

Court File No. CV-22-00685736-00CL

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

**IN THE MATTER OF THE *CREDIT UNIONS AND CAISSES POPULAIRES ACT, 2020*,
S.O 2020, C.36, SCHED. 7, AS AMENDED**

AND IN THE MATTER OF PACE SAVINGS & CREDIT UNION LIMITED

**APPLICATION OF PACE SAVINGS & CREDIT UNION LIMITED UNDER SECTION
240 OF THE *CREDIT UNIONS AND CAISSES POPULAIRES ACT, 2020*, S.O. 2020, C. 36,
SCHED. 7, AS AMENDED**

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S.O 2020, C.36, SCHED. 7, AS AMENDED**

AND IN THE MATTER OF PACE SAVINGS & CREDIT UNION LIMITED

**APPLICATION OF PACE SAVINGS & CREDIT UNION LIMITED UNDER SECTION
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3 Draft Order

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NOTICE OF MOTION

KPMG INC. (“KPMG”), in its capacity as Court-Appointed Liquidator of Pace Savings & Credit Union Limited (the “**Liquidator**”), will make a motion to a Judge of the Ontario Superior Court of Justice (Commercial List) on Wednesday, February 8, 2023, at 12 p.m., or as soon after that time as the motion can be heard, via Zoom coordinates to be provided.

PROPOSED METHOD OF HEARING: The motion is to be heard:

- In writing under subrule 37.12.1 (1);
- In writing as an opposed motion under subrule 37.12.1 (4);
- In person
- By telephone conference
- By video conference

THE MOTION IS FOR:

1. an order approving the Former Directors Settlement Agreement (defined below);
2. an order approving the CUMIS Settlement Agreement (defined below);
3. an order sealing the Confidential Appendix to the First Report of the Liquidator dated January 27, 2023 (the “**First Report**”); and
4. such further and other relief as this Honourable Court may deem just.

THE GROUNDS FOR THE MOTION ARE:

Introduction

1. On August 24, 2022, PACE Savings & Credit Union Limited (“**PCU**” or the “**Credit Union**”) was ordered to be wound up pursuant to section 240 of the *Credit Unions and Caisses Populaires Act, 2020* (the “**CUCPA**”) by an Order of this Court, and KPMG was appointed as Liquidator.

Recovery Litigation

2. Prior to the Liquidator’s appointment, on March 18, 2019, PCU commenced an action against the former President and the former Chief Executive Officer (“**CEO**”) of the Credit Union (Larry and Phillip Smith (the “**Smiths**”)), their associated corporations and affiliates, certain of the Credit Union’s former directors (the “**Former Directors**”), and a number of other parties who PCU alleges received improper benefits from the Credit Union (the “**Claim Against Smiths et al**”). This claim advances causes of action including breach of fiduciary duty, fraud, conspiracy, breach of contract and employment duties, breach of trust, knowing proceeds of breach of trust, conversion, unjust enrichment and negligence against the Smiths, the Former Directors, and the other parties.

3. Before issuing this claim, PCU sought and obtained an interim *Mareva* injunction against the Smiths. The Credit Union and the Smiths subsequently agreed to the terms of a permanent preservation order which was made on May 7, 2019, and remains in effect.

4. The defendants to this claim deny the allegations, and several of them have commenced counterclaims against PCU. The Smiths have commenced third-party claims against two of the

Credit Union's former directors and Phillip Smith also brought a separate claim for wrongful dismissal against the Credit Union in September 2019.

5. On February 28, 2022, PCU also commenced an action against CUMIS General Insurance Company (“**CUMIS**”) in relation to a claim detailed in a proof of loss filed by the Credit Union dated October 16, 2019 under a fidelity insurance coverage bond issued by CUMIS, in respect of losses incurred by PCU in connection with various dishonest acts of the former President, and CEO of the Credit Union (the “**CUMIS Fidelity Bond Claim**”).

6. The above claims of the Credit Union and all related counterclaims, crossclaims and third-party claims are referred to herein collectively as the “**Recovery Litigation**”.

Status of the Recovery Litigation

7. The Recovery Litigation is currently pending before the Ontario Superior Court of Justice under three separate actions¹. Pleadings have been exchanged between the parties, but documentary and oral discovery have not yet taken place.

Settlements in the Recovery Litigation

8. The main parties to the Recovery Litigation agreed to participate in a mediation session in an effort to try and settle all claims. The mediation also addressed the CUMIS Fidelity Bond Claim. The mediation took place on November 28 and 29 and December 1, 2022.

¹ The main action bears Court File No. CV-19-00616388-00CL, the action against CUMIS bears Court File No. CV-22-00677550 and Phillip Smith’s wrongful dismissal action bears Court File No. CV-19-00628710.

9. While a global settlement was not reached, the mediation resulted in a partial settlement as follows:
- a. a settlement agreement dated December 1, 2022 between PCU, by the Liquidator, and the Former Directors (the “**Former Directors Settlement Agreement**”); and
 - b. a settlement agreement dated December 1, 2022, between PCU, by the Liquidator, and CUMIS in respect of the CUMIS Fidelity Bond Claim (the “**CUMIS Settlement Agreement**”, and together with the Former Directors Settlement Agreement, the “**Settlement Agreements**”).
10. The Former Directors Settlement Agreement contains the following key terms²:
- a. The Former Directors shall cause CUMIS to pay the Settlement Funds within 30 days following the effective date of the Former Directors Settlement Agreement;
 - b. On the effective date, the parties will enter into a full and final mutual release which shall be held in escrow until PCU’s receipt of the Settlement Funds;
 - c. PCU will amend the Statement of Claim in the Recovery Litigation to remove the claims against the Former Directors and to clarify that any damages it is seeking from the Non-Settling Defendants do not include any amount apportionable to the fault or negligence of the Former Directors;

² Capitalized terms not defined herein have the meaning defined in the Former Directors Settlement Agreement.

- d. PCU will obtain orders dismissing the Recovery Litigation as against the Former Directors. The Former Directors will consent to dismissal of their counterclaim against PCU;
- e. If requested by PCU, the Former Directors shall cooperate with counsel for PCU and/or the Liquidator in the prosecution of the Recovery Litigation against the Non-Settling Defendants, including by appearing and giving sworn evidence as witnesses at the trial of the Recovery Litigation as against the Non-Settling Defendants. PCU will pay the reasonable legal fees incurred by the Former Directors in connection with such cooperation;
- f. CUMIS will not rely on the inclusion of an obligation to provide evidence in paragraph 5 of the Former Directors Settlement Agreement to allege that it constitutes a basis for denial of coverage. Should PCU exercise any rights to obtain such evidence, CUMIS may allege that it constitutes a basis for denial of coverage and PCU will be free to allege it does not constitute such a breach;
- g. The Liquidator will seek an order from the Court approving the terms of the Former Directors Settlement Agreement on notice to all of the parties to the Recovery Litigation and CUMIS. The Former Directors and CUMIS will consent to the order; and
- h. PCU will disclose the existence and terms of the Former Directors Settlement Agreement to the Non-Settling Defendants as required by law and as necessary to obtain the Approval Order. The parties shall otherwise keep the existence and terms of the Former Directors Settlement Agreement confidential and shall not reveal its

existence and terms except to their respective legal and financial advisors and insurers, or as otherwise required by law.

11. The CUMIS Settlement Agreement contains the following key terms³:
 - a. CUMIS shall pay the Settlement Funds from the CUMIS Fidelity Bond within 30 days following the effective date of the CUMIS Settlement Agreement;
 - b. On the effective date, the parties will enter into a full and final mutual release of the CUMIS Fidelity Bond Claim and any claims under the EPL Policy which shall be held in escrow until PCU's receipt of the Settlement Funds;
 - c. CUMIS agrees that it has waived or will waive any subrogation and/or recovery rights which arose or may otherwise arise under the terms of the CUMIS Fidelity Bond or the EPL Policy;
 - d. PCU will obtain an order dismissing the action in relation to the Fidelity Bond Claim on a with-prejudice and without-costs basis; and
 - e. PCU will seek an order from the Court approving the terms of the CUMIS Settlement Agreement. CUMIS will consent to the order.

Court Approval of the Settlement Agreements

12. The Liquidator is seeking Court approval of the Settlement Agreements pursuant to their terms.

³ Capitalized terms not defined herein have the meaning defined in the CUMIS Settlement Agreement.

13. In the view of the Liquidator, the terms of the Settlement Agreements are fair and reasonable, they provide substantial benefits to the Credit Union's stakeholders, and they are consistent with the purpose and spirit of the winding up provisions of the CUCPA.

14. The quantum of the Settlement Funds and other information contained in Confidential Appendix "A" are not being publicly disclosed. The Liquidator respectfully requests an order sealing Confidential Appendix "A" until further order of the Court to maintain its confidentiality during the pendency of the Claim Against Smiths et al. It contains commercially sensitive information, public disclosure of which would be materially prejudicial to the interests of PCU and its stakeholders, which have an interest in maximizing recoveries from those defendants who have not settled. There is no alternative measure available to protect this information, and no party is materially prejudiced by the sealing of this information.

Other

15. Rules 1.04, 1.05, 2.01, 2.03, 3.02, 20 and 37 of the *Rules of Civil Procedure*, R.R.O. 1990, Reg. 194, as amended.

16. Such further and other grounds as counsel for the Investors may advise and this Honourable Court may permit.

THE FOLLOWING DOCUMENTARY EVIDENCE will be used at the hearing of the motion:

1. the First Report; and
2. such further and other materials as counsel may advise and this Honourable Court may permit.

Date: January 27, 2023

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SUPERIOR COURT OF JUSTICE
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PROCEEDING COMMENCED AT
TORONTO

NOTICE OF MOTION

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**FIRST REPORT OF KPMG INC. in its capacity as
LIQUIDATOR OF PACE SAVINGS & CREDIT UNION LIMITED**

JANUARY 27, 2023

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I. INTRODUCTION

1. On August 24, 2022, PACE Savings & Credit Union Limited (“PCU” or the “**Credit Union**”) was ordered to be wound up pursuant to section 240 of the *Credit Unions and Caisses Populaires Act, 2020* (the “**CUCPA**”) by an Order (the “**Liquidation Order**”) of the Ontario Superior Court of Justice (Commercial List) (the “**Court**”), and KPMG Inc. (“**KPMG**”) was appointed as liquidator (in such capacity, the “**Liquidator**”) of all the remaining assets, undertakings and properties of PCU. A copy of the Liquidation Order is attached hereto as **Appendix “A”**.
2. Prior to the Liquidator’s appointment, on March 18, 2019, PCU commenced a claim in the Ontario Superior Court of Justice (Commercial List) bearing Court File No. CV-19-00616388-00CL against the former President and the former Chief Executive Officer (“**CEO**”) of the Credit Union (Larry and Phillip Smith), their associated corporations and affiliates, certain of the Credit Union’s former directors, and a number of other parties (the “**Claim Against Smiths et al**”).
3. On February 28, 2022, PCU also commenced an action bearing Court File No. CV-22-00677550 against CUMIS General Insurance Company (“**CUMIS**”) in relation to a claim detailed in a proof of loss filed by the Credit Union dated October 16, 2019 under a fidelity insurance coverage bond issued by CUMIS (the “**CUMIS Fidelity Bond**”), in respect of losses incurred by PCU in connection with various dishonest acts of the former President and CEO of the Credit Union (the “**CUMIS Fidelity Bond Claim**”).
4. The above claims of the Credit Union and all related counterclaims, crossclaims and third-party claims are referred to herein collectively as the “**Recovery Litigation**”.

II. PURPOSE OF REPORT

5. The purpose of this report, which is the Liquidator’s first report to the Court (the “**First Report**”) is to provide information to this Honourable Court in respect of:
 - a. Certain background on PCU;
 - b. The history of the Recovery Litigation and related mediation;

- c. Details of settlements that have been entered into by the Liquidator in relation to the Recovery Litigation; and
- d. The Liquidator's motion for orders substantially in the forms attached to the Liquidator's Notice of Motion seeking approval of the aforesaid settlements and ancillary relief.

III. TERMS OF REFERENCE

6. In preparing this First Report, the Liquidator has been provided with, and has relied upon, the books and records and other information of PCU, including unaudited financial information and information provided by former management, advisors, and the former administrator of the Credit Union (collectively, the "**Information**"). In accordance with industry practice, except as otherwise described in this First Report, the Liquidator has reviewed the Information for reasonableness, internal consistency and use in the context in which it was provided. However, the Liquidator has not audited or otherwise attempted to verify the accuracy or completeness of the Information in a manner that would wholly or partially comply with Generally Accepted Auditing Standards ("**GAAS**") pursuant to the Chartered Professional Accountants of Canada Handbook and, accordingly, the Liquidator expresses no opinion or other form of assurance contemplated under GAAS in respect of the Information.
7. Future oriented financial information reported or relied on in this First Report is based on assumptions regarding future events; actual results may vary from this forecast and such variations may be material.
8. Copies of the Liquidator's reports and all motion records and Orders in the liquidation proceedings are available on the Liquidator's website at <http://www.kpmg.com/ca/pacecu>.
9. Unless otherwise stated, all monetary amounts contained herein are expressed in Canadian dollars.

IV. BACKGROUND ON PCU

10. PCU was formerly an operating credit union headquartered in Vaughan, Ontario, which had approximately 34,000 members, 13 branches in the greater Toronto and surrounding area, and approximately \$900 million in assets on its balance sheet. The Credit Union is incorporated under the CUCPA and is regulated by the Financial Services Regulatory Authority of Ontario (“FSRA”).
11. Since September 28, 2018, and up until the Liquidator’s appointment, PCU was under administration by FSRA, formerly the Deposit Insurance Corporation of Ontario (“DICO”). The administration was initiated by DICO in response to, among other things, certain misconduct and regulatory breaches committed by the Credit Union's former President and CEO. The affidavit of Mehrdad Rastan, Executive Vice-President, Credit Union & Insurance Prudential of FSRA, sworn on August 17, 2022 (the “**Rastan Affidavit**”) in support of the motion brought by FSRA seeking the appointment of KPMG as Liquidator, sets out in further detail the background relating to the administration of the Credit Union. A copy of the Rastan Affidavit (without exhibits) is attached hereto as **Appendix “B”**.
12. As discussed in detail in the Rastan Affidavit, at the outset of the administration, it was DICO’s intent, in its capacity as administrator of the Credit Union (in such capacity, the “**Administrator**”¹), to resolve the governance issues which gave rise to the administration and return the Credit Union to a member-controlled governance in due course. For a number of reasons, including the onset of the COVID-19 pandemic, which are more particularly described in the Rastan Affidavit, the Administrator ultimately determined that the Credit Union’s financial position had deteriorated to such extent that it would not be possible to do so. Accordingly, the Administrator made the decision to pursue a purchase and assumption transaction for the Credit Union and a sale of PCU’s then wholly-owned subsidiary, Continental Currency Exchange (“CCE”), through separate but parallel competitive sale processes.

¹ FSRA succeeded DICO as administrator of PCU and accordingly, the defined term ‘Administrator’ also refers to FSRA in its capacity as administrator of the Credit Union.

13. On January 11, 2022, PCU, FSRA and DUCA Credit Union entered into a share purchase agreement in respect of the sale of all of the issued and outstanding share capital of CCE (the “**CCE Transaction**”). The CCE Transaction closed on March 31, 2022.
14. On April 20, 2022, PCU and FSRA entered into a purchase and assumption agreement (the “**Purchase and Assumption Agreement**”) with Alterna Savings and Credit Union Limited (“**Alterna**”). Pursuant to the Purchase and Assumption Agreement, Alterna acquired substantially all of the business and assets and assumed substantially all of the liabilities, member deposits and employees of the Credit Union except for certain excluded assets and liabilities (the “**Purchase and Assumption Transaction**”). The Purchase and Assumption Transaction closed on June 30, 2022. Alterna has agreed to provide certain transition services to PCU for a limited period of time. The services include various finance and accounting services and information technology services for the purposes of facilitating the Credit Union's dealing with its remaining assets and liabilities.
15. Following the completion of the Purchase and Assumption Transaction, PCU no longer had any active business operations (other than a small prepaid card business which is being wound down) and accordingly, for the reasons set out in the Rastan Affidavit, the Administrator sought the appointment of KPMG as Liquidator for purposes of dealing with the Credit Union’s remaining assets and liabilities and ultimately winding down the Credit Union.
16. The remaining assets and liabilities of the Credit Union include, among other things, proceeds from the CCE Transaction, the prepaid card business and related litigation, claims asserted in the Recovery Litigation, certain member deposits and accounts, certain loans, insurance claims or entitlements to proceeds of insurance, certain funds held in trust by the Credit Union for the benefit of former employees, and claims made in the winding-up proceedings of PACE Securities Corporation and its direct and indirect subsidiaries. Further details regarding PCU’s remaining assets and liabilities are provided in the Rastan Affidavit. In addition to the above, the investment, profit, and membership shareholdings of PCU’s approximately 34,000 members remain with the Credit Union.

V. RECOVERY LITIGATION

Background of the Recovery Litigation

Claim Against Smiths et al

17. Attached hereto as **Appendix “C”** is a copy of PCU’s Further Amended Fresh-as-Amended Statement of Claim dated October 18, 2022², commenced against Larry and Phillip Smith (the “**Smiths**”), their associated corporations and affiliates, certain of the Credit Union's former directors (the “**Former Directors**”) and a number of other parties who PCU alleges received improper benefits from the Credit Union. The Claim Against Smiths et al advances causes of action including breach of fiduciary duty, fraud, conspiracy, breach of contract and employment duties, breach of trust, knowing proceeds of breach of trust, conversion, unjust enrichment and negligence against the Smiths, the Former Directors, and the other parties.
18. Before issuing the claim, PCU sought and obtained an interim *Mareva* injunction against the Smiths. The Credit Union and the Smiths subsequently agreed to the terms of a permanent preservation order which was made on May 7, 2019, and remains in effect.
19. The defendants deny the allegations, and several have commenced counterclaims against PCU. The Smiths have commenced third-party claims against two of the Credit Union's former directors and Phillip Smith also brought a separate claim for wrongful dismissal against the Credit Union in September 2019. A copy of the Further Amended Statement of Defence, Counterclaim and Crossclaim of Larry Smith, 1428245 Ontario Ltd. and 809755 Ontario Limited (collectively, the “**Larry Parties**”) dated October 26, 2022³, is attached hereto as **Appendix “D”**. A copy of the Statement of Defence, Counterclaim and Crossclaim of Phillip Smith dated July 8, 2021, is attached hereto as **Appendix “E”**. A copy of Phillip Smith’s Statement of Claim dated October 7, 2019, is attached hereto as **Appendix “F”**. A copy of the Statement of Defence, Counterclaim and Crossclaim of the Former Directors dated June 10, 2022, is attached hereto as **Appendix “G”**. A copy of the Statement of Defence and Counterclaim of Brian Hogan dated March 25, 2021, is attached

² PCU’s Further Amended Fresh-as-Amended Statement of Claim dated October 18, 2022, has not yet been filed.

³ The Further Amended Statement of Defence, Counterclaim and Crossclaim of the Larry Parties dated October 26, 2022, has not yet been filed.

hereto as **Appendix “H”**. A copy of the Amended Statement of Defence, Counterclaim and Crossclaim of Frank Klees and Klees & Associated Ltd. (collectively, the “**Klees Parties**”) dated June 8, 2022, is attached hereto as **Appendix “I”**.

20. PCU has a directors and officers insurance policy (the “**D&O Policy**”) which provides coverage to every director or officer of the Credit Union in connection with any loss arising from a claim made against them for which they are not indemnified by PCU, up to a limit of \$15 million. It covers losses arising from “wrongful acts”, a term which includes breach of duty, neglect, and error. The D&O Policy also restricts coverage for claims brought by PCU, except where the claim is, *inter alia*, a derivative claim. The D&O Policy has a diminishing limit given that the defence costs of the directors and officers are covered under the policy.
21. Certain of the Credit Union’s former directors and officers (including the Smiths) sought coverage from CUMIS in respect of PCU’s claims against them for breach of duty and negligence. CUMIS denied defence coverage on the basis that the claim was brought by PCU itself. The directors and officers brought an application for coverage and in an endorsement dated May 18, 2021, the Court found that PACE’s claim was a derivative action, and that CUMIS is therefore obliged to defend the directors and officers. Although CUMIS has not formally conceded any obligation to indemnify under the D&O Policy, PCU has taken the position that CUMIS will be liable to the directors and officers for any damages award against them in favour of PCU in the Recovery Litigation, up to the remaining policy limit.

CUMIS Fidelity Bond Claim

22. The CUMIS Fidelity Bond provides fidelity insurance coverage with an effective date of January 1, 2018, and an expiry date of January 1, 2019. Pursuant to the terms of the CUMIS Fidelity Bond, CUMIS is liable to indemnify PCU for covered losses, which include losses resulting from dishonest or fraudulent acts of any director, employee, or contractor of the Credit Union to a maximum of \$10.025 million.
23. PCU had claimed the maximum amount available under the CUMIS Fidelity Bond pursuant to the CUMIS Fidelity Bond Claim. Prior to the settlement discussed further in this report, CUMIS had made a partial payment to PCU in the amount of approximately \$1

million. PCU commenced an action against CUMIS in relation to the unpaid portion of the CUMIS Fidelity Bond Claim. A copy of PCU's Amended Statement of Claim dated August 5, 2022, is attached hereto as **Appendix "J"**. A copy of CUMIS' Statement of Defence dated October 12, 2022, is attached hereto as **Appendix "K"**.

Status of the Recovery Litigation

24. The Recovery Litigation is currently pending before the Ontario Superior Court of Justice under three separate actions⁴. Pleadings have been exchanged between the parties, but documentary and oral discovery have not yet taken place.
25. The Smiths and the Former Directors brought motions to dismiss or permanently stay PCU's claims against them as an abuse of process on the basis of an alleged failure to immediately disclose settlement agreements that PACE entered into in 2020 and 2021 with other defendants in the Recovery Litigation (the "**Stay Motions**").
26. The Stay Motions were scheduled to be heard on December 19, 2022; however, as a result of scheduling issues, the Court vacated that date. The Stay Motions are now scheduled to be heard on March 20, 2023.

Efforts to Settle the Recovery Litigation and the Recent Mediation

27. The main parties to the Recovery Litigation agreed to participate in a mediation session before Larry Banack in an effort to try and settle all claims. The mediation took place on November 28 and 29 and December 1, 2022.
28. While a global settlement was not reached, the mediation did result in two settlements which are discussed further in this report. Larry Banack continues to have discussions with the non-settling parties regarding a potential global settlement.

VI. SETTLEMENTS IN THE RECOVERY LITIGATION

29. The mediation before Larry Banack resulted in a partial settlement of the Claim Against Smiths et al and a settlement of the CUMIS Fidelity Bond Claim as follows:

⁴ The main action bears Court File No. CV-19-00616388-00CL, the action against CUMIS bears Court File No. CV-22-00677550 and Phillip Smith's wrongful dismissal action bears Court File No. CV-19-00628710.

- a. A settlement agreement dated December 1, 2022, between PCU, by the Liquidator, and the Former Directors (the “**Former Directors Settlement Agreement**”). A copy of the Former Director Settlement Agreement (redacted to remove the settlement amount) is attached hereto as **Appendix “L”**; and
- b. A settlement agreement dated December 1, 2022, between PCU, by the Liquidator, and CUMIS in respect of the CUMIS Fidelity Bond Claim (the “**CUMIS Settlement Agreement**”, and together with the Former Directors Settlement Agreement, the “**Settlement Agreements**”). A copy of the CUMIS Settlement Agreement (redacted to remove the settlement amount) is attached hereto as **Appendix “M”**.

The Former Directors Settlement Agreement

30. The Former Directors Settlement Agreement contains the following key terms⁵:
 - a. The Former Directors shall cause CUMIS to pay the Settlement Funds within 30 days following the effective date of the Former Directors Settlement Agreement;
 - b. On the effective date, the parties will enter into a full and final mutual release of the claims against the Former Directors which shall be held in escrow until PCU’s receipt of the Settlement Funds;
 - c. PCU will amend the Statement of Claim in the Recovery Litigation to remove the claims against the Former Directors and to clarify that any damages it is seeking from the Non-Settling Defendants do not include any amount apportionable to the fault or negligence of the Former Directors;
 - d. PCU will obtain orders dismissing the Recovery Litigation as against the Former Directors. The Former Directors will consent to dismissal of their counterclaim against PCU;
 - e. If requested by PCU, the Former Directors shall cooperate with counsel for PCU and/or the Liquidator in the prosecution of the Recovery Litigation against the Non-Settling Defendants, including by appearing and giving sworn evidence as witnesses at the trial of the Recovery Litigation as against the Non-Settling Defendants. PCU will pay the

⁵ Capitalized terms not defined herein have the meaning defined in the Former Directors Settlement Agreement.

- reasonable legal fees incurred by the Former Directors in connection with such cooperation;
- f. CUMIS will not rely on the inclusion of an obligation to provide evidence in paragraph 5 of the Former Directors Settlement Agreement to allege that it constitutes a basis for denial of coverage. Should PCU exercise any rights to obtain such evidence, CUMIS may allege that it constitutes a basis for denial of coverage and PCU will be free to allege it does not constitute such a breach;
 - g. The Liquidator will seek an order from the Court approving the terms of the Former Directors Settlement Agreement on notice to all of the parties to the Recovery Litigation and CUMIS. The Former Directors and CUMIS will consent to the order; and
 - h. PCU will disclose the existence and terms of the Former Directors Settlement Agreement to the Non-Settling Defendants as required by law and as necessary to obtain the Approval Order. The parties shall otherwise keep the existence and terms of the Former Directors Settlement Agreement confidential and shall not reveal its existence and terms except to their respective legal and financial advisors and insurers, or as otherwise required by law.

The CUMIS Settlement Agreement

31. The CUMIS Settlement Agreement contains the following key terms⁶:
- a. CUMIS shall pay the Settlement Funds from the CUMIS Fidelity Bond within 30 days following the effective date of the CUMIS Settlement Agreement;
 - b. On the effective date, the parties will enter into a full and final mutual release of the CUMIS Fidelity Bond Claim and any claims under the EPL Policy which shall be held in escrow until PCU's receipt of the Settlement Funds;
 - c. CUMIS agrees that it has waived or will waive any subrogation and/or recovery rights which arose or may otherwise arise under the terms of the CUMIS Fidelity Bond or the EPL Policy;

⁶ Capitalized terms not defined herein have the meaning defined in the CUMIS Settlement Agreement.

- d. PCU will obtain an order dismissing the action in relation to the Fidelity Bond Claim on a with-prejudice and without-costs basis; and
- e. PCU will seek an order from the Court approving the terms of the CUMIS Settlement Agreement. CUMIS will consent to the order.

Status of the Settlements

- 32. PCU's counsel in the Recovery Litigation, Lax O'Sullivan Lisus Gottlieb LLP, provided written notice of the Settlement Agreements, including a redacted copy of the Former Directors Settlement Agreement, to all defendants in the Recovery Litigation on December 1, 2022.
- 33. The Settlement Funds under the Settlement Agreements were paid by CUMIS to the Liquidator on December 22, 2022.
- 34. All releases under the Settlement Agreements have been exchanged.

Court Approval of the Settlement Agreements

- 35. The Liquidator is seeking Court approval of the Settlement Agreements pursuant to their terms.
- 36. Attached hereto as **Confidential Appendix "A"** is a summary of relevant information pertaining to the Liquidator's decision to enter into the Settlement Agreements.
- 37. In the view of the Liquidator, the terms of the Settlement Agreements are fair and reasonable, they provide substantial benefits to the Credit Union's stakeholders, and they are consistent with the purpose and spirit of the winding up provisions of the CUCPA.
- 38. The quantum of the Settlement Funds and other information contained in Confidential Appendix "A" are not being publicly disclosed. The Liquidator respectfully requests an order sealing Confidential Appendix "A" until further order of the Court to maintain its confidentiality during the pendency of the Claim Against Smiths et al. It contains commercially sensitive information, public disclosure of which would be materially prejudicial to the interests of PCU and its stakeholders, which have an interest in maximizing recoveries from those defendants who have not settled. There is no alternative

measure available to protect this information, and no party is materially prejudiced by the sealing of this information.

VII. LIQUIDATOR'S CONCLUSIONS AND RECOMMENDATIONS

39. The Liquidator submits this First Report to the Court in support of the Liquidator's Motion for the relief as set out in the Notice of Motion and recommends that the Court grant such relief.

All of which is respectfully submitted at Toronto, Ontario this 27th day of January 2023.

**KPMG Inc.,
in its capacity as Liquidator of
Pace Savings & Credit Union Limited
and not in its personal capacity**



Per: _____

Anamika Gadia
Senior Vice President

TAB A

Court File No. CV-22-00685736-00CL

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

| | | |
|----------------|---|---------------------|
| THE HONOURABLE |) | WEDNESDAY, THE 24TH |
| |) | |
| JUSTICE CONWAY |) | DAY OF AUGUST, 2022 |

IN THE MATTER OF THE *CREDIT UNIONS AND CAISSES POPULAIRES ACT, 2020*, S.O. 2020, C. 36, SCHED. 7, AS AMENDED

AND IN THE MATTER OF PACE SAVINGS & CREDIT UNION LIMITED

APPLICATION OF PACE SAVINGS & CREDIT UNION LIMITED UNDER SECTION 240 OF THE *CREDIT UNIONS AND CAISSES POPULAIRES ACT, 2020*, S.O. 2020, C. 36, SCHED. 7, AS AMENDED

**ORDER
(WINDING UP & APPOINTING LIQUIDATOR)**

THIS APPLICATION made by the Applicant, PACE Savings & Credit Union Limited (the “**Applicant**” or “**Credit Union**”), by its administrator, Financial Services Regulatory Authority of Ontario (“**FSRA**”), for an Order pursuant to section 240 of the *Credit Unions and Caisses Populaires Act, 2020*, S.O. 2020, c. 36, Sched. 7, as amended (the “**CUCPA**”) winding up the Credit Union and appointing KPMG Inc. (“**KPMG**”) as liquidator (in such capacity, the “**Liquidator**”) without security, of all of the remaining assets, undertakings and properties of the Credit Union was heard this day at 330 University Avenue, Toronto, Ontario.

ON READING the affidavit of Mehrdad Rastan sworn August 17, 2022 (the “**Rastan Affidavit**”) and the Exhibits thereto and on hearing the submissions of counsel for FSRA, KPMG, Larry Smith, 1428245 Ontario Ltd., 809755 Ontario Ltd. and Phillip Smith (collectively,

the “**Recovery Litigation Parties**”), Peter Budd, and Frank Klees and on reading the consent of KPMG to act as the Liquidator,

1. THIS COURT ORDERS that the capitalized terms which are not defined herein have the meaning given to them in the Rastan Affidavit.

SERVICE

2. THIS COURT ORDERS that the time for service of the Notice of Application and the Application is hereby abridged and validated so that this motion is properly returnable today and hereby dispenses with further service thereof.

WINDING UP

3. THIS COURT ORDERS that the Credit Union be wound up pursuant to section 240 of the CUCPA and in accordance with the terms of this Order.

APPOINTMENT

4. THIS COURT ORDERS that, pursuant to section 240 of the CUCPA, KPMG is hereby appointed Liquidator, without security, of all of the remaining assets, undertakings and properties of the Credit Union, including all proceeds thereof (the “**Property**”).

LIQUIDATOR’S POWERS

5. THIS COURT ORDERS that the Liquidator is hereby empowered and authorized, but not obligated, to act at once in respect of the Property and, without in any way limiting the generality of the foregoing, the Liquidator is hereby expressly empowered and authorized to do any of the following where the Liquidator considers it necessary or desirable:

- (a) to take possession of and exercise control over the Property and any and all proceeds, receipts and disbursements arising out of or from the Property;
- (b) to receive, preserve, and protect the Property, or any part or parts thereof, including, but not limited to, the relocating of Property to safeguard it and the placement of such insurance coverage as may be necessary or desirable;
- (c) to manage, operate, and carry on the business of the Credit Union so far as may be necessary for the beneficial winding up of the Credit Union, including the powers to enter into any agreements, incur any obligations in the ordinary course of business, cease to carry on all or any part of the business, or cease to perform any contracts of the Credit Union;
- (d) without limiting the generality of (c), to manage, operate, and carry on the Prepaid Card Business so far as may be necessary for the beneficial winding up or transition of the Prepaid Card Business, including, without limitation, the authority to deal with the Prepaid Cardholder Amounts, which include any amounts held in one or more commercial accounts, at The Toronto-Dominion Bank or elsewhere, in the name of 1961783 Ontario Limited (the “**Prepaid Card Entity**”);
- (e) to engage consultants, appraisers, agents, experts, auditors, accountants, managers, counsel and such other persons from time to time and on whatever basis, including on a temporary basis, to assist with the exercise of the

Liquidator's powers and duties, including without limitation those conferred by this Order;

- (f) to receive and collect all monies and accounts now owed or hereafter owing to the Credit Union and to exercise all remedies of the Credit Union in collecting such monies, including, without limitation, to enforce any security held by the Credit Union;
- (g) to settle, extend or compromise any indebtedness owing to the Credit Union;
- (h) to execute, assign, issue and endorse documents of whatever nature in respect of any of the Property, whether in the Liquidator's name or in the name and on behalf of the Credit Union, for any purpose pursuant to this Order;
- (i) to initiate, prosecute and continue the prosecution of any and all proceedings and to defend all proceedings now pending or hereafter instituted with respect to the Credit Union, the Property or the Liquidator, including, without limitation, the Recovery Litigation and Other Ongoing Litigation, and to settle or compromise any such proceedings. The authority hereby conveyed shall extend to such appeals or applications for judicial review in respect of any order or judgment pronounced in any such proceeding;
- (j) to market any or all of the Property, including advertising and soliciting offers in respect of the Property or any part or parts thereof and negotiating such terms and conditions of sale as the Liquidator in its discretion may deem appropriate;

(k) to sell, convey, transfer, lease or assign the Property or any part or parts thereof out of the ordinary course of business,

(i) without the approval of this Court in respect of any transaction not exceeding \$250,000.00, provided that the aggregate consideration for all such transactions does not exceed \$750,000.00; and

(ii) with the approval of this Court in respect of any transaction in which the purchase price or the aggregate purchase price exceeds the applicable amount set out in the preceding clause;

and in each such case notice under subsection 63(4) of the Ontario *Personal Property Security Act* shall not be required.

(l) to apply for any vesting order or other orders necessary to convey the Property or any part or parts thereof to a purchaser or purchasers thereof, free and clear of any liens or encumbrances affecting such Property;

(m) to carry out a claims process for the purpose of identifying and determining claims against the Credit Union and/or its current and former directors and officers, as this Court may direct by further order made on not less than two weeks' notice to the Recovery Litigation Parties and to such other Persons as the Liquidator deems appropriate or this Court may direct;

(n) to bring a motion for the power to borrow monies it may consider necessary or desirable for the purpose of carrying out its mandate under this Order, if

necessary, on such terms and upon such security over the Property as the Court may determine on such motion, which motion shall be brought on not less than two weeks' notice to the Recovery Litigation Parties and to such other Persons as the Liquidator deems appropriate or this Court may direct;

- (o) to report to, meet with and discuss with such affected Persons (as defined below), including, without limitation, FSRA, as the Liquidator deems appropriate on all matters relating to the Property and the winding up, and to share information with such Persons, subject to such terms as to confidentiality as the Liquidator deems advisable;
- (p) to apply for any permits, licences, approvals or permissions as may be required by any governmental authority and any renewals thereof for and on behalf of and, if thought desirable by the Liquidator, in the name of the Credit Union;
- (q) to enter into agreements with any trustee in bankruptcy appointed in respect of the Credit Union, including, without limiting the generality of the foregoing, the ability to enter into occupation agreements for any property owned or leased by the Credit Union;
- (r) to exercise any shareholder, partnership, joint venture or other rights which the Credit Union may have, including, without limitation, with respect to the Prepaid Card Entity, as the Liquidator deems necessary or desirable in connection with the Prepaid Card Business;

- (s) to take any steps reasonably incidental to the exercise of these powers or the performance of any statutory obligations; and
- (t) after the monetization or other disposition of the Property, to distribute the proceeds thereof only in accordance with this Order or any subsequent order of this court,

and in each case where the Liquidator takes any such actions or steps, it shall be exclusively authorized and empowered to do so, to the exclusion of all other Persons (as defined below), including the Credit Union, and without interference from any other Person.

LIQUIDATION NOMINATION AGREEMENT

6. THIS COURT ORDERS that the terms of the Liquidation Nomination Agreement between FSRA and KPMG dated August 17, 2022, appended as Exhibit “K” to the Rastan Affidavit, are hereby approved, and the Liquidator is hereby authorized and directed to perform the obligations thereunder.

DUTY TO PROVIDE ACCESS AND CO-OPERATION TO THE LIQUIDATOR

7. THIS COURT ORDERS that (i) the Credit Union, (ii) all of its current and former directors, officers, employees, agents, accountants, legal counsel and shareholders, and all other persons acting on its instructions or behalf, and (iii) all other individuals, firms, corporations, governmental bodies or agencies, or other entities having notice of this Order (all of the foregoing, collectively, being “**Persons**” and each being a “**Person**”) shall forthwith advise the Liquidator of the existence of any Property in such Person’s possession or control, shall grant

immediate and continued access to the Property to the Liquidator, and shall deliver all such Property to the Liquidator upon the Liquidator's request.

8. THIS COURT ORDERS that all Persons shall forthwith advise the Liquidator of the existence of any books, documents, securities, contracts, orders, corporate and accounting records, and any other papers, records and information of any kind related to the business or affairs of the Credit Union, and any computer programs, computer tapes, computer disks, or other data storage media containing any such information (the foregoing, collectively, the "**Records**") in that Person's possession or control, and shall provide to the Liquidator or permit the Liquidator to make, retain and take away copies thereof and grant to the Liquidator unfettered access to and use of accounting, computer, software and physical facilities relating thereto, provided however that nothing in this paragraph 8 or in paragraph 9 of this Order shall require the delivery of Records, or the granting of access to Records, which may not be disclosed or provided to the Liquidator due to the privilege attaching to solicitor-client communication or due to statutory provisions prohibiting such disclosure.

9. THIS COURT ORDERS that if any Records are stored or otherwise contained on a computer or other electronic system of information storage, whether by independent service provider or otherwise, all Persons in possession or control of such Records shall forthwith give unfettered access to the Liquidator for the purpose of allowing the Liquidator to recover and fully copy all of the information contained therein whether by way of printing the information onto paper or making copies of computer disks or such other manner of retrieving and copying the information as the Liquidator in its discretion deems expedient, and shall not alter, erase or destroy any Records without the prior written consent of the Liquidator. Further, for the

purposes of this paragraph, all Persons shall provide the Liquidator with all such assistance in gaining immediate access to the information in the Records as the Liquidator may in its discretion require including providing the Liquidator with instructions on the use of any computer or other system and providing the Liquidator with any and all access codes, account names and account numbers that may be required to gain access to the information.

NO PROCEEDINGS AGAINST THE LIQUIDATOR

10. THIS COURT ORDERS that no proceeding or enforcement process in any court or tribunal (each, a “**Proceeding**”), shall be commenced or continued against the Liquidator except with the written consent of the Liquidator or with leave of this Court.

NO PROCEEDINGS AGAINST THE CREDIT UNION OR THE PROPERTY

11. THIS COURT ORDERS, subject to paragraph 12 of this Order, that no Proceeding against or in respect of the Credit Union or the Property shall be commenced or continued (including but not limited to the actions commenced by Ying Jiang against All Trans Financial Services Credit Union Limited in the Court of Queen’s Bench for Saskatchewan in Regina under Court File Q.B.G. 2024/14 and in the Supreme Court of British Columbia in Vancouver under Court File No. S-147229) except with the written consent of the Liquidator or with leave of this Court, and any and all Proceedings currently under way against or in respect of the Credit Union or the Property are hereby stayed and suspended pending further Order of this Court.

12. THIS COURT ORDERS that nothing in this Order shall:

- (a) affect or in any way restrain the continuation of any of the proceedings or claims asserted, or the enforcement of any orders made, in the Recovery Litigation (including, but not limited to, the motions brought by the Recovery Litigation Parties relating to settlement enforcement, stay of the Recovery Litigation, and preservation of claims, which motions are pending in the Recovery Litigation), and any order made in the Recovery Litigation shall be binding on the Liquidator; or
- (b) affect the Order of this Court dated December 22, 2020 in proceedings bearing court file number CV-20-00651509-00CL between the Applicant (as Applicant) and Arn Reisler, 1428245 Ontario Ltd, Larry Smith, Phillip Smith and Mary Benincasa (as Respondents).

NO EXERCISE OF RIGHTS OR REMEDIES

13. THIS COURT ORDERS that all rights and remedies against the Credit Union, the Liquidator, or affecting the Property, are hereby stayed and suspended except with the written consent of the Liquidator or leave of this Court, provided however that nothing in this paragraph shall (i) empower the Liquidator or the Credit Union to carry on any business which the Credit Union is not lawfully entitled to carry on, (ii) exempt the Liquidator or the Credit Union from compliance with statutory or regulatory provisions relating to health, safety or the environment, (iii) prevent the filing of any registration to preserve or perfect a security interest, or (iv) prevent the registration of a claim for lien.

NO INTERFERENCE WITH THE LIQUIDATOR

14. THIS COURT ORDERS that no Person shall discontinue, fail to honour, alter, interfere with, repudiate, terminate or cease to perform any right, renewal right, contract, agreement, licence or permit in favour of or held by the Credit Union, without written consent of the Liquidator or leave of this Court.

CONTINUATION OF SERVICES

15. THIS COURT ORDERS that all Persons having oral or written agreements with the Credit Union or statutory or regulatory mandates for the supply of goods and/or services, including without limitation, all computer software, communication and other data services, centralized banking services, payroll services, insurance, transportation services, utility or other services to the Credit Union are hereby restrained until further Order of this Court from discontinuing, altering, interfering with or terminating the supply of such goods or services as may be required by the Liquidator, and that the Liquidator shall be entitled to the continued use of the Credit Union's current telephone numbers, facsimile numbers, internet addresses and domain names, provided in each case that the normal prices or charges for all such goods or services received after the date of this Order are paid by the Liquidator in accordance with normal payment practices of the Credit Union or such other practices as may be agreed upon by the supplier or service provider and the Liquidator, or as may be ordered by this Court.

LIQUIDATOR TO HOLD FUNDS

16. THIS COURT ORDERS that all funds, monies, cheques, instruments, and other forms of payments received or collected by the Liquidator from and after the making of this Order from any source whatsoever, including without limitation the sale of all or any of the

Property and the collection of any accounts receivable in whole or in part, whether in existence on the date of this Order or hereafter coming into existence, may be deposited into existing accounts in the name of the Credit Union, or with respect to the Prepaid Card Business, in the existing accounts at The Toronto-Dominion Bank or elsewhere, or into one or more new accounts to be opened by the Liquidator, all of which shall be held by the Liquidator to be distributed in accordance with the terms of this Order or any further Order of this Court.

PIPEDA

17. THIS COURT ORDERS that, pursuant to clause 7(3)(c) of the Canada *Personal Information Protection and Electronic Documents Act*, the Liquidator shall disclose personal information of identifiable individuals to prospective purchasers or bidders for the Property and to their advisors, but only to the extent desirable or required to negotiate and attempt to complete one or more sales of the Property (each, a “Sale”). Each prospective purchaser or bidder to whom such personal information is disclosed shall maintain and protect the privacy of such information and limit the use of such information to its evaluation of the Sale, and if it does not complete a Sale, shall return all such information to the Liquidator, or in the alternative destroy all such information. The purchaser of any Property shall be entitled to continue to use the personal information provided to it, and related to the Property purchased, in a manner which is in all material respects identical to the prior use of such information by the Credit Union, and shall return all other personal information to the Liquidator, or ensure that all other personal information is destroyed.

LIMITATION ON THE LIQUIDATOR'S LIABILITY

18. THIS COURT ORDERS that the Liquidator shall incur no liability or obligation as a result of its appointment or the carrying out the provisions of this Order, save and except for any gross negligence or wilful misconduct on its part. Nothing in this Order shall derogate from the protections afforded the Liquidator by any applicable legislation.

LIQUIDATOR'S ACCOUNTS

19. THIS COURT ORDERS that the Liquidator and counsel to the Liquidator shall be paid their reasonable fees and disbursements incurred in relation to the winding up and liquidation of the Credit Union (including in connection with this application), in each case at their standard rates and charges unless otherwise ordered by the Court on the passing of accounts, and that the Liquidator and counsel to the Liquidator shall be entitled to and are hereby granted a charge (the "**Liquidator's Charge**") on the Property, as security for such fees and disbursements, both before and after the making of this Order in respect of these proceedings, and that the Liquidator's Charge shall form a charge on the Property in priority to all security interests, trusts, liens, charges and encumbrances, statutory or otherwise, in favour of any Person, but subordinate in priority to validly perfected security interests on the Property existing as of the date of this Order.

20. THIS COURT ORDERS that the Liquidator and its legal counsel shall pass its accounts from time to time, and for this purpose the accounts of the Liquidator and its legal counsel are hereby referred to a judge of the Commercial List of the Ontario Superior Court of Justice.

21. THIS COURT ORDERS that prior to the passing of its accounts, the Liquidator shall be at liberty from time to time to apply reasonable amounts, out of the monies in its hands, against its fees and disbursements, including legal fees and disbursements, incurred at the standard rates and charges of the Liquidator or its counsel, and such amounts shall constitute advances against its remuneration and disbursements when and as approved by this Court.

SERVICE AND NOTICE

22. THIS COURT ORDERS that the E-Service Protocol of the Commercial List (the “**Protocol**”) is approved and adopted by reference herein and, in this proceeding, the service of documents made in accordance with the Protocol (which can be found on the Commercial List website at <http://www.ontariocourts.ca/scj/practice/practice-directions/toronto/e-service-protocol/>) shall be valid and effective service. Subject to Rule 17.05 this Order shall constitute an order for substituted service pursuant to Rule 16.04 of the Rules of Civil Procedure. Subject to Rule 3.01(d) of the Rules of Civil Procedure and paragraph 21 of the Protocol, service of documents in accordance with the Protocol will be effective on transmission. This Court further orders that a Case Website shall be established in accordance with the Protocol with the following URL: www.home.kpmg/ca/pacecu.

23. THIS COURT ORDERS that if the service or distribution of documents in accordance with the Protocol is not practicable, the Liquidator is at liberty to serve or distribute this Order, any other materials and orders in these proceedings, any notices or other correspondence, by forwarding true copies thereof by prepaid ordinary mail, courier, personal delivery or facsimile transmission to the Credit Union’s creditors or other interested parties at

their respective addresses as last shown on the records of the Credit Union and that any such service or distribution by courier, personal delivery or facsimile transmission shall be deemed to be received on the next business day following the date of forwarding thereof, or if sent by ordinary mail, on the third business day after mailing.

GENERAL

24. THIS COURT ORDERS that the Liquidator may from time to time apply to this Court for advice and directions in the discharge of its powers and duties hereunder.

25. THIS COURT ORDERS that nothing in this Order shall prevent the Liquidator from acting as a trustee in bankruptcy of the Credit Union.

26. THIS COURT HEREBY REQUESTS the aid and recognition of any court, tribunal, regulatory or administrative body having jurisdiction in Canada or in the United States to give effect to this Order and to assist the Liquidator and its agents in carrying out the terms of this Order. All courts, tribunals, regulatory and administrative bodies are hereby respectfully requested to make such orders and to provide such assistance to the Liquidator, as an officer of this Court, as may be necessary or desirable to give effect to this Order or to assist the Liquidator and its agents in carrying out the terms of this Order.

27. THIS COURT ORDERS that the Liquidator, or FSRA on behalf of the Credit Union, be at liberty and is hereby authorized and empowered to apply to any court, tribunal, regulatory or administrative body, wherever located, for the recognition of this Order and for assistance in carrying out the terms of this Order, and that the Liquidator is authorized and

empowered to act as a representative in respect of the within proceedings for the purpose of having these proceedings recognized in a jurisdiction outside Canada.

28. THIS COURT ORDERS that the Applicant shall have its costs of this motion, up to and including entry and service of this Order, on a substantial indemnity basis to be paid by the Liquidator from the Credit Union's estate with such priority and at such time as this Court may determine.

29. THIS COURT ORDERS that any interested party may apply to this Court to vary or amend this Order on not less than seven (7) days' notice to the Liquidator and to any other party likely to be affected by the order sought or upon such other notice, if any, as this Court may order.



IN THE MATTER OF THE *CREDIT UNIONS AND CAISSES POPULAIRES ACT, 2020*, S.O. 2020, C. 36, SCHED. 7, AS AMENDED
AND IN THE MATTER OF PACE SAVINGS & CREDIT UNION LIMITED
APPLICATION OF PACE SAVINGS & CREDIT UNION LIMITED UNDER SECTION 240 OF THE *CREDIT UNIONS AND CAISSES POPULAIRES ACT, 2020*, S.O. 2020, C. 36, SCHED. 7, AS AMENDED

Court File No. CV-22-00685736-00CL

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

**Proceeding commenced at
Toronto**

**ORDER
(WINDING UP & APPOINTING LIQUIDATOR)**

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TAB B

Court File No.

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

IN THE MATTER OF THE *CREDIT UNIONS AND CAISSES POPULAIRES ACT, 2020*, S.O. 2020, C. 36, SCHED. 7, AS AMENDED

AND IN THE MATTER OF PACE SAVINGS & CREDIT UNION LIMITED

APPLICATION OF PACE SAVINGS & CREDIT UNION LIMITED UNDER SECTION 240 OF THE *CREDIT UNIONS AND CAISSES POPULAIRES ACT, 2020*, S.O. 2020, C. 36, SCHED. 7, AS AMENDED

**AFFIDAVIT OF MEHRDAD RASTAN
(SWORN AUGUST 17, 2022)**

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**AFFIDAVIT OF MEHRDAD RASTAN
(SWORN AUGUST 17, 2022)**

I, Mehrdad Rastan, of the City of Toronto, in the Province of Ontario, MAKE OATH AND SAY:

1. I am the Executive Vice President, Credit Union & Insurance Prudential (“**CU&IP**”) of the Financial Services Regulatory Authority of Ontario (“**FSRA**”), the administrator (in such capacity, the “**Administrator**”) of the applicant, PACE Savings & Credit Union Limited (the “**Applicant**” or “**Credit Union**”) appointed pursuant to the Administration Orders (defined below). Prior to assuming my current position with FSRA in January 2022, I was the Head, Relationship and Risk Management for CU&IP of FSRA since December 2019, and in that capacity, have been a key contact at FSRA for the Credit Union. Before joining FSRA, I worked for the Financial Institutions Commission, now the British Columbia Financial Services Authority, as the Executive Director, Regulation which included responsibilities for the regulatory oversight of credit unions in British Columbia.

2. As a result of serving in these capacities, as well as from my discussions with representatives of the Credit Union, including David Finnie, the former Chief Executive Officer, and Benjamin Choi, the former Chief Financial Officer, FSRA’s management team, KPMG Inc. (which acted as financial advisor to FSRA in certain matters involving the Credit Union, as described below), and other advisors, and my review of relevant documents and information, I am generally familiar with the Credit Union’s former business and operations as well as its financial affairs, books, and records. I therefore have personal knowledge of the matters contained in this affidavit, except where such matters are stated to be based upon information and belief, and where so stated, I have identified the source of the information and believe it to be true.

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3. I swear this affidavit in support of the application made by the Credit Union, under the direction and authority of the Administrator, for an Order pursuant to section 240 of the *Credit Unions and Caisses Populaires Act, 2020*, S.O. 2020, c. 36, Sched. 7, as amended (the “**CUCPA**”) winding up the Credit Union and appointing KPMG Inc. (“**KPMG**”) as liquidator (in such capacity, the “**Liquidator**”), without security, of all of the remaining assets, undertakings, and properties of the Credit Union following completion of the Alterna Sale Transaction (defined below).

PART 1 - OVERVIEW

4. The Applicant is a credit union incorporated under the CUCPA and regulated by FSRA. The Credit Union has been under administration by FSRA, formerly DICO (defined below), since September 28, 2018, which DICO initiated in response to, among other things, certain misconduct and regulatory breaches committed by the Credit Union’s former President and CEO.

5. The initial purpose and goal of the administration was to resolve the governance issues which gave rise to the administration and to return the Credit Union to member-controlled governance in due course. Between September 2018 and April 2020 (i.e., the onset of the COVID-19 pandemic), the Credit Union, under FSRA’s administration, made significant initial progress on the path toward exiting administration and returning to member-controlled governance.

6. For the reasons set out below, the consequences of the COVID-19 pandemic on the Credit Union, combined with certain other factors, compromised the Credit Union’s financial position to such an extent that the Administrator was forced to explore additional options for the

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Credit Union rather than just the “recovery option” which had been the primary goal up until that point. These additional options included exploring a purchase and assumption transaction for the Credit Union and/or a liquidation and winding up of the Credit Union.

7. The Credit Union’s financial position continued to deteriorate throughout 2020 and 2021. Because of these challenging circumstances, the Credit Union’s newly-appointed board of directors and most of the Credit Union’s senior management team resigned in late 2020. In this context, the Administrator determined that potential losses to the Credit Union’s stakeholders could be mitigated more effectively, and the Administrator’s regulatory objectives better served, by pursuing a purchase and assumption transaction for the Credit Union and a sale of the Credit Union’s subsidiary, CCE (defined below), followed by a liquidation and wind-up strategy. This determination ultimately led to the Alterna Sale Transaction (defined below) and CCE Sale Transaction (defined below)—which closed in June 2022 and March 2022, respectively—and, ultimately, to this Application.

8. At present, as a result of the Alterna Sale Transaction, the Credit Union has no employees, no member deposits,¹ and no branches. Further, virtually all of the Credit Union’s members have been granted membership in and are being served by another credit union, Alterna (defined below). As described further below, all that remains of the Credit Union is a collection of certain assets and liabilities which were excluded from the Alterna Sale Transaction.

¹ With certain limited exceptions.

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9. Under the provisions of the CUCPA, the Credit Union may apply to this Court for an order winding up the Credit Union where it cannot continue its business and it is advisable to wind the Credit Union up or it is just and equitable that the Credit Union should be wound up.

10. Because of the events described herein, the Credit Union is no longer operating as a credit union and can no longer perform the statutory object of a credit union under the CUCPA. In the circumstances of this case, including having regard to the nature and complexity of the remaining assets, operations, and liabilities of the Credit Union, the Administrator is of the view that a court-ordered winding up of the Credit Union by a court-appointed liquidator pursuant to the CUCPA is advisable and would be just and equitable.

11. As part of this Application, the Credit Union is seeking to have KPMG appointed as Liquidator. KPMG is well-known for its expertise in complex commercial matters and liquidation proceedings and is an appropriate choice to serve in this capacity. KPMG, through a previous advisory engagement, also has experience with the Credit Union and its assets, undertakings, properties, liabilities, and claims, all of which will benefit the Credit Union, its stakeholders, and the Court if KPMG were appointed as Liquidator.

12. The Applicant is also seeking, among other things, the following additional relief: (a) approval of the Liquidator Nomination Agreement (defined below) between FSRA and KPMG; (b) granting and approval of the Liquidator's Charge (defined below); (c) granting and approval of the Liquidator's power to borrow funds; and (d) granting and approval of the Liquidator's Borrowings Charge (defined below).

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13. The Administrator believes that all of the relief requested on this Application is reasonable and appropriate in the circumstances of this case, and is reasonably necessary to ensure the successful and timely winding up of the Credit Union.

PART 2 - THE PARTIES

(A) FSRA

14. FSRA is a corporation established without share capital under the *Financial Services Regulatory Authority of Ontario Act, 2016*, S.O. 2016, c. 37, Sched. 8 (the “**FSRA Act**”). Since its launch in June 2019 and its amalgamation with DICO (defined below), FSRA has been the regulator of credit unions in Ontario under the CUCPA.

15. The objects of FSRA, as they pertain to credit unions in Ontario, and as set out in the *FSRA Act*, include, without limitation: providing insurance against the loss of deposits with credit unions; promoting and otherwise contributing to the stability of the credit union sector in Ontario; and pursuing the foregoing for the benefit of persons having deposits with credit unions and in such manner as will minimize the exposure of the DIRF (defined below) to loss (the “**Objects**”).

16. Under the CUCPA, FSRA has three main responsibilities with respect to credit unions in Ontario:

- (a) FSRA oversees insured deposit protection for credit unions in Ontario through its administration of the Deposit Insurance Reserve Fund (the “**DIRF**”), providing coverage of non-registered insurable deposits up to \$250,000 and coverage of deposits in registered accounts (e.g., RRSPs or TFSAs) up to an unlimited amount;

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- (b) FSRA is the prudential and market conduct regulator of credit unions in Ontario;
and
- (c) FSRA can act as a “supervisor”, “administrator”, or “liquidator” of credit unions
(as those terms are defined in the CUCPA), in appropriate circumstances.

17. Effective June 8, 2019, FSRA amalgamated with the Deposit Insurance Corporation of Ontario (“DICO”), the former entity that carried out the prudential regulation of credit unions in Ontario under the CUCPA and provided deposit insurance through the DIRF. For ease of reference, the regulator and Administrator of the Credit Union shall sometimes be referred to as FSRA or the Administrator regardless of whether the event described took place before or after June 8, 2019.

(B) The Credit Union

18. The Applicant is a credit union incorporated under the CUCPA and is therefore an entity regulated by FSRA. Before the Alterna Sale Transaction (defined below), the Credit Union had approximately 34,000 members and 13 branches throughout southwestern Ontario and had approximately \$900 million in assets recorded in its financial statements.

PART 3 - RELEVANT BACKGROUND RELATING TO THE ADMINISTRATION OF THE CREDIT UNION

(A) DICO Orders the Credit Union into Administration

19. DICO had issued an administration order on September 28, 2018, pursuant to its authority under section 294(1) of the *Credit Unions and Caisses Populaires Act, 1994*, S.O. 1994,

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c. 11 (which legislation was repealed effective March 1, 2022, and replaced with the CUCPA)² ordering that the Credit Union be subject to administration by the Administrator (the “**First Administration Order**”, attached as **Exhibit “A”**).

20. The First Administration Order issued by DICO was supported by written reasons issued on the same day (the “**Reasons**”, attached as **Exhibit “B”**). The Reasons are titled “*Preliminary* Reasons for Issuance of Administration Order” [emphasis added] because they were intended to provide the Credit Union’s then board of directors with an opportunity to file submissions in response to the First Administration Order. The board of directors did not respond to or oppose the First Administration Order, and therefore DICO did not issue any additional or “final” reasons.

21. Broadly speaking, the Reasons identified five prudential findings (i.e., misconduct related to the prudence of actions, conflicts of interest, and breaches of fiduciary duties) and five regulatory findings (i.e., breaches of the CUCPA and the regulations thereunder) which caused DICO to issue the First Administration Order. The prudential findings included:³

- (a) borrowers of the Credit Union and others made payments to employees of the Credit Union, including to its former President (Larry Smith), and others in relation to various off-market loans and investments the Credit Union had made; these payments were incapable of being legally approved by the Credit Union’s board of

² For ease of reference, the 1994 and 2020 Acts are both hereinafter referred to as the CUCPA, regardless of whether the event being described took place before or after March 1, 2022.

³ See the Reasons at paragraph 25. See also Schedule “A” to the Reasons, which contains the details of the transactions of which DICO was aware at the time and on which it relied in issuing the First Administration Order. I note that Schedule “A” is not exhaustive and other unlawful, improper, or imprudent transactions, payments, and conduct were discovered after Schedule “A” was drafted.

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directors and were in breach of the relevant conflict of interest provisions under the CUCPA;

- (b) the Credit Union's board of directors approved consulting arrangements which allowed the Credit Union's former President to be compensated by borrowers and partners of the Credit Union for transactions involving the Credit Union without proper disclosure;
- (c) the Credit Union's former President offered or distributed various payments, contracts, positions, and other benefits to his family members and friends for their benefit and to the detriment of the Credit Union, including offering and distributing executive positions, consulting positions, and payments in the nature of secret commissions;
- (d) the making of various off-market loans by the Credit Union, which were not in the best interests of the Credit Union and were imprudent and inconsistent with the Credit Union's minimum risk tolerance and were made without proper due diligence; generally speaking, these loans were made to companies in which the former President of the Credit Union or his associates or relatives held ownership interests and were made for the purpose of self-dealing; and
- (e) other loans and investments which appeared on off-market terms and represented undue risk to the Credit Union.

22. The regulatory findings included: (a) failure to disclose the true beneficial ownership of the Credit Union's borrowers, investees, and subsidiaries; (b) properties being

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improperly held by the Credit Union; (c) repeated establishment and operation of subsidiaries (including CCE and PSC, as defined and discussed below) without DICO's approval and with awareness of contraventions of the CUCPA; (d) breach of the investment limit in an existing subsidiary; and (e) inaccurate disclosure of total annual compensation on audited financial statements.⁴

23. DICO concluded it had reasonable grounds to believe that the Credit Union was conducting its affairs in a way that might be expected to harm the interests of members, depositors, or shareholders, or that would tend to increase the risk of claims by depositors against DICO, and that it was therefore appropriate to issue the First Administration Order to effect certain, necessary changes.⁵

24. Further administration orders were issued in respect of the Credit Union on February 19, 2020, April 28, 2020, and March 26, 2021 (the "**Second, Third, and Fourth Administration Orders**", respectively, attached as **Exhibits "C", "D", and "E"**). Together, the First, Second, Third, and Fourth Administration Orders, and any other administration orders which may be issued in respect of the Credit Union, are hereinafter referred to, collectively, as the "**Administration Orders**".

25. FSRA has published the Administration Orders and other documents related to its administration of the Credit Union on its website at <https://www.fsrao.ca/enforcement-and-monitoring/pace-credit-union-administration>.

⁴ See the Reasons at paragraph 27.

⁵ See the Reasons at paragraph 29.

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(B) Unanticipated Circumstances Ultimately Caused the Administrator to Implement a Resolution Strategy for the Credit Union

(i) Steps Taken In Furtherance of Initial Recovery Strategy

26. In the First Administration Order, issued September 28, 2018, the Administrator suspended the powers of the Credit Union's board of directors (with certain limited exceptions) and assumed the powers of the board of directors, thereby effectively taking control of the Credit Union. At this time, the purpose and goal of the administration was to resolve the governance issues which gave rise to the First Administration Order and to return the Credit Union to member-controlled governance in due course. To that end, an Interim CEO was hired by the Administrator, effective January 7, 2019, who was responsible for the day-to-day management of the Credit Union under the supervision of the Administrator. The Interim CEO was to remain in place for approximately one year and assist the Administrator with the recovery (i.e., recover financial strength) of the Credit Union.

27. With a view toward that goal, the Administrator had initially determined that the Credit Union could be removed from administration after a new board of directors had been elected and that board had hired a new management team. The Credit Union members elected a new board of directors at a special membership meeting held on January 27, 2020. The Administrator then issued the Second Administration Order on February 19, 2020, which appointed the new board members and granted them the authority to, among other things, take certain actions to orient themselves with the business and affairs of the Credit Union and recruit and appoint a new management team.

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28. The new board of directors proceeded to hire a new Chief Executive Officer (CEO), Chief Financial Officer (CFO), and Chief Risk Officer (CRO) in early April 2020. The Administrator then issued the Third Administration Order on April 28, 2020, which granted the Credit Union's new board of directors and management team the authority to, among other things, carry on the management and conduct the operations of the Credit Union, subject to, among other things, the Administrator retaining the authority to: (a) order the Credit Union not to exercise powers granted to it under the Third Administration Order, (b) manage the Recovery Litigation (defined below) and certain other legal proceedings that had been commenced or would be commenced by the Administrator in relation to the events giving rise to the First Administration Order and (c) respond to claims, counterclaims, and cross-claims that had been or may yet still be filed in response to actions taken during the administration proceedings.

29. With a new board of directors and management team in place, the Credit Union continued to make significant initial progress on the path toward exiting administration and returning to member-controlled governance, as was initially intended by the Administrator.

(ii) *The COVID-19 Pandemic and Other Circumstances Prevented the Credit Union from Exiting Administration*

30. At the time of the Third Administration Order, Canada was more than one month into the COVID-19 pandemic. The economic impact of the pandemic and the related Investor Claims (defined below) represented unanticipated events which ultimately forced the Administrator to conclude that a recovery strategy was not possible and to consider other options, such as a purchase and assumption transaction and/or a wind-up and liquidation strategy. The

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various impacts of the pandemic and the Investor Claims on the Credit Union and their significance are described below in this section.

The Failure of CCE

31. Continental Currency Exchange (“CCE”) was a wholly-owned subsidiary of the Credit Union engaged in the business of a retail currency exchange that had been acquired by the Credit Union under its former management in contravention of the CUCPA and which was one of the bases for the First Administration Order. The pandemic had a drastic impact on the business of CCE, and it sustained significant operating losses in the 2020 financial year. After determining that a recovery of the Credit Union was not likely, the Administrator ultimately caused the Credit Union to sell CCE as part of the CCE Sale Transaction (defined and described in more detail below).

The Failure of PSC and the Related Investor Claims

32. PACE Securities Corporation (“PSC”) was a wholly-owned subsidiary of the Credit Union engaged in the business of a securities dealer. Among other things, PSC distributed preferred shares of its subsidiary, Pace Financial Limited (“PFL”) and preferred shares of First Hamilton Holdings (“FHH”), an unaffiliated entity under the control of persons managing PSC or related to such persons. On March 21, 2020, PSC notified the Administrator of certain developments caused by the pandemic, which, taken together, presented a significant solvency challenge for PSC and its direct and indirect subsidiaries. A copy of the Credit Union’s organizational chart showing the Credit Union’s relationship to the above entities is attached as **Exhibit “F”**.

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33. Ultimately, the Credit Union, as sole shareholder of PSC, applied to the Ontario Superior Court of Justice to have PSC and its direct and indirect subsidiaries, including PFL, wound up, which order was granted on May 14, 2020. The same Court ordered that FHH be wound up on May 21, 2020.

34. The court-ordered wind up of PSC, PFL, and FHH crystallized substantial losses by investors in the preferred shares of PFL and FHH and gave rise to complaints from Credit Union members and the investors in the preferred shares of PFL and FHH. The Administrator identified misconduct by and potential claims against the Credit Union and its former officers and directors in relation to the business of PSC and the sale of the preferred shares of PFL and FHH that was not known in 2018 when the Credit Union was first placed under administration by DICO.

35. In early August 2020, the Ontario Superior Court of Justice appointed Paliare Roland Rosenberg Rothstein LLP as representative counsel (“**Representative Counsel**”) in the wind-up proceedings for the investors in the preferred shares of PFL and FHH. Ultimately, after an expedited court-ordered mediation process, the claims of these investors (the “**Investor Claims**”) were settled in June 2021 for \$40 million, with a significant portion to be paid by the Credit Union (the “**Investor Settlement**”). The Investor Settlement received court approval on July 30, 2021. In connection with the Investor Settlement, FSRA, as administrator of the DIRF, provided an assurance that if the Credit Union was unable to fund its contribution towards the settlement for any reason, FSRA would ensure payment in full of the Credit Union’s contribution. This assurance gave rise to an unsecured non-interest bearing promissory note in the amount of \$25 million issued by the Credit Union in favour of the DIRF, dated October 27, 2021 (the “**FSRA Promissory Note**”).

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Resignation of the Directors and Senior Management of the Credit Union and the Fourth Administration Order

36. In late 2020, the Credit Union was still in the midst of the pandemic and dealing with the Recovery Litigation (defined below) and the various claims asserted therein as well as the continued operating losses at CCE and the failure of PSC and related Investor Claims. The Credit Union was also facing regulatory capital shortfalls which would require regulatory forbearance and an aggressive plan to restore capital adequacy. In this context, in late 2020, all of the directors of the Credit Union and its CEO and CRO resigned from their positions. This left the Credit Union without a functioning Board of Directors and with only one member of senior management, its CFO.

37. In response to these events, and following the appointment of a new CEO of the Credit Union on December 21, 2020, the Administrator issued the Fourth Administration Order on March 26, 2021, granting the Credit Union's newly-appointed CEO and other members of the Credit Union's senior management team, including the CFO, the authority to, among other things, carry on the ordinary management and conduct the operations of the Credit Union and its subsidiaries subject to, among other things, the Administrator's authority to (a) exercise the powers of the Credit Union for matters outside the ordinary course of business, and of the directors, officers, and committees, (b) manage the Recovery Litigation (defined below) and certain other legal proceedings that had been commenced or would be commenced by the Administrator in relation to the events giving rise to the First Administration Order, and (c) respond to claims, counterclaims, and cross-claims that had been or may yet still be filed in response to actions taken during the administration.

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Administrator's Decision to Pursue a Purchase and Assumption Transaction and Wind-Up and Liquidation Strategy

38. Following the issuance of the Fourth Administration Order, the Credit Union's long-term viability remained uncertain in light of the ongoing pandemic, and the Credit Union's financial condition continued to deteriorate throughout 2021. Indeed, in or around early 2021, the Credit Union was required to seek a variance from the CEO of FSRA regarding its regulatory capital requirements. A copy of a letter from the CEO of FSRA to the Credit Union's members describing the capital variance decision is attached as **Exhibit "G"**.

39. In light of the foregoing circumstances, the Administrator ultimately determined that the long-term operation of the Credit Union's business was not reasonably likely to minimize the losses to the Credit Union's depositors and other creditors and ultimately to the DIRF. The Administrator further determined that these losses would be mitigated more effectively, and the Objects would be better served, by pursuing a purchase and assumption transaction for the Credit Union and a sale of CCE followed by a liquidation and wind-up strategy. This strategy was initiated by the Administrator in late May 2021 with the commencement of the CCE Sale Process (defined below), and the commencement of the Alterna Sale Process (defined below) in June 2021.

40. Following the completion of the CCE Sale Process and the Alterna Sale Process, the Administrator publicly announced that there would be a liquidation of the remaining assets and liabilities of the Credit Union by press release dated July 6, 2022, attached as **Exhibit "H"**.

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(C) Alterna’s Acquisition of Substantially all of the Credit Union’s Assets and Operations

(i) The Alterna Sale Transaction

41. On April 20, 2022, following a careful assessment of the various options available to the Credit Union and the completion of a formal competitive sale process conducted in consultation with the proposed liquidator, KPMG⁶ (the “**Alterna Sale Process**”), the Credit Union and FSRA entered into a purchase and assumption agreement (the “**Alterna Sale Agreement**”) with Alterna Savings and Credit Union Limited (“**Alterna**”). Pursuant to the Alterna Sale Agreement, Alterna would acquire and assume substantially all of the assets and liabilities of the Credit Union except for certain excluded assets and liabilities and would continue the Credit Union’s normal course business operations as part of Alterna (the “**Alterna Sale Transaction**”). On closing, Alterna acquired and assumed substantially all of the member deposits, both insured and uninsured, and substantially all retail and commercial loans. As part of the Alterna Sale Transaction, Alterna offered employment to substantially all of the Credit Union’s employees, assumed all of the Credit Union’s existing branches and agreed to keep them open for a period of time following the Alterna Closing Date, and provided substantially all of the Credit Union’s existing members with membership in Alterna. The Alterna Sale Agreement contains a confidentiality provision; accordingly, I am not attaching the agreement as an exhibit.

42. FSRA, as Administrator of the Credit Union and according to the Objects, determined that the Alterna Sale Transaction was in the best interests of the members of the Credit Union whose accounts would be seamlessly transferred to Alterna and would continue to be served

⁶ At the time, KPMG was acting solely as a financial advisor and was not proposed to be the liquidator in these proceedings.

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as members of Alterna, and the Credit Union's employees who would be hired by Alterna. The transaction was also consistent with the Objects, including to ensure that losses to the DIRF were minimized and the credit union sector continued to be stable. KPMG served as financial advisor to the Administrator in connection with the Alterna Sale Process and Alterna Sale Transaction. The Alterna Sale Transaction closed on June 30, 2022 (the "**Alterna Closing Date**").

43. A critical aspect of the Alterna Sale Transaction was continuity for members of the Credit Union: on the Alterna Closing Date, the Credit Union's existing members became Alterna members served by the Credit Union's former employees and branches, both of which were also assumed by Alterna. The membership of the Credit Union was not changed by the Alterna Sale Transaction; those individuals who were members of the Credit Union prior to the closing retained their membership in the Credit Union after closing and also (with very few exceptions) became members of Alterna.

44. Under the Alterna Sale Transaction, the Credit Union has certain potential post-closing liabilities, which may or may not result in certain payments to Alterna. This exposure is guaranteed by FSRA, subject to a monetary cap. The guarantee provides certain subrogation rights to FSRA.

45. In addition, Alterna has agreed to provide certain transition services to the Credit Union for a limited period of time. The services include various finance and accounting services and information technology services for the purpose of facilitating the Credit Union's dealing with its remaining assets and liabilities.

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(ii) *Assets and Liabilities Remaining in the Credit Union Subsequent to the Alterna Sale Transaction*

46. Subsequent to the Alterna Sale Transaction, the Credit Union retained certain assets and liabilities which relate to, among other things, the CCE Sale Transaction (defined below), the Prepaid Card Business (defined below), claims asserted in the Recovery Litigation (defined below), the FSRA Promissory Note, certain member deposits and accounts, certain loans, certain insurance claims or entitlements to proceeds of insurance, certain funds held in trust by the Credit Union for the benefit of former employees, and certain severance obligations which may be owed by the Credit Union to former employees. The remaining assets and liabilities of the Credit Union are described in more detail below in Part 4 of this affidavit.

(D) The CCE Sale Transaction

47. As indicated above, CCE is a retail currency exchange business which, until March 31, 2022, was a wholly-owned subsidiary of the Credit Union. The acquisition of CCE by the Credit Union was one of several transactions that led to the Credit Union being placed under administration. According to the Reasons, the former President and CEO caused the Credit Union to acquire a controlling interest in CCE, without the necessary regulatory approvals, using a corporation controlled by them.

48. On January 11, 2022, following a careful assessment of the various options available to the Credit Union and including the completion of a formal competitive sale process conducted in consultation with KPMG which served as financial advisor to the Administrator in connection with the sale of all of the shares of CCE held by the Credit Union (the “**CCE Sale Process**”), which was run in parallel to the Alterna Sale Process, the Credit Union, FSRA, and the

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successful bidder, DUCA Credit Union (“DUCA”), entered into a share purchase agreement (the “CCE Sale Agreement”) in respect of the sale of all of the issued and outstanding shares in the capital of CCE (the “CCE Sale Transaction”). The CCE Sale Transaction closed on March 31, 2022 and resulted in a loss to the Credit Union which further eroded its already diminished financial capacity. The CCE Sale Agreement contains a confidentiality provision; accordingly, I am not attaching that agreement as an exhibit.

PART 4 - REMAINING ASSETS, OPERATIONS, AND LIABILITIES OF THE CREDIT UNION REQUIRING RESOLUTION BY THE LIQUIDATOR

49. In my current and former role at FSRA, I worked closely with KPMG, the financial advisor to the Administrator in connection with the Alterna Sale Transaction and the proposed Liquidator in these proceedings. Based on the analysis and information provided to me by KPMG, certain assets and liabilities remained with the Credit Union following the closing of the Alterna Sale Transaction, which assets and liabilities are described below in this Part of the affidavit.

(A) The Recovery Litigation

50. On April 17, 2019, the Credit Union commenced a claim in the Ontario Superior Court of Justice (Commercial List) against the former CEO and former President of the Credit Union (Phillip Smith and Larry Smith), their affiliates, certain of the Credit Union’s former directors, and a number of other parties who received improper benefits from the Credit Union. The Credit Union through its Administrator is represented by the law firm of Lax O’Sullivan Lisus Gottlieb LLP in this claim.

51. The Credit Union’s claim advances causes of actions including breach of fiduciary duty, fraud, conspiracy, breach of contract and employment duties, breach of trust, knowing receipt

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of proceeds of breach of trust, conversion, unjust enrichment, and negligence against the Smiths.

The grounds for these claims include the following alleged misconduct:

- (a) the Smiths intentionally or recklessly underreported the income they received directly or indirectly from the Credit Union, contrary to their obligations under the CUCPA and its associated regulation; this under-reporting amounted to millions of dollars; the Smiths also took steps to conceal monies they had misappropriated from the Credit Union;
- (b) the Smiths caused the Credit Union to purchase the entirety of CCE, contrary to regulatory limits which prohibit a credit union from acquiring more than 30% of any other corporation without FSRA's permission; they did so surreptitiously to avoid these regulatory limits, and received secret payments in connection with the transaction; the purchase of CCE caused significant risk of loss to the Credit Union, which came to pass when CCE suffered a downturn in its operations in 2020 and 2021 as a result of the COVID-19 pandemic;
- (c) the Smiths, along with other former directors of the Credit Union, failed to properly supervise the business of PSC, which led to its failure and winding-up, and consequent claims against the Credit Union by a number of investors in PSC;
- (d) the Smiths directed the Credit Union to make improvident loans, advance funds, and make other payments to parties connected to them, including corporations they controlled, friends, and relatives; these payments were not *bona fide* and/or were contrary to the Credit Union's best interests; and

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- (e) the Smiths overstated the value of loans on the Credit Union's books and records, thereby misrepresenting the Credit Union's financial position and performance.

52. The defendants to the Credit Union's claim deny the allegations and several have commenced counterclaims against the Credit Union. Phillip and Larry Smith have commenced third party claims against two of the Credit Union's former directors. Phillip Smith also brought a separate claim for wrongful dismissal against the Credit Union in September 2019. The Credit Union's claim, the Smiths' third party claims, Phillip Smith's claim, and all related counterclaims and crossclaims against the Credit Union are referred to herein collectively as the "**Recovery Litigation**".⁷

53. The Smiths' counterclaims, and Phillip Smith's separate claim, allege that the Credit Union breached their employment contracts by terminating them for cause following the issuance of the First Administration Order, that they have suffered damages as a result of the *Mareva* order (described below) and the freezing of their accounts at the Credit Union, that the Credit Union has defamed them, and that the Administrator has committed the torts of malfeasance in public office and regulatory negligence during the course of the administration. Two other defendants, Brian Hogan and Frank Klees, have also counterclaimed against the Credit Union for defamation and infliction of emotional distress (Hogan) and breach of contract (Klees).

⁷ The Credit Union's claim bears the Court File No. CV-19-00616388-00CL. Phillip Smith's third party claim bears the Court File No. CV-19-00616388-CLA2, and his wrongful dismissal claim bears the Court File No. CV-19-00628710-0000.

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54. The Recovery Litigation is currently pending before the Ontario Superior Court of Justice (Commercial List), where it is being case managed by Justice Gilmore. Pleadings have been exchanged, but documentary and oral discovery have not yet taken place.

55. Before issuing its claim, the Credit Union brought a motion for a *Mareva* injunction against Larry and Phillip Smith, which was heard on March 19, 2019. Following the hearing, Justice Hainey made an interim *Mareva* order against the Smiths. The Credit Union and the Smiths subsequently agreed to the terms of a permanent preservation order, which was made by Justice Conway on May 7, 2019. Justice Conway's preservation order remains in effect to this date.

56. Beginning in May 2019, the Credit Union collapsed certain accounts held by Larry Smith at the Credit Union (the "**Smith Accounts**") pursuant to its right of set off against him. In December 2019, Mr. Smith commenced an application, seeking an order that the amounts in the Smith Accounts be paid out to him or paid into court. The application was heard on August 5, 2020. On October 26, 2020, Justice Koehnen issued an endorsement finding that, while Mr. Smith had no right to demand the return of the funds held in the Smith Accounts, the Credit Union was not entitled to collapse the accounts. Justice Koehnen directed the Credit Union to reconstitute the Smith Accounts and to preserve the status quo with respect to them. The Credit Union continues to maintain the Smith Accounts on its financial statements as a liability, consistent with the endorsement of Justice Koehnen. The total value of the Smith Accounts is approximately \$5 million. A copy of Justice Koehnen's endorsement is attached as **Exhibit "I"**.

57. On July 19, 2022, Larry and Phillip Smith brought a motion in the Recovery Litigation seeking another order requiring the Credit Union to pay funds in the Smith Accounts to

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them or into trust, and to set aside a fund to satisfy a future judgment and/or costs award in favour of the Smiths, as well as security for costs. On July 25, 2022, Justice Gilmore ordered the Credit Union to maintain the status quo pending the return of the Smiths' motion. She also ordered that, in the event the Credit Union seeks to take additional steps, including "further dissipation of assets", it may do so on the consent of the parties or order of the Court. A copy of Justice Gilmore's endorsement is attached as **Exhibit "J"**.

58. Should this Application be granted, the Applicant expects that the Liquidator will continue to prosecute the claims, and defend the counterclaims, made in the Recovery Litigation, subject to the terms of the Liquidator Nomination Agreement (defined below). Accordingly, the Applicant is not seeking to stay the Recovery Litigation, and that proceeding will be expressly excluded from the stay provision in the Winding Up Order.

(B) Default Loans and Liabilities

59. The Credit Union has retained certain loans and accounts that are in default, having a face value of more than \$8 million in Credit Union assets. A Credit Union member associated with most of these loans and accounts commenced a claim against the Credit Union in January 2022, which remains outstanding.

(C) Proceeds of CCE Sale Transaction

60. As indicated above, the Credit Union completed the sale of all of the issued and outstanding shares of CCE to DUCA on March 31, 2022. As of May 31, 2022, the Credit Union held net proceeds from the CCE Sale Transaction in the amount of approximately \$16.3 million.

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(D) The CUMIS Bond Claim

61. The Credit Union has a claim against CUMIS General Insurance Company (“CUMIS”) in relation to a proof of loss filed on October 16, 2019 under the fidelity insurance coverage bearing Policy Number 01501254 and with an Effective Date of January 1, 2018, and an Expiry Date of January 1, 2019 (the “CUMIS Bond”), contained in the contract of insurance issued by CUMIS (the “CUMIS Policy”), in respect of losses incurred by the Credit Union in connection with the various dishonest acts of former employees and directors of the Credit Union, including its former President and CEO (the “CUMIS Bond Claim”). In the proof of loss, the Administrator calculated the Credit Union’s losses to be approximately \$23,579,078.00.

62. Pursuant to the terms of the CUMIS Bond, CUMIS is liable to indemnify the Credit Union for covered losses, which includes losses resulting from dishonest or fraudulent acts of any director, employee, or contractor, to a maximum of \$10,000,000.00. The Credit Union, by its Administrator, FSRA, has claimed the maximum amount available under the CUMIS Bond. To date, CUMIS has only made partial payment to the Credit Union in the amount of approximately \$1.0 million. The balance of the CUMIS Bond Claim remains outstanding.

63. The Credit Union has commenced an action bearing Court File No. CV-22-00677550-0000 against CUMIS in relation to the unpaid portion of the CUMIS Bond Claim. An amended statement of claim was served on CUMIS on August 9, 2022. The relief sought in the claim includes a demand for payment under the CUMIS Bond as well as damages against CUMIS for breach of the CUMIS Bond and the duty of good faith. The claim has not yet been defended and the period for delivering a statement of defence has not yet expired.

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(E) The Berkshire Bond Claim

64. The Credit Union also has a claim against National Liability & Fire Insurance Company, carrying on business as Berkshire Hathaway Specialty Insurance (“**Berkshire**”) in relation to a proof of loss filed on December 17, 2021 under Financial Institution Bond for Banking Institutions Bond Number 43-EPF-306798-03 (the “**Berkshire Bond**”) issued in connection with insurance policies bearing Asset Manager Protection Policy Number 43-EPF-306800-03 and any relevant predecessor and successor policies (collectively, the “**Berkshire Policies**”), in respect of losses incurred by the Credit Union in connection with dishonest or fraudulent acts of the Credit Union’s former Manager Retail Loans, acting alone or in collusion with other individuals or entities, and certain litigation arising therefrom (the “**Berkshire Bond Claim**”). In the proof of loss, the Administrator calculated the Credit Union’s losses to be approximately \$9,445,000.00.

65. Pursuant to the terms of the Berkshire Bond, Berkshire is liable to indemnify the Credit Union for covered losses, which includes losses resulting from dishonest or fraudulent acts of any director, employee, or contractor, to a maximum of \$10,000,000.00. The Credit Union, by its Administrator has claimed the \$9,445,000.00 under the Berkshire Bond, which amount has not been paid by Berkshire as of the date of the swearing of this affidavit.

(F) Prepaid Card Business

66. The Credit Union acts as the issuer of prepaid cards (the “**Prepaid Cards**”) pursuant to various prepaid card programs transacting on the Mastercard and Visa networks and operated in conjunction with several program managers (the “**Prepaid Card Business**”). The Credit Union has the power to issue prepaid cards in all Canadian jurisdictions, and prepaid cards have been issued across Canada.

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67. All amounts loaded by consumers (“**Prepaid Cardholders**”) on the Prepaid Cards (the “**Prepaid Cardholder Amounts**”) are held separate and apart for the benefit of cardholders in a commercial account at The Toronto-Dominion Bank in the name of a subsidiary of the Credit Union, 1961783 Ontario Limited (the “**Prepaid Card Entity**”). The sole function and activity of the Prepaid Card Entity is to receive and hold the Prepaid Cardholder Amounts for the benefit of the Prepaid Card Holders and ultimately to disburse the Prepaid Cardholder Amounts on behalf of the Prepaid Card Holders for the benefit of merchants.

68. Pursuant to the cardholder agreements entered into with consumers, the amounts loaded by consumers onto their Prepaid Cards are not considered deposits and the amounts are not insured by the Canada Deposit Insurance Corporation or the DIRF.

69. The Credit Union is in the process of transitioning or winding-down the Prepaid Card Business. This process of transition and wind-down is expected to take a period of months to complete and while that is occurring, the Prepaid Card Business will continue to operate in the normal course.

(G) Expected Distributions from the Wind Up of PACE Securities Corporation and Its Subsidiaries

70. In connection with the court-ordered wind-up of the Credit Union’s wholly-owned subsidiary, PSC and its direct and indirect subsidiaries, including PFL and PACE Capital Partners LP (“**PCP**”), the Credit Union expects to receive certain interim distributions both as creditor and sole shareholder of PSC.

71. Ernst & Young Inc. (“**EY**”) is the court-appointed liquidator of PSC, PFL, and Pace General Partner Limited, the general partner of PCP. On November 1, 2021, on the application of

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the Credit Union, the Ontario Superior Court of Justice in Bankruptcy made a bankruptcy order in respect of PSC and appointed EY trustee in bankruptcy of PSC.⁸

72. On November 20, 2021, the Credit Union filed a proof of claim in the bankruptcy proceeding of PSC stating an unsecured claim against PSC in the total amount of approximately \$4.7 million. I am advised by EY that the Credit Union can expect to receive interim distributions which would satisfy most, if not all, of the Credit Union's claims against PSC sometime in late 2022, but that the timing of any such distribution remains subject to the receipt of comfort letters from Canada Revenue Agency and approvals of the Court.

(H) BC Class Action

73. The Credit Union and others are named defendants in a certified class action in the British Columbia Supreme Court, BCSC Action No. S-147229, Vancouver Registry (the "**BC Class Action**"), in which the plaintiff, on behalf of the class, alleges, among other things, that the defendants (which includes the Credit Union) breached provisions of the *British Columbia Business Practices and Consumer Protection Act* by selling prepaid credit cards that allegedly have an expiry date and contain fees for the purchase and use of such cards. The BC Class Action remains in the documentary discovery phase. The Credit Union's potential exposure in the BC Class Action, if any, cannot be determined with reasonable precision at this time.

74. The Applicant is seeking a stay of the BC Class Action in order to see if a consensual resolution can be achieved.

⁸ Court File No. BK-21-208520-OT31; Estate No. 32-2780716

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(I) Potential Claims by FSRA

75. The Credit Union remains subject to certain potential claims by FSRA in its capacities as both the administrator of the DIRF and the statutory Administrator of the Credit Union. These include a potential claim relating to FSRA's guarantee of certain post-closing obligations owed by the Credit Union in connection with the Alterna Sale Transaction, which may or may not ultimately result in payments to Alterna.

(J) Other Excluded Assets, Liabilities, and Obligations

76. The Credit Union's other excluded assets and liabilities include the following:
- (a) a relatively small asset reflecting the Credit Union's remaining investments in certain completed joint venture projects;
 - (b) an accrued dividend and capital payments in connection with certain Class A profit and Class B investment shares it issued;
 - (c) a deferred tax asset in the form of an accrued credit for past losses; and
 - (d) other ordinary course litigation and claims, which exist or may in the future exist.

PART 5 - THE LIQUIDATOR NOMINATION AGREEMENT

77. Given all of the circumstance described herein—including, without limitation, that FSRA has certain claims against the Credit Union, both existing and contingent, all of which are in respect of the DIRF—KPMG and FSRA, in its capacity as the Administrator of the Credit Union, have entered into a liquidator nomination agreement (the "**Liquidator Nomination Agreement**"), attached as **Exhibit "K"**. Pursuant to the Liquidator Nomination Agreement, the

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Administrator agreed to nominate or support the nomination of KPMG, and KPMG agreed to accept such nomination and consent to its appointment, as court-appointed liquidator of the Credit Union in these proceedings on the terms set out therein and in the form of the winding-up order sought on this application.

78. In connection with the appointment of the proposed Liquidator, the Applicant is seeking the Court's approval of the Liquidator Nomination Agreement. The appropriateness of KPMG as proposed Liquidator is addressed below in Part 6 of this affidavit.

PART 6 - APPLICATION TO WIND UP THE CREDIT UNION

(A) A Court-Ordered Wind Up of the Credit Union is Appropriate

79. The Administrator is of the view that: (a) having completed the Alterna Sale Transaction, the Credit Union no longer has member deposits, employees or branches and therefore can no longer fulfil its statutory object under section 23(1) of the CUCPA "to provide on a co-operative basis financial services primarily for its members"; (b) an orderly wind-up of the Credit Union is appropriate; and (c) in the circumstances, including having regard to the nature and complexity of the remaining assets, operations, and liabilities of the Credit Union, a court-ordered winding up of the Credit Union by a court-appointed liquidator pursuant to the CUCPA would be appropriate.

80. In particular, as a result of the sale of substantially all of its assets to Alterna and the departure of all of its employees, the substratum of the Credit Union's business no longer exists. The Credit Union is left with miscellaneous assets to administer and significant litigation to be prosecuted or defended. The Credit Union, by reason of the sale of its business and the liabilities being asserted against it, cannot continue its business and it is advisable to wind it up. In

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addition, in view of all the circumstances herein, including the absence of any employees to deal with the Credit Union's remaining assets, operations, and liabilities, it is just and equitable that the Credit Union be wound up.

81. If appointed, the Liquidator will monetize or dispose of the remaining assets of the Credit Union, identify and determine claims against the Credit Union and/or its current and former directors and officers, defend or resolve the outstanding litigation described herein, and seek directions from the Court regarding any proposed distribution.

(B) Standing and Jurisdiction

82. The Chief Executive Officer of FSRA ordered that the Credit Union be subject to administration pursuant to the provisions of the CUCPA. Pursuant to the Administration Orders, the Administrator was granted and has retained the authority to, among other things, exercise the powers of the Credit Union for matters outside of the ordinary course of business, and of the directors, officers, and committees. Under the provisions of the CUCPA, the Credit Union may apply to the Ontario Superior Court of Justice (Commercial List) (the "**Court**") for an order winding up the Credit Union where it cannot continue its business and it is advisable to wind it up or it is just and equitable that it should be wound up. Those circumstances exist in this case. Accordingly, the Administrator may cause the Credit Union to bring an application to the Court seeking an order winding-up the Credit Union under the provisions of the CUCPA.

83. There is some urgency in commencing the winding up process as it will be beneficial for the Liquidator to have access to the transition services and information available from Alterna, as referred to in paragraph 45 above.

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(C) Appointment of KPMG as Liquidator

84. Under the provisions of the CUCPA, the Court may appoint one or more persons as liquidator of the estate and effects of the Credit Union for the purpose of winding up its affairs and distributing its property.

85. The Administrator nominates KPMG to serve as the court-appointed liquidator of the Credit Union in these proceedings. KPMG is well-known for its expertise in complex commercial matters and liquidation proceedings and is an appropriate choice to serve in this capacity. FSRA believes that KPMG's engagement in respect of the Alterna Sale Process, Alterna Sale Transaction, CCE Sale Process, and CCE Sale Transaction and the background and experience gained in its financial advisory role regarding the Credit Union, its assets, undertakings, properties, liabilities, and claims will benefit the Credit Union, its stakeholders, and the Court if KPMG were appointed as Liquidator.

86. The proposed Liquidator has requested a charge on the remaining assets of the Credit Union to secure payment of its reasonable fees and expenses and those of its counsel, in each case at their standard rates and charges unless otherwise ordered by this Court on the passing of accounts (the "**Liquidator's Charge**"). The Administrator believes that the Liquidator's Charge is reasonable and appropriate in the circumstances of this case.

87. The proposed Liquidator may have to borrow monies for the purpose of funding the exercise of its powers and duties related to the winding-up of the Credit Union. For this reason, the Applicant is seeking an Order (a) empowering the Liquidator to borrow such monies, provided that the outstanding principal amount does not exceed \$3,000,000.00 and (b) granting a fixed and

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specific charge on the remaining assets of the Credit Union as security for the payments of the monies borrowed, together with interest and charges thereon (the “**Liquidator’s Borrowings Charge**”). The Administrator believes that the Liquidator’s Borrowings Charge is reasonable and appropriate in the circumstances of this case.

PART 7 - CONCLUSION

88. For the reasons stated herein, the Administrator believes that the relief requested by the Applicant on this Application is reasonable and appropriate in the circumstances of this case, and is reasonably necessary to ensure the successful and timely winding up of the Credit Union.

SWORN by Mehrdad Rastan of the City of Toronto, in the Province of Ontario, before me at the City of Toronto, in the Province of Ontario, on August 17, 2022 in accordance with O. Reg. 431/20, Administering Oath or Declaration Remotely.

DocuSigned by:



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Commissioner for Taking Affidavits
(or as may be)

MITCH STEPHENSON

DocuSigned by:



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MEHRDAD RASTAN

TAB C

Court File No. CV-19-00616388-00CL

**ONTARIO
SUPERIOR COURT OF JUSTICE
COMMERCIAL LIST**

B E T W E E N:

(Court Seal)

PACE Savings & Credit Union Limited, by its liquidator, KPMG Inc. by its
Administrator, FINANCIAL SERVICES REGULATORY AUTHORITY

Plaintiff

and

LARRY SMITH, PHILLIP SMITH, 1428245 ONTARIO LTD.,
809755 ONTARIO LTD. (a.k.a. ELECTIVE BENEFIT INSURANCE SERVICES),
MALEK SMITH, 1916761 ONTARIO LTD., 1724725 ONTARIO LTD., FRANK KLEES,
KLEES & ASSOCIATES LTD., RON WILLIAMSON,
R. WILLIAMSON CONSULTANTS LIMITED, RON WILLIAMSON QUARTER
HORSES INC., BRIAN HOGAN, BRENT BAILEY, DEBORAH BAKER, IAN
GOODFELLOW, AL JONES, WENDY MITCHELL, GEORGE POHLE, PETER
REBELLATI, JIM TINDALL, PAULINE WAINWRIGHT, NEIL WILLIAMSON, and
JOANNA WHITFIELD

Defendants

FURTHER AMENDED FRESH-AS-AMENDED STATEMENT OF CLAIM
(Notice of Action issued March 18, 2019)

TO THE DEFENDANT

A LEGAL PROCEEDING HAS BEEN COMMENCED AGAINST YOU by the Plaintiff. The Claim made against you is set out in the Statement of Claim served with this Notice of Action.

IF YOU WISH TO DEFEND THIS PROCEEDING, you or an Ontario lawyer acting for you must prepare a Statement of Defence in Form 18A prescribed by the *Rules of Civil Procedure*, serve it on the Plaintiff's lawyer or, where the Plaintiff does not have a lawyer, serve

it on the Plaintiff, and file it, with proof of service in this court office, WITHIN TWENTY DAYS after this Notice of Action is served on you, if you are served in Ontario.

If you are served in another province or territory of Canada or in the United States of America, the period for serving and filing your Statement of Defence is forty days. If you are served outside Canada and the United States of America, the period is sixty days.

Instead of serving and filing a Statement of Defence, you may serve and file a Notice of Intent to Defend in Form 18B prescribed by the *Rules of Civil Procedure*. This will entitle you to ten more days within which to serve and file your Statement of Defence.

IF YOU FAIL TO DEFEND THIS PROCEEDING, JUDGMENT MAY BE GIVEN AGAINST YOU IN YOUR ABSENCE AND WITHOUT FURTHER NOTICE TO YOU. IF YOU WISH TO DEFEND THIS PROCEEDING BUT ARE UNABLE TO PAY LEGAL FEES, LEGAL AID MAY BE AVAILABLE TO YOU BY CONTACTING A LOCAL LEGAL AID OFFICE.

IF YOU PAY THE PLAINTIFF'S CLAIM, and \$5,000.00 for costs, within the time for serving and filing your statement of defence, you may move to have this proceeding dismissed by the court. If you believe the amount claimed for costs is excessive, you may pay the plaintiff's claim and \$400.00 for costs and have the costs assessed by the court.

TAKE NOTICE: THIS ACTION WILL AUTOMATICALLY BE DISMISSED if it has not been set down for trial or terminated by any means within five years after the action was commenced unless otherwise ordered by the court.

Date ~~March 4, 2022~~
October 18, 2022

Issued by

Local Registrar

Address of court office: Superior Court of Justice
330 University Avenue, 9th Floor
Toronto ON M5G 1R7

TO: Larry Smith
53 Treegrove Circle
Aurora, Ontario L4G 6M2

AND TO: Phillip Smith
53 Treegrove Circle
Aurora, Ontario L4G 6M2

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AND TO: 1428245 Ontario Ltd.
53 Treegrove Circle
Aurora, Ontario L4G 6M2

AND TO: 809755 Ontario Ltd.
53 Treegrove Circle
Aurora, Ontario L4G 6M2

AND TO: Malek Smith
59 East Liberty Street, Suite 605
Toronto, Ontario M6K 3R1

AND TO: 1916761 Ontario Ltd.
59 East Liberty Street, Suite 605
Toronto, Ontario M6K 3R1

AND TO: 1724725 Ontario Ltd.
8111 Jane Street, Suite 1, Vaughan, Ontario L4K 4L7; and
111 Civic Square Gate, Suite 316, Aurora, Ontario L4G 0S6
53 Treegrove Circle, Aurora, Ontario L4G 6M2

AND TO: Frank Klees
106 Golf Links Drive
Aurora, Ontario L4G 3V3

AND TO: Klees & Associates Ltd.
106 Golf Links Drive
Aurora, Ontario L4G 3V3

AND TO: Ron Williamson
86 Carrick Trail
Gravenhurst, Ontario P1P 0A6

AND TO: R. Williamson Consultants Limited
86 Carrick Trail
Gravenhurst, Ontario P1P 0A6

AND TO: Ron Williamson Quarter Horses Inc.
86 Carrick Trail, Gravenhurst, Ontario P1P 0A6
604 South Elm Street, Denton, Texas, United States 76201

AND TO: Brian Hogan
297 Ridley Boulevard
Toronto, Ontario M5M 2M5

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AND TO: Brent Bailey
90 Anglesey Boulevard
Toronto, Ontario M9A 3C4

AND TO: Deborah Baker
15334 Argyll Road
Georgetown, Ontario L7G 5P3

AND TO: Ian Goodfellow
97 Davis Trail
Thornton, Ontario L0L 2N0

AND TO: Al Jones
43 Barre Drive
Barrie, Ontario L4N 7N8

AND TO: Wendy Mitchell
26 Brooke Avenue
Collingwood, Ontario L9Y 5L2

AND TO: George Pohle
5479 Yonge Street
Gilford, Ontario L0L 1R0

AND TO: Peter Rebellati
12 Hardwick Drive
Brampton, Ontario L6W 2Z4

AND TO: Jim Tindall
6390 Owen Road R.R. 1
Uxbridge, Ontario L9P 1R1

AND TO: Pauline Wainwright
3 Stornwood Court
Brampton, Ontario L6W 4H4

AND TO: Neil Williamson
790 Millbank Road
Pickering, Ontario L1V 3L5

AND TO: Joanna Whitfield

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CLAIM

1. The Plaintiff claims against the defendants Larry Smith, Phillip Smith, 1428245 Ontario Ltd., and 809755 Ontario Ltd. the following amounts, to be reduced by the amounts set-off by the Credit Union (as defined below):
 - (a) damages, compensation and disgorgement in an amount to be specified before trial for fraud, deceit, conspiracy, breach of contract, breach of employment duties, breach of fiduciary duty, breach of trust, knowing assistance of breach of fiduciary duty and breach of trust, knowing receipt of proceeds of breach of fiduciary duty and breach of trust, conversion and unjust enrichment in connection with their participation in and involvement in the transactions as identified below, provided that the amounts sought do not include any amount apportionable to the actions or omissions of Alison Golanski, Stan Dimakos and Ken Topping, Kim Colacicco, Brian Mullan, Mitch Vininsky, Mary Benincasa, Benjamin Choi, David Finnie, Frederick Kreutlein, Heather Sarnecki and Lauren Thompson Cacovic;
 - (b) an accounting of all amounts received, directly or indirectly, as a result of any of the conduct of the Defendants set out herein;
 - (c) a tracing order and a constructive trust over the property directly or indirectly acquired with the proceeds from the improper conduct described herein; and
 - (d) damages for the costs of enforcing and realizing on the Plaintiff's security in the CCE Receivership Proceedings (Court File No. CV-18-00610186-OOCL) on a full indemnity basis.

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2. The Plaintiff claims against the defendant 1724725 Ontario Ltd.:
 - (a) damages, compensation and disgorgement in an amount to be specified before trial for breach of contract, knowing assistance of breach of fiduciary duty and breach of trust, knowing receipt of proceeds of breach of fiduciary duty and breach of trust, conspiracy, conversion and unjust enrichment in connection with its participation in and involvement in the transactions as identified below;
 - (b) an accounting of all amounts received, directly or indirectly, as a result of any of the conduct of the Defendants set out herein; and
 - (c) a tracing order and a constructive trust over the property directly or indirectly acquired with the proceeds from the improper conduct described herein.

3. The Plaintiff claims against the defendants Malek Smith and 1916761 Ontario Ltd.:
 - (a) damages, compensation and disgorgement in an amount to be specified before trial for knowing assistance of breach of fiduciary duty and breach of trust, knowing receipt of proceeds of breach of fiduciary duty and breach of trust, conspiracy, conversion and unjust enrichment in connection with their participation in and involvement in the transactions as identified below;
 - (b) an accounting of all amounts received, directly or indirectly, as a result of any of the conduct of the Defendants set out herein; and
 - (c) a tracing order and a constructive trust over the property directly or indirectly acquired with the proceeds from the improper conduct described herein.

4. The Plaintiff claims against the defendants Frank Klees and Klees & Associates Ltd.:
 - (d) damages, compensation and disgorgement in an amount to be specified before

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trial for fraud, deceit, conspiracy, breach of contract, breach of employment duties, breach of fiduciary duty, breach of trust, knowing assistance of breach of fiduciary duty and breach of trust, knowing receipt of proceeds of breach of fiduciary duty and breach of trust, conversion and unjust enrichment in connection with their participation in and involvement in the transactions as identified below;

- (e) an accounting of all amounts received, directly or indirectly, as a result of any of the conduct of the Defendants set out herein; and
- (f) a tracing order and a constructive trust over the property directly or indirectly acquired with the proceeds from the improper conduct described herein.

5. The Plaintiff claims against Ron Williamson, R. Williamson Consultants Limited, and Ron Williamson Quarter Horses Inc.:

- (g) damages, compensation and disgorgement in an amount to be specified before trial for fraud, deceit, conspiracy, knowing assistance of breach of fiduciary duty and breach of trust, knowing receipt of proceeds of breach of fiduciary duty and breach of trust, conversion and unjust enrichment in connection with their participation in and involvement in the transactions as identified below;
- (h) an accounting of all amounts received, directly or indirectly, as a result of any of the conduct of the Defendants set out herein; and
- (i) a tracing order and a constructive trust over the property directly or indirectly acquired with the proceeds from the improper conduct described herein.

6. The Plaintiff claims against Brian Hogan:

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- (j) damages, compensation and disgorgement in an amount to be specified before trial for breach of employment duties, breach of fiduciary duties, knowing assistance of breach of fiduciary duty and breach of trust, conversion, conspiracy, and unjust enrichment in connection with their participation in and involvement in the transactions as identified below.

7. The Plaintiff claims against Joanna Whitfield:

- (a) damages, compensation and disgorgement in such amount to be specified before trial for deceit, breach of fiduciary duty, breach of trust, breach of contract, conspiracy, knowing assistance of breach of fiduciary duty and breach of trust, knowing receipt of proceeds of breach of fiduciary duty and breach of trust in connection with her involvement in the CCE Transaction (described below); and
- (b) damages for the costs of enforcing and realizing on the Plaintiff's security in the CCE Receivership Proceedings (Court File No. CV-18-00610186-OOCL) on a full indemnity basis.

8. The Plaintiff claims against the Directors (as defined below):

- (a) damages and compensation in an amount to be specified before trial for negligence in connection with involvement in the matters as identified below, provided that the amounts sought do not include any amount apportionable to the fault or negligence actions of Golanski, Stan Dimakos, and Ken Topping, Kim Colacicco, Brian Mullan, Mitch Vininsky, Mary Benincasa, Benjamin Choi, David Finnie, Frederick Kreutlein, Heather Sarnecki and Lauren Thompson Cacovic; and

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- (b) contribution and indemnity for any damages arising from or in connection with the negligent failure to supervise or manage the Credit Union's relationship and interactions with Pace Securities Corp. and its direct and indirect subsidiaries, provided that the Plaintiff does not claim for any contribution and indemnity from Stan Dimakos and Ken Topping.
9. The Plaintiff claims against the defendants Larry Smith, Phillip Smith and the Directors (as defined below):
- (a) for contribution and indemnity pursuant to the provisions of the *Negligence Act*, R.S.O. 1990, c. N.1, as amended, for the \$25,000,000 paid to Investor Claimants (as defined below) in settlement of their claim for damages arising out of the design, development, offering, promotion, sale and the ultimate failure of the Preferred Shares (as defined below), to the extent any of those damages were caused or contributed to by any of them and provided that the Plaintiff does not claim for any contribution and indemnity from Stan Dimakos and Ken Topping.
10. The Plaintiff's claim against all of the Defendants:
- (k) does not seek any damages or compensation that are found to be attributable to the fault or negligence of Golanski, Dimakos or Topping, Colacicco, Mullan, Vininsky, Benincasa, Choi, Finnie, Kreutlein, Sarnecki or Thompson Cacovic;
- (l) for pre-judgment and post-judgment interest on all amounts claimed herein in accordance with the *Courts of Justice Act* R.S.O. 1990, c. C.42, as amended;

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- (m) for costs of this action; and
- (n) for such further and other relief as the Plaintiff may request and this Honourable Court consider just.

B. The Parties

11. Financial Services Regulatory Authority (“**FSRA**” or the “**Administrator**”) is the regulator of credit unions in Ontario pursuant to *Credit Unions and Caisses Populaires Act, 1994* (the “**Act**”). FSRA administers deposit insurance to members of Ontario’s credit unions and is the regulatory supervisor and, where required, administrator and liquidator of credit unions (as those terms are defined by the Act). Effective June 8, 2019, FSRA amalgamated with Deposit Insurance Corporation of Ontario, the former entity that carried out the prudential regulation of credit unions in Ontario under the Act. For ease of reference, the regulator shall be referred to as FSRA regardless of whether the event described took place prior to or after June 8, 2019.
12. PACE Savings & Credit Union Limited (“**PACE**” or the “**Credit Union**”) is a credit union incorporated under the Act. It is therefore an entity that is regulated by FSRA. The Credit Union has 17 branches throughout southwestern Ontario and has over \$1 billion in assets under management. PACE undertook substantial growth in the five to six years leading up to 2019, having acquired a number of other credit unions throughout southwestern Ontario.
13. Larry Smith (“**Larry**”) is an individual who resides at 53 Treegrove Circle, Aurora, Ontario (“**Treegrove**”), with his common law partner Alison Golanski, who was

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purportedly a consultant with the Credit Union (“**Golanski**”). Larry was both the President and CEO of the Credit Union in its various forms for approximately 20 years, until he appointed his son Phillip Smith (“**Phil**”) as the CEO in 2016, after which Larry continued to act as the President of the Credit Union. Both Larry and Phil were placed on administrative leave with pay upon the issuance of the Administration Order (as defined below) dated September 28, 2018. Both were terminated by the Administrator for cause on December 5, 2018.

14. Phil is an individual who, with his wife and children, resides with Larry and Golanski at the Treegrove residence. The Treegrove residence is registered in Phil’s name.
15. 1428245 Ontario Ltd. (“**142**”) is a corporation incorporated under the laws of Ontario with a registered address of 53 Treegrove Circle, Aurora, Ontario.
16. 809755 Ontario Ltd. (“**809**”) is a corporation incorporated under the laws of Ontario with a registered address of 53 Treegrove Circle, Aurora, Ontario. Elective Benefit Insurance Services (“**EBS**”) appears to be an unincorporated division or alternative name of 809.
17. 1724725 Ontario Ltd. (“**172**”) is a corporation incorporated under the laws of Ontario with a registered address of 8111 Jane Street, Suite 1, Vaughan, Ontario, the same address as the Credit Union. 172 is controlled by Larry and was used by him for his own benefit at all material times.
18. Malek Smith (“**Malek**”) is another adult son of Larry. Malek lives in a condominium at 59 East Liberty Street, Suite 605, Toronto, Ontario.

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19. 1916761 Ontario Ltd. (“**1916**”) is corporation incorporated under the laws of Ontario with a registered address of 59 East Liberty Street, Suite 605, Toronto, Ontario. 1916 is a holding company owned and controlled by Malek and Larry. Malek is the sole director and officer of 1916.
20. Larry, Phil, 142, 809, Malek, 1916, and 172 are together referred to as the “**Smith Defendants**”.
21. Frank Klees (“**Klees**”) is a long-time friend of Larry and Vice President of the Credit Union. Klees is also a consultant of the Credit Union through his company, Klees & Associates Ltd. Klees was also purportedly appointed as a director of the Credit Union in or around April 2018.
22. Ron Williamson (“**Williamson**”) is an individual residing at 86 Carrick Trail, Gravenhurst, Ontario, and Naples, Florida. Ron Williamson Quarter Horses Inc. (“**Quarter Horses**”) is a corporation incorporated under the laws of Texas with a registered address of 604 South Elm Street, Denton, Texas. Williamson is the President of Quarter Horses. R. Williamson Consultants Ltd. (“**Williamson Consultants**”) and together with Williamson and Quarter Horses, the “**Williamson Defendants**”) is a corporation connected to Williamson. Its registered address is believed to be 86 Carrick Trail, Gravenhurst, Ontario.
23. Brian Hogan (“**Hogan**”) is a former Vice President of the Credit Union and was Larry’s “right-hand man”.
24. Joanna Whitfield (“**Whitfield**”) is an individual residing in Toronto, Ontario. Whitfield

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is a real estate agent. Whitfield had a long-term intimate personal relationship with Larry.

25. Brent Bailey, Deborah Baker, Ian Goodfellow, Al Jones, Wendy Mitchell, Peter Rebellati, Jim Tindall, Pauline Wainwright, Neil Williamson, George Pohle, and Klees (together, the “**Directors**”) served as directors of the Credit Union during some or all of the material times. Each of Brent Bailey, Deborah Baker, Ian Goodfellow, Al Jones, Klees, Wendy Mitchell, Peter Rebellati, Jim Tindall, Pauline Wainwright, and Neil Williamson served as directors at the time of the Administration Order. George Pohle served as a director until in or around February 2018, when his term concluded and he was purportedly replaced by Klees.

C. FSRA’s Issuance of the Administration Order

26. FSRA issued an Administration Order pursuant to section 294 of the Act on September 28, 2018. Pursuant to the Administration Order, FSRA, as Administrator, took control of the Credit Union and now exercises the powers of the board of directors and controls the management of the Credit Union.

D. The Claims

(i) Failure to Disclose All Compensation in Contravention of the Act

27. Pursuant to section 140(5) of the Act and section 28(1) and (2) of the General Regulation, O. Reg. 237/09 (one of the two regulations promulgated under the Act) (the “**Regulations**”), Larry and Phil, as President and CEO, were required to ensure that the compensation of the five highest paid officers of the Credit Union earning over \$150,000 was reported in the Credit Union’s audited financial statements.

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28. Larry and Phil knowingly or recklessly underreported the income that they received both directly and indirectly from the Credit Union for years, including, but not limited to, each of the last six years of their employment. They underreported the income by millions of dollars.
29. Larry divided the income he received from the Credit Union between three separate agreements: (i) an employment agreement between the Credit Union and Larry; (ii) a consulting agreement between the Credit Union and 142; and (iii) a consulting agreement between the Credit Union and 809. Neither Larry nor Phil reported all of this income in the audited financial statements for the Credit Union as required under the Act and Regulations.
30. During the periods in which their income was underreported, Phil was an officer, director or shareholder of 142 and 809, and also received funds from 142 and/or 809.
31. In 2014, Larry's actual income was \$624,878 more than his reported income. In 2015, Larry's actual income was \$1,341,624 more than his reported income. In 2016, Larry's actual income was \$1,398,972 more than his reported income. In 2017, Larry's actual income was \$3,007,056 more than his reported income.
32. The failure of Larry and Phil to properly report the full amounts they were receiving as required by the Act and Regulations concealed and prevented the detection of the improper conduct described herein and misrepresented the true financial position of the Credit Union.
33. Larry and Phil, as the two most senior executives of the Credit Union, were ultimately

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responsible for the financial reporting of the Credit Union, particularly as it relates to the amounts each of them were receiving.

34. Larry and Phil are liable to the Credit Union for all amounts received from the Credit Union in excess of their reported income. Their conduct amounts to a breach of the Act and its Regulations, fraud, deceit, breach of employment duties, breach of fiduciary duties, knowing assistance of breach of fiduciary duties, conversion and unjust enrichment.

(ii) CCE Transaction

35. The Act and the Regulations prescribe limits on any investment that a credit union may make in a company without receiving FSRA's approval. Section 200 of the Act requires a credit union to obtain FSRA's prior approval before forming a subsidiary. Section 198 of the Act and Section 64 of the Regulations provide that a credit union may not directly or indirectly acquire more than a 30% ownership interest without first obtaining FSRA's approval.
36. Larry and Phil were aware of the 30% limit, as they had previously applied for approvals and had been censured by FSRA in 2014 for failing to obtain such approvals.
37. In 2016, Larry and Phil developed a scheme to evade their statutory and regulatory requirements in connection with the Credit Union's acquisition of Continental Currency Exchange Canada Ltd. ("CCE"). This scheme involved: (i) causing PACE to acquire a 30% interest in CCE for \$9.5 million; (ii) causing PACE to lend 2340938 Ontario Ltd. ("2340") another \$15 million to acquire 45% of CCE; and (iii) agreeing with 2340 and

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the vendor that, pursuant to a Unanimous Shareholders Agreement, as of March 31, 2019 the vendor could exercise a put option to force PACE to purchase the vendor's remaining 25% interest in CCE (**"CCE Transaction"**).

38. 2340 was a sham entity controlled by Larry and Phil. It was a company that was ostensibly owned by Whitfield, who had a personal relationship with Larry, and was a failed, defunct company that was still indebted to the Credit Union for over \$2 million following a previous failed and problematic loan that Larry had caused PACE to provide to it. Whitfield had no involvement in the negotiation of the CCE deal or management or control of 2340. Moreover, 2340 had no employees, and it was principally Larry's personal assistant at the Credit Union who administered the affairs of 2340 at Larry's direction.
39. Although the board of the Credit Union ostensibly approved the CCE Transaction, there was no actual or informed approval by the board of the transaction that Larry and Phil implemented. Larry and Phil did not disclose important and material information that was required to be disclosed to the board, including 2340's role in the transaction or Larry and Whitfield's personal relationship. Larry's connections to and interest in 2340, and with Whitfield in particular, were also never disclosed to the Board.
40. In connection with the CCE Transaction, Larry and Phil caused certain funds that should have been paid to the Credit Union from 2340 to instead be paid to themselves and certain others under the false pretence that the funds were being paid by CCE (the operating company) as fees for services provided to CCE when in fact the funds were paid by 2340 from funds that were to be paid to the Credit Union or held in trust for the Credit Union.

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41. Larry and Phil also directed and/or acquiesced to the improper diversion of \$591,000 of funds held by 2340, which were to be paid to or held in trust for the Credit Union, as follows:
- (a) 2340 received quarterly dividends from CCE of \$450,000 to service interest on the loan payments from PACE. These dividend payments were more than the amounts 2340 required to pay the interest on its loan from PACE. Whitfield received \$141,000 in payments from 2340 since January 2017 but did no work for the company; and
 - (b) After the Administration Order was issued, Larry, Phil or Whitfield misdirected the \$450,000 dividend payment from CCE that was payable on November 1, 2018, and caused it to be paid into an account at Royal Bank of Canada in contravention of the various contracts with PACE requiring that the dividends be deposited at PACE.
42. The \$591,000 in diverted funds and the other payments directed by Larry and Phil to themselves and others total approximately \$800,000.
43. In December 2018, the Administrator commenced receivership proceedings in respect of 2340 in order to protect the Credit Union's interests in the funds that had been misdirected (the "**2340 Receivership Proceedings**"). The Fuller Landau Group Inc. was appointed as the receiver, and the receiver was able to locate and recover the diverted \$450,000 from another bank. The receivership proceedings are on-going. The Credit Union has suffered damages in the amount of the costs associated with the prosecution

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of the 2340 Receivership Proceedings.

44. As part of the 2340 Receivership Proceedings, the shares of CCE held by 2340 have been transferred to the Credit Union.
45. The transactions through which Larry and Phil caused the Credit Union to acquire the interests in CCE also required the Credit Union to acquire the remainder of the shares from CCE's founder ("Penfound") anytime after March 2019 pursuant to a put option., Penfound exercised the option, and as a result, the Credit Union was left owning the entirety of CCE, contrary to the provisions of the Act and Regulations.
46. In addition to the foregoing, Larry and Phil failed to cause the Credit Union to obtain the necessary professional assistance and advice, or to take the necessary steps, to conduct appropriate or adequate due diligence into CCE, the proposed transaction, valuations of CCE, and the agreement giving effect to the transaction. As a result of such failures, the Credit Union will suffer a loss on its investment in CCE for which Larry and Phil are liable.
47. In total, the Credit Union has paid approximately \$35 million for the acquisition of CCE, which acquisition only occurred because of Larry's and Phil's fraudulent scheme. CCE has lost most of its value since the CCE Transaction was entered into, resulting in significant loss to the Credit Union.
48. The Credit Union has recently been able to sell CCE for \$16 million in mitigation of its losses. The sale of CCE to DUCA Financial Services Credit Union Ltd. is scheduled to close March 31, 2022.
49. Larry and Phil are liable to the Credit Union for fraud, deceit, breach of fiduciary duties,

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knowing assistance of breach of fiduciary duties, knowing assistance of breach of trust, breach of employment duties, conversion, and unjust enrichment.

50. Whitfield is liable to the Credit Union for deceit, breach of fiduciary duty, breach of trust, breach of contract, conspiracy, knowing assistance of breach of fiduciary duty and breach of trust, knowing receipt of proceeds of breach of fiduciary duty and breach of trust.
51. The issues raised in respect of the CCE Transaction are also the subject of the proceedings in Court File No. CV-18-00610186-00CL, which is currently stayed as a result of the Receivership Order that was granted by the Ontario Superior Court of Justice (Commercial List). The allegations and claims against Larry, Phil and Whitfield made in the Notice of Action, dated December 5, 2018, in Court File No. CV-18-00610186-00CL are incorporated herein. Whitfield has consented to be added as a defendant to this action so that all claims in relation to the CCE Transaction can be advanced in a single proceeding.

(iii) Geranium Joint Ventures

52. Geranium Corporation (“**Geranium**”) is a company that develops residential real estate projects.
53. Larry and Phil caused the Credit Union to enter into a number of joint venture projects with, and to make loans to, certain of Geranium’s projects.
54. Larry and Phil structured these agreements so PACE ostensibly owned only the statutory-limit of 30% of each joint-venture entity, but PACE in fact owned greater ownership rights by being contractually entitled to more than 30% of the profits and was obligated

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to provide more than 30% of the capital for each of the projects. This structure was in breach of sections 198 and 200 of the Act and section 64 of the Regulations.

55. Further, Larry caused the Credit Union to pay \$5.33 million to himself (directly and indirectly through 142, 809, 1916 and other defendants) from PACE and companies related to Geranium (who took such funds from monies paid by, or owing to, PACE). These amounts were not earned by Larry or the companies who received the payments, and were not approved by the Credit Union.
56. In addition to these payments, Larry caused PACE to pay Klees, who purportedly had a consulting agreement that also made him an officer of the Credit Union, \$2.7 million in connection with the Geranium projects, despite the fact that the board was only advised that Klees would receive \$1.6 million over the life of certain of these projects and despite the fact that those projects were in early stages of development and the funds were not due and owing. Klees kept these funds despite not being entitled to such funds.
57. Furthermore, Larry directed Geranium (or companies related or connected to it) to pay him, directly or indirectly through one of the other corporate defendants, additional sums on account of “consulting fees” or commissions. These amounts were taken from funds advanced by the Credit Union to Geranium or funds that were the Credit Union’s share of profits from the various joint ventures.
58. These secret commissions, many of them styled as “advance” payments, were not disclosed to the Credit Union or the Credit Union’s board as required by the Act or Regulations.

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59. To the extent that Larry directed such improper payments through 172 or 1916, 172, 1916, and Malek were aware, were wilfully blind, or ought to have been aware of these improper transactions, and took no steps to inquire about the legitimacy or the source of the funds.
60. Larry, Phil, and Klees (acting as consultant and officer) failed to cause the Credit Union to obtain the necessary professional assistance and advice, or to take the necessary steps, to conduct appropriate or adequate due diligence into Geranium and the proposed transactions, valuations of the various transactions entered into with Geranium and the compensation being taken by Larry, Klees and others in connection with these transactions.
61. Klees misrepresented and concealed the true extent of his relationship with Larry and the Credit Union from the other directors and officers, including the fact he received monthly payments under an alleged consulting agreement and his purported appointment as a Vice President of the Credit Union. In particular, Klees did not disclose these facts to the other directors when he applied to be a director of the Credit Union, despite the fact that such disclosure was required by the Act and the director nomination forms he completed.
62. As a result of the foregoing conduct:
 - (a) Larry and Phil are liable to the Credit Union for fraud, deceit, breach of fiduciary duties, breach of employment duties, conversion, unjust enrichment, knowing assistance of breach of fiduciary duty and breach of trust, and knowing receipt of proceeds from breach of fiduciary duty and breach of trust;

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- (b) Klees is liable to the Credit Union for fraud, deceit, breach of fiduciary duties, conversion, unjust enrichment, knowing assistance of breach of fiduciary duty and breach of trust, and knowing receipt of proceeds from breach of fiduciary duty and breach of trust; and
- (c) To the extent that Larry directed payments through 142, 809, 172, or 1916, those companies, and Malek (to the extent that 1916 was involved), are liable to the Credit Union for conversion, unjust enrichment, knowing assistance of breach of fiduciary duty and breach of trust, and knowing receipt of proceeds from breach of fiduciary duty and breach of trust.

(iv) SusGlobal Energy Corp.

- 63. Larry and Phil caused the Credit Union to advance funds to SusGlobal Energy Corp. (“**SusGlobal**”), a borrower of the Credit Union, in a highly improvident and improper manner, and contrary to the Credit Union’s risk tolerance.
- 64. Larry caused PACE to advance \$1.6 million as part of the first tranche of a loan when at that time SusGlobal’s only asset – a contract with two municipalities – had been terminated.
- 65. As part of the advancement of this tranche, Larry and/or Phil caused PACE to pay the defendant Williamson (or other of the Williamson Defendants or another company owned or controlled by Williamson) a “finder’s fee” representing 25% of the funds advanced, from which Larry thereafter directly or indirectly received a secret commission of USD\$150,000 back from one of the Williamson Defendants (or another company owned or controlled by Williamson) by directing the funds to 172, Golanski, 1916 and Malek.

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66. Additionally, Larry and Williamson each received 810,000 shares in SusGlobal as part of their secret commission.
67. 172, 1916, and Malek were aware, were wilfully blind, or ought to have been aware of these improper transactions, and took no steps to inquire about the legitimacy or the source of the funds.
68. Subsequently, in September 2017, PACE advanced an additional \$3.9 million to SusGlobal for a combined total exposure of \$5.5 million, which also violated the Credit Union's risk tolerance.
69. The advancement of this \$1.6 million tranche, and the total \$5.5 million loan to SusGlobal, was contrary to the Credit Union's risk tolerance and policies, and was contrary to any reasonable loan underwriting practices.
70. To date, the SusGlobal loan has not been repaid and the anticipated loss to the Credit Union is anticipated to be \$3.8 million.
71. As a result of the foregoing conduct:
 - (a) Larry and Phil are liable to the Credit Union for fraud, deceit, breach of fiduciary duties, conversion, unjust enrichment, knowing assistance of breach of fiduciary duty and breach of trust, and knowing receipt of proceeds from breach of fiduciary duty and breach of trust against the Credit Union; and
 - (b) the Williamson Defendants, 172, Malek and 1916 are liable to the Credit Union for fraud, deceit, conversion, unjust enrichment, knowing assistance of breach of

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fiduciary duty and breach of trust, and knowing receipt of proceeds from breach of fiduciary duty and breach of trust.

(v) Inveraray Glen

72. Inveraray Glen is a real estate project in the Bracebridge, Ontario area. It is related to Evanco Corporation, which dealt with certain operational matters at the project (Inveraray Glen and Evanco Corporation are together referred to as “**Inveraray Glen**”).
73. As of the date of the Administration Order, Inveraray Glen had \$11.4 million in outstanding loans to the Credit Union, including accrued interest (the “**Inveraray Glen Loans**”). The loans have been in default since 2015.
74. Larry and Phil intentionally refused to record the bad loan charges required by sections 90 and 264(1)(g) of the Act or FSRA By-Law No. 6 (described in more detail below), which provide that charges for bad loans must be booked in the Credit Union’s records on a monthly basis. The required charge with respect to the Inveraray Glen Loans would have eliminated the Credit Union’s profits for the year in which the charge was booked.
75. Larry and Phil refused to book those charges despite the fact that they were in possession of two appraisals that showed that both the loan and the collateral were materially impaired. Larry and Phil instructed three members of the credit committee to hide or not disclose the appraisals, including from the Credit Union’s CFO. As a result, they intentionally overstated the Credit Union’s profits in the audited financial statements.
76. Larry advised certain employees at the Credit Union, in addition to certain directors, that he was allegedly in discussions with a developer in the Muskoka area who was interested

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in creating a “fund” that would have acquired the Inveraray Glen properties for more than the outstanding loan. No such arrangement was possible or actually contemplated.

77. As a result of the foregoing conduct, Larry and Phil are liable to the Credit Union for fraud, deceit, breach of fiduciary duties, breach of employment duties, conversion and unjust enrichment.

(vi) Lora Bay

78. Larry and Phil caused PACE to advance \$6 million, in the form of a convertible debenture that was converted to equity, to the Lora Bay Corporation (“**Lora Bay**”), a real estate development project company. Lora Bay is a company that is majority owned by Larry Dunn (“**Dunn**”) or a company related to him. Dunn already had millions of dollars in loans with the Credit Union at the time of the Credit Union’s investment in Lora Bay.
79. The advancement of the initial loan to Lora Bay was contrary to the Credit Union’s risk tolerance and policies, and was contrary to any reasonable loan underwriting practices.
80. In January 2017, Larry caused the Credit Union to directly or indirectly pay \$180,000 to 1916 or Malek for “consulting and referral” fees in connection with Lora Bay, which fees were not payable, not earned, and were in fact a secret commission.
81. 1916 and Malek were aware, were wilfully blind, or ought to have been aware of these improper transactions, and took no steps to inquire about the legitimacy or the source of the funds.
82. As a result of the foregoing conduct:

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- (a) Larry and Phil are liable to the Credit Union for fraud, deceit, breach of fiduciary duties, breach of employment duties, conversion, unjust enrichment, knowing assistance of breach of fiduciary duty and breach of trust, and knowing receipt of proceeds from breach of fiduciary duty and breach of trust; and
- (b) 1916 and Malek are liable to the Credit Union for fraud, deceit, conversion, unjust enrichment, knowing assistance of breach of fiduciary duty and breach of trust, and knowing receipt of proceeds from breach of fiduciary duty and breach of trust.

(vii) Noble House Development Corporation

- 83. Noble House Development Corporation (“**Noble House**”) owns a public storage facility in Huntsville, Ontario.
- 84. Larry and Hogan caused PACE to advance a \$5.5 million secured line of credit to Noble House to replace the incumbent lender.
- 85. Larry and Hogan caused the loan to Noble House to be advanced despite the fact that the loan to value ratio of this loan is in violation of both section 184 of the Act and section 48 of the Regulations, and despite the fact they knew the borrower could not service the interest.
- 86. The advancement of this loan was contrary to the Credit Union’s risk tolerance and policies, and was contrary to any reasonable loan underwriting practices. The Credit Union has incurred a \$4.9 million loss on the loan.

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87. The funds advanced by PACE were also used to pay a \$452,000 “broker fee” to Williamson Consultants, who then paid 50% of the “broker fee” as a secret commission directly or indirectly to 1916 for Larry and Malek’s benefit.
88. 1916 and Malek were aware, were wilfully blind, or ought to have been aware of these improper transactions, and took no steps to inquire about the legitimacy or the source of the funds.
89. As a result of the foregoing conduct:
- (a) Larry and Phil are liable to the Credit Union for fraud, deceit, breach of fiduciary duties, breach of employment duties, conversion, unjust enrichment, knowing assistance of breach of fiduciary duty and breach of trust, and knowing receipt of proceeds from breach of fiduciary duty and breach of trust; and
 - (b) Williamson, Williamson Consultants, Malek and 1916 are liable to the Credit Union for fraud, deceit, breach of fiduciary duties, conversion, unjust enrichment, knowing assistance of breach of fiduciary duty and breach of trust, and knowing receipt of proceeds from breach of fiduciary duty and breach of trust
- (viii) 1934811 Ontario Ltd. (“193”)**
90. Larry and Hogan caused PACE to provide 193 with a loan facility of up to \$10 million. The current amount outstanding under the facilities is approximately \$8.2 million.

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91. The advancement of this loan was contrary to the Credit Union's risk tolerance and policies, and was contrary to any reasonable loan underwriting practices.
92. Larry received payments in the nature of a secret commission in connection with this transaction. Hogan facilitated the arrangement. As part of an agreement between the parties involved in the transaction, Larry was paid \$275,000 plus HST for causing PACE to advance funds to 193, while Williamson (or his companies) received \$300,000. Larry directed this secret commission, with Hogan's involvement, to 172.
93. 172 was aware, was wilfully blind, or ought to have been aware of these improper transactions, and took no steps to inquire about the legitimacy or the source of the funds.
94. Bill Player ("**Player**") is a friend or associate of Larry, and was previously sentenced to fourteen years in jail for fraud involving the notorious collapse of certain savings and loan companies in the 1980s. As part of the 193 transaction, Player was to receive certain rights to 193's future profits. These rights were then later given by Player to Ray Jarvis ("**Jarvis**") in exchange for Jarvis obtaining a loan from PACE, through Larry, and giving the proceeds of the loan to Player to pay his creditors in a formal consumer proposal under the *Bankruptcy and Insolvency Act* (the "**Jarvis Transaction**"). The Jarvis Transaction was an improvident loan, the exact nature of which Larry misrepresented to PACE, and was contrary to the Credit Union's risk tolerance and policies and any reasonable loan underwriting practices.
95. The Administrator interceded to prevent this loan from being advanced, but incurred significant professional fees in doing so.

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96. As a result of the foregoing conduct:

- (a) Larry and Hogan are liable to the Credit Union for fraud, deceit, breach of fiduciary duties, breach of employment duties, conversion, unjust enrichment, knowing assistance of breach of fiduciary duty and breach of trust, and knowing receipt of proceeds from breach of fiduciary duty and breach of trust; and
- (b) the Williamson Defendants; and 172 are liable to the Credit Union for fraud, deceit, conversion, unjust enrichment, knowing assistance of breach of fiduciary duty and breach of trust, and knowing receipt of proceeds from breach of fiduciary duty and breach of trust.

(ix) Lagasco Transaction

97. In connection with loans made to Lagasco Inc. (“**Lagasco**”), Larry and Phil undertook efforts to evade the restrictions in the Act and Regulations that limit the amount that may be lent to any group of persons who are connected.
98. The principal of Lagasco is Jane Lowrie (“**Lowrie**”). Both Larry and Lowrie are connected to another business, Tribute Resources Inc. (“**Tribute**”), a publicly traded company. Larry is a director of Tribute, as is Lowrie.
99. Section 191 of the Act stipulates that a credit union “shall not make loans in excess of such lending limits as may be prescribed or as may be ordered under subsection (2) or (5)”. The lending limits for credit unions are specified in the Regulations. Under section 58(2) of the Regulations, “a credit union may make a loan to a person if, as a result of

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making the loan, the total amount of all outstanding loans made to the person and any connected persons *would not* exceed 25% of the credit union's regulatory capital".

[emphasis added]

100. At the time, PACE's regulatory lending limit was approximately \$16.8 million to a single borrower or a group of "connected" persons (as defined by the Regulations).
101. Larry, Phil and Hogan (until he retired) undertook efforts to advance a loan to Lagasco of almost \$30 million in connection with Lagasco's attempt to purchase the assets of Dundee Oil & Gas through its CCAA proceedings that were then proceeding before the Ontario Superior Court of Justice (Commercial List).
102. Larry, Phil and Hogan actively worked with Lagasco and Lowrie to divide the loan between Lagasco and a brand new company, Forbes Resources Inc. ("Forbes"), that they alleged was separate and independent despite it purportedly being controlled by Lowrie's four adult children. In doing so, Larry and Phil ignored information and advice from the Credit Union's staff and the Credit Union's own counsel that the loans were improvident and contrary to the Act and Regulations. Moreover, they proceeded with the transaction despite the fact that they knew, or ought to have known, the transaction in substance was only one loan to Lagasco. In attempting to create the appearance of complying with the Act and Regulations, Larry, with the knowledge or awareness of Hogan or Phil, gave up normal, customary and prudent protection for the Credit Union, such as guarantees, which would customarily be required for transactions of this nature.
103. Although the Administrator was able to stop the bulk of this transaction after the

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commencement of the Administration proceedings, the Credit Union incurred substantial costs and damages in stopping the loan and in attempting to limit the damage caused as a result of Larry's, Phil's and Hogan's breaches of fiduciary duties. Further, the Credit Union has not recovered the initial \$3 million advanced in another connected loan as part of the same transaction.

104. The advancement of the Lagasco loans was contrary to the Credit Union's risk tolerance and policies, and was contrary to any reasonable loan underwriting practices.
105. As a result of the foregoing actions, Larry, Phil and Hogan are liable for fraud, deceit, breach of fiduciary duties, breach of employment duties, conversion and unjust enrichment.

(x) Diversion of Funds to Golanski, Larry's Common Law Partner

106. Larry engaged in a number of transactions in which he caused the amounts owing to the Credit Union to be diverted to either his common law partner Golanski or to 172, which is a company ostensibly controlled by Golanski but is *de facto* controlled by Larry, without the required disclosure to the board of directors.
107. One such situation that exhibits Larry's efforts to transfer PACE's funds to persons related to him pertains to PACE's arrangement with City View Bus Sales & Service Ltd. ("**City View**"), in which Larry directed that 172 be paid commission for work that Golanski did not do, or which could have been done by an existing employee at no additional cost to the Credit Union.

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108. On or about October 2016, Larry agreed to provide City View, through PACE, with a \$5 million asset-based financing facility which City View would draw upon based on purchase orders it received for the construction of buses. In addition, PACE would charge a fee or commission of 30% of the gross margin expected under the purchase orders. Larry required that this fee owing to PACE to be split between PACE and his common law spouse, Golanski, despite Golanski not providing any meaningful services to City View or PACE in relation to the business.
109. Furthermore, Larry caused PACE to enter into a consulting agreement with 172 under which 172 received monthly payments from PACE for purported consulting services provided by Golanski. However, this consulting agreement was merely another means of diverting funds to Golanski or Larry through the payment of retainers and expenses. Between January 1, 2015 and September 30, 2018, 172 received \$149,160 in monthly retainers but only earned \$9,788 in commissions, illustrative of the minimal work done by her. Larry exercised control over 172's accounts and affairs and used the company for his own benefit.
110. Larry prepared the consulting agreement for 172, and subsequent revisions to the consulting agreement, without Golanski's knowledge or involvement. Neither Golanski nor 172 performed any services or any meaningful services to warrant the payments made pursuant to the alleged consulting agreement.
111. As a result of the foregoing conduct, Larry and 172 are liable to the Credit Union for fraud, conversion, unjust enrichment, knowing assistance of breach of fiduciary duty and breach of trust, and knowing receipt of proceeds from breach of fiduciary duty and

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breach of trust. The damages claimed by the Credit Union do not include any amount apportionable to the actions of Golanski.

(xi) Failure to Abide by By-Law No. 6

112. Larry and Phil, who were directly and ultimately responsible for the commercial loan portfolio, failed to abide by the Credit Union's Credit Policy as well as the Act and the Regulations.
113. According to FSRA By-Law No. 6, Larry and Phil were required to follow the processes in By-Law No. 6 to value and, if necessary, write-down the value of loans on the Credit Union's books and records whose values had declined as determined by By-Law No. 6
114. Larry and Phil misrepresented the value of a number of loans in the Credit Union's books and records. They misrepresented the value of loans by intentionally or negligently failing to properly review, or cause to be reviewed, the loans pursuant to FSRA By-Law No. 6, which has the force of a Regulation, as against the value of such loans on the books and records of the Credit Union, thereby misstating the Credit Union's financial position to FSRA and the Credit Union's members, and misrepresenting their performance.
115. The failure and refusal of Larry and Phil to properly review the value of the Credit Union's loans, and to cause such review to be done, and to adjust the books and records as required, concealed the true financial position of the Credit Union from the members and the regulators and allowed Larry and Phil to continue to advance loans that were contrary to the Credit Union's policy and risk tolerance. As a result, they prevented detection of the loan underwriting problems, which would have prompted corrective actions, and thus they

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were able to ensure that they continued to receive their salary and bonuses based on an inaccurate view of the Credit Union's activities and financial position, and prevent earlier regulatory intervention. Accordingly, the Credit Union continued to make bad loans, and failed to collect on loans when appropriate, thereby incurring additional losses.

116. As a result of their failure to appropriately abide by By-Law No. 6, the Act and the Regulations in respect of the required ongoing valuation of commercial loans, Larry and Phil are liable to the Credit Union for breach of fiduciary duties, knowing assistance of breach of fiduciary duties, conversion, and unjust enrichment against the Credit Union.

(xii) False Invoices

117. Larry caused, with Phil's acquiescence, the Credit Union to pay invoices purportedly rendered by 142, 809 (a.k.a. EBS), 1916, and 172 for services that were not in fact rendered to the Credit Union. In the alternative, if the services were rendered, the quantum of the invoices was grossly disproportionate to the value of the services rendered.
118. The types of services allegedly rendered, as described on the invoices, include "trust fund administration" for the trust fund established for the Impugned Employment Contracts. There were ostensibly fees for managing the trust fund holding the termination or severance payments for certain employees at the Credit Union (discussed above). Arn Reisler, a lawyer and long-time friend of Larry's, was the trustee of the trust fund, while Kim Colacicco ("**Colacicco**") administered the trust fund at the Credit Union. Further, the trust fund required little-to-no administration. Despite this, Larry caused 142 and 809 (a.k.a. EBS) to invoice the Credit Union and to be paid by the Credit

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Union at least \$215,000 in improper trust fund administration fees between 2011 and 2018. Larry caused 142 and 809 to invoice these amounts to the Credit Union despite the fact that the contract for 142 provided that the amounts paid to it was on account of trust fund administration.

119. Additional false invoices were rendered by Larry through the various companies for pension administration, consulting fees, referral fees, retainers, commissions, for “contractual adjustments”, and for other miscellaneous services.
120. The total amount of such false invoices is approximately \$2,649,343.
121. As a result of the foregoing conduct, Larry, Phil, 142, 809 (a.k.a. EBS), 1916, and 172 are liable to the Credit Union for fraud, deceit, breach of fiduciary duties, conversion, unjust enrichment, knowing assistance of breach of fiduciary duty and breach of trust, and knowing receipt of proceeds from breach of fiduciary duty and breach of trust.

(xiii) Conspiracy

122. The Administrator states that the Smith Defendants, amongst themselves, and with Klees, Klees & Associates Ltd., the Williamson Defendants, Whitfield and Hogan, at precise dates and times known only to them, agreed amongst themselves to unlawfully engage in the above-mentioned conduct in order to unlawfully obtain money and other assets of value from and at the expense of the Credit Union. In particular, the Administrator states that the above-noted defendants agreed amongst themselves to carry out the various transactions as is described above, to violate the Act, to obtain or pay secret commissions, and to provide false invoices to the Credit Union, all as is detailed above. The

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Administrator further states that the conduct described above:

- (a) was undertaken with the predominant purpose of injuring the Credit Union and its economic interests; and/or
- (b) was directed toward the Credit Union and the above-noted defendants ought to have known that, in the circumstances, injury and economic harm to the Credit Union would ensue.

(xiv) Concealment of Monies Taken by the Smith Defendants

- 123. Larry brought a folder with him to board meetings and audit committee meetings. This folder contained various invoices, agreements, and other documents, including documents that purported to justify the payment of amounts to Larry or other Smith Defendants. Documents were added to the folder by Colacicco or Larry's personal assistant on his instruction.
- 124. No other officers other than Larry, Phil, and Colacicco were aware of the contents of the folder prior to a meeting.
- 125. Larry brought the folder to various board and committee meetings. The documents inside the folder were already stamped with an "Approved by Audit Committee" stamp. This stamp was kept in the vicinity of Colacicco's desk, which she left unlocked.
- 126. During or after a board or committee meeting, Larry sat with two directors and caused or instructed them to sign or initial beside the stamp. Larry purposefully did not give

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accurate or sufficient information to the two directors as to the contents of the documents or the relationship of Larry and the other Smith Defendants to the various individuals and companies named within those documents. Nor did Larry show the contents of the folder to the whole board or committee members. Larry discouraged any inquiries by other directors as to the contents of the folder.

127. Larry purposefully provided insufficient disclosure in order to conceal and obfuscate the existence of the amount of the monies being taken by him or otherwise being directed to the other Smith Defendants.
128. Moreover, the information contained in the folder was not sufficient to describe the nature and purpose of the payments or the basis on which the payments were justified. As a result, the documents within the folder were not properly approved by the board.
129. This “folder method” was purposefully employed by Larry, and acquiesced to by Phil, so that they could create a record that made it appear that the monies received by the Smith Defendants were ostensibly approved by the board, even though they knew or ought to have known that the board was in fact not made aware of the payments that were purporting to be “approved” by the board. By the use of the folder method, Larry and Phil were able to conceal the true amounts being taken directly by Larry, Phil, and the other Smith Defendants. The use of the folder method was part of Larry’s and Phil’s on- going concealment and obfuscation of the improper and dishonest receipt of monies taken directly or indirectly from the Credit Union, as described above.

(xv) Compensation Agreements

130. Larry and Phil caused the Credit Union to enter into certain compensation agreements

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with themselves and certain other officers and employees that provided for salary, bonus, and severance payments that were materially unreasonable (“**Impugned Employment Contracts**”) and contrary to the Credit Union’s interests.

131. The Impugned Employment Contracts contain the following provisions that were not reasonable or in the interests of the Credit Union:
- (c) a provision providing that the employees would receive a substantial termination payment whether or not termination was for cause or the employee resigned;
 - (d) some of these agreements provided these employees (including themselves) with termination payments far in excess of the amounts contemplated by law; and
 - (e) the termination payments were to be paid into a trust account without regard to the resulting tax requirements of establishing such an arrangement, including any requirement to pay withholding taxes, thereby exposing the Credit Union to potential penalties and other adverse financial consequences for failure to comply with requirements under the applicable tax laws.
132. Larry and Phil failed to cause the Credit Union to engage proper compensation and professional consultants or otherwise take the necessary steps to determine whether these extraordinary salary, bonus, and severance payments were reasonable or appropriate.
133. Moreover, they failed to engage the necessary experts to ensure that the termination trusts were organized in a manner that complied with the applicable tax laws. As a result, the termination trusts were organized in a manner that may be contrary to the applicable tax laws, thereby exposing the Credit Union to penalties and other damages as a result.

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134. As a result of the foregoing, Larry and Phil are liable to the Credit Union for breach of fiduciary duties and negligence.

(xvi) **De-risking Credit Union's Loan Portfolio**

135. Larry and Phil caused and/or permitted the Credit Union to enter into numerous irregular and improper commercial loans. These loans were all sourced, directed or acquiesced in by Larry and Phil in breach of their duties to the Credit Union. In many instances, the loans were made to Larry's and/or Phil's associates and business partners on terms that were not commercially-reasonable and that were not in the Credit Union's interest.

136. In addition, Larry and Phil failed to fulfill their fiduciary and employment duties by properly overseeing the Credit Union's commercial and retail loan portfolio. They failed to ensure that appropriate loan approval and review processes were in place. As a result, the Credit Union made loans that were not prudent and were outside of any reasonable risk tolerance for a credit union. These loans and the loans referred to in paragraph 147 are the "Imprudent Loans".

137. The Credit Union recently discovered that Larry's and Phil's failure to implement proper controls and oversight of the Credit Union's retail loan business allowed a former employee to commit fraud in a number of loan accounts and account transfers.

138. To mitigate its losses on the Imprudent Loans, the Credit Union has had to de-risk and unwind these loans. Approximately \$205 million of Imprudent Loans have been de-risked since 2019 and the process is ongoing.

139. The Imprudent Loans include loans that were made to Lowrie, Peter Budd and related

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parties, Applefest, Silicorp and 124 Wellington.

140. The losses to date on these Imprudent Loans exceeds \$8 million. Further losses are expected as the unwinding of the Imprudent Loans continues.
141. Larry and Phil are liable to the Credit Union for damages in relation to the Imprudent Loans. The damages suffered by the Credit Union include the lost opportunity to deploy the loan amounts towards other more prudent and commercially-reasonable loans and transactions.

(xvii) Directors' Breach of the Standard of Care

142. Each of Brent Bailey, Deborah Baker, Ian Goodfellow, Al Jones, Wendy Mitchell, Peter Rebellati, Jim Tindall, Pauline Wainwright, and Neil Williamson were directors of the Credit Union at all material times and served in that capacity until the time of the Administration Order.
143. George Pohle served as a director until in or around February 2018, when his term concluded and he did not seek re-election.
144. Klees, Larry's long-time friend, Vice President of the Credit Union, and consultant of the Credit Union through his company, was elected as a director of the Credit Union in or about April 2018 to fill the vacancy left by George Pohle's departure.
145. Brent Bailey, Deborah Baker, Ian Goodfellow, Al Jones, Wendy Mitchell, Peter Rebellati, Jim Tindall, Pauline Wainwright, Neil Williamson, George Pohle, and Klees (together, the "**Directors**") each owed a duty of care to the Credit Union pursuant to the Act and at common law, such that each of them had an obligation to act with the care, skill and

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diligence reasonably required by the circumstances.

146. In each of the capacities occupied by these Directors there was a foreseeable risk that the Credit Union would be harmed if the actions of Larry, Phil, and the other employees of the Credit Union fell below the applicable standard of care.
147. The Directors, individually and collectively, had the ability to cause the Credit Union to take actions and enter into transactions that would affect the Credit Union's legal and practical rights and interests. The Credit Union and its members relied upon each of the Directors to exercise their powers and discretion in a manner that was consistent with sound business and lending practices, the Credit Union's regulatory requirements, the Act and the Credit Union's policies, and their duty of care.
148. Each of the Directors exercised their powers and discretion negligently and in breach of their duty of care to the Credit Union in relation to the transactions described above and their supervision of Larry, Phil, and the management of the Credit Union generally. In particular:
 - (a) The Directors had a duty to exercise their powers to ensure that the Credit Union's lending activities and the investments it was entering into were being undertaken in compliance with the Credit Union's policies and statutory obligations. The Directors failed to conduct sufficient or meaningful due diligence, or to ensure competent professionals were retained by the board or the Credit Union to conduct sufficient due diligence, and to ensure such compliance; and

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- (b) The Directors had a duty to exercise their powers so as to oversee and supervise the Credit Union's officers – in particular Larry and Phil, as President and CEO respectively. This duty required that they make meaningful enquiries as to payments being made to Larry, Phil, their family members and friends, and their related numbered companies received in excess of their contractual salary and in relation to transactions entered into by the Credit Union. The Directors failed to make such meaningful enquiries. In the alternative, if the Directors made such meaningful enquiries, they breached their duty of care in failing to prevent the improper payments.
149. Among the matters for which the Directors failed to exercise the necessary duty of care in considering the CCE Transaction, the Geranium Joint Ventures and matters relating to Pace Securities Corp. ("PSC") (described below), by failing to engage, or cause management to engage, the necessary independent experts to assist them in their decision-making process, and by failing to exercise the decision-making function sufficiently independently from management.
150. PSC is a wholly-owned subsidiary of the Credit Union.
151. PSC was an investment dealer regulated by the Investment Industry Regulatory Organization of Canada and an investment fund manager regulated by the Ontario Securities Commission.
152. One of PSC's subsidiaries was Pace Financial Limited ("PFL"). PFL carried on business as an investment vehicle for accredited investors to earn fixed dividends from an

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- investment in a basket of high-yield bonds (the “Preferred Shares”). PSC provided brokerage, investment and business management services to PFL in respect of the Preferred Shares.
153. On May 14, 2020, the Ontario Superior Court of Justice issued a Winding-Up Order in Court File No. CV-2000641059-00CL (the “PSC Application”) directing that PSC and its subsidiaries, including PFL, be wound-up and appointing Ernst & Young Inc. as the liquidator of the estates and effects of PSC and its subsidiaries.
154. On August 6, 2020, the Ontario Superior Court of Justice appointed Representative Counsel to advance the interest of “Investor Claimants” within the PSC Application. Investor Claimants included all individuals asserting or who may be entitled to assert a claim or cause of action as against PSC or any related organizations (including the Credit Union) in respect of certain investments made by the Investor Claimants.
155. The Investor Claimants asserted that they suffered significant actionable losses in connection with their investments in the Preferred Shares issued by PFL, and issued by another company, First Hamilton Holdings Inc. (“FHH”), to which PSC also provided certain management services. The Investor Claimants claimed that the Credit Union is liable for their losses, at least in part because the Investor Claimants (or some of them) allege they were referred to PSC by the Credit Union or were sold Preferred Shares directly by the Credit Union.
156. The Credit Union resolved the Investor Claimants’ claims by paying \$25,000,000.

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157. The Directors, as well as Larry and Phil, owed both a duty of care and fiduciary duties to the Credit Union to properly supervise and manage the Credit Union, including its relationship with PSC and its subsidiaries, and to ensure that the distribution of the Preferred Shares was conducted in a regulatory compliant manner. The damages claimed by the Investor Claimants were caused or contributed to, in whole or in part, by the Directors', and Larry and Phil's, negligence and/or breach of fiduciary duty in that they failed to properly supervise and manage the Credit Union, including with respect to its relationship with PSC and its subsidiaries.
158. The Directors, and Larry and Phil, are liable to the Credit Union for contribution and indemnity for the \$25,000,000 that was paid to the Investor Claimants to resolve their claims. The Credit Union pleads and relies upon sections 1 and 2 of the *Negligence Act*, R.S.O. c. N. 1, as amended.
159. The conduct described above was contrary to the interests of the Credit Union and a breach of the duty of care owed by the Directors. These breaches caused losses to the Credit Union, as set out in these pleadings. As a result, the Directors are liable to the Credit Union for negligence for the losses described above. The amounts sought against the Directors, and Larry and Phil, do not include any amount properly apportioned to the actions of Stan Dimakos and Ken Topping.
- E. Defendants Are Jointly and Severally Liable to the Credit Union As A Result of Their Misconduct**
160. Each of the Defendants has engaged in wrongful conduct against the Credit Union. Such wrongful conduct includes, but is not limited to, fraud, deceit, breach of fiduciary duties,

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breach of employment duties, negligence, conversion, unjust enrichment, breach of trust, knowing assistance of breach of fiduciary duty and breach of trust, knowing receipt of the proceeds from breach of fiduciary duty and breach of trust, and breach of contract, all as set out above. The Defendants are liable to compensate and pay damages to the Credit Union on a joint and several basis for the losses suffered by the Credit Union with respect to the wrongful conduct they were involved with, and to disgorge any amounts that they received on account of such wrongful conduct. The damages claimed by the Credit Union do not include damages apportionable to the actions of Golanski, Stan Dimakos, and Ken Topping, Kim Colacicco, Brian Mullan, Mitch Vininsky, Mary Benincasa, Benjamin Choi, David Finnie, Frederick Kreutlein, Heather Sarnecki and Lauren Thompson Cacovic.

161. This claim may be served outside Ontario, without leave, on the Defendant Quarter Horses, pursuant to Rules 17.02(a), (f), (g), (i), and (p). The action is in respect of property in Ontario, a contract or contracts made in Ontario, breaches of contract or contracts committed in Ontario, and/or torts committed in Ontario, and Quarter Horses is an ordinary resident in or carries on business in Ontario.

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March 4, 2022
October 18, 2022

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~~FINANCIAL SERVICES REGULATORY~~
~~AUTHORITY~~

PACE Savings & Credit Union Limited, by its liquidator, KPMG -and- LARRY SMITH et al.
Inc. by its Administrator, FINANCIAL SERVICES
REGULATORY AUTHORITY
 Plaintiff Defendants

Court File No. CV-19-00616388-00CL

ONTARIO
SUPERIOR COURT OF JUSTICE
COMMERCIAL LIST

PROCEEDING COMMENCED AT TORONTO

FURTHER AMENDED FRESH-AS-AMENDED
STATEMENT OF CLAIM
(Notice of Action issued March 18, 2019)

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TAB D

Schedule "A"

Court File No. CV-19-00616388-00CL

**ONTARIO
SUPERIOR COURT OF JUSTICE
COMMERCIAL LIST**

B E T W E E N:

PACE SAVINGS & CREDIT UNION LIMITED, by its liquidator, KPMG INC.
~~by its administrator, FINANCIAL SERVICES REGULATORY AUTHORITY~~

Plaintiff

and

LARRY SMITH, PHILLIP SMITH, 1428245 ONTARIO LTD., 809755
ONTARIO LTD. (A.K.A. ELECTIVE BENEFIT INSURANCE SERVICES),
MALEK SMITH, 1916761 ONTARIO LTD., ~~ALISON GOLANSKI~~, 1724725
ONTARIO LTD., FRANK KLEES, KLEES & ASSOCIATES LTD., RON
WILLIAMSON, R. WILLIAMSON CONSULTANTS LIMITED, RON
WILLIAMSON QUARTER HORSES INC., BRIAN HOGAN, BRENT
BAILEY, DEBORAH BAKER, IAN GOODFELLOW, AL JONES, WENDY
MITCHELL, GEORGE POHLE, PETER REBELLATI, JIM TINDALL,
PAULINE WAINWRIGHT, NEIL WILLIAMSON ~~and, KIM COLACICCO~~ and
JANE LOWRIE and JOANNA WHITFIELD

Defendants

A N D B E T W E E N:

LARRY SMITH, 1428245 ONTARIO LTD., and 809755 ONTARIO LTD.
(A.K.A. ELECTIVE BENEFIT INSURANCE SERVICES)

Plaintiffs by Counterclaim

and

PACE SAVINGS & CREDIT UNION LIMITED, by its liquidator, KPMG INC.
~~BY ITS ADMINISTRATOR, FINANCIAL SERVICES REGULATORY
AUTHORITY and ARN REISLER~~

Defendants by Counterclaim

and

BRENT BAILEY, DEBORAH BAKER, IAN GOODFELLOW, AL JONES,
WENDY MITCHELL, PETER REBELLATI, JIM TINDALL, PAULINE
WAINWRIGHT, NEIL WILLIAMSON, and GEORGE POHLE

Defendants by Crossclaim

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**FURTHER AMENDED STATEMENT OF DEFENCE AND,
COUNTERCLAIM AND CROSSCLAIM OF THE DEFENDANTS,
LARRY SMITH,
1428245 ONTARIO LTD. and 809755 ONTARIO LTD.**

TO THE DEFENDANTS TO THE COUNTERCLAIM

A LEGAL PROCEEDING has been commenced against you by way of a Counterclaim in an action in this Court. The Claim made against you is set out in the following pages.

IF YOU WISH TO DEFEND THIS COUNTERCLAIM, you or an Ontario lawyer acting for you must prepare a Defence to Counterclaim in Form 27C prescribed by the *Rules of Civil Procedure*, serve it on the Plaintiff by counterclaim's lawyer or, where the Plaintiff by Counterclaim does not have a lawyer, serve it on the Plaintiff by Counterclaim, and file it, with proof of service, in this Court, WITHIN TWENTY DAYS after this Statement of Defence and Counterclaim is served on you.

If you are not already a party to the main action and you are served in another province or territory of Canada or in the United States of America, the period for serving and filing your defence is forty days. If you are served outside Canada and the United States of America, the period is sixty days.

If you are not already a party to the main action, instead of serving and filing a Defence to Counterclaim, you may serve and file a Notice of Intent to Defend in Form 18B prescribed by the *Rules of Civil Procedure*. This will entitle you to ten more days within which to serve and file your defence to Counterclaim.

IF YOU FAIL TO DEFEND THIS COUNTERCLAIM, JUDGMENT MAY BE GIVEN AGAINST YOU IN YOUR ABSENCE AND WITHOUT FURTHER NOTICE TO YOU. IF YOU WISH TO DEFEND THIS PROCEEDING BUT ARE UNABLE TO PAY LEGAL FEES, LEGAL AID MAY BE AVAILABLE TO YOU BY CONTACTING A LOCAL LEGAL AID OFFICE.

Date October 19, 2020

Issued by "Maggie Sawka"
Local Registrar

Address of court office: Superior Court of Justice
330 University Avenue, 9th Floor
Toronto ON M5G 1R7

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TO: **LAX O'SULLIVAN LISUS GOTTLIEB LLP**
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FURTHER AMENDED STATEMENT OF DEFENCE AND COUNTERCLAIM OF THE DEFENDANTS, LARRY SMITH, 1428245 ONTARIO LTD. and 809755 ONTARIO LTD.

1. The defendants, Larry Smith (“**Larry**”), 1428245 Ontario Ltd. (“**142**”), and 809755 Ontario Ltd. (“**809**”) (herein collectively called the “**Larry Parties**”), deny each of the allegations in the Amended Fresh as Amended Statement of Claim (the “**Claim**”).

Overview

2. The Financial Services Regulatory Authority of Ontario (“**FSRA**”), as Administrator for PACE Savings & Credit Union Limited (“**PACE**” or the “**Credit Union**”), has made a series of meritless, and sometimes unprecedented, allegations against Larry, 142, and 809. FSRA’s allegations fall into ~~two~~ three broad categories:

- a) That Larry “caused” PACE to enter into a series of improvident loans and transactions, for which he ought to be personally liable; ~~and~~
- b) That Larry, 142, and 809 received improper payments, either from third parties on projects relating to PACE’s business, or from PACE itself, pursuant to ‘impugned’ contracts; ~~and~~ and
- c) That Larry is liable to PACE for contribution and indemnity to the extent that PACE is liable for damages to any Investor Claimants (as defined in the Claim) associated with the Preferred Shares (as defined in the Claim).

3. FSRA’s allegations are entirely without merit. A significant part of the claim against Larry imputes personal liability for alleged impairments to loans and investments made by PACE, all of which were made with corporate approvals and which have been subject to internal and external audit. To date, FSRA has not pled a legal or factual basis for its allegation that Larry is personally liable to PACE for loan impairments.

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4. The remaining damages claimed relate to amounts received by Larry, 142, or 809 from PACE or others throughout his time as President or CEO of PACE. Notwithstanding the liberal use by FSRA of terms such as “secret commissions”, “fraud”, and “deceit”, there has been no misappropriation of funds by Larry, nor is there any conduct at issue that can reasonably be categorized as fraudulent or even potentially fraudulent. Rather, in all cases, compensation was paid to Larry personally or to 142 or 809 pursuant to written and signed consulting agreements, signed board resolutions and acknowledgments, and a raft of individually stamped and initialed Audit Committee and board of directors approvals.

5. Underlying the claims by FSRA, and the administration order issued over PACE on September 28, 2018 (the “**Administration Order**”), is a fundamental disagreement about what business a credit union ought to be engaged in. Throughout his time at PACE, Larry helped PACE to grow its assets from around \$50 million to over \$2 billion in loans, investments, cash, deposits, and equity. A significant part of this growth was accomplished through the diversification of the business lines, including the formation of PACE Securities Corp. (“**PACE Securities**”), the introduction of property development as a line of business, and the purchase of Continental Currency Exchange Canada Ltd. (“**CCE**”). That diversification was intended to provide new revenue sources for PACE, as it tried to keep pace with the Schedule 1 banks, which had been similarly diversifying.

6. FSRA disagrees. As Brian Mullen (the “**Administrator**”) stated to Scott Penfound of CCE, FSRA’s goal in undertaking the administration of PACE is to ‘take the credit union back to a traditional share/loan operation’. Since appointing itself as administrator, FSRA’s actions have

systematically destroyed the value that would have accrued to the members of the Credit Union.

For example:

- a) FSRA has been taking steps to call loans that have been performing according to their terms, and which were not in default. FSRA continues to harass Credit Union members by calling loans prematurely, by recommending increases in loan rates to as high as 16% and imposing unreasonable and usurious additional fees or “pay downs”, with the effect of reducing PACE’s commercial loan portfolio by some \$200 million in performing, well secured transactions. In many cases, the borrowers have been able to secure more favourable loan terms from other financial institutions, resulting in direct losses to PACE and, ultimately, to its members; and
 - b) FSRA is threatening to sell PACE’s interest in profitable investments such as CCE and various real estate joint ventures for liquidation prices, rather than allow those investments to perform as planned. By doing so, FSRA has destroyed the significant value that those loans and investments would have created for PACE and has harmed the Credit Union’s long-term financial position.
7. All of these actions will have long-term detrimental effects on PACE itself, which will trickle down to its members.
8. In addition, FSRA has taken unprecedented and, frankly, alarming steps with respect to the assets that the Larry Parties had kept on deposit at PACE. On appointing itself administrator of PACE, FSRA unilaterally froze over \$5,000,000 of their assets on deposit at PACE, taking the position that it was entitled to ‘set off’ the amounts on deposit against amounts claimed – but not proven – in its lawsuit. It has since collapsed those accounts outright and used the Larry Parties’

money to pay the fees of its own investigator and legal counsel, with PACE simply keeping the remainder for its own uses. It has done so without having proven any of its allegations against any of the Larry Parties and without having obtained any judgment.

The Parties

9. PACE is a credit union incorporated under the *Credit Union and Caisses Populaires Act, 1994*, S.O. 1994, c. 11 (the “**Act**”). PACE can trace its roots back to the Farm United Credit Union that began in 1940. Over the years, PACE has grown organically and through amalgamation with a number of smaller credit unions. When Larry joined PACE’s predecessors, the Credit Union had approximately \$50 million in assets, a number that grew to a total of approximately \$2 billion in deposits, investments, loans, equity and property by the time of the Administration Order.

10. FSRA is an Ontario Provincial Agency that, in part, regulates and acts as the deposit insurer for credit unions in Ontario. Prior to June 8, 2019, credit unions were regulated by the Deposit Insurance Corporation of Ontario (“**DICO**”).¹

11. Larry is the former President of PACE. Larry was an employee of PACE and its predecessors from 1988 until his employment was terminated for alleged cause in December 2018.

12. The defendant 142 is a corporation that, until September 28, 2018, performed business development services for PACE starting in 2001. Larry is an officer and director of 142. The shares of 142 are held in trust for Larry by Phillip Smith (“**Phil**”), Larry’s son and the former Chief Executive Officer of PACE.

¹ For the purposes of this document, FSRA and DICO will be referred to interchangeably.

13. The defendant 809 is a corporation formed under the laws of Ontario. Larry is the sole shareholder, officer, and director of 809. Starting in June 2006, 809 performed property development services for PACE.

14. The defendant by counterclaim, Arn Reisler (“**Reisler**”) is a lawyer licenced to practice law by the Law Society of Ontario. Reisler is the trustee for the Severance Trust, as herein defined.

Compensation Received by Larry, 142, and 809

I. Contracts between PACE and Larry, 142, or 809 Are All Valid and Enforceable

15. Contrary to the allegations in the Claim, prior to FSRA’s takeover of PACE, Larry’s relationship with PACE and its predecessors was structured through employment agreements entered into personally by Larry, alongside consulting agreements between PACE and either 142 or 809. During the relevant time, PACE (or its predecessors) entered into the following contracts with Larry, 142, and 809, each of which was presented for approval to PACE’s board of directors (the “**Board**”), was approved by resolution of directors, and was commercially reasonable:

- a) An initial agreement (the “**IBM Agreement**”) between IBM Employees (Toronto) Credit Union Ltd. (“**IBM Credit Union**”), a predecessor in interest to PACE, and MAS Consulting Services (“**MAS**”), (which later became 809);
- b) A consulting agreement between Larry and IBM Credit Union, dating to 1991;
- c) A consulting agreement (the “**Markham Stouffville Agreement**”) between MAS and Markham-Stouffville Community Credit Union Limited (“**Markham-Stouffville Credit Union**”), a predecessor in interest to PACE, dated October 10, 1994 (the “**1994 Agreement**”);

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- d) In or about July 1997, a consulting agreement between 809 and Greater Toronto Area (GTA) Savings and Credit Union (“**GTA Credit Union**”), upon Markham-Stouffville Credit Union’s merger with Uxbridge Credit Union Limited;
- e) An employment agreement, dated April 2000, between Larry and GTA Credit Union, pursuant to which he was employed as the CEO of GTA Credit Union;
- f) On January 1, 2001, 142 entered into a consulting agreement with GTA Credit Union pursuant to which 142 agreed to provide management services and advice to GTA Credit Union;
- g) In October 2002, 142 and PACE entered into a consulting agreement pursuant to which 142 agreed to perform management, data processing, and other services to PACE. This agreement was reapproved by the Board on December 13, 2006;
- h) In or around November 2002, GTA Credit Union and PACE took steps to amalgamate and continue as PACE. As a result of that amalgamation, Larry entered into an employment agreement with PACE dated November 7, 2002 pursuant to which he was engaged as the Chief Executive Officer of PACE;
- i) In May 2006, Larry entered into an additional agreement with PACE confirming his appointment as President of PACE effective May 1, 2006 and continuing until his 65th birthday;
- j) On June 26, 2006, 809 entered into a consulting agreement with PACE (although Larry had been using 809 or its predecessors as a vehicle for providing services to the Credit Union since 1988);

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- k) In July 2007, 142 and PACE entered into an updated consulting agreement (the “**142 Agreement**”). The 142 Agreement was amended in November 2012 and, most recently, on December 14, 2017;
 - l) On February 1, 2012, Larry entered into a subsequent employment agreement with PACE, in advance of PACE’s amalgamation with Peoples Credit Union Limited (which was effective January 2013) (the “**2012 Agreement**”);
 - m) On March 27, 2015, a further consulting agreement between 809 and PACE was concluded (the “**809 Agreement**”); and
 - n) On May 1, 2015, Larry and PACE entered into an agreement amending the terms of the 2012 Agreement (the “**2015 Agreement**”), pursuant to which Larry surrendered his role as CEO of PACE and continued as President and Managing Director.
16. All of the employment agreements and consulting contracts, as well as the payments made pursuant to them, were presented for approval to the Board and were, in fact, approved by the Board and the Audit Committee in the normal course.
17. Contrary to the allegations in the Claim, Larry could not “cause” PACE to enter into any of these agreements. There is no particular mystery to these documents, and it was known throughout that Larry was the beneficial owner of 142 and 809. These contracts were available to PACE’s auditors and to FSRA throughout the relevant time and were, in fact, reviewed by those entities.
18. FSRA’s view that any particular payment to Larry, 142, or 809 *should not* have been made is irrelevant, as all payments to Larry by PACE were made pursuant to valid contracts, and moneys received from third parties were properly accounted for and disclosed. FSRA’s allegations that