Court File No. CV-24-00715773-00CL

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

IN THE MATTER OF THE *COMPANIES' CREDITORS ARRANGEMENT ACT*, R.S.C. 1985, c. C-36, AS AMENDED

AND IN THE MATTER OF A PLAN OF COMPROMISE OR ARRANGEMENT OF BZAM LTD., BZAM HOLDINGS INC., BZAM MANAGEMENT INC., BZAM CANNABIS CORP., FOLIUM LIFE SCIENCE INC., 102172093 SASKATCHEWAN LTD., THE GREEN ORGANIC DUTCHMAN LTD., MEDICAN ORGANIC INC., HIGH ROAD HOLDING CORP. and FINAL BELL CORP.

Applicants

# REPLY FACTUM OF CORTLAND CREDIT LENDING CORPORATION

## (Threshold Legal Issue re Cortland Priority)

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**TO:** SERVICE LIST

***Overview***

1. Final Bell's response to Cortland's threshold motion is a further exercise in misdirection. Final Bell has not addressed, at any time, its own failure to oppose or seek to vary the ARIO. Instead, Final Bell now attempts to put forward a straw man argument by claiming, without any supporting facts or law, that Cortland's DIP priority must be subordinated to Final Bell's claims because of Cortland's alleged constructive knowledge of BZAM's purported misdeeds, which are unproven and contested by BZAM. Notably, Final Bell alleged this for the first time nearly a month after this motion was scheduled and approximately five months after commencing its claim.

2. The intention of this tactic is apparent: to reverse the decision made by the Court at the case conference of August 7, 2024, and convince the Court that there are additional facts to explore.

3. The focus of this motion is not, however, Cortland's knowledge but Final Bell's. Final Bell's knowledge of the ARIO. Final Bell's knowledge of the basis for its fraudulent misrepresentation claim at the time of the ARIO. Final Bell's knowledge of its claims at the time of the security for costs motion – when it proclaimed Cortland to be an innocent party. And Final Bell's knowledge of its claims at the August 7 case conference, where it did not raise its current speculations.

4. Moreover, Final Bell's new speculations founder on their own internal inconsistencies. It is a false syllogism to move from the proposition that Cortland's possible knowledge of excise tax liabilities provide it with objective knowledge of BZAM's alleged wrongdoing. It is also a disguised claim for equitable subordination of Cortland's

priority – a doctrine the Court of Appeal has explicitly ruled does not exist under the CCAA.

***Final Bell's Knowledge and Prior Positions***

5. There is nothing about Final Bell's speculations regarding Cortland's constructive knowledge that could not previously have been raised in this proceeding.

6. From the date of the ARIO, Final Bell was aware that to succeed on its claim (whether a rescission claim or constructive trust claim) it would need to leapfrog Cortland's security. Nothing prevented Final Bell from asserting in the past that Cortland had a degree of knowledge of Final Bell's excise tax filings and payments.

7. It is not an unusual inference that a secured lender would have some degree of knowledge regarding their borrower's financial status, including with respect to its priority payables. Presumably Final Bell did not previously articulate the much larger leap from that concept to constructive knowledge of BZAM's alleged misdeeds with Final Bell because it would undermine the credibility of its positions.

8. Notably, Final Bell's theory that Cortland had or could have had some degree of knowledge of BZAM's excise tax status arises at least in part from the reporting covenants in the ARCA. However, the ARCA was in the record before the ARIO was made and was no doubt reviewed by Final Bell during its self-described extensive due diligence.[1]

[1] Affidavit of Matthew Milich, sworn February 28, 2024 at para 82, Case Centre (Bundle 015), pp B-2-520 - B-2-521 (Current).

9. Final Bell has provided no explanation for its failure to raise these issues until now, despite having amended its pleading three times to date. Final Bell has equally failed to give any reason why it should be permitted to reverse its position to this Court, including from the security for costs motion, where it stated:

(a) "[…] Final Bell does not allege wrongdoing against Cortland";

(b) "Cortland is not a 'defendant' to an action. It is, at best, an intervenor on a motion. Final Bell does not seek any relief against Cortland: it does not seek damages or a declaration, or otherwise allege any wrongdoing against Corland. Cortland is only participating in this proceeding because, if Final Bell is successful, the relief it seeks will likely lead to Cortland recovering less than the full amount of the secured debt owed to it by BZAM"; and

(c) "No party alleges that [Cortland] committed any wrongdoing; it is only participating to seek to avoid an outcome that might affect its recovery in this CCAA proceeding."[2]

10. Final Bell similarly fails to explain why it did not raise this theory at the August 7 case conference, or why, despite its recent demand for new documents, it stated in its Aide Memoire on August 6 that the record was "fully-baked".[3] The only available conclusion and the only adverse inference that could be drawn on this motion is that the evolution of Final Bell's case theory is based entirely on expedience.

***Final Bell's Theories are Untenable***

11. Final Bell seeks to assert, with *no* supporting precedent, that the principles repeatedly upheld by the Supreme Court of Canada concerning the primacy of DIP

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[2] Responding Factum of Final Bell Holdings International Inc. (Cortland Motion for Security for Costs), dated May 22, 2024 at paras 1-2 and 41, Case Centre (Bundle 015), pp B-2-804 and B-2-814 (Current).
[3] Aide Memoire of Final Bell Holdings International Ltd. (August 7, 2024 Case Conference seeking Directions), dated August 6, 2024 at para 1, Case Centre (Bundle 015), p B-2-849 (Current).

charges can be disregarded on the basis of Cortland's alleged constructive knowledge of BZAM's fraud.

12. Problematically for Final Bell, its own theory has been judicially considered and rejected under the rubric of equitable subordination. Final Bell seeks to override the priority of the DIP by arguing that Cortland is somehow complicit in BZAM's alleged misrepresentation. That is the very essence of an equitable subordination claim. The Court of Appeal, however, has ruled such claims are not permitted under the CCAA:

> I would not grant the relief sought because, applying the principles of statutory interpretation, **nowhere in the words of the *CCAA* is there authority, express or implied, to apply the doctrine of equitable subordination. Nor does it fall within the scheme of the statute**, which focuses on the implementation of a plan of arrangement or compromise. The *CCAA* does not legislate a scheme of priorities or distribution, because these are to be worked out in each plan of compromise or arrangement. The subordination of "equity claims" is directed towards a specific group, shareholders, or those with similar claims. It also has a specific function, consistent with the purpose of the *CCAA*: to facilitate the arrangement or compromise without shareholders' involvement.[4] [emphasis added]

13. Final Bell's assertion of equitable subordination in this case is even more extreme. If the Court were to hold, as suggested by Final Bell, that a secured lender (not to mention a DIP lender) could have their security subordinated to a shareholder simply by having *constructive knowledge* of some underlying fact that might give rise to a claim against the borrower by that shareholder, it would undermine the entire lending industry; no lender would ever be able to comfortably rely on their security. It is presumably for that reason, among others, that the Court of Appeal has ruled out such claims.

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[4] *U.S. Steel Canada Inc (Re)*, 2016 ONCA 662 at para 101.

14. Equally, Final Bell has not properly pleaded, nor could it, a basis for constructive knowledge and knowing receipt in the current circumstances. The totality of Final Bell's factual allegations to support Cortland's alleged constructive knowledge in its Second Further Amended Notice of Motion are set out below:

> …Pursuant to BZAM's credit agreements with Cortland, BZAM reported its payables to Cortland on a monthly and weekly basis, including its excise taxes payable. This reporting provided Cortland on notice or inquiry that BZAM had failed to pay excise taxes due on or before the date of closing of the SEA by January 5, 2024, as required, and that BZAM used post-closing funds to pay pre-closing excise tax expenses, in breach of its representations to Final Bell.[5]

15. Even if true (which the Court does not need to presume), this allegation does not give rise to Cortland's constructive knowledge that a fraud was committed. It does not imbue Cortland with knowledge of what BZAM told Final Bell, or an understanding of the materiality of those representations to Final Bell or BZAM's level of fault (if any).

16. Constructive knowledge is assessed objectively.[6] The notion that a similarly situated lender would be expected to investigate and police representations made by a borrower (BZAM) to a counterparty (Final Bell) in a transaction that the lender (Cortland) is not party to, is not objectively reasonable.

17. There is no allegation that Cortland was tasked with conducting diligence on the representations and warranties made by BZAM to Final Bell, and that expectation is not reasonable to infer on an objective basis.

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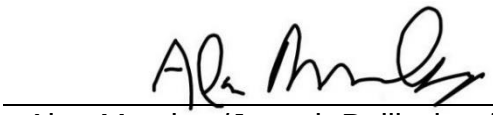
[5] Second Further Amended Notice of Motion at para 55.1, Case Centre (Bundle 015), p B-2-835 (Current).
[6] *Quantum Dealer Financial Corporation v Toronto Fine Cars and Leasing Inc*, 2023 ONCA 256 at paras 52-53.

18. For all of the above reasons, Cortland's motion should be granted with costs.

**ALL OF WHICH IS RESPECTFULLY SUBMITTED** this 16th day of September, 2024.



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**SCHEDULE "A"**

**LIST OF AUTHORITIES**

1. *Quantum Dealer Financial Corporation v Toronto Fine Cars and Leasing Inc*, 2023 ONCA 256

2. *U.S. Steel Canada Inc (Re)*, 2016 ONCA 662

## SCHEDULE “B”

## TEXT OF STATUTES, REGULATIONS & BY - LAWS

Nil.

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**PROCEEDING COMMENCED AT TORONTO**

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