

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



THE HONOURABLE)

WEDNESDAY, THE 30th

MR. JUSTICE MYERS)

DAY OF AUGUST, 2017

BETWEEN:

KSV KOFMAN INC. IN ITS CAPACITY AS RECEIVER AND MANAGER OF CERTAIN PROPERTY OF SCOLLARD DEVELOPMENT CORPORATION, MEMORY CARE INVESTMENTS (KITCHENER) LTD., MEMORY CARE INVESTMENTS (OAKVILLE) LTD., 1703858 ONTARIO INC., LEGACY LANE INVESTMENTS LTD., TEXTBOOK (525 PRINCESS STREET) INC. AND TEXTBOOK (555 PRINCESS STREET) INC.

Plaintiff

- and -

JOHN DAVIES AND AEOLIAN INVESTMENTS LTD.

Defendants

ORDER

THIS MOTION, made by the plaintiff, KSV Kofman Inc. (“**KSV**” or the “**Plaintiff**”), solely in its capacity as receiver and manager of certain property of Scollard Development Corporation, Memory Care Investments (Kitchener) Ltd., Memory Care Investments (Oakville) Ltd., 1703858 Ontario Inc., Legacy Lane Investments Ltd., Textbook (525 Princess Street) Inc. and Textbook (555 Princess Street) Inc. and not in its personal capacity or in any other capacity, for an order granting leave to amend the notice of action and statement of claim, was heard this day at 330 University Avenue, Toronto, Ontario.

ON READING KSV's Fourth Report dated June 6, 2017 with the appendices thereto, KSV's Sixth Report dated July 12, 2017 with the appendices thereto, KSV's Supplement to the Sixth Report dated August 8, 2017 with the appendices thereto, and the affidavits of John Davies sworn July 14 and July 27, 2017 (collectively, the "**Davies Affidavits**"), the transcript of the cross-examination of John Davies on the Davies Affidavits and the affidavit of Joseph Blinick sworn August 29, 2017 with the exhibits thereto,

AND ON HEARING the submissions of counsel for the Plaintiff, and counsel for John Davies, Aeolian Investments Ltd. and Judith Davies, with Gregory Harris's counsel having advised that he consents to the relief sought on this motion,

1. **THIS COURT ORDERS** that service of the Notice of Motion and Motion Record is hereby abridged and validated.
2. **THIS COURT ORDERS** that the Plaintiff be and is hereby granted leave to amend its notice of action and statement of claim to add all or any of the following individuals and entities as parties to the action: John Davies in his capacity as the trustee and/or representative of both the Davies Family Trust (the "**Family Trust**") and the Davies Arizona Trust (the "**Arizona Trust**"), Judith Davies in her personal capacity and in her capacity as trustee and/or representative of the Family Trust, and Gregory Harris solely in his capacity as trustee and/or representative of the Family Trust (collectively, the "**Defendants**").
3. **THIS COURT ORDERS** that the Plaintiff be and is hereby granted leave to issue, serve and/or file the Fresh as Amended Statement of Claim attached hereto as Schedule "A".

4. **THIS COURT FURTHER ORDERS** that the title of the proceeding in all documents issued, served or filed after the date of this Order be as follows:

KSV KOFMAN INC. IN ITS CAPACITY AS RECEIVER AND MANAGER OF CERTAIN PROPERTY OF SCOLLARD DEVELOPMENT CORPORATION, MEMORY CARE INVESTMENTS (KITCHENER) LTD., MEMORY CARE INVESTMENTS (OAKVILLE) LTD., 1703858 ONTARIO INC., LEGACY LANE INVESTMENTS LTD., TEXTBOOK (525 PRINCESS STREET) INC. AND TEXTBOOK (555 PRINCESS STREET) INC.

Plaintiff

- and -


AEOLIAN INVESTMENTS LTD., JOHN DAVIES IN HIS PERSONAL CAPACITY AND IN HIS CAPACITY AS TRUSTEE OF BOTH THE DAVIES ARIZONA TRUST AND THE DAVIES FAMILY TRUST, JUDITH DAVIES IN HER PERSONAL CAPACITY AND IN HER CAPACITY AS TRUSTEE OF THE DAVIES FAMILY TRUST, AND GREGORY HARRIS SOLELY IN HIS CAPACITY AS TRUSTEE OF THE DAVIES FAMILY TRUST

Defendants


The Honourable Mr. Justice Myers

ENTERED AT / INSCRIT À TORONTO
ON / BOOK NO:
LE / DANS LE REGISTRE NO:

AUG 31 2017

PER / PAR: 

Schedule "A"

Court File No. CV-17-11822-00CL

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

B E T W E E N:

KSV KOFMAN INC., IN ITS CAPACITY AS RECEIVER AND MANAGER OF CERTAIN PROPERTY OF SCOLLARD DEVELOPMENT CORPORATION, MEMORY CARE INVESTMENTS (KITCHENER) LTD., MEMORY CARE INVESTMENTS (OAKVILLE) LTD., 1703858 ONTARIO INC., LEGACY LANE INVESTMENTS LTD., TEXTBOOK (525 PRINCESS STREET) INC. AND TEXTBOOK (555 PRINCESS STREET) INC.

Plaintiff

- and -

AEOLIAN INVESTMENTS LTD., JOHN DAVIES IN HIS PERSONAL CAPACITY AND IN HIS CAPACITY AS TRUSTEE OF BOTH THE DAVIES ARIZONA TRUST AND THE DAVIES FAMILY TRUST, JUDITH DAVIES IN HER PERSONAL CAPACITY AND IN HER CAPACITY AS TRUSTEE OF THE DAVIES FAMILY TRUST, AND GREGORY HARRIS SOLELY IN HIS CAPACITY AS TRUSTEE OF THE DAVIES FAMILY TRUST

Defendants

**FRESH AS AMENDED STATEMENT OF CLAIM
Notice of Action issued on June 6, 2017**

TO THE DEFENDANTS

A LEGAL PROCEEDING HAS BEEN COMMENCED AGAINST YOU by the plaintiff. The claim made against you is set out in the following pages.

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 statement of claim 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.

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: August 30, 2017

Issued by: _____

Local Registrar

Address of Court Office:

330 University Avenue
Toronto, ON M5G 1R7

TO:

DENTONS CANADA LLP
77 King Street West, Suite 400
TD Centre
Toronto, ON M5K 0A1

Michael Beeforth
Phone: (416) 367-6779
Email: michael.beeforth@dentons.com
Facsimile: (416) 863-4592

Lawyers for the Defendants,
John Davies, Judith Davies and Aeolian
Investments Ltd.

AND TO:

GREGORY HARRIS
2355 Skymark Avenue, Suite 300
Mississauga, ON L4W 4Y6

CLAIM

1. The plaintiff, KSV Kofman Inc. (“**KSV**”), solely in its capacity as receiver and manager of certain property of Scollard Development Corporation (“**Scollard**”), Memory Care Investments (Kitchener) Ltd. (“**Kitchener**”), Memory Care Investments (Oakville) Ltd. (“**Oakville**”), 1703858 Ontario Inc. (“**Burlington**”), Legacy Lane Investments Ltd. (“**Legacy Lane**”), Textbook (525 Princess Street) Inc. (“**525 Princess**”) and Textbook (555 Princess Street) Inc. (“**555 Princess**”) (collectively, the “**Receivership Companies**”), and not in its personal capacity or in any other capacity, claims against the defendants, Aeolian Investments Ltd. (“**Aeolian**”), John Davies (“**Mr. Davies**”) in his personal capacity and in his capacity as trustee and/or representative of both the Davies Arizona Trust (the “**Arizona Trust**”) and the Davies Family Trust (the “**Family Trust**”), Judith Davies (“**Ms. Davies**”) in her personal capacity and in her capacity as trustee and/or representative of the Family Trust, and Gregory Harris solely in his capacity as trustee and/or representative of the Family Trust (“**Mr. Harris**” and collectively with Aeolian, Mr. Davies and Ms. Davies, the “**Defendants**”), jointly and severally (as applicable):

- (a) a constructive trust and/or damages in the sum of \$50,000,000 or, in the alternative, damages in an amount to be assessed or determined by this Honourable Court, for the Defendants’ fraud, deceit, conspiracy, conversion, unlawful means tort and/or unjust enrichment, and for Mr. Davies’ breach of fiduciary duty and negligence;
- (b) orders for restitution, an accounting, and disgorgement of all assets, properties, and funds belonging to the Receivership Companies and improperly diverted by or to the Defendants or any person, corporation or other entity on their behalf;

- (c) a declaration that the plaintiff is entitled to trace the Receivership Companies' assets, properties, and funds into the hands of the Defendants, and a declaration that the Defendants hold those assets, properties, and funds as constructive trustees for the plaintiff;
- (d) a constructive trust and tracing or following order in respect of all assets, properties, and funds belonging to the Receivership Companies and improperly diverted by or to the Defendants or any person, corporation or other entity on their behalf, and in respect of the traceable products thereof;
- (e) an interim, interlocutory and permanent order, in the form of a worldwide *Mareva* injunction, restraining the Defendants and, as applicable, their respective servants, employees, agents, assigns, officers, directors and anyone else acting on their behalf or in conjunction with any of them, whether directly or indirectly, from selling, liquidating, removing, dissipating, alienating, transferring, assigning, encumbering, or similarly dealing with any of their assets, wherever situate;
- (f) a declaration that the liability of Mr. Davies arises out of fraud, embezzlement, misappropriation and/or defalcation while acting in a fiduciary capacity, and/or that the liability of Mr. Davies, Ms. Davies and Mr. Harris arises from obtaining property or services by false pretences or fraudulent misrepresentation, for purposes of sections 178(1)(d) and/or 178(1)(e) of the *Bankruptcy and Insolvency Act*, RSC, 1985, c B-3, as amended;

- (g) special damages, including all costs and expenses arising out of the detection, investigation, and quantification of the losses suffered by the Receivership Companies, in an amount to be particularized prior to trial;
- (h) punitive and/or exemplary damages in an amount to be particularized prior to trial;
- (i) pre-judgment and post-judgment interest on a compound basis or, alternatively, pursuant to the *Courts of Justice Act*, RSO 1990, c C 43, as amended;
- (j) costs of this action, including the costs of any and all interim and interlocutory motions, on a full indemnity or other appropriate scale, including all applicable taxes; and
- (k) such further and other relief, including equitable relief and constructive trusts in favour of the plaintiff, as this Honourable Court deems just.

Parties

2. The plaintiff, KSV, is the court-appointed receiver and manager of certain property of the Receivership Companies appointed pursuant to orders of the Ontario Superior Court of Justice (Commercial List) dated February 2, April 28 and May 2, 2017. Each of the Receivership Companies in respect of which KSV has been appointed receiver and manager was advanced monies on a secured basis by various trust corporations, which monies had been raised from investors through syndicated mortgage investments (“SMIs”) for particular real estate development projects specific to the respective Receivership Companies. In particular:

- (a) Scollard is a company incorporated pursuant to the laws of Ontario. It was advanced monies on a secured basis by Scollard Trustee Corporation (“**Scollard Trust Co.**”), which monies had been raised from investors through a SMI for a particular real estate development project specific to Scollard. The sole officer and director of Scollard is Mr. Davies.
- (b) Kitchener is a company incorporated pursuant to the laws of Ontario. It was advanced monies on a secured basis by MC Trustee (Kitchener) Ltd. (“**Kitchener Trust Co.**”), which monies had been raised from investors through a SMI for a particular real estate development project specific to Kitchener. The sole officer and director of Kitchener is Mr. Davies.
- (c) Oakville is a company incorporated pursuant to the laws of Ontario. It was advanced monies on a secured basis by 2223947 Ontario Limited (“**Oakville/Burlington/Legacy Lane Trust Co.**”), which monies had been raised from investors through a SMI for a particular real estate development project specific to Oakville. The sole officer and director of Oakville is Mr. Davies.
- (d) Burlington is a company incorporated pursuant to the laws of Ontario. It was advanced monies on a secured basis by the Oakville/Burlington/Legacy Lane Trust Co., which monies had been raised from investors through a SMI for a particular real estate development project specific to Burlington. The sole officer and director of Burlington is Mr. Davies.
- (e) Legacy Lane is a company incorporated pursuant to the laws of Ontario. It was advanced monies on a secured basis by the Oakville/Burlington/Legacy Lane Trust

Co., which monies had been raised from investors through a SMI for a particular real estate development project specific to Legacy Lane. The sole officer and director of Legacy Lane is Mr. Davies.

- (f) 525 Princess is a company incorporated pursuant to the laws of Ontario. It was advanced monies on a secured basis by Textbook Student Suites (525 Princess Street) Trustee Corporation (“**525 Trust Co.**”), which monies had been raised from investors through a SMI for a particular real estate development project specific to 525 Princess. The only officers and directors of 525 Princess are Mr. Davies and Walter Thompson (“**Mr. Thompson**”).
- (g) 555 Princess is a company incorporated pursuant to the laws of Ontario. It was advanced monies on a secured basis by Textbook Student Suites (555 Princess Street) Trustee Corporation (“**555 Trust Co.**” and together with Scollard Trust Co., Kitchener Trust Co., Oakville/Burlington/Legacy Lane Trust Co. and 525 Trust Co., the “**Trust Companies**”), which monies had been raised from investors through a SMI for a particular real estate development project specific to 555 Princess. The only officers and directors of 555 Princess are Mr. Davies and Mr. Thompson.

3. The defendant, Mr. Davies, is an individual residing in King City, Ontario. He was, at all material times, a director and officer of the Receivership Companies and other relevant entities. He was also, at all material times, the trustee and/or representative of the Family Trust, together with Ms. Davies and Mr. Harris. He was also, at all material times, the sole trustee and/or representative of the Arizona Trust.

4. The defendant, Ms. Davies, is an individual residing in King City, Ontario. She is Mr. Davies' spouse. She was, at all material times, the trustee and/or representative of the Family Trust, together with Mr. Davies and Mr. Harris.

5. The defendant, Mr. Harris, is an individual residing in the Town of Nobleton, Ontario. He is a licensed Ontario lawyer in private practice. He was, at all material times, the trustee and/or representative of the Family Trust, together with Mr. Davies and Ms. Davies. Mr. Harris is a party to this litigation solely in his capacity as the trustee and/or representative of the Family Trust and not in his personal capacity or in any other capacity. All allegations and claims against Mr. Harris relate exclusively to his role as trustee and/or representative of the Family Trust.

6. While the plaintiff's investigation into the SMI scheme is presently ongoing, the plaintiff has discovered no reason to date to believe that Ms. Davies or Mr. Harris, in their capacities as trustees of the Family Trust, engaged in any fraudulent, deceitful or other misconduct relating to the Family Trust. Nevertheless, given that the Family Trust improperly received and retained funds that were initially sourced from SMI monies advanced to the Receivership Companies, one or more of the trustees of the Family Trust caused, directed and/or had knowledge of such improper transfers. The role that each of the trustees played (or did not play) in these improper transfers is known only to the Defendants. In any event, each of the trustees of the Family Trust must be named as a defendant to allow the plaintiff to obtain the sought after relief regarding the assets improperly funneled to the Family Trust.

7. The Family Trust and the Arizona Trust are trusts that were established by or at the direction of Mr. Davies in or around 2003 and 2013, respectively. The beneficiaries of the Family Trust are Mr. Davies, Ms. Davies and the Davies children: Jessica Deborah Davies, Sarah Ramona

Davies, Andrew John Davies and Walter Robert Jackson Davies (collectively, the “**Davies Children**”), as well as any future children and issue of Mr. Davies. The beneficiaries of the Arizona Trust are the Davies Children. Mr. Davies, in his capacity as sole trustee of the Arizona Trust, owns, among other things, real property municipally described as 35411 N. 66th Place in Carefree, Arizona, United States (the “**Arizona Property**”), that was acquired with funds from Aeolian, which were initially sourced from SMI monies advanced to the Receivership Companies and related entities.

8. The defendant, Aeolian, is a company incorporated pursuant to the laws of Ontario. Aeolian’s mailing address is Mr. and Ms. Davies’ personal residence in King City, Ontario. Aeolian is directly owned by Ms. Davies and the Davies Children. Mr. Davies is Aeolian’s sole officer and director. Aeolian is a direct or indirect shareholder of each of the Receivership Companies. Specifically, Aeolian is a direct shareholder of Scollard and Legacy Lane. Aeolian is also a shareholder of Memory Care Investments Ltd. (“**MCIL**”), which is a shareholder of Kitchener, Oakville and Memory Care Investments Burlington Ltd. (“**MC Burlington**”), which wholly owns Burlington. Aeolian is a shareholder of Textbook Student Suites Inc. (“**TSSI**”), which is a shareholder of 525 Princess and 555 Princess. Aeolian is also a shareholder of Textbook Suites Inc. (“**TSI**”), which is a shareholder of Textbook (445 Princess Street) Inc. (“**445 Princess**”), a non-Receivership Company.

Background

9. This action is in respect of a fraudulent SMI scheme whereby the Defendants conspired with one another to misappropriate millions of dollars from the investing public by diverting funds from the Receivership Companies (and the respective real estate development projects (the

“**Projects**”) for which the funds were specifically advanced) through corporate structures Mr. Davies directly and/or indirectly controlled to, *inter alia*, himself, his family members (including Ms. Davies) and other parties related to them (including Aeolian, the Family Trust and the Arizona Trust).

10. For each of the Receivership Companies’ Projects, the applicable Receivership Company was advanced monies that were raised from investors through SMI offerings, which were sourced by Tier 1 Transaction Advisory Inc. and/or related entities (collectively, “**Tier 1**”).

11. To support the amounts raised, the Receivership Companies retained an appraiser to provide estimated hypothetical market values of the subject sites, assuming they could be developed. The appraisals were based on several other assumptions, including: (i) development costs, as estimated by the applicable Receivership Company and as set out in the applicable Project pro forma, remaining consistent with the budget; (ii) the necessary planning approvals being obtained in a timely manner; and (iii) the development being commenced in a timely manner.

12. Importantly, certain of the Project pro formas on which the appraisals were based contained false and/or materially inaccurate and misleading information. For instance, certain of the pro formas:

- (a) reflected an equity injection by the respective Receivership Company, but in no case was such an equity contribution ever made by Mr. Davies or any of the other shareholders of the Receivership Companies;
- (b) failed to account for a significant portion of the initial costs, consisting of fees payable to Tier 1, amounts due to agents who sold the SMI products to investors,

professional costs and amounts to fund a one-year interest reserve (the “**Initial Costs**”); and

- (c) did not reflect the payment of dividends, which, as described in more detail below, were paid from the initial SMI advances for each of 525 Princess and 555 Princess.

13. Further, certain appraisals were based on unrealistic and unattainable development plans that could never come to fruition given, among other things, zoning, planning and other restrictions.

14. Investors were led to believe that the advances from the Trust Companies to the Receivership Companies would be used for, and fully secured against, specific real property with a first-ranking security interest. However, this was not the case. Each initial SMI fundraise significantly exceeded the purchase price of the real property, resulting in the loans from each of the Trust Companies to the Receivership Companies being under-secured from the day they were made. Further, contrary to the representations made to investors, in some instances the Receivership Companies borrowed funds on a first-ranking secured basis against the real property *after* raising the SMIs.

15. Of the SMI monies raised, approximately 30% of the proceeds was immediately used to pay the Initial Costs.

16. The remaining amounts were routinely used for other Projects in respect of which the investors had no security interest.

17. Certain (and perhaps all) of the Receivership Companies were insolvent from the date of the first SMI advance and the Projects undertaken by the Receivership Companies had virtually

no prospect of success due to, among other things, the lack of equity capital (which necessitated further borrowing to advance the Projects), the significant Initial Costs, the use of monies to fund expenses on other unrelated projects, and the front-end loading of excessive dividends, management fees and other undue payments to Mr. Davies and to affiliates of, and persons related to, Mr. Davies and others.

18. Notwithstanding that approximately \$65 million was raised from investors through SMIs during a booming real estate market, the Receivership Companies currently only have properties for which they collectively paid approximately \$13.5 million,¹ all of which remain in the pre-construction phase (with the exception of the Burlington Project, which has footings and foundations), and no available cash to further develop the Projects. Had there not been new financings in other projects that raised additional funds from new investors, which funds were loaned to and among the Receivership Companies to fund pre-existing liabilities, the Receivership Companies would have been unable to service interest and other obligations they were required to pay. Accordingly, the scheme had all of the hallmarks of a Ponzi scheme as its continuance was dependent upon the raising of ever increasing sums of new money.

19. Mr. Davies, Ms. Davies and entities related to them collectively received approximately \$5 million from the Receivership Companies, yet the investors, who were advised they would have safe and fully secured investments in real property with a first-ranking charge (which would only be subordinated to construction financing intended to create additional value), stand to lose the majority of their investment.

¹ Pursuant to a Court Order dated August 3, 2017, the Scollard property, which was acquired for \$9 million, was sold.

20. The Defendants' conduct has exposed the Receivership Companies to significant liabilities in the form of claims for damages and losses from their creditors, including the innocent investors whose funds they misappropriated.

The Loan Agreements

21. Under the loan agreements between the respective Receivership Companies and the applicable Trust Companies (the "**Loan Agreements**"), the funds advanced from the Trust Companies to the Receivership Companies were to be used to purchase real property and to pay soft costs associated with the Projects for which the funds were invested and advanced.

22. In raising the monies from investors, the Receivership Companies covenanted that they would not, without the consent of the applicable Trust Company (subject to certain limited exceptions), "use the proceeds of any Loan Instalment for any purposes other than the development and construction of the project on the Property".

Prohibited Management Fees

23. Pursuant to Section 7.02(c) of the Loan Agreements with Scollard, Oakville, Kitchener, Burlington and Legacy Lane, the payment of management fees to shareholders is prohibited absent the written consent of the applicable Trust Company.

24. Pursuant to Section 7.02(c) of the Loan Agreements with 525 Princess and 555 Princess, ordinary course payments to shareholders for amounts related to the management, development

and operation of the Property are permitted, but only if such payments are reasonable in relation to the services rendered, unless the written consent of the applicable Trust Company is obtained.

25. Contrary to these Loan Agreements and the Receivership Companies' contractual and legal obligations, Mr. Davies caused the Receivership Companies to improperly pay millions of dollars in management fees directly to Aeolian, notwithstanding that, among other things, the Receivership Companies never (i) received the written consent of the Trust Companies for these payments, (ii) entered into any management services agreements, or (iii) received services that would justify such payments.

26. Specifically, Mr. Davies caused certain Receivership Companies, including Scollard, Oakville, Kitchener, Burlington and Legacy Lane, to transfer \$3.795 million in prohibited management fees directly to Aeolian:

- (a) Scollard transferred approximately \$1,244,000 to Aeolian;
- (b) Oakville transferred approximately \$1,112,000 to Aeolian;
- (c) Kitchener transferred approximately \$506,000 to Aeolian;
- (d) Burlington transferred approximately \$592,000 to Aeolian; and
- (e) Legacy Lane transferred approximately \$341,000 to Aeolian.

27. These payments are all prohibited under the Loan Agreements.

28. Mr. Davies also caused 525 Princess and 555 Princess to transfer to Aeolian (purportedly in respect of management fees) amounts that are unreasonable, particularly given that these Receivership Companies never entered into any management agreements with Aeolian, the

Projects for which the funds were advanced have achieved very limited progress (they both remain in the pre-construction phase), and the intended Projects are unlikely to ever be developed because of, among other things, zoning and other restrictions that preclude such developments.

29. These payments are also all prohibited under the Loan Agreements.

30. Further, the management fees in respect of each of the Projects were paid at an accelerated rate inconsistent with the stage of development of the Projects.

31. These payments are all in addition to other improper payments that Mr. Davies caused certain non-Receiverhip Companies that Mr. Davies controls, including McMurray Street Investments Inc. (“**McMurray**”) and Textbook Ross Park Inc. (“**Ross Park**”), to make to Aeolian, purportedly also in respect of management fees.

Improper Transfers to TSI, TSSI and MCIL

32. Contrary to the Loan Agreements and the Receiverhip Companies’ contractual and legal obligations, Mr. Davies caused certain of the Receiverhip Companies to improperly transfer approximately \$2.1 million to TSI, TSSI and MCIL, the parent companies of Kitchener, Oakville, Burlington, 525 Princess and 555 Princess, all three of which are owned, in part, by Aeolian.

33. These funds were transferred to TSI, TSSI and MCIL by cheque. The memo line on each of the cheques indicated that payment was a “loan”, notwithstanding that:

- (a) none of these “loans” were documented;
- (b) none of these “loans” were secured in any way;

- (c) no interest has been received by any of the applicable Receivership Companies on account of any such “loan”; and
- (d) the relevant Loan Agreements do not permit the applicable Receivership Companies to make these loans.

Improper Dividends

34. Mr. Davies also caused certain Receivership Companies to improperly pay significant dividends to Aeolian and others. Specifically, Mr. Davies caused 525 Princess and 555 Princess to respectively pay \$250,000 each in dividends to Aeolian (for a total of \$500,000). Mr. Davies further caused an additional \$1.5 million in dividends to be paid from 525 Princess and 555 Princess to the companies’ other shareholders.

35. While the payment of dividends is permitted under the Loan Agreements in certain circumstances, dividends are only to be paid from the “excess proceeds after the [real estate development property] has been acquired”. In each instance, Mr. Davies caused the dividends to be paid to Aeolian and the other shareholders immediately after 525 Princess and 555 Princess received the funds from the applicable Trust Company at a time when 525 Princess and 555 Princess had no profits and insufficient cash to develop the respective Projects. As a result of the payment of dividends and the payments to related parties, 525 Princess and 555 Princess essentially had no further monies to advance their respective Projects.

36. These dividend distributions caused 525 Princess and 555 Princess to become insolvent or contributed to their insolvency (if they were not already insolvent at the time of payment).

Improper Payments to Mr. Davies' Family Members

37. Mr. Davies also caused certain of the Receivership Companies to make further payments directly, and indirectly through Aeolian, to Ms. Davies and certain Davies Children for services purportedly rendered by them in connection with the Projects. To the extent these services were not provided, or the payments in respect of any services that were provided are unreasonable, these payments are prohibited under the applicable Loan Agreements and constitute a breach of the Loan Agreements.

Improper Inter-Company Transfers and Transfers to Affiliates

38. In further contravention of the Loan Agreements, Mr. Davies routinely caused the Receivership Companies to improperly transfer monies between entities and to affiliates, including over \$17 million to and among the Receivership Companies and certain non-Receivership Companies that Mr. Davies controls, including 445 Princess, Textbook (774 Bronson Avenue) Inc. ("**Bronson**"), Ross Park and McMurray as well as TSI, TSSI and MCIL, amongst others.

39. Mr. Davies caused such intercompany transfers to be made as the Receivership Companies' Projects were facing a liquidity crisis, which necessitated the making of intercompany loans to perpetuate the scheme and avoid defaulting on the loans from the Trust Companies and the Receivership Companies' other obligations. This has all of the hallmarks of a Ponzi scheme.

40. Mr. Davies also caused certain Receivership Companies to improperly transfer monies to Lafontaine Terrace Management Corporation ("**Lafontaine**") and Memory Care Investments (Victoria) Ltd. ("**MC Victoria**") – two companies in respect of which Mr. Davies is the sole

director and officer, which are both owned, in different proportions, by Mr. Davies and/or Aeolian, amongst others. Specifically:

- (a) Scollard, Legacy Lane, Burlington and Oakville improperly transferred a total of \$324,000 to Lafontaine; and
- (b) Legacy Lane improperly transferred \$15,000 to MC Victoria.

41. These transfers are prohibited under the applicable Loan Agreements and constitute a breach of the Loan Agreements.

Misappropriation of Funds to Finance the Purchase of the Ottawa Property

42. Mr. Davies also improperly diverted further funds from 555 Princess and Kitchener (and the respective Projects in which the funds were required to be invested) to a non-Receiver'ship Company that Mr. Davies controlled, Generx (Byward Hall) Inc. (formerly Textbook (256 Rideau St.) Inc.) ("**Rideau**"), which is also now in receivership, to finance Rideau's purchase of real property municipally described as 256 Rideau Street, Ottawa, Ontario and 211 Besserer Street, Ottawa, Ontario (collectively, the "**Ottawa Property**").

43. The Ottawa Property was purchased by Rideau on or around November 6, 2015 for \$11 million.

44. Immediately prior to Rideau's purchase of the Ottawa Property, on October 27, 2015, Mr. Davies caused 555 Princess to improperly transfer \$1.39 million to Rideau, and Mr. Davies caused Kitchener to improperly transfer \$111,000 to Rideau, both by way of cheque. The cheques were both signed by Mr. Davies.

45. The funds were transferred from 555 Princess and Kitchener to Rideau for no consideration, with no security, for an illegitimate business purpose and in contravention of the relevant Loan Agreements.

46. Despite the fact that the funds were required to be used for specific Projects to be respectively undertaken by 555 Princess and Kitchener, Mr. Davies caused the funds to be transferred to Rideau with complete disregard for the separate corporate identities of 555 Princess, Kitchener and Rideau and the contractual and legal obligations of the parties, which had the result of sheltering assets and frustrating creditors of both 555 Princess and Kitchener.

47. Following Rideau's acquisition of the Ottawa Property, Mr. Davies caused a further \$61,200 to be improperly transferred to Rideau from 555 Princess, 525 Princess and Burlington by way of cheques, each of which was also signed by Mr. Davies. Specifically:

- (a) \$2,200 was transferred by Burlington to Rideau on November 5, 2015;
- (b) \$36,000 was transferred by 555 Princess to Rideau on December 17, 2015;
- (c) \$7,000 was transferred by 555 Princess to Rideau on May 31, 2016; and
- (d) \$16,000 was transferred by 525 Princess to Rideau on June 20, 2016.

48. Despite the fact that these funds were required to be used for the specific Projects to be respectively undertaken by 555 Princess, 525 Princess and Burlington, the \$61,200 was transferred to Rideau for no consideration, with no security, for an illegitimate business purpose and in contravention of the relevant Loan Agreements.

The Arizona Property

49. The Arizona Property was purchased by the Arizona Trust for US\$1.2 million. The funds used to purchase the Arizona Property came from Aeolian, with the BofI Federal Bank having a US\$600,000 mortgage on the Arizona Property. Almost US\$2 million was spent to renovate the Arizona Property following its acquisition. Aeolian funded substantially all of the costs to purchase and renovate the Arizona Property (at least in part through the Family Trust and the Arizona Trust), which funds came directly and/or indirectly from the Receivership Companies and related entities. Ms. Davies and/or Mr. Harris, as trustees and/or representatives of the Family Trust, had knowledge of these payments.

Aeolian and Ms. Davies

50. Aeolian transferred over \$2.5 million, which it received from the Receivership Companies and other related entities, directly to Ms. Davies, purportedly in respect of management fees, although she performed no work for or on behalf of Aeolian or any of the Receivership Companies. Aeolian further used \$1.3 million, which it received from the Receivership Companies and other related entities, to pay day-to-day living and other personal expenses charged on an American Express card used by Mr. and Ms. Davies. Additionally, over US\$1.8 million, which initially came from the Receivership Companies and other related entities, went from Aeolian toward the purchase and renovation of the Arizona Property.

51. At all material times, Aeolian and Ms. Davies knowingly acted as a conduit for Mr. Davies to improperly divert and funnel millions of dollars from the Receivership Companies to himself, his family members and others for their own personal use and benefit.

Current Status of Projects

52. Millions of dollars were paid by the Receivership Companies to Mr. Davies, Ms. Davies and other related parties in respect of management fees, dividends and other amounts; however, all of the Projects remain in the early stages of development and none of the Receivership Companies has any capital to further develop their respective Projects.

53. Mr. Davies was fully aware that the Projects would suffer, and were in fact suffering, from a liquidity crisis. Notwithstanding this knowledge, rather than addressing the liquidity issues in a reasonable and appropriate manner in accordance with his legal obligations, Mr. Davies instead raised, and/or facilitated the raising of, further funds from investors, purportedly for particular Projects, with full knowledge, and with the intention, that those funds would instead be used to improperly pay interest payments and other expenses in relation to other Projects that had no connection to the specific Projects for which the funds were purportedly raised, in contravention of the Loan Agreements. This allowed the Defendants to perpetuate, and continue to perpetuate, their fraudulent scheme.

54. The acts and omissions of Mr. Davies purposefully mislead and defrauded the Receivership Companies and their creditors, including the innocent investors whose funds were misappropriated. Specifically, investors were intentionally lead to believe that they were investing on the basis of a particular Loan Agreement (and the attributes of a specific Project), when Mr. Davies specifically knew and intended that the funds would go elsewhere, resulting in the misappropriation and pilfering of funds.

Fraud and Deceit

55. The Defendants perpetrated the fraudulent scheme described herein. Although the precise particulars of the fraudulent scheme are only fully known to the Defendants at this time, they include, without limitation:

- (a) With respect to Mr. Davies:
 - (i) intentionally creating and/or facilitating the creation of Project pro formas that in no way reflected commercial reality to obtain artificially inflated appraisals that were used in connection with the SMI offerings and the raising of capital from investors;
 - (ii) misrepresenting the nature of the Projects and the potential for the Project development to be successfully executed, including the likelihood of obtaining the necessary planning approvals;
 - (iii) knowingly concealing and falsely representing the capital structure of the Receivership Companies, including the purported equity injections that would be made by shareholders; and/or
 - (iv) intentionally and deceitfully raising and/or facilitating the raising of funds from investors, and diverting those funds from the Receivership Companies to which they were advanced, for purposes inconsistent with the purposes for which the funds were purportedly invested and advanced;
- (b) With respect to Mr. Davies, Ms. Davies and/or Aeolian:

- (i) knowingly concealing and falsely representing the relationships between themselves and other related, non-arm's length parties;
 - (ii) knowingly directing, causing, facilitating and/or allowing prohibited payments and transfers to be made by the Receivership Companies to such related, non-arm's length parties, including payments and transfers for which no goods or services, or no goods or services of any material value, were provided;
 - (iii) dishonestly diverting funds from the Receivership Companies to shell corporations and a network of non-arm's length parties to obtain secret profits for their own benefits; and/or
 - (iv) intentionally and deceitfully directing and/or facilitating payments to shell corporations and a network of non-arm's length parties to covertly divert funds from the Receivership Companies, shelter the funds, avoid detection and thwart recovery attempts;
- (c) With respect to some or all of the Defendants:
- (i) knowingly receiving, retaining and/or using funds, which rightfully belonged to the Receivership Companies; and/or
 - (ii) failing to take any steps, or any reasonable or sufficient steps, to stop the improper conduct or mitigate the harm being caused by it.

56. Mr. Davies, Ms. Davies and entities related to them (including Aeolian, the Family Trust and the Arizona Trust) perpetrated and/or facilitated the fraudulent scheme described herein in order to profit, and continue to profit, through the receipt of millions in undue management fees (which exceeded \$3.8 million from the Receivership Companies), dividends (\$500,000 from the Receivership Companies) and/or other amounts to which they were not properly entitled.

57. All of the above caused detriment and deprivation to the Receivership Companies.

Conspiracy

58. Some or all of the Defendants acted in combination or in concert, by agreement or with a common design, to perpetrate the fraudulent scheme described herein. The full particulars of the agreement or common design are only fully known to these Defendants at this time, but further particulars will be provided in advance of trial.

59. The conduct of these Defendants in perpetrating the fraudulent scheme was unlawful (including the torts and other wrongful acts and omissions described herein) and directed towards the Receivership Companies and their creditors, including the innocent investors whose funds they misappropriated. These Defendants knew that injury to the Receivership Companies and their creditors was likely to result in the circumstances, and such injury did result.

60. The predominant purpose of these Defendants' conduct was to intentionally harm the Receivership Companies and their creditors, and the conduct of these Defendants did harm them.

61. These Defendants are liable to the Receivership Companies for predominant purpose conspiracy and unlawful act conspiracy, amongst other things.

Mr. Davies' Breach of Fiduciary Duty and Negligence

62. By virtue of the positions Mr. Davies held, he was a fiduciary of each of the Receivership Companies and owed each of them fiduciary duties, contractual duties, statutory duties (including pursuant to sections 71 and 134 of the *Business Corporations Act*, RSO 1990, c B 16, as amended) and a duty of care to, among other things:

- (a) act honestly and in good faith with a view to their best interests;
- (b) avoid improper self-dealing;
- (c) avoid conflicts of interest; and
- (d) exercise the care, diligence and skill that reasonably prudent persons would exercise in comparable circumstances.

63. By reason of the facts described above, Mr. Davies breached these duties and failed to act in a manner that was required of him as a director and officer of the Receivership Companies.

64. The Receivership Companies were vulnerable to the unilateral exercise of Mr. Davies' discretion and power, particularly given that he was the controlling mind and management of the Receivership Companies. By reason of the facts described above, Mr. Davies breached his duties to the Receivership Companies, including his fiduciary and other duties owed, including but not limited to his duties of good faith, honest performance and loyalty.

65. By reason of the facts described above, Mr. Davies also breached express and/or implied terms of his employment agreements with the respective Receivership Companies. Among other things, Mr. Davies was, at a minimum, required to conduct himself and the operations of the

Receivership Companies in a competent and lawful manner, which he failed to do. Mr. Davies' conduct breached the standard of care required of him and he was grossly negligent in the performance of his duties as an officer of each of the Receivership Companies.

66. Mr. Davies effectively treated the respective Receivership Companies as his own personal fiefdom, without due regard for transparency, disclosure, the avoidance of self-dealing and conflicts of interest, or corporate separateness, amongst other things. He effectively operated each of the Receivership Companies as his own personal corporation and saw their assets as his own. This resulted in his failure to act in the best interests of the Receivership Companies, including by defrauding the Receivership Companies and enriching himself and parties related to him at the expense of the Receivership Companies and their creditors.

Unlawful Means Tort

67. By virtue of their acts and omissions as described herein, some or all of the Defendants intentionally inflicted economic harm on the Receivership Companies and their creditors. In doing so, they used unlawful means (including but not limited to fraud, deceit and conspiracy) as against third parties, including the innocent investors whose funds they misappropriated.

Conversion

68. The Receivership Companies were in possession of, or entitled to immediate possession of, the specific and identifiable funds described above. Some or all of the Defendants intentionally and wrongfully converted the Receivership Companies' funds for their own use inconsistent with the Receivership Companies' right of possession and other rights, and thereby deprived the Receivership Companies (and their creditors) of the benefit of the funds, exposing them to

significant liabilities. The plaintiff is entitled to recover the entire amount that these Defendants have converted.

Unjust Enrichment

69. By virtue of the facts set out above, some or all of the Defendants and/or parties related to them have been unjustly enriched. The Receivership Companies have suffered a corresponding deprivation, and there is no juristic reason for these Defendants' enrichment or for the Receivership Companies' corresponding deprivation. There is no juristic reason why these Defendants should not be held to account for their enrichment and for the damages they have caused.

Constructive Trust(s)

70. Some or all of the Defendants received and retained the Receivership Companies' funds with full knowledge of the fraud, deceit, conspiracy, conversion and other unlawful acts they had committed, and with full knowledge of Mr. Davies' breach of his fiduciary and other legal duties owed to the Receivership Companies. By virtue of facts described herein, these Defendants hold all assets, properties, and funds that they diverted, misappropriated and improperly received from the Receivership Companies, and all traceable products thereof, as trustees of a constructive trust (or trusts) for the benefit of the plaintiff.

Mr. and Ms. Davies' Liquidation and Alienation of Assets

71. Following their improper conduct as described above, and after the commencement of the receivership proceeding in January 2017, Mr. and Ms. Davies embarked on a course of conduct designed to liquidate their assets and put them beyond the reach of the Receivership Companies

and their creditors. Among other things, on April 25, 2017, Mr. Davies sold his family cottage located in Gravenhurst, Ontario for approximately \$3 million.

72. Mr. and Ms. Davies also attempted, and continue to attempt, to sell their personal residence located in King City, Ontario, which they jointly own in their capacities as trustees of the Family Trust.

Losses and Harm

73. The conduct of the Defendants as described above has caused, and is continuing to cause, reasonably foreseeable and proximate damage to the Receivership Companies and their creditors, including financial losses and loss of profitable business opportunities, the full extent of which has not yet fully materialized and is not yet fully known to the plaintiff at this time.

74. The secured debt obligations of the Receivership Companies currently total approximately \$60,243,000, including approximately \$54,231,000 owing to the Trust Companies (being monies raised by the Trust Companies from investors) and the balance owing to other lenders, primarily mortgagees. Virtually the only valuable assets the Receivership Companies currently have to satisfy these secured debt obligations (and all the other debt obligations and liabilities of the Receivership Companies) are the real properties for which the Receivership Companies collectively paid approximately \$13,455,000.²

75. Some or all of the Defendants not only stripped the Receivership Companies of millions of dollars, and preferred their own interests over those of the Receivership Companies and their

² On August 3, 2017, the Receiver obtained an approval and vesting Order from the Court authorizing the sale of the Scollard property (which was acquired by Scollard for \$9 million). In accordance with the Order, the Receiver subsequently sold the Scollard property, which resulted in an initial distribution from Scollard to the Scollard Trust Co. in the amount of approximately \$5.1 million, thereby reducing the Receivership Companies' secured debt obligations accordingly.

creditors (including the investing public), but they also deprived the Receivership Companies of the opportunity to pursue legitimate and profitable real estate development and other revenue-generating business opportunities, causing considerable additional losses and damages to the Receivership Companies.

76. Full particulars of the Receivership Companies' damages will be provided prior to trial.

77. The conduct of the Defendants as described above has also caused, and is continuing to cause, irreparable harm to the Receivership Companies and their creditors. In the absence of relief from this Honourable Court, Mr. and Ms. Davies (and the entities they control, including Aeolian, the Arizona Trust and the Family Trust) will be able to liquidate and alienate assets, and/or continue to liquidate and alienate assets, thereby causing the Receivership Companies and their creditors further harm which would not be compensable in damages alone.

78. The plaintiff has incurred, and is continuing to incur, costs and out-of-pocket expenses relating to investigations into the Defendants' acts and omissions, which special damages shall be particularized prior to trial.

79. Some or all of the Defendants' actions constitute a wanton, callous, high-handed and outrageous disregard for the Receivership Companies' rights and interests, and for the rights and interests of their creditors, including the investing public whose funds they misappropriated. These Defendants deliberately and willfully undertook the fraudulent and unlawful activities described herein in an underhanded manner, knowing that their conduct was wrong and would cause harm to the Receivership Companies and their creditors. The conduct of these Defendants ought to attract the disapproval of this Honourable Court and result in a material award of punitive and/or exemplary damages.

80. Given the duplicitous and deceitful manner in which Mr. Davies, Ms. Davies and Aeolian have acted, together with all the surrounding circumstances, including Mr. Davies' sale of the family cottage and Mr. and Ms. Davies' attempted sale of their personal residence, there is a real and demonstrated risk that Mr. and Ms. Davies as well as Aeolian, the Family Trust and the Arizona Trust (all three of which are controlled by Mr. Davies and/or Ms. Davies) will dissipate assets and/or permanently abscond with the Receivership Companies' funds to avoid enforcement of any judgment the plaintiff may ultimately obtain. In all the circumstances, interim, interlocutory and permanent injunctive relief, *inter alia*, enjoining the Defendants from accessing, liquidating, dissipating, alienating or otherwise dealing with their assets is necessary, just and appropriate.

Place of Trial

81. The plaintiff proposes that the trial of this action take place in the City of Toronto in the Province of Ontario.

August 30, 2017

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**KSV KOFMAN INC. in its capacity as Receiver and Manager of
Certain Property of Scollard Development Corporation et al.**
Plaintiff

v.

JOHN DAVIES et al.

Defendants

Court File No: CV-17-11822-00CL

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

PROCEEDING COMMENCED AT
TORONTO

**FRESH AS AMENDED STATEMENT OF CLAIM
Notice of Action issued on June 6, 2017**

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