CS Estate's allegations about related parties potentially sound in both negligence (as against KPMG) and as a claim for a breach of fiduciary duty as against Cassels in relation to the particular role of Mr. Stein.

[392] The claim in respect of related party transactions begins with the uncontested fact that in Cash Store's public disclosures, it repeatedly referred to the TPLs as "independent TPLs."

[393] CS Estate alleges that this characterization of "independence" was inaccurate and misleading.

[394] First, CS Estate notes, and the evidence confirms, that Mr. Reykdal had close relationships with principals of many of the TPLs. He acknowledged in his evidence that he had a number of friends at the TPLs.

[395] Second, CS Estate alleges that Assistive Financial, Cash Store's largest TPL, was far from independent. Assistive Financial was controlled by Randy Shiffner, who began working with Mr. Reykdal in 1984. Randy Shiffner's son, Cameron Shiffner, held various roles at Cash Store, and also, as of 2004, was married to Mr. Reykdal's daughter. Randy Shiffner's other son, Slade Shiffner, was also employed by Cash Store, in Australia.

[396] Third, 367 Alberta, Cash Store's second largest TPL as of 2011, had as investors, Bruce Hull – a director of Cash Store Australia – and Linda Shaw, whose husband was a director of Cash Store from 2009 to 2013.

[397] Finally on this topic, as noted above, Mr. Stein, who was the Cassels relationship partner for the Cash Store relationship, was a long-time friend of Mr. Reykdal, and at Mr. Reykdal's suggestion and with Mr. Reykdal's encouragement, established FSC Abel, of which he was the principal, as a TPL.

[398] It is alleged, as against KPMG, that it knew or ought to have known of these various relationships, that KPMG's confirmation letters to inquire about any such relationships were inadequate to unearth relevant information, and that the relationships in each case ought to have been disclosed in Cash Store's public documents, particularly given that the TPLs were having their loan positions paid out in full with the proceeds of the Note Offering and as part of the LIT.

[399] KPMG's answer to these allegations is, first, that the relationships at issue were only uncovered following an in-depth internal investigation that went well beyond typical and required audit procedures, and that, second, there is no evidence in any event to suggest either that Cash Store (qua plaintiff) or any user of the financial statements at issue was misled by, or even relied upon the representations omitting the related parties.

[400] In my view, while of course an important issue generally, the related party allegations here, leaving aside for the moment the breach of fiduciary duty claim relating to the role of Mr. Stein, are something of a tempest in a teapot.

[401] The confirmations sent out by KPMG to inquire about relationships of concern, accompanied as they were by relevant excerpts from the CICA Handbook describing relationships that would be of concern and ought to have been disclosed, were sufficient to, and ought to have, elicited disclosure from the TPLs about the relevant connections.

[402] On the other hand, CS Estate argues, KPMG was generally aware of some of these relationships as a result of its long tenure as auditor, and arguably should have been alert to, and investigated more deeply, the potential relationships of concern.

[403] However, there was no evidence led before me, whatsoever, to suggest that either Cash Store or any of its investors suffered any damages as a result of the relationships at issue, nor that the interests of any such alleged related parties were given more favourable treatment, as compared to other TPLs, as a result of these relationships.

[404] Accordingly, even if I were persuaded that KPMG's investigation or consideration of the related party issue fell short of the standard of care required, which on balance I am not, these allegations would in any even founder on the basis of causation.

[405] Ultimately, the same holds true with respect to the claim relative to Mr. Stein's dual role.

[406] As noted above, in my view as a general proposition lawyers should avoid taking on roles within their clients' businesses or, as here, within businesses that transact with their clients.

[407] That said, there is no doubt that Cash Store, based on at least the knowledge of its CEO Mr. Reykdal, was aware of Mr. Stein's role at FSC Abel (in addition to his role with Cash Store's main external counsel, Cassels).

[408] More importantly, there is no information that Mr. Stein's interests were somehow preferred in his capacity at FSC Abel (and indeed the evidence shows that Mr. Stein/FSC Able suffered substantial losses as a result of their dealings with Cash Store), and no evidence that anyone, including Cash Store or anyone else, suffered any damages as a result of Mr. Stein's dual role. As is the case with respect to the tort of negligence, a claim for a breach of fiduciary duty must likewise prove causation (see for example the Supreme Court of Canada's decision in *Southwind v. Canada*, 2021 SCC 28, [2021] 2 S.C.R. 450, and the Court of Appeal for Ontario's decision in *Stirrett v. Cheema*, 2020 ONCA 288, 150 O.R. (3d) 561, leave to appeal refused, 39268 (November 26, 2020)).

[409] Accordingly, these claims fail on the basis of a lack of proof of causation, both with respect to the negligence claim and the claim for a breach of fiduciary duty.

3. Analysis of Causation

[410] In my view the other aspects of the plaintiff's claims – the negligence claims as against both KPMG and Cassels – also fail on the basis of causation.

[411] As discussed above, I find that the two main factors in Cash Store's path to insolvency were: (a) The substantial over-valuation of the Loan Portfolio in the context of the LIT; and (b) The increasing regulatory pressure on Cash Store, during the 2009-2013 period, to discontinue or remake various core aspects of its business, leading to court and regulatory decisions in Ontario requiring the complete cessation of Cash Store's Ontario operations, and regulatory pressures in other jurisdictions driving in similar directions.

[412] I have concluded that CS Estate has failed to prove a breach of the standard of care by KPMG (and reach the same conclusion relative to the claim against Cassels, below). Even if I had found a breach of the standard of care by either defendant, however, the evidence does not allow me to conclude that but for certain actions or omissions by one or the other or both defendants, Cash Store would have either avoided insolvency or, as CS Estate alleges, would have recognized its insolvency in late 2011 or early 2012 and entered into an orderly winding up of its affairs, thereby avoiding the deepened insolvency culminating in the CCAA proceedings in 2014.

[413] The Supreme Court of Canada has repeatedly held that the test for factual causation in tort is the “but for” test. A leading articulation of the principle is found in *Clements v. Clements*, 2012 SCC 32, [2012] 2 S.C.R. 181, in which the court explained:

“The test for showing causation is the ‘but for’ test. The plaintiff must show on a balance of probabilities that “but for” the defendant’s negligent act, the injury would not have occurred. Inherent in the phrase ‘but for’ is the requirement that the defendant’s negligence was necessary to bring about the injury – in other words that the injury would not have occurred without the defendant’s negligence. This is a factual inquiry. If the plaintiff does not establish this on a balance of probabilities, having regard to all the evidence, her action against the defendants fails” (para 8).

[414] Again in my view, the but-for causes of Cash Store’s demise, neither of which can fairly be attributed to any breach by either defendant, are the ill-fated LIT, and the increasing and ultimately crushing regulatory pressures brought to bear on Cash Store’s business. I do not find that these causes had crystallized, to the point that Cash Store ought to have acknowledged its insolvency and wound up its business by early 2012.

[415] The plaintiff characterizes its causation theory as requiring only a “simple application” of the but-for test.

[416] It argues that, had KPMG and Cassels, respectively, discharged their duties, the Cash Store board of directors, and then Cash Store’s shareholders and the investing public would have understood as materially misleading:

- “(a) the description of Cash Store as a ‘broker’ of payday loans;
- (b) the resulting failure to present Cash Store’s balance sheet in accordance with the debtor-creditor relationship of Cash Store and the TPLs, which would have required the funds advanced by the TPLs to Cash Store to be recorded as a liability, and the loans receivable from Cash Store’s customers (valued at net realizable value) to be presented as an asset;
- (c) the failure to disclose that Cash Store, instead of the TPLs, bore the responsibility for losses suffered on account of uncollectible loans including because of the failure to disclose that retention payments were not voluntary;

- (d) the claim that Cash Store conducts its business in accordance with the applicable law in the 2011 financial statements and Q2 and Q3 2012 financial statements as well as the description of Cash Store's business in the Offering Memorandum (for the Note Offering);
- (e) the description of the 'Use of Proceeds' in the Offering Memorandum, including the failure to disclose that the Loan Portfolio was being acquired at a significant premium to market value and as to the allocation and distribution of the purchase price;
- (f) the failure to disclose the fair value of the Loan Portfolio at \$50 million on the Q2 and Q3 2012 interim financial statements;
- (g) the description of the TPLs as "independent";
- (h) the failure to disclose related party transactions; and
- (i) the failure to disclose that Cash Store was operating in breach of the TPL Agreements, and particularly the disclosure that Cash Store manages its risk of exposure to the TPLs through compliance with loan limits, procedures and selection criteria established by the TPLs."

[417] CS Estate continues that, had KPMG and Cassels appropriately discharged these duties, Cash Store's board would have become aware of the "proper legal and accounting treatment" of Cash Store's business and the misleading nature of the public disclosures as enumerated in the paragraph above.

[418] In particular, CS Estate alleges, Cash Store's board would have learned that Cash Store was not a broker but in fact a lender, that Cash Store was in a debtor-creditor relationship with the TPLs and that the Loan Portfolio would have to be recognized on the balance sheet.

[419] It would then follow, CS Estate says, that Cash Store's shareholders and investors would in turn have discovered the loan impairments within the Loan Portfolio and the "true extent of the regulators' serious concerns" about Cash Store's regulatory compliance.

[420] This, in the plaintiff's formulation, would then have led immediately to the orderly winding up.

[421] I will discuss some of these assumptions in discussing the 'deepening insolvency' theory in the section on damages below, but in terms of the causation analysis, as discussed at length above, I have not found that CS Estate has proved on the balance of probabilities that the breaches and related alleged shortcomings set out in paragraph 416 above are made out. In particular, breaking the chain of causation at the first link, I do not agree that Cash Store's business was mischaracterized as a broker. Moreover, and again, I find that the deficiencies alleged are not in any event but-for causes of the damages alleged, and that there are other causes for the damages claimed.

Morawetz R.S.J.'s (As He Then Was) Decision

[422] I have discussed above the implications for my analysis of Morawetz R.S.J. (as he then was)'s decision in the context of the CCAA proceedings, on which the plaintiff, Mr. Aziz and the plaintiff's accounting liability expert place so much emphasis.

[423] As will be evident, I find that that decision, while entitled to deference in terms of the dispute that it addressed – being a priority dispute between the TPLs and the DIP lenders over funds within the estate – is not determinative of the issues before me.

[424] Leaving aside the evidentiary problems associated with seeking to prove the underlying facts in a decision simply by filing that decision, both the parties and the issues before His Honour were different than the parties and issues before me.

[425] Even if I were to accept the facts recited by Morawetz R.S.J. as proven before me, those facts do not provide evidence relative to the negligence claims against the defendants before me (nor the fiduciary duty claim against Cassels). There was no evidence before His Honour concerning the accounting issues relative to Cash Store's financial statements, nor evidence concerning the relevant interactions with regulators for purposes of the claim against Cassels.

[426] As also noted above, it appears that His Honour was given only a partial picture and explanation of the Retention Payments, and not advised concerning the accrual of amounts as Retention Payments separate and apart from monthly amounts paid based on a stated interest rate.

[427] In short, given the different parties and different issues involved, given concerns about the evidence that was put before His Honour, and given the limits on the use I could make of factual findings from that motion in the context of the trial before me in any event, I find that I am not bound, in making the determinations that I must make, by the decision in that motion.

VIII. Detailed Analysis of the Claim Against Cassels

(A) Allegations Against Cassels in the Nature of Negligence

[428] There are a number of allegations that the plaintiff makes against Cassels. A number of those claims overlap to some extent with the claims against KPMG, and I do not propose to repeat my analysis of those items here.

(1) Allegation that Cassels Ought to have Dissuaded Cash Store from Using Broker Model

[429] One of the standalone claims against Cassels appears to be that Cassels ought to have advised Cash Store against the establishment and continued operation of the Cash Store business using a broker model.

[430] I have a couple of threshold concerns about this allegation. First, I do not find that the plaintiff has proved that the broker model was somehow impermissible. I appreciate that the claim

is not necessarily that a broker model was impermissible, but rather that, as Cash Store's business unfolded over the years, and as it developed the practices that it did for dealing with the TPLs, the broker model in effect became a fiction.

[431] As is evident from the discussion above, I am not persuaded that this was the case.

[432] Moreover, and the second threshold concern about this claim, there is no evidence before me that Cassels was ever asked to opine on the structure of the Cash Store business as a broker.

[433] Rather, as mentioned in passing above, Cash Store appears to have received an opinion from the Reynolds Mirth firm at or about the time of the creation of Cash Store, recommending or countenancing the use of the broker model. I use the word "appears" advisedly here, in that, despite apparent requests, the plaintiff has never produced a copy of that original opinion from Reynolds Mirth. There are snippets in the record before me which seem to confirm not only that Reynolds Mirth provided that original opinion, but that Reynolds Mirth reinforced its view of the appropriateness of Cash Store using a broker model from time to time over the subsequent years.

[434] My point here is not to further discuss the appropriateness or otherwise of Cash Store's structure as a broker, but rather to observe that Cassels did not provide an opinion, and nor is there any evidence to suggest that it was asked for an opinion, about Cash Store's use of that structure. I do not find in the evidence any basis on which I could conclude that Cassels breached any relevant standard relative to Cash Store's business model; it does not appear to have been consulted in that regard.

(2) Allegations that Cassels Allowed or Facilitated Misrepresentation

[435] An important prong of the theory of the plaintiff's claim against Cassels, which occupied a larger portion of the evidence at trial, appears to be that a lawyer, in this case Mr. Pinos, and other members of the Cassels firm, may not, if he or they believe(s) that aspects of a client's operations are non-compliant with the regulatory framework within which the business operates, or knows that the regulator holds that view, make representations in public disclosure or in submissions on behalf of the client that do not openly, fully, and explicitly divulge and reflect the regulator's views. At times, the plaintiff's view seemed to go further than that, and to assert that a lawyer may not take strong positions, in advocating for a client, contrary to what the lawyer knows to be the opposing positions of a regulator.

[436] That is, in terms of the facts of this case, the plaintiff emphasizes that Mr. Pinos and others at Cassels made or condoned representations suggesting that Cash Store was in "substantial compliance" with the relevant regulations as promulgated or amended from time to time, and/or suggested that technical shortcomings in the regulator's positions meant that Cash Store's operations were in fact in accordance with the regulatory regime (notwithstanding Cash Store's knowledge, and that of Cassels, that the regulator felt otherwise).

[437] Mr. Pinos and Cassels also made submissions on Cash Store's behalf, both in ongoing correspondence and within the context of regulatory proceedings, at odds with the various regulators' positions as to how the relevant legislative and/or regulatory provisions were to be

interpreted. Again, CS Estate's position appears to be that such submissions were and are impermissible.

[438] In my view, the plaintiff's position in this respect misconceives the legitimate role of an advocate in formulating and advancing positions on his or her client's behalf.

[439] I acknowledge that of course an advocate may not knowingly assert positions that the advocate knows to be false, or misrepresent a client's operations or conduct to a trier of fact, and that to do so may not only breach professional obligations, but may constitute an abuse of process (or abetting a client's abuse of process).

[440] However, in my view, the actions of Mr. Pinos and Cassels are not fairly construed or understood as crossing any such lines.

[441] Rather, I find that the advocacy work undertaken by Cassels on Cash Store's behalf, including in particular as led by Mr. Pinos, was not only reasonable, appropriate, and entirely in accordance with the duty of an advocate to forcefully advance his or her client's best interests, but that in fact the arguments that Mr. Pinos and Cassels made on Cash Store's behalf were skillful, and well-conceived to put Cash Store's positions in their best light.

[442] At no point, in my view, did Mr. Pinos/Cassels, in representing Cash Store's interests, stray into or anywhere near territory that could be characterized as abusive, unethical, or otherwise inappropriate.

[443] Accordingly, I reject the allegations in the statement of claim, as encapsulated for example in paragraphs 21 and 22 of the fresh as amended claim against Cassels, that Cassels advised and assisted Cash Store to implement business practices to circumvent payday loan laws and regulations, and to "conceal such circumvention from payday borrowers and regulators".

[444] Rather, I find, Cassels and Mr. Pinos appropriately took issue with the "black and white" positions being asserted by provincial regulators, and appropriately explored proposed competing interpretations and compliance strategies on behalf of Cash Store, in circumstances in which Cash Store's very ability to continue in business was threatened.

[445] By way of overview of the exchanges with provincial regulators, and to illustrate the increasingly existential implications for Cash Store of the regulators' positions, in Ontario (largely replicated in other provinces) the Ontario Registrar initially asserted that Cash Store was, by offering cheques or cards (debit or credit) pre-loaded with cash, in breach of the legislative requirement that cash immediately be made available to a payday loan customer to whom a loan was provided. Moreover, by levying an additional charge, albeit modest, for the cards, the Registrar alleged that Cash Store was improperly offering additional products and charging additional amounts not sanctioned by the payday loan legislation. In addition, since many of Cash Store's customers did not have bank accounts or credit ratings, and since initially cheques were not issued immediately but had to be generated and sent to customers, it often took a few days before customers who opted for cheques were "in funds".

[446] As a result of ongoing debate and dialogue with the Registrar about these assertions, Cash Store initially installed printers in each of its Ontario branches so that cheques could be printed immediately, and took steps to clarify that the modest charges for the cards were not levied by Cash Store – and generated no revenue for Cash Store – but were instead charges made by the financial institution, DirectCash Bank (“DC Bank”), with which Cash Store had aligned for these purposes.

[447] The Registrar continued to express concerns about these responses. In the case of the cheques, notwithstanding that cheques were now immediately available to customers on site, it was still the case that, for the reasons outlined above, many Cash Store customers could not cash cheques instantaneously, such that there was still a lag before a customer obtained the cash contemplated by the Loan Agreement.

[448] To remedy this concern, through the arrangement with DC Bank, Cash Store implemented a program by which customers could immediately cash cheques at DC Bank branches.

[449] As is evident, throughout the interactions with the Registrar, Cash Store was striving to maintain its “cashless” model, and to avoid the need to house cash within its individual branches. As Cash Store pointed out to the Registrar (and equivalent administrators in other provinces), a requirement for “cash on hand” would require a substantial rebuild or reconfiguration of all Cash Store branches to install the extensive security features that would be necessary to protect its employees and customers in the presence of cash.

[450] When the Registrar continued to express dissatisfaction with the use of cheques and cards, Cash Store pivoted to develop a plan to deliver funds to payday loan customers through electronic transfer of funds (“ETF”). I note that this plan, while understandable in circumstances in which regulators were making clear their unwillingness to accept central features of Cash Store’s existing operational model, reflected a resignation by Cash Store to a scenario that would, at least in the near term, significantly curtail Cash Store’s customer base.

[451] That is, as noted, many of Cash Store’s payday loan customers did not have bank accounts, such that for those customers, the availability of ETFs was illusory, since they had no bank account to which funds could be electronically transferred. To address this significant problem, Cash Store continued to enlist the services of DC Bank, and established a program by which payday loan customers could receive EFTs at DC Bank branches.

[452] I should note as well that during the course of these exchanges, evidently in response to Cash Store’s attempts to devise technically and functionally compliant practices and products, additional regulations were promulgated, in Ontario and elsewhere, with an evident view to “filling holes” that Cash Store sought to exploit in the regulatory framework. Cash Store and Cassels then in turn reformulated their strategies with a view to achieving compliance with the revised provisions.

[453] I describe this back and forth between the Registrar (and equivalent regulators in other provinces), and Cash Store (and Cassels and other counsel on Cash Store’s behalf), without judgment as to who was right and who was wrong about reasonable interpretations of the

legislative and regulatory provisions. Ultimately the regulators “prevailed” in the sense that their insistence on certain interpretations, combined with Morgan J.’s decision in February of 2014, rang the death knell for Cash Store’s ongoing model of operations.

[454] However in my view what the ongoing exchanges between Cash Store/Cash Store’s counsel on one hand and the regulators on the other illustrate is that Cash Store was working and negotiating with the regulators to try to find a way forward that would allow Cash Store to satisfy the regulators and meet the evolving regulatory provisions in order to allow Cash Store to stay in business.

[455] That this effort ultimately proved unsuccessful in no way, in my opinion, means that Cassels, in advocating for interpretations that would allow its client to survive, was acting improperly or in breach of its duties. Rather, I find that Cassels’ efforts were reasonable and creative in the circumstances, and not at odds with Cassels’ duties in that capacity.

(3) No Expert Evidence Led Against Cassels

[456] I note here that, in its evidence against Cassels, CS Estate did not offer expert evidence as to what Cassels’ duties were in the circumstances, nor the standards against which Cassels’ performance was to be measured, let alone expert evidence that Cassels somehow breached those duties and standards or thereby caused harm to Cash Store. Similarly, there was no evidence to confirm that any stakeholders of Cash Store relied on Cassels’ work to their detriment, or incurred any damages caused by Cassels’ conduct.

(4) Discussion of Claims Based on Content of Disclosures

[457] In that regard, the second and related basis on which the plaintiff proceeds against Cassels relates to the nature of public disclosures made by Cash Store, in part in reliance on advice from Cassels, during the period in which Cash Store’s ongoing dialogue with its regulators, summarized above, was underway.

[458] There were a number of specific disclosures that CS Estate alleged to have been wanting during the period in question, including in Cash Store’s financial statements (both interim review statements and audited year-end statements), its AIFs, and its MD&As. In each case, the disclosures by Cash Store, in its specific discussions of the details and status of the regulatory issues, provide that Cash Store believes that it is in “substantial compliance” with the new and evolving regulatory requirements (or uses language to similar effect).

[459] The plaintiff argues that this is a material misrepresentation. It says that, as Cash Store knew full well, the regulatory reality was much more precarious than Cash Store’s representation of “substantial compliance” conveys.

[460] Cash Store and Cassels were aware, the plaintiff argues, that the regulators across the country were not satisfied with aspects of Cash Store’s operations, and that, far from agreeing that Cash Store was in substantial compliance with the regulatory regimes, the regulators were, to varying degrees but largely consistently, expressing the view that many aspects of Cash Store’s

operations were not compliant. The regulators were going so far, in some instances, as to threaten Cash Store with suspension or even revocation of its provincial licenses under applicable payday loan legislation.

[461] While the discrepancy, pitched as the plaintiff argues, is potentially problematic for Cassels, the evidence concerning Cash Store's disclosures is not quite so cut and dried.

[462] First, and importantly, in other parts of the disclosure documents at issue Cash Store makes more specific disclosure of the state of the interactions with the regulators.

[463] For example, using Cash Store's MD&A for the three months and year ended September 30, 2012 as an example, under the heading "Industry: Regulatory Change" Cash Store's management state that "The Company believes that it complied with applicable provincial regulations" and that "The Company believes it is important to continue to work with compliance bodies in each Regulated Province in order to remain current with the regulatory environment."

[464] Read in isolation, these passages convey that Cash Store believes itself to be in compliance with provincial regulations, and is making an ongoing effort to work with regulators to ensure ongoing compliance. At that time, Cash Store was in fact at odds with different provincial regulators, to varying degrees, and in fact in some provinces was facing threats that the regulator might take actions to suspend or revoke Cash Store's license to operate in those provinces.

[465] In that regard, elsewhere in the MD&A, under the heading "Risks Related to the Business" and the sub-heading "Regulatory Environment", while reiterating that "The Company believes that it complies with applicable regulations related to payday loan products in each of the above listed provinces [B.C., Alberta, Saskatchewan, Manitoba, Ontario and Nova Scotia]" Cash Store also refers to both risks and ongoing regulatory enforcement proceedings.

[466] It says that "as the Company introduces new products and services, it may become subject to additional laws and regulations" which "may restrict the Company's ability to operate the way it does today or its ability to expand operations and may have a negative effect on the Company's business, results of operations and financial condition." It goes on to say that "The Company is currently, and may in the future be, subject to litigation and regulatory proceedings which could generate adverse publicity or cause the Company to incur substantial expenditures or modify the way the Company conducts its business" and that "Changes in laws or regulations, or a failure to comply with applicable laws and regulations, may have a material adverse effect on the business, prospects, results of operations, and financial condition of the Company."

[467] In addition, Cash Store specifically discloses regulatory proceedings in B.C, as a result of which "the Company was issued a compliance order and administrative penalty" and that Consumer Protection B.C. had issued a supplementary compliance order that Cash Store was appealing.

[468] Similarly, and by way of another example, in the Offering Memorandum dated January 24, 2012 with respect to Cash Store's Note Offering of \$132 million of 11.5% senior secured notes in

conjunction with the LIT, Cash Store stated: “We believe that we are in substantial compliance with all federal and provincial laws and regulations” but coupled that statement with the qualification that “many of the rules that apply to us have only recently been implemented, are complex and sometimes ambiguous and, accordingly, we cannot assure that we are in 100% compliance with all applicable laws, much less that all courts, arbitrators and regulators would agree that we are in 100% compliance.”

[469] The Offering Memorandum goes on to describe the regulatory proceedings and compliance order in B.C., an order from the regulatory authority in Alberta directing Cash Store to cease certain alleged practices in contravention of the Alberta payday loan regulations, and advises that in Ontario recent amendments to the general regulation under the *Payday Loans Act* “may significantly impact the profitability of our business in Ontario.” The document notes that Cash Store had commenced an application for judicial review relative to the amendments, and that, while the company has made changes to its business practices to comply with the new regulations, “those changes and our regulatory compliance may be subject to review and challenge in Ontario.”

[470] There are many other disclosures by Cash Store throughout the relevant timeframe, and it is fair to say that the pattern of Cash Store stating that it believes it is in compliance, or substantial compliance, coupled with specific disclosures about regulatory threats or proceedings, is by and large repeated.

[471] Again, with respect to this issue, the plaintiff tendered no expert evidence.

[472] I accept that, in relation to disclosure that is obviously inadequate or inaccurate or misleading, I may not require expert guidance to identify those shortcomings.

[473] However, where disclosure includes qualifying language, and is provided within the framework of corporate and securities disclosure requirements, I find that expert evidence is necessary and ought to have been tendered to guide the court’s determination of the extent and contents of appropriate public disclosure. For example, while it seems to me that, in order to assess the sufficiency and appropriateness of disclosure it is reasonable to consider all comments within a given document, and to assess the disclosure on the basis of the totality of representations within that document, I do not know, absent expert evidence, whether that is a practice that is used and countenanced within the relevant regulatory regime(s).

[474] It is not plain and obvious to me that Cash Store’s disclosure is deficient, or below the standard required for such disclosure and, in the absence of expert evidence I am unable to make that determination.

[475] On this basis as well, I find that the plaintiff has failed to prove its claim against Cassels on a balance of probabilities.

(B) Issues Raised Regarding Role of Paul Stein

[476] The next plank in the plaintiff’s case against Cassels relates to the role of Paul Stein.

[477] Mr. Stein was at the relevant times a senior partner at Cassels, whose practice encompassed corporate and securities matters, with a particular emphasis on the mining sector.

[478] Mr. Stein had assisted Mr. Reykdal with the launch of a company – unrelated to Cash Store – in the mid-1980s, and over the years had become Mr. Reykdal’s friend and trusted advisor.

[479] Accordingly Mr. Reykdal involved Mr. Stein and Cassels on Cash Store’s behalf from the outset of Cash Store’s operations, and Mr. Stein served as the “relationship partner” for Cassels in its dealings with Cash Store over the years from Cash Store’s origins in the early 2000s until the CCAA proceedings in 2014.

[480] In the early part of the relationship, Mr. Stein served as corporate secretary for Cash Store, which he explained was not unusual in circumstances in which a client has not yet assembled a full suite of executive officers, and was frankly a useful business development strategy to establish a trusted “insider” relationship with the client. Mr. Stein also acquired shares in Cash Store early on (there was no evidence as to the extent of Mr. Stein’s shareholding, nor as to whether or not he continued to hold shares as of the date of the events at issue, but the plaintiff did not assert that Mr. Stein’s shareholding itself created any concerns).

[481] Throughout the years that Cassels served as one of Cash Store’s key external counsel (and it appears, its main external counsel), Mr. Stein oversaw the relationship, deploying teams of appropriately qualified lawyers on mandates that came in from Cash Store regularly over the years. In terms of the extent of the relationship, the evidence indicated that during a five-year span from 2009 to 2014, Cassels billed Cash Store upwards of seven million dollars.

[482] It is clear that at a certain point, at the suggestion and with the encouragement of Mr. Reykdal, Mr. Stein incorporated FSC Abel to be a TPL to Cash Store. The amount of funds advanced by FSC Abel to Cash Store to be deployed in loans to payday loan customers was relatively modest compared to a number of other TPLs. FSC Abel advanced a total of \$600,000.00 to Cash Store, in two equal tranches, in 2009 and 2010, respectively. Those funds, Mr. Stein explained, largely or entirely came from an existing family trust in favour of Mr. Stein’s two sons. The shareholders of FSC Abel were Mr. Stein and his wife. It is clear that the investment made through FSC Abel was intended to benefit Mr. Stein’s family.

[483] The plaintiff alleges that, by being the relationship partner at Cassels for the Cash Store relationship, and at the same time being the principal of a TPL loaning funds to Cash Store, Mr. Stein was in an untenable conflict of interest. More particularly, the plaintiff alleges that, FSC Abel, as a TPL, received unfairly preferential treatment by virtue of the LIT, in which FSC Abel, like the other TPLs, was repaid the full face value of its loans to Cash Store in circumstances in which it is also alleged that Cash Store was insolvent, thus further eroding the position of other stakeholders by way of the preferential payments to TPLs.

[484] I note in passing in this regard that, while it does not address the question of whether or not Mr. Stein was in an untenable conflict, he was not ultimately advantaged by FSC Abel’s advances to Cash Store. Like many of the TPLs, FSC Abel was paid in the LIT by way of a combination of cash and Notes (from the Note Offering in conjunction with the LIT). In the case

of FSC Abel the cash component was approximately \$100,000.00 and the Notes totaled about \$500,000.00. As a result of Cash Store's insolvency and CCAA proceedings, the Note-holders ultimately suffered losses on their Notes, such that FSC Abel (and indirectly Mr. Stein) lost approximately \$500,00.00 of its investment of \$600,000.00.

[485] As to the conflict, I would say as a general proposition, as noted above, that potentially conflicting roles like those occupied by Mr. Stein are not to be encouraged.

[486] However, I find no evidence that Mr. Stein's dual roles in any way negatively or otherwise influenced any advice that Mr. Stein (or Cassels) provided to Cash Store, nor, as noted, that Mr. Stein received any preference in the LIT. While it was generally beneficial for the LITs to have their positions purchased at "fair value" (subject to those LITs who were paid in whole or in part by Notes from the Note Offering, who presumably, like FSC Abel did not fare well), this approach was taken to the TPLs collectively; there is no suggestion that TPLs whose principals had particular relationships with Cash Store received any preferential treatment.

[487] As set out in the discussion about causation above, I also find no evidence of the plaintiff or any other party suffering damages as a result of Mr. Stein's dual role.

[488] For these reasons, I dismiss the claim against Cassels as well.

IX. Plaintiff's Formulation of Damages

[489] Notwithstanding my findings on liability, I turn now to discuss the quantification of damages. Given the amount at stake here, there is obviously a possibility that this matter will be the subject of further proceedings, and I expect that a discussion of the damages issues will or may be of assistance in that context.

[490] As set out above, the plaintiff's theory of damages is that the defendants' alleged negligence caused, between late 2011 and Cash Store's commencement of CCAA proceedings in April of 2014, a deepening of Cash Store's insolvency.

[491] As the plaintiff explains, the theory is that, but for the defendants' negligence, Cash Store would have sought creditor protection at a particular (much earlier) time under the CCAA or other insolvency statutes.

[492] The operative notion is that the defendants' alleged negligence caused Cash Store to continue its operations such that the consequent losses – the "deepening" of the corporation's insolvency – are attributable to the defendants.

[493] CS Estate asserts that "this theory of damages has been adopted and applied in Canada" and suggests that the "most notable example" is the decisions of this court, of the Court of Appeal for Ontario and of the Supreme Court of Canada in *Livent Inc. (Receiver of) v. Deloitte & Touche*, 2014 ONSC 2176, 11 C.B.R. (6th); 2016 ONCA 11, 128 O.R. (3d) 225; and 2017 SCC 63, [2017] 2 S.C.R. 855.

(A) Consideration and Criticism of “Deepening Insolvency” Theory in the United States and Canada

[494] With respect, it appears to me that the deepening insolvency theory of damages has not particularly taken hold in Canada, and that *Livent* is not just the most notable example, but perhaps the only notable example of its application.

[495] Indeed, for reasons having to do most particularly with legal causation, the Court of Appeal for Ontario, in particular, sounded a cautionary note about potential traction of the “deepening insolvency” theory in Canadian jurisprudence, and as to the need or utility of importing the “deepening insolvency” concept into Canadian jurisprudence. The Court of Appeal, having cited a definition of deepening insolvency as “the artificial prolongation of a corporation’s existence past the point of insolvency” (para. 331), observed:

“I do not think it necessary, or useful, in this case to determine whether ‘deepening insolvency’ is to be recognized as a cause of action or a theory of damages in Canada. It is a label that describes many of the same considerations that underlie the debate about whether the damages for the *Livent* claims are available under traditional tort and contract principles” (para. 338).

[496] The law in Canada requires, in addition to factual causation, that a plaintiff seeking to recover damages for negligence must also establish legal causation, i.e. that its damages are not too remote. That notion is imbedded within the but-for analysis.

[497] In general terms, the question of remoteness (or proximate cause) inquires as to whether the “harm is too unrelated to the wrongful conduct to hold the defendant fairly liable” (*Mustapha v. Culligan of Canada Ltd.*, 2008 SCC 27, [2008] 2 S.C.R. 114). As noted by the Supreme Court of Canada in its decision in *Livent*, the test for remoteness is reasonable foreseeability – the plaintiff’s injury “will be sufficiently related to the wrongful conduct if it is a reasonably foreseeable consequence of that conduct.”

[498] Cassels argues that by “advancing a ‘deepening insolvency’ theory of damages that purports to entitle it to all losses between the hypothetical insolvency date in 2011 and the actual liquidation date in 2014, [CS Estate] has completely failed to lead evidence on what caused the alleged increase in deficit, whether that cause was a reasonably foreseeable consequence of Cassels’ negligence, and whether Cassels’ negligence was a but-for cause of the increased deficit.”

[499] It appears that the risk in deploying a “deepening insolvency” theory of damages, is to assume away the issue of causation, and in particular to overlook the need to demonstrate reasonable foreseeability. Cassels points to literature and case law in the United States, where there has been a brief “rise and fall” of the “deepening insolvency” theory, suggesting that this tendency to skip over legal causation in the analysis has led to the “deepening insolvency” theory being widely rejected and jettisoned in the United States (which rejection dovetails with the Court of Appeal for Ontario’s cautionary note in *Livent* about the use of this theory of damages).

[500] The deepening insolvency theory appears first to have emerged in the United States in a 1980 case called *Bloor v. Danskere (In re Investors Funding Corp. of New York Securities Litigation)*, 523 F. Supp. 533 (N.Y. Dist. Ct. 1980) which posited that a “corporation is not a biological entity for which it can be presumed that any act which extends its existence is beneficial to it.”

1. Problems with Application of Deepening Insolvency Theory Including in *Livent* and in this Case

[501] After its initial promulgation, ‘deepening insolvency’ featured as a cause of action in certain American cases in circumstances of fraud. However, within a few years (by the early 2000s) it was rejected by the Delaware Court of Chancery as an “incoherent doctrine” (*Trenwick America Litigation Trust v. Ernst & Young, LLP*, 906 A.2d 168 (Del. Ch. 2006)).

[502] As aptly summarized in Cassels’ submissions, the U.S. Courts quickly came to recognize that, as a theory of damages, ‘deepening insolvency’ “suffers from a ‘proximate causation’ problem: “Between the initial act (the injecting of money into the business) and the end result (the expansion of the company’s debt relative to where it was prior to the cash infusion) stand the intervening acts of the company’s management (i.e. what it chose to do with the money)” (*Marion v. TDI Inc.*, 591 F.3d 137 (3rd Cir. 2010)).

[503] As Cassels submits, the problem is that those intervening acts, as well as other external causes, can break the legal causation link. Cassels quotes from an American article entitled “Lawyer Liability and the Vortex of Deepening Insolvency” (Douglas R. Richmond et al. (2006) 51:1 Saint Louis U.L.J. 127), which lays out the difficulty with the doctrine as follows:

“A deepening insolvency claim effectively alleges that the lawyer participated in certain matters, failed to prevent the client from making certain business decisions, or failed to share particular information concerning the company’s financial conditions with certain players. This conduct, according to typical allegations, assisted the allegedly culpable corporate fiduciaries in further depleting the client’s assets and driving it deeper into insolvency. It is plain that this theory suffers from a fatal inability to establish that the lawyer’s conduct proximately caused the corporation’s alleged injuries.

[...] The importance of establishing proximate cause is heightened in a deepening insolvency case, where multiple factors surely contributed to the company’s downfall and the lawyers are convenient scapegoats for their client’s business misjudgments.

Given the many factors that combine to produce corporate success or failure, the notion that a corporation’s demise could have been averted or that its ultimate insolvency could have been materially lessened but for a lawyer’s alleged negligence generally defies logic. Lawyers are not guarantors of their client’s business judgment. A lawyer does not have the ability to compel a company’s officers or directors to pursue a particular course of action. This fact alone will in most cases turn causation into speculation and thus defeat a plaintiff’s claim.

The long and the short of it is that absent exceptional circumstances involving fraud or similar misconduct, a bankruptcy trustee or other representative of an insolvent entity will simply be unable to eliminate with sufficient certainty the effect of other factors contributing to the company's demise. Such additional factors may include economic conditions, competitive forces, governmental action, and fundamental aspects of the business at issue such as operating or production costs, financing costs, and the like. Of course, a lawyer cannot be held liable for injuries caused by other forces or the actions of others" (pp. 157-159; citations omitted).

[504] I would observe that, while the excerpt from "the Vortex of Deepening Insolvency" article focuses on the difficulties of a claim against a company's lawyers, the same concerns would hold true with respect to a claim against a company's auditors.

[505] Moreover, among potential "other factors contributing to the company's demise" I have found that the company's valuation of the Loan Portfolio within the LIT, and the effect of regulatory pressure and antagonism aimed at key constituent elements of Cash Store's operations were each significant causes, which I have found were not the responsibility of the defendants, leading to the collapse of the Cash Store business.

[506] As such, in addition to the other aspects of the but-for analysis set out above, and by reference to the causation concerns identified in the American literature and case law relative to the application of the 'deepening insolvency' theory, CS Estate's claim cannot survive this aspect of the analysis either.

[507] Returning to *Livent*, as set out above the Court of Appeal for Ontario expressed reservations, in its decision, concerning the need and utility of importing the deepening insolvency theory.

[508] Justice Gans, the trial judge in *Livent*, had himself noted that, while the experts before him, and therefore the parties had agreed upon the formula for assessing damages, the agreed formula did not permit a robust assessment of remoteness (*Livent*, ONSC, at paras 318-319).

[509] The Court of Appeal for Ontario, in its analysis of damages, specifically emphasized the need to assess which causes of Livent's increased deficit were a reasonably foreseeable consequence of Deloitte's negligence, and which causes were attributable to other factors. The court said:

"[W]hile the Measurement Date [the but-for insolvency date] is the triggering moment for the measurement of damages, it does not follow that Deloitte is responsible for any and all losses sustained by Livent during the delta period. What *Livent* is entitled to recover is "the increase in the liquidation deficit that would not have occurred but for Deloitte's negligence" but not those losses that, to paraphrase *Mustapha*, are too remote to hold Deloitte fairly liable. In short, Deloitte is only responsible for those losses that are reasonably foreseeable as a result of its negligence" (para. 372).

[510] All levels of court in *Livent* concluded that Livent had largely established legal causation on the evidence. As Gans J. concluded at trial:

“Livent’s losses after the Measurement Date are largely attributable to the very fraud which Deloitte should have detected[...]. The use of fraudulently misstated financial statements to induce people to invest in a company is entirely predictable” (para 318).

[511] Nonetheless, Gans J., expressing a concern that the basic measure of damages as the increase in the liquidation deficit that would not have occurred but for Deloitte’s negligence did not permit him to “readily ascertain” the amount of damages that “ought to be seen as a result of the normal vagaries of Livent’s business and therefore too remote to be recoverable” (para 319). His Honour, on that basis, reduced the damages by 25%. This approach was upheld by the Court of Appeal.

[512] As can be seen, in the only significant case in which the ‘deepening insolvency’ theory has been considered in Canada, the court(s) expressed concerns about the inherent problems of determining foreseeability and proximate cause, and adjusted the analysis to incorporate and emphasize the need to address these elements of the tort. There was not in *Livent*, nor in any other Canadian case cited by the plaintiff here, any unqualified acceptance of the ‘deepening insolvency’ theory. Instead, consistent with the concerns and cautions emanating from the American experience with ‘deepening insolvency’ the court in *Livent* instead applied the time-tested components of causation in tort law.

[513] Cassels points out that the analysis undertaken by the Canadian courts in *Livent* (and in particular the Supreme Court of Canada’s confirmation that liability for pure economic loss depends on the defendant’s undertaking and the plaintiff’s reasonable reliance on that undertaking) has also characterized the approach of leading U.K. cases in dealing with the question of remoteness in professional liability cases. In *South Australian Asset Management Corporation v. York Montague Ltd.*, [1996] U.K.H.L. 10 (often referred to as SAAMCO), the House of Lords used the example of a mountaineer to explain that damages cannot be awarded where an alternate cause that is unrelated to the defendant’s negligence is the true source of the plaintiff’s injury:

“A mountaineer about to undertake a difficult climb is concerned about the fitness of his knee. He goes to a doctor who negligently makes a superficial examination and pronounces the knee fit. The climber goes on the expedition, which he would not have undertaken if the doctor had told him the true state of his knee. He suffers an injury which is an entirely foreseeable consequence of mountaineering but has nothing to do with his knee” (para. 19).

[514] As explained by the court, using the mountaineering example to illustrate the point, “a person under a duty to take reasonable care to provide information on which someone else will decide upon a course of action is, if negligent, not generally regarded as responsible for all the consequences of that course of action. He is responsible only for the consequences of that information being wrong. A duty of care which imposes upon the informant responsibility for losses which would have occurred even if the information which he gave had been correct is not

in my view fair and reasonable as between the parties” (at para. 23). Similarly, in my view, Cash Store’s overvaluation of the Loan Portfolio, and/or the increasing antagonism of the regulators towards Cash Store’s business were not foreseeable consequences of the work of KPMG or Cassels, respectively.

[515] In my view, for the reasons explained above, I must take the same approach here, founded on the traditional elements of the tort, and I see no basis to embrace the checkered notion of ‘deepening insolvency’. Moreover, unlike the court(s) in *Livent*, in my view there is no aspect of the damages claimed that can readily be attributed to KPMG or Cassels.

B. Additional Problems with Plaintiff’s Calculation of Damages

[516] Nor is CS Estate’s claim salvaged or ameliorated by the evidence of its damages expert, Mr. Pappas.

[517] The plaintiff, consistent with the approach taken in *Livent*, posits as the appropriate equation for the measurement of the increase in the losses suffered by Cash Store between the time of the defendants’ alleged breaches and the time of Cash Store’s eventual CCAA filing, the following: “Loss (L) = Actual Liquidation Deficit (“ALD”) minus Estimated Liquidation Deficit (“ELD”).

[518] In this equation, the ELD is calculated as at the “measurement date”, which the plaintiff says is “the date when: (a) the defendants breached the standard of care; (b) the true state of Cash Store’s business would have been discovered; (c) Cash Store would thus have been unable to access the capital markets in any meaningful way; and (d) this would, in turn, have led to Cash Store’s insolvency.”

(1) Pappas Opinion and Defendants’ Responses

[519] The plaintiff’s damages expert, Mr. Pappas, opines that the appropriate dates to use as the measurement dates were September 30, 2011 and December 31, 2011 (the “Measurement Dates”) because those were the dates closest to the date of the Note Offering and LIT (January 31, 2012) that coincided with the previous fiscal year end (September 30, 2011) and the month that is one month prior to the date of the note offering transaction.

[520] While the defendants’ experts, Errol Soriano on behalf of KPMG and Christopher Milburn on behalf of Cassels, used those Measurement Dates for purposes of their respective analyses, it is their view that the evidence does not demonstrate that Cash Store was in fact insolvent on either proposed date.

[521] The plaintiff in its submissions says that “At a high level, the parties’ experts disagree about two issues relating to damages (each of which contain several sub-issues): first, whether Cash Store was truly insolvent as of the Measurement Dates and second, the proper measurement of both the ELD and the ALD.”

[522] Mr. Pappas in his original expert report opined that had the true nature of Cash Store's business been disclosed by KPMG or Cassels in accordance with Mr. Koch's formulation of that true nature, then regardless of whether or not the Note Offering and LIT were completed, Cash Store would have been insolvent as of the Measurement Dates.

[523] The plaintiff alleges that there was no response from the defendants' experts contesting that opinion, and says that "with no challenge from the Defendants, Mr. Pappas's opinion should be accepted by the court" such that "the first Damages Issue can be resolved on this basis alone."

[524] I do not think that the plaintiff's claim that Mr. Pappas's theory on this point is uncontested is quite apt. First, to varying degrees, it is implicit in the defendants' experts' opinions that they do not accept that Cash Store was insolvent as of the Measurement Dates. Indeed Mr. Soriano explicitly opines that Cash Store was solvent as of the Measurement Dates. Moreover, as set out above, I do not find that the plaintiff has proved on a balance of probabilities that Cash Store was insolvent prior to the LIT, and do not accept Mr. Koch's assertion that Cash Store was obfuscating the true nature of its business.

[525] Moreover, while the defendants' experts disagree with Mr. Pappas' methodologies, they assert, and I accept, that the more fundamental problems with Mr. Pappas' approach are evidentiary.

[526] It is undoubted that the plaintiff bears the burden of proving both the existence and the quantum of damages on a balance of probabilities (*The North West Company L.P. v. Classic Furs Company Ltd.*, 2025 ONCA 295).

[527] As the British Columbia Supreme Court said in *Anani et al. v. Uniglobe Travel (Western Canada) Inc.*, 2004 BCSC 824, [2004] B.C.T.C. 824, quoting *S.C. Fed. Savings Bank v. Thorton-Crosby*, 399 S.E. 2d 8 (S.C. App. 1990), while "mathematical certainty" is not required,

"...[t]he estimation of damages...cannot be based on conjecture or speculation; it must pass the realm of opinion not founded on the facts and must rest on evidence from which a reasonably accurate conclusion regarding the amount of loss can be logically and rationally drawn" (para. 92).

[528] In the case of Mr. Pappas' opinion, the defendants both maintain that, with respect to the plaintiff/Mr. Pappas' purported use of the equation described above, there is no proper evidence before the court to substantiate the asserted components of the ALD.

[529] More particularly, the defendants say, with the exception of the asset recoveries in the CCAA (which is a positive number) the plaintiff has not provided any evidence on the components of the ALD, nor for the rationale for including certain (unproved) administrative costs and settlement agreements within it.

[530] In cross-examination in that regard, Mr. Aziz testified that Mr. Pappas "did his own research based on financial reports" and "documents related to the CCAA" and that defence counsel could "ask him where he got the documents." As an initial matter I would observe that

this misstates the proper approach to the basis for an expert's calculation and of the component pieces of his or her opinion. The basis for those calculations, including the documentation or other evidence on which the expert relied should be clearly identified in the expert's report, including the source for such documents, and should be produced upon request by the defendant(s) in order to be tested by the defendant's expert, or in cross-examination, or both. For the plaintiff to say, as it does here through the evidence of Mr. Aziz at trial, "well you can ask the expert and he'll tell you what information he relied on," is both too late and otherwise unsatisfactory.

[531] Moreover, the problems with that "leave it to the expert's evidence in cross-examination at trial" approach are compounded here by Mr. Pappas' evidence.

[532] In Mr. Pappas' testimony, he repeatedly said that the ALD, and its components, were based on assumption(s) and instructions from counsel.

[533] As Cassels puts it in its submissions, this means that "With Aziz pointing to Pappas, and Pappas pointing to Plaintiff's counsel, one half of the Plaintiff's damages equation is in an evidentiary void."

[534] There are certain figures included within Figure 2 in Mr. Pappas' first report, purporting to explain the line items in that Figure, in turn making up the alleged ALD.

[535] However, Figure 2 itself was not properly proved; neither Mr. Aziz nor any other witness identified the source of Figure 2, and more importantly neither the individual components of Figure 2 nor the notes within it are substantiated by the evidence at trial.

[536] For example, Notes 2 and 3 of Figure 2 state that the plaintiff had "DIP Financing Costs" and "Professional Fees" totaling approximately \$32.3 million. The only evidence supporting these figures is an assertion in the witness statement of Mr. Aziz. However, as C.J. of this court recently reaffirmed in *Riva Plumbing Limited v. Ferrari*, 2025 ONSC 3219, "[n]either the defendants nor the court are required simply to take [the witness] at his word. The defendants are entitled to test the accuracy of [the witness'] evidence against the source documents..." (para. 279).

[537] During cross-examination, Mr. Aziz testified that the DIP Financing Costs came from a spreadsheet he "recovered from his files." When asked in cross-examination why the spreadsheet was not produced during discovery, Mr. Aziz said that the defendant should ask the plaintiff's counsel. The alleged spreadsheet is not in evidence.

[538] Similarly, Mr. Aziz testified that the professional fees in Mr. Pappas' Figure 2 came from an Excel Spreadsheet that he received from Dorothy Chan (a former Cash Store employee who testified at trial). The spreadsheet was marked as an exhibit during Mr. Aziz's examination in chief under defence counsel's objection that authenticity had not been admitted, and its observation that Mr. Aziz could not speak to the qualifying elements of the business records exception (including whether or not the record was made on a regular basis, routinely or systematically, whether it was made in the ordinary course of business, and/or whether the document was made pursuant to a

business duty at the time it was made). As such, on the basis of Mr. Aziz's testimony, the document was not shown to be a business records exception to hearsay and it cannot carry any weight.

[539] The plaintiff then called Ms. Chan as a witness, but led no evidence from her about the production of the spreadsheet, and in fact did not put the document to her at all. As a result, the plaintiff again failed to qualify the document as admissible under the business records exception.

[540] There are numerous other shortcomings in the plaintiff's evidence in support of the elements of the ALD.

[541] As another example, Note 4 within Figure 2 of Mr. Pappas' report references \$12 million in senior secured notes under a Secured Credit Agreement which the evidence indicates was settled during the CCAA proceedings for \$9.15 million. Note 4 also includes nearly \$4 million in deferred lease inducements and deferred taxes (shown in Cash Store's December 2013 financial statements). However, as the defendants fairly point out, neither of these items are liabilities that Cash Store would owe upon an insolvency. The defendants assert that these issues alone result in an overstatement of Existing Liabilities of at least \$10 million.

[542] The plaintiff now argues that the full \$12 million amount of the Secured Credit Agreement should be included in the ALD because "that [\$9.15 million] settlement did not take place until well after the valuation date in April 2014." However, that purported explanation is at odds with the plaintiff's general approach to the ALD, which takes into account the actual sale of Cash Store's assets from over a year after the CCAA filing, and also includes settlement agreements said to have been entered into during the course of the CCAA Proceedings.

[543] The defendants hasten to add that their focus, by way of example, on the deficiencies in Note 4, does not mean that the balance of the ALD figure has been substantiated. The defendants emphasize, and it is fair to say, that "The Court has no evidence before it on what Cash Store's existing liabilities were as of April 14, 2014, including no evidence why they would have increased by \$3.5 million between the end of 2013 and April 14, 2014" (which is what the plaintiff asserts).

[544] The other components of the ALD are similarly beset by a lack of evidentiary foundation.

[545] The defendants assert that the plaintiff's failure to provide documentary support for the ALD raises serious questions. The defendants note that, as in the recent *Riva Plumbing* case, the "defendants tried to help the plaintiffs by asking for production of the...documents underpinning the damages claim." Here, the defendants' lawyers repeatedly asked the plaintiff for support for the components of the ALD, as did Mr. Milburn, Cassels' damages expert.

[546] Cassels submits that, given the plaintiff's failure to provide this information in response to the defendants' repeated requests, the court ought to draw an adverse inference. In my view, while perhaps an adverse inference could fairly be drawn in the circumstances, the problem is more fundamental than that, and I need not get to an adverse inference. That is, I find that the plaintiff has simply failed to prove the components or total of the ALD.

[547] Cassels also expresses concerns, vis-à-vis the claim against it, relative to the ELD side of the equation. In particular, Cassels notes, Mr. Pappas' ELD numbers come entirely from Mr. Koch's purported re-cast of the relevant financial statements of Cash Store, which re-cast statements were produced by Mr. Koch in service of the claim alleging negligence on the part of KPMG.

[548] Cassels argues that there is no basis for holding it responsible for damages based on these financial statement issues arising from the claim against KPMG.

[549] In any event, given the absence of proper evidence to prove any aspect of the ALD, I find that I am unable to assess the plaintiff's alleged damages in these claims.

[550] For sake of completeness, I should add that I did not find Mr. Pappas to be a compelling witness.

[551] Mr. Pappas' experience testifying in court before this matter was quite limited. As noted, with respect to the all-important ALD, Mr. Pappas simply accepted an assumption that counsel provided, and appeared to have done little work to confirm the constituent elements of that assumption.

[552] Moreover, I found that Mr. Pappas regularly during the course of his testimony lapsed into the stance of an advocate rather than a dispassionate expert, routinely evincing a willingness and propensity to make unsupported assertions outside his area of defined expertise.

[553] Where Mr. Pappas' evidence conflicted with the evidence of Mr. Milburn and Mr. Soriano, respectively, which it did on virtually every aspect of each of the calculations at issue, I prefer the evidence of each of Mr. Milburn and Mr. Soriano.

[554] I do not propose to undertake a granular review of all such differences. In my view, given the fundamental evidentiary problems reflected in the plaintiff's approach to the calculation of damages, and in particular the failure to prove, by proper evidence before the court, the entire ALD half of the equation on which it relies, even leaving aside the problems of foreseeability and proximity in its 'deepening insolvency' theory of damages, the plaintiff cannot be taken to have proved any damages at all.

[555] I do note that, on the ELD side of the equation, as referenced in passing above, Mr. Soriano, in particular, opined that the evidence he reviewed did not show Cash Store to be insolvent as of Mr. Pappas' proposed Measurement Dates.

[556] To the contrary, Mr. Soriano observed that Cash Store had a long history of profitable operations in the years leading up to 2011, had an historic excess of working capital, and was current in respect of its ordinary course obligations.

[557] Moreover, Cash Store had historically paid dividends from 2008 to 2011, from surplus cash (being cash flow not required to maintain operations).

[558] In terms of Cash Store's forecasted operating performance, Mr. Soriano relied on numerous contemporaneous management forecasts of revenue, branch operating margin, and EBITDA (supported and adopted by EY and Canaccord in their work in the 2011-2012 period). He also reviewed and considered third-party projections relative to Cash Store, including by acknowledged experts in the payday loan industry, which were in a range similar to management prepared forecasts. All of these forecasts projected continued growth and profitability.

[559] Using those inputs, Mr. Soriano undertook a cash flow test that showed that, as at September 30 and December 31, 2011, Cash Store was projected to generate sufficient cash flow to settle its obligations as they came due. He also prepared a related sensitivity analysis to test the cash flow under different growth and margin assumptions, which did not impact the conclusion.

[560] With respect to the balance sheet test, Mr. Soriano conducted a discounted cash flow valuation (which he described as the "gold standard" in valuation) and concluded that Cash Store had positive equity value in 2011 (meaning that the fair market value of its net assets was greater than the fair market value of its liabilities). Mr. Soriano tested this conclusion using a market approach (using both Cash Store's share price and peer group public companies) which did not impact the conclusion.

[561] In the result, Mr. Soriano concluded that Cash Store was solvent as at September 30 and December 31, 2011. This opinion is consistent with Cash Store's historical performance and consistent with the fact that Cash Store continued to operate for about 2.5 years after those dates, notwithstanding the ongoing and increasing regulatory pressure on its operations, and notwithstanding the financial impact of the overpayment for the Loan Portfolio.

[562] I accept Mr. Soriano's evidence, and therefore find that neither the ELD nor the ALD side of Mr. Pappas' opinion is supported by the evidence.

(C) The Claim for Disgorgement

[563] As noted near the outset of this endorsement, CS Estate also claims disgorgement, from Cassels, of the total fees paid by Cash Store to Cassels between October 2009 and April 2014.

[564] I have already determined that CS Estate's claim against Cassels for a breach of fiduciary duty must fail.

[565] However, I note nonetheless that, by pitching its claim as seeking a disgorgement of all fees paid to Cassels, the plaintiff again misses the mark. While a claim for disgorgement of profits is potentially tenable, CS Estate conflates disgorgement of profits with disgorgement of fees. There is no evidence before me as to what portion of the overall fees charged reflects profits.

[566] Even in cases in which courts have ordered disgorgement of profits, including in cases in which courts have found significant breaches of fiduciary duty (see for example *Morris v. Jackson*, (1984), 27 A.C.W.S. (2d) 280, O.J. No. 1341 (Ont. H.C.) and *Strother v. 3464920 Canada Inc.*, 2007 SCC 24, [2007] 2 S.C.R. 177), courts have nonetheless allowed faithless fiduciary lawyers to keep the payments properly attributable to legal fees.

[567] As noted, in the case of FSC Abel (Mr. Stein's company), that company lost \$500,000 of its \$600,000 investment. There is no profit for FSC Abel to disgorge.

X. The Limitations Defence

[568] Both defendants take the position that CS Estate's claim is statute-barred.

[569] It is common ground that the claims were commenced by Notice of Action dated November 27, 2014.

[570] It is also common ground that the relevant limitation period is the two-year limitation set out in the *Limitations Act*, S.O. 2002, c. 24 (the "*Limitations Act*").

[571] Subsection 5(1) of the *Limitations Act* sets out the test for discoverability as follows :

“5(1) A claim is discovered on the earlier of,

- (a) the day on which the person with the claim first knew,
 - (i) that the injury, loss or damage had occurred,
 - (ii) that the injury, loss or damage was caused by or contributed to by an act or omission,
 - (iii) that the act or omission was that of the person against whom the claim is made, and
 - (iv) that, having regard to the nature of the injury, loss or damage, a proceeding would be an appropriate means to seek to remedy it; and
- (b) the day on which a reasonable person with the abilities and in the circumstances of the person with the claim first ought to have known of the matters referred to in clause (a).”

[572] Subsection 5(2) of the *Limitations Act* sets out the presumption that:

“(2) A person with a claim shall be presumed to have known of the matters referred to in clause (1)(a) on the day the act or omission on which the claim is based took place, unless the contrary is proved.”

[573] The plaintiff asserts that the limitation clock did not start running until November 23, 2012. It says that “The question of whether a restatement of prior financial statements was necessary only emerged in late November 2012, with the delivery of Mr. Warnock's November 23, 2012 memorandum identifying a potential problem with the reported value of the loans purchased under the Loan Internalization, based on lower recoveries on collections than had been previously reported.”

[574] The defendants each say that the facts on which the claim is based against them – the earlier restatement of the 2011 financial statements in the case of KPMG, and the earlier ongoing exchanges with provincial regulators about Cash Store’s regulatory compliance in the case of Cassels, were in each case known well before Mr. Warnock’s memo of November 23, 2012.

[575] In my view, while there is merit to those submissions, there is a bigger problem for the plaintiff – in tying the commencement of the running of the limitation to knowledge that the Loan Portfolio may have been overvalued.

[576] That is, in Mr. Woollcombe’s letter to Cash Store’s board of directors dated August 27, 2012, Mr. Woollcombe makes specific allegations that the value of the Loan Portfolio acquired in the LIT was overstated in Cash Store’s public disclosures.

[577] In my view CS Estate cannot credibly say, if it asserts that the limitation period only began to run when it had knowledge that the Loan Portfolio was (or may) have been overvalued, that it can ignore Mr. Woollcombe’s allegations to that effect and only accept knowledge of the issue when it was later raised by Mr. Warnock.

[578] For this reason, I find that CS Estate’s claims are also statute-barred.

OVERALL CONCLUSION

[579] For the reasons set out in detail above, I dismiss the plaintiff’s claims.

COSTS

[580] It follows that the defendants are entitled to their costs of this action. I do not know, of course, whether there are any offers to settle that should be taken into account in assessing costs, or other factors that the parties say I should consider.

[581] I direct that the defendants provide costs outlines, together with written submissions on costs not to exceed five pages in length, within 10 days of the release of this decision.

[582] The plaintiff will then have 14 further days within which to deliver responding costs submissions, in the plaintiff’s case not to exceed seven pages in length. The plaintiff has the option of submitting its costs outline (but should consider the risk that a failure to do so may lead to an adverse inference).

Gratitude to Counsel

[583] I should say before concluding this endorsement that I am grateful to all counsel in this matter.

[584] As will be evident, this was a complex and hotly contested matter, and the trial was completed on the basis of an agreed but tight timetable.

[585] Despite the pressures that this combination of circumstances created, all counsel maintained at all times admirable levels of cooperation, civility and professionalism.

[586] Counsel's presentation of the evidence, and their submissions, both written and oral, were also first rate, and I am indebted to counsel for this excellent work.

W.D. BLACK J.

Released: October 14, 2025