Docket: 2004-2787(IT)G

BETWEEN:

ALLAN GARBER,

Appellant,

and

HER MAJESTY THE QUEEN,

Respondent,

Appeal heard during the weeks of January 10, 2012; February 6, 2012; February 14, 2012; February 21, 2012; February 27, 2012; March 26, 2012; April 24, 2012; May 15, 2012; June 4, 2012; June 11, 2012; October 2, 2012; October 9, 2012; October 30, 2012, November 5, 2012; December 4, 2012; December 10, 2012; January 22, 2013; February 5, 2013; February 12, 2013; April 16, 2013; April 29, 2013 and May 15, 2013, at Toronto, Ontario

By: Associate Chief Justice E.P. Rossiter

Appearances:

Counsel for the Appellants:	Howard Winkler
Counsel for the Respondent:	Gordon Bourgard, John Shipley and Julian Malone

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JUDGMENT

The appeals from the reassessments made under the *Income Tax Act* for the 1984, 1985, 1986 and 1987 taxation years are dismissed, in accordance with the attached Reasons for Judgment.

Signed at Ottawa, Ontario, this day of 7th[rd] day of January, 2014.

"E.P. Rossiter"

Rossiter A.C.J.

Docket: 91-1946(IT)G

BETWEEN:

GEOFFREY D. BELCHETZ,

Appellant,

and

HER MAJESTY THE QUEEN,

Respondent,

Appeal heard during the weeks of January 10, 2012; February 6, 2012; February 14, 2012; February 21, 2012; February 27, 2012; March 26, 2012; April 24, 2012; May 15, 2012; June 4, 2012; June 11, 2012; October 2, 2012; October 9, 2012; October 30, 2012, November 5, 2012; December 4, 2012; December 10, 2012; January 22, 2013; February 5, 2013; February 12, 2013; April 16, 2013; April 29, 2013 and May 15, 2013, at Toronto, Ontario

By: Associate Chief Justice E.P. Rossiter

Appearances:

Counsel for the Appellants:	Howard Winkler
Counsel for the Respondent:	Gordon Bourgard, John Shipley and Julian Malone

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JUDGMENT

The appeals from the reassessments made under the *Income Tax Act* for the 1986, 1987 and 1988 taxation years are dismissed, in accordance with the attached Reasons for Judgment.

Signed at Ottawa, Ontario, this 7th day of January, 2014.

"E.P. Rossiter"

Rossiter A.C.J.

Docket: 91-1816(IT)G
91-509(IT)G

AND BETWEEN:

LINDA LECKIE MOREL,

Appellant,

and

HER MAJESTY THE QUEEN,

Respondent.

Appeal heard during the weeks of January 10, 2012; February 6, 2012; February 14, 2012; February 21, 2012; February 27, 2012; March 26, 2012; April 24, 2012; May 15, 2012; June 4, 2012; June 11, 2012; October 2, 2012; October 9, 2012; October 30, 2012, November 5, 2012; December 4, 2012; December 10, 2012; January 22, 2013; February 5, 2013; February 12, 2013; April 16, 2013; April 29, 2013 and May 15, 2013, at Toronto, Ontario

By: Associate Chief Justice E.P. Rossiter

Appearances:

Counsel for the Appellants:	Howard Winkler
Counsel for the Respondent:	Gordon Bourgard, John Shipley and Julian Malone

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JUDGMENT

The appeals from the reassessments made under the *Income Tax Act* for the 1985, 1986, 1987 and 1988 taxation years are dismissed, in accordance with the attached Reasons for Judgment.

Signed at Ottawa, Ontario, this 7th day of January, 2014.

"E.P. Rossiter"

Rossiter A.C.J.

Citation: 2014TCC1
Date: 20140107
Docket: 2004-2787(IT)G

BETWEEN:

ALLAN GARBER,

Appellant,

and

HER MAJESTY THE QUEEN,

Respondent,

Docket: 91-1946(IT)G

AND BETWEEN:

GEOFFREY D. BELCHETZ,

Appellant,

and

HER MAJESTY THE QUEEN,

Respondent,

Docket: 91-1816(IT)G
91-509(IT)G

AND BETWEEN:

LINDA LECKIE MOREL,

Appellant,

and

HER MAJESTY THE QUEEN,

Respondent.

REASONS FOR JUDGMENT

Rossiter, A.C.J.

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A: OVERVIEW

[1] The Appellants subscribed through Overseas Credit and Guaranty Corporation (the "OCGC") for one of three types of Limited Partnerships. OCGC promoted and marketed the Limited Partnerships as an opportunity to invest in a luxury yacht chartering business structured to provide very attractive tax advantages to investors with limited personal risk. OCGC acted as the general partner for each Limited Partnership. Einar Bellfield incorporated OCGC in 1984 as its sole shareholder and was the operating mind of the entity.

[2] The investment involved each Limited Partnership purchasing a luxury yacht from OCGC that was to be delivered by a specified date. As the general partner, OCGC was committed to building, marketing, and managing a luxury yacht chartering business known as "Fantaseas" that would market and manage the yacht fleet of the Limited Partnerships. OCGC contracted to provide each Limited Partnership with various goods and services, in return for certain fees from the Limited Partnership. The investment plan anticipated significant start-up costs, with profits projected only in the long-term. However, as a Limited Partnership's expenses exceeded its revenue, the losses would flow down and be divided amongst the investors in each Limited Partnership and deductible from their respective incomes.

[3] The Fantaseas charters targeted the high-end luxurious yacht chartering market. In this market at the time, generally only an entire yacht could be chartered. Fantaseas aimed at an unfilled market niche: the chartering of individual cabins in luxury yachts. The Fantaseas concept was that each Limited Partnership yacht of a 60-foot catamaran or an 80 feet plus monohull would have four equally sized staterooms available individually for charter, along with crew quarters. Charter guests would enjoy gourmet food, excellent full-staff service, and upscale accommodations. Charters were to alternate between the Caribbean and the Mediterranean, according to the season.

[4] Starlight Canada Ltd., a company related to OCGC, was to coordinate the sale and marketing of the yacht chartering business. An additional company related to OCGC, Fabu D'Or, had the stated purpose of developing a commissary to prepare gourmet food within the luxurious standards of the Fantaseas brand. OCGC had made commitments to 36 Limited Partnerships to provide yachts of certain specifications, but the how, where, and when the yachts would be built and delivered changed several times. Depending on the timing, the yachts were supposed to be built

by companies in France (Dynamique, Chantier Yachting France, or Maxi-Yachts), or at a site in Picton, Ontario. Various naval architects and yacht builders participated at different points to design and build the yachts promised by OCGC. As it turned out, only two yachts that met the Fantaseas standards were ever purportedly built for the Canadian Limited Partnerships.

[5] The entire luxury yacht chartering investment opportunity and the Fantaseas concept were the brainchild of Einar Bellfield. The marketing and promotion of investment opportunities in the luxury yacht Limited Partnerships was one of OCGC's main investment projects, although the corporation also developed and sold other investment opportunities whose main premise appeared to have been that they were of a tax advantageous nature.

[6] The luxury yacht Limited Partnerships were promoted by various accountants, lawyers, and others, as tax shelters to their higher income-earning clients. The promoters received a commission for each investor that subscribed. The promoters heavily emphasized the tax advantages offered by the investment, which was the focus of much of the promotional material provided to potential investors. The tax attractions included the flow-through of losses from the substantial expenses incurred during the start-up phase before any revenue was generated, as well as the ability to claim depreciation on each yacht. For example, the Offering Memorandum for the S/Y Garbo Limited Partnership provided an overview of the tax advantageous nature of the investment opportunity as follows:

> The OCG Corporation is dedicated and organized to provide the taxpayer with attractive tax deals.
>
> Tax investments differ from other investments and they should be evaluated with certain objectives in mind. When considering a regular investment, the basic concerns are risk versus return.
>
> When evaluating tax investment, your main concerns are maximum capital depreciation with a low or no-risk exposure, and besides, there should be a good chance to obtain a reasonable return on invested capital, plus a capital appreciation further down the line.[1]
>
> …
>
> Due to this investment's initial high deductions and the declining capital cost allowance available to purchasers of marine vessels, the calculation of owners [sic] net income may be substantially influenced.[2]

[1] Exhibit A-44, Tab 1 - 1984 Offering Memorandum Garbo LP at 1.
[2] Exhibit A-44, Tab 1 - 1984 Offering Memorandum Garbo LP at 5.

[7] The structure of the transaction was tax advantageous for the investor as explained by OCGC in the Offering Memorandum for the S/Y Garbo Limited Partnership:

> The Financing Program has been tailored by OCG Corporation to maximize the available tax benefits for an Investor and at the same time eliminate any cash outlay by the purchaser of a Unit.[3]

[8] During the taxation years in question, from 1984 until 1988, depending on the Limited Partnership type, the investors claimed their share of their Limited Partnership's losses using the yearly loss schedules provided by OCGC. Investors also claimed their interest payments on a promissory note, which was part of the consideration on the purchase of a unit, as well as professional fees paid upon acquisition, in the year of subscription.

[9] In approximately April 1986, losses claimed by one Limited Partnership investor came to the attention of the Canada Revenue Agency (the "CRA").[4] An audit was commenced in October 1986. The CRA's Tax Avoidance department became involved and ultimately the CRA's Special Investigations department ended up conducting, in conjunction with the RCMP, search and seizures as well as interviews of staffers and investors of OCGC. In the end, the CRA came to the belief that OCGC was engaged in fraudulent activity in all the partnerships. The Minister of National Revenue disallowed all losses, interest, and professional fees claimed by the investors.

[10] The CRA's theory was that fraud had occurred by or through OCGC. Criminal charges were prosecuted. In 1994, Einar Bellfield was charged with two counts of fraud and two counts of uttering false documents. Mr. Bellfield's right hand man, Osvaldo Minchella, was charged with the same counts several months later. A jury found both Mr. Bellfield and Mr. Minchella guilty on all charges after a trial before the Ontario Superior Court of Justice. These convictions were upheld on appeal and leave to appeal to the Supreme Court of Canada was denied. Another player, Pierre Rochat, was arrested in 1995. He pled guilty to uttering forged documents in 1996, and was sentenced to six months in prison.

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[3] Exhibit A-44, Tab 1 - 1984 Offering Memorandum Garbo LP at 5.
[4] Revenue Canada at the time, referred to as the CRA henceforth.

[11] Of the over 600 investors that were reassessed, approximately 300 settled with the CRA. The great majority of the investors however, proceeded with appeals before the Tax Court of Canada. The Appellants before the Court are representative of those appeals by other Appellants, save and except for a few that have decided not to be bound by the result of these appeals.

[12] The central issue is whether each Limited Partnership constituted a genuine yacht charter business between 1984 and 1988, the range of taxation years in which the Appellants claimed Limited Partnership losses, interest, and professional fees relating to their investment in a Limited Partnership unit. If the Limited Partnerships were engaged in genuine businesses, then there was a source of income, and the expenses claimed may be deductible depending on the resolution of other issues.[5] If instead, I conclude that the Appellants were defrauded from the very beginning of their investment, then the Limited Partnership cannot constitute an income source for the Appellants and no amounts claimed are deductible.

[13] These appeals have a lengthy procedural history. Notices of Assessment and/or Reassessment were first issued in 1989 and/or 1990. Notices of Objection were filed in those same years. The appeals were held in abeyance for many years pending negotiations between the litigants and the final outcome of Mr. Bellfield and Mr. Minchella's trials and appeals in the criminal process. The criminal matters ultimately came to a close in 2004. A number of Motions came before the Tax Court of Canada regarding these appeals and caused further delays.

[14] The taking of evidence began on December 6, 2010 under the General Procedure Rule 119 over twenty years after the first Notices of Assessment were issued. The trial proper began on January 11, 2012, and in total, over 62 days of evidence was given with some 34 witnesses plus some 23 Agreed Statements of Facts. The hearing of the evidence occurred over an extended period to facilitate availability of witnesses and to allow for a better organization and presentation of evidence by both. As an aside, counsel for both parties worked together most impressively and cooperatively in most instances to put evidence presented before the Court that included tens of thousands of pages of multiple volumes of exhibits that by my count has accumulated to the point of filling over 100 bankers boxes.

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[5] As will be recited later, there are numerous other issues to be canvassed if the Limited Partnerships are determined to be an income source.

B: THE APPELLANTS' CLAIMS

[15] Four appeals were heard on common evidence with each of the three Appellants having invested in one of three Limited Partnership types. The 36 Limited Partnerships in which units were sold were divided into three types according to whether they were marketed and purchased in 1984, 1985, or 1986.

[16] The Type 1 Limited Partnerships were marketed and sold by OCGC in 1984. The 1984 Limited Partnership before the Court is the "S/Y Garbo Limited Partnership" (the "S/Y Garbo LP"). The Appellant Allan Garber purchased one of the 24 units in the S/Y Garbo LP and held the unit in trust for himself, Stacy Mitchell and David Sugarman.

[17] The following year, in 1985, OCGC marketed and sold Type 2 Limited Partnerships. The 1985 Limited Partnership before the Court is the "S/Y Midnight Kiss Limited Partnership" (the "S/Y Midnight Kiss LP"). The appellant Dr. Linda Leckie-Morel purchased one of the 24 units in the S/Y Midnight Kiss LP.

[18] The Type 3 Limited Partnerships were marketed and sold in 1986. This last type of Limited Partnership before the Court bears some transactional difference due to the new "at-risk rules" for Limited Partnerships introduced in the February 26, 1986 federal budget. OCGC designed the transactional history of the 1986 Limited Partnerships differently in an effort to grandfather them under the pre-1986 *Income Tax Act* rules. The appellant Geoffrey Belchetz purchased one of the 25 units in the 1986 Limited Partnership before the Court, the "S/Y Close Encounters Limited Partnership" (the "S/Y Close Encounters LP").

[19] The next three subsections set out the claims and the procedural history associated with each of the Appellants.

1. Allan Garber, 2004-2787(IT)G: The S/Y Garbo LP (Type 1 Limited Partnership)

[20] Allan Garber is a chartered accountant and businessperson residing in Ontario. Mr. Garber's appeal concerns deductions from his income relating to his

investment in the S/Y Garbo LP, a Type 1 Limited Partnership. The deductions were claimed in the taxation years 1984, 1985, 1986, and 1987.

[21] Mr. Garber learned about the opportunity to invest in the Limited Partnership from a promoter, who presented the Limited Partnerships as an investment in a capital asset, the luxury yacht "the S/Y Garbo", to be used in a yacht sailing chartering business. The S/Y Garbo LP had 24 units available, with each full unit price being $97,500. Mr. Garber purchased one-third of a unit for $32,500 in 1984.

[22] Mr. Garber claimed a share of the S/Y Garbo LP's losses proportionate to his ownership of one-third of a unit as business losses incurred as a result of making outlays and incurring expenses for the purpose of gaining or producing business income, under section 3, subsection 9(2), and section 96 of the *Income Tax Act* (the "*Act*"), as follows:

- $15,058 out of $1,084,064 total losses in the 1984 taxation year;
- $5,381 out of $378,457 total losses in the 1985 taxation year;
- $6,651 out of $478,902 total losses in the 1986 taxation year;
- $6,552 out of $471,769 total losses in the 1987 taxation year.

[23] Mr. Garber, per his Fresh as Amended Notice of Appeal dated September 19, 2008, claimed the interest he paid on one of two promissory notes used to purchase his one-third of a unit in the S/Y Garbo LP and deducted from his income in each year that was incurred, pursuant to paragraph 20(1)(*c*)(ii) of the *Act*, as follows:

- $635 in the 1984 taxation year;
- $3,859 in the 1985 taxation year;
- $2,512 in the 1986 taxation year;
- $2,167 in the 1987 taxation year.

[24] Finally, Mr. Garber claimed $150 in professional fees he paid as part of his acquisition of one-third of a unit, deducted in the year the expenses were incurred, pursuant to paragraph 20(1)(*e*) of the *Act*.

[25] The deductions for each of the taxation years were disallowed by Notices of Assessment issued July 28, 1989. Mr. Garber filed Notices of Objection in October 1989, and appeals to the Tax Court of Canada under paragraph 169(1)(*b*) of the *Act*.

[26] Early in the trial, Mr. Garber withdrew several of his claims. As of his Final Submissions, Mr. Garber only pursues the expenses outlined in table below. The table is reproduced from the Appellant's Final Submissions:

Expenses Claimed as of Final Submissions - Type 1 Partnership - The S/Y Garbo LP-Allan Garber (1/3 interest):[6]

1984

Interest expense on Note #1			$2,166.00
Professional fees			$150.00
Feasibility study		$100,000	
Production costs and professional fees		$120,000	
Sales commissions and issue costs		$274,000	
Linen, cutlery, china and utensils		$15,000	
Marketing and advertising		$60,000	
	Subtotal:	$569,000	
1/24 share x 1/3 of a unit			$7,902.78
	Total:		$10,218.78

1985

Interest expense on Note #1			$2,166.00
Marketing and advertising		$60,000	
Commissary Services		$90,700	
Management Fees		$70,000	
	Subtotal:	$220,700	
1/24 share x 1/3 of a unit			$3,065.28
	Total:		$5,231.28

1986

Interest expense on Note #1	$2,166.00

[6] This is a copy of the table found at page 12-13 of the Appellant's Final Submissions.

Charter expenses		$12,663	
Feasibility study update fee (50%)		$25,000	
Management fee		$7,129	
Marketing and advertising costs		$60,000	
Moorage fees		$52,405	
Depreciation		$139,696	
	Subtotal:	$296,893	
1/24 share x 1/3 of a unit			$4,123.51
	Total:		$6,289.51

1987

Interest expense on Note #1			$2,166.00
Charter expenses		$96,383	
Feasibility study update fee (50%)		$25,000	
Management fee		$100,000	
Marketing and advertising		$60,000	
Moorage fees		$55,139	
Travel, consulting and general research		$35,000	
Depreciation		$118,696	
	Subtotal:	$490,218	
1/24 share x 1/3 of a unit			$6,808.58
	Total:		$8,974.58

1988

Interest expense on Note #1			$2,166.00
Charter expenses		$123,788	
Management fees		$100,000	
Marketing and advertising		$64,200	
Moorage fees		$58,424	
Depreciation		$100,892	
	Subtotal:	$447,304	
1/24 share x 1/3 of a unit			$6,212.55
	Total:		$8,378.55

[27] It should be noted that the amount of the interest expenses claimed by Mr. Garber, in his Final Submissions is not consistent with the expenses claimed in his Fresh as Amended Notice of Appeal. In addition, as per the pleadings and

notwithstanding a schedule for expenses claimed as of March 26, 2012, which includes the taxation year 1988, under this appeal Mr. Garber did not claim relief in the 1988 taxation year.

2. Linda Leckie Morel, 1991-1816(IT)G, 1991-509(IT)G: The S/Y Midnight Kiss LP (Type 2 Limited Partnership)

[28] Dr. Linda Leckie Morel is a medical doctor residing in Scarborough, Ontario. Dr. Leckie Morel's appeals concern deductions from her income in the taxation years 1985, 1987, and 1988 in appeal number 1991-1816(IT)G, and the 1986 taxation year in appeal number 1991-509(IT)G. Both appeals relate to her investment in the Limited Partnership, S/Y Midnight Kiss LP", a Type 2 Limited Partnership.

[29] Dr. Leckie Morel was presented with the opportunity to invest in the Limited Partnership by her accountant. In 1985, she purchased one of 24 units in the S/Y Midnight Kiss LP at a purchase price of $97,500. Her understanding was that the S/Y Midnight Kiss LP was purchasing one yacht, the "S/Y Midnight Kiss", to be used in a luxury yacht chartering business.

[30] Dr. Leckie Morel deducted from her income the share of the S/Y Midnight Kiss LP's losses proportionate to her unit ownership as business losses incurred as a result of making outlays and incurring expenses for the purpose of gaining or producing business income, under section 3, subsection 9(2), and section 96 of the *Act*, as follows:

- $48,308 out of $1,159,392 total losses in the 1985 taxation year;
- $21,422 out of $514,120 total losses in the 1986 taxation year;
- $15,565 out of $373,565 total losses in the 1987 taxation year;
- $15,245 out of $365,878 total losses in the 1988 taxation year.

[31] Dr. Leckie Morel also deducted the interest paid on one of two promissory notes used to purchase her unit of the S/Y Midnight Kiss LP, in each year that the interest was incurred, pursuant to paragraph 20(1)(*c*)(ii) of the *Act*, as follows:

- $11,757 in the 1985 taxation year;
- $6,500 in the 1986 taxation year;
- $6,500 in the 1987 taxation year;
- $6,500 in the 1988 taxation year.

[32] Finally, Dr. Leckie Morel deducted $250 in professional fees paid in 1985, the taxation year the expenses were incurred, relating to borrowing funds to purchase her unit in the S/Y Midnight Kiss LP, pursuant to paragraph 20(1)(*e*) of the *Act*.

[33] The deductions Dr. Leckie Morel claimed for each of the taxation years were disallowed in Notices of Assessment issued on September 7, 1989 for the 1985, 1986, and 1987 years; and May 23, 1990 for the 1988 year. A Notice of Reassessment was issued on December 22, 1989 for the 1986 year. Dr. Leckie Morel filed Notice of Objections for each taxation year.

[34] On March 26, 2012, Dr. Leckie Morel reduced the number of expenses she is claiming in these appeals. The table below outlines the Appellant's claims as of the Appellant's Final Submissions.

Expenses Claimed as of Final Submissions-Type 2 Partnership-S/Y Midnight Kiss LP-Linda Leckie-Morel:[7]

1985

Interest expense on Note #1		$6,500.00
Professional fees		$250.00
Sales commissions and issue costs	$274,000	
Production costs and professional fees	$120,000	
Feasibility study	$100,000	
Marketing and advertising	$60,000	
Commissary services	$90,700	
Office expenses	$50,000	
Subtotal:	$694,700	

[7] This is a copy of the table found at page 13-14 of the Appellant's Final Submissions.

1/24 share			$28,945.83
	Total:		$35,695.83

1986

Interest expense on Note #1			$6,500.00
Marketing and advertising		$60,000	
International promotion		$35,000	
Feasibility study update (50%)		$25,000	
Management fee		$100,000	
	Subtotal:	$220,000	
1/24 share			$9,166.67
	Total:		$15,666.67

1987

Interest expense on Note #1			$6,500.00
Marketing and advertising		$60,000	
International promotion		$40,000	
Feasibility study update (50%)		$25,000	
Management fee		$100,000	
Consulting fees		$35,000	
	Subtotal:	$260,000	
1/24 share			$10,833.33
	Total:		$17,333.33

1988

Interest expense on Note #1			$6,500.00
Marketing and advertising		$64,200	
International promotion		$40,000	
Management fee		$100,000	
	Subtotal:	$204,200	
1/24 share			$8,508.33
	Total:		$15,008.33

3. Geoffrey Belchetz, 1991-1946(IT)G: The S/Y Close Encounters LP (Type 3 Limited Partnership)

[35] Geoffrey Belchetz is a businessperson residing in Toronto, Ontario. Mr. Belchetz appeals the disallowance of deductions from his income relating to his investment in the Limited Partnership, the "S/Y Close Encounters LP", a Type 3 partnership, for the taxation years 1986, 1987, and 1988.

[36] A promoter of the Limited Partnerships presented Mr. Belchetz with the opportunity to invest in a Limited Partnership that would own a capital asset, the luxury yacht "S/Y Close Encounters", to be used in a yacht chartering business. In 1986, Mr. Belchetz purchased one of the 25 units in the S/Y Close Encounters LP at a purchase price of $116,000.

[37] Mr. Belchetz deducted his proportionate share of the S/Y Close Encounters LP's losses as business losses incurred as a result of making outlays and incurring expenses for the purpose of gaining or producing business income, under section 3, subsection 9(2), and section 96 of the *Act*, as follows:

- $35,900 out of $897,500 total losses for the 1986 taxation year;
- $22,507 out of $562,675 total losses for the 1987 taxation year;
- $26,932 out of $673,294 total losses for the 1988 taxation year.

[38] Mr. Belchetz also deducted the interest paid on one of two promissory notes used to purchase his unit of the S/Y Close Encounter LP pursuant to paragraph 20(1)(*c*)(ii) of the *Act*. The amounts in each year were:

- $9,000 in the 1986 taxation year;
- $9,445 in the 1987 taxation year;
- $750 in the 1988 taxation year.

[39] In addition, Mr. Belchetz deducted $6,000 in professional fees paid to borrow funds to purchase his partnership unit in 1986, the taxation year the expenses were incurred, pursuant to paragraph 20(1)(*e*) of the *Act*.

[40] Mr. Belchetz's deductions for each of the taxation years, 1986, 1987, and 1988, were disallowed by Notices of Assessment issued on November 2, 1990. Mr. Belchetz filed Notices of Objection for each taxation year on November 12, 1990. On June 14, 1991, the Minister of National Revenue confirmed the assessments by Notice of Confirmation.

[41] Just as the other two Appellants did early in the trial, Mr. Belchetz reduced the expenses he is claiming. Mr. Belchetz's current claims as of Final Submissions are set out in the table below:

Expenses Claimed as of Final Submissions-S/Y Close Encounters LP-Geoffrey Belchetz:[8]

[8] This is a copy of the table found at page 14-15 of the Appellant's Final Submissions.

1986

Interest expense on Note #1			$9,000.00
Professional fees			$6,000.00
Sales and marketing consulting fees and other issue costs		$290,000	
Feasibility study		$100,000	
Production costs and professional fees		$90,000	
Inspecting building of yacht		$60,000	
Travel and building consulting fee		$35,000	
Management fee		$30,000	
Marketing and advertising		$25,000	
	Subtotal:	$630,000	
1/25 share			$25,200.00
	Total:		$40,200.00

1987

Interest expense on Note #1			$9,445.00
Feasibility study update (50%)		$25,000	
Inspecting building of yacht		$60,000	
Travel and building consultation fee		$35,000	
Marketing and advertising		$30,000	
Travel and promotion		$35,000	
Management fee		$100,000	
	Subtotal:	$285,000	
1/25 share			$11,400.00
	Total:		$20,845.00

1988

Interest expense on Note #1			$750.00
Feasibility update fee (50%)		$25,000	
Inspecting building of yacht		$60,000	
Travel and building consultation fee		$35,000	
Management fee		$100,000	
Marketing and advertising		$140,000	
Travel and promotion		$40,000	
	Subtotal:	$400,000	
1/25 share			$16,000.00
	Total:		$16,750.00

C: THE RESPONDENT'S GROUNDS RELIED ON FOR DISALLOWANCE

1. Sections 3 and 4 of the *Income Tax Act*

[42] The Respondent submits numerous grounds for the disallowance of the partnership losses, interest, and professional fees claimed by the Appellants. Firstly, the Respondent argues that the Limited Partnerships did not constitute an income source under sections 3 and 4 of the *Act* because there was no genuine yacht charter operation business; no yacht chartering business was ever carried on, and there was no reasonable expectation of profit. The Respondent asserts that the Limited Partnerships were not true partnerships in law because OCGC did not carry on business in common with the investors in any of the 36 Limited Partnerships in which units were sold.

2. Sham

[43] The Respondent further argues that the transactions were mere shams entered into with the Limited Partnerships and that OCGC and Mr. Bellfield never had the intention to carry on a business in common with the Limited Partnerships. The promissory notes were presented as mere shams used by OCGC and Mr. Bellfield as part of his scheme to defraud the Minister and the investors.

3. Expenses Not Incurred

[44] In the alternative, the Respondent argues that the Limited Partnerships did not actually incur expenses for the purpose of gaining or producing business or property income.

4. Timing of Expenses Deducted

[45] Again, in the alternative, the Respondent asserts that under subsection 9(1) and 18(9), certain expenses incurred are not deductible for timing reasons because no deduction is available for outlays or expenses incurred in the taxation year when the services are to be rendered after the end of that taxation year.

5. No Loans

[46] The Respondent also submits that the promissory notes do not constitute actual loans. The Respondent asserts that no money was lent or advanced to the investors and therefore no interest can be deducted under subparagraphs 20(1)(*c*)(i) or 20(1)(*c*)(ii) of the *Act* or under the meaning of an outlay or expense found in paragraph 18(1)(*a*).

6. S/Y Garbo Capital Cost Allowance Restricted

[47] Specifically regarding the Type 1 Limited Partnership, the S/Y Garbo LP, the Respondent asserts that any capital cost allowance deductions claimed pursuant to paragraph 20(1)(*a*) in the taxation years of 1986, 1987, and 1988 are restricted by the leasing property rules found in the *Income Tax Regulations* at subsections 1100(15), 1100(17), 1100(17.2), and 1100(17.3).

7. S/Y Garbo Interest Limitation

[48] Alternately, the Respondent submits that interest claimed under paragraph 20(1)(*a*) must be limited by the half-year rule outlined in subsection 1100(2) of the *Income Tax Regulations* because the S/Y Garbo yacht was not acquired in the years prior to 1986.

8. S/Y Close Encounters LP - At-Risk Rules

[49] Regarding the Type 3 Limited Partnership, the S/Y Close Encounters LP, the Respondent submits that Mr. Belchetz's partnership interest is not exempt from the at-risk rules introduced on February 26, 1986 because it was not actively carrying on a business on a regular and continuous basis before that date. The Respondent further submits that as a non-exempt partnership unit, Mr. Belchetz's claims are limited to the amount he was at-risk for. Under the new rules introduced, his claims are limited to a maximum of $6,000 in losses.

9. Section 245(1)

[50] The Respondent further claims that the deductions sought by the Appellants are barred by (former) subsection 245(1) of the *Act* because to allow the expenses or disbursements would unduly or artificially reduced the Appellants' income.

10. Section 67

[51] Further, the Respondent submits that even if the Limited Partnerships are determined to be a source of income, the expenses claimed are barred from deductibility under section 67 because they were not reasonable and were not incurred to earn income.

D: ISSUES

[52] The issues for the Court to determine are as follows:

1. Did each of the three Limited Partnerships constitute a source of income pursuant to sections 3 and 4 of the *Act* and are capable of suffering a loss under sections 3, 96, and subsection 9(2)?

2. If the Limited Partnerships are determined to constitute a source of income, did they actually suffer the losses claimed by the Appellants?

3. If the Limited Partnerships actually suffered the losses claimed, did they properly compute the timing of partnership losses claimed for the taxation years in question?

4. If there was a source with genuine losses taken at the correct times, what is the amount of capital cost allowance, if any, that the S/Y Garbo LP is entitled to deduct?

5. Did each of the Appellants incur the interest expenses claimed pursuant to paragraphs 18(1)(*a*) and 20(1)(*c*) of the *Act*?

6. Did the Minister properly disallow the partnership losses, interest, and professional fees?

E: TRANSACTIONAL FACTS

[53] The general structure of each Limited Partnership type is set out below, followed by a description of the subscription process for all investors and a detailed review of the individual investor subscription process using one of the Limited Partnership types as an example.

1. The Three Types of Limited Partnerships

[54] OCGC registered 79 Limited Partnerships, of three different types depending on the year registered. Of the 79 Limited Partnerships, units were sold in 36 Limited Partnerships. Einar Bellfield was the controlling mind of the general partner and all original limited partners.

[55] OCGC entered into Limited Partnership Agreements with each Limited Partnership. The signatory was the original limited partner, who was either Einar Bellfield (in trust), for Type 1 and Type 2 Limited Partnerships, or OCGC Enterprises (in trust) for Type 3 Limited Partnerships.

a) Type 1 Limited Partnerships – 1984 LPs

[56] The original limited partner of the Type 1 Limited Partnerships was Einar Bellfield, as bare trustee, and the general partner was OCGC. There were 24 units per Type 1 Limited Partnership. The price per unit in the Type 1 Limited Partnerships was $97,500. If fully capitalized, each Type 1 Limited Partnerships would have born a total capitalization of $2.34 million.

[57] The two Type Limited partnerships that the OCGC sold units in, both registered on November 28, 1984, were:

1. The S/Y Garbo Limited Partnership
2. The S/Y Gable Limited Partnership

[58] To provide a broad overview of the subscription process, an investor subscribed to a Type 1 Limited Partnership by providing two Promissory Notes ("Promissory Note #1" and "Promissory Note #2") for a total amount of $97,500. In addition, a payment of $450 in professional fees was made for the unit acquisition. The $6,500 in interest for the 1984 year was also payable.

b) Type 2 Limited Partnerships – 1985 LPs

[59] The 1985 Limited Partnerships' original limited partner was Einar Bellfield, as bare trustee, and their general partner was again OCGC. There were 24 units per Type 2 Limited Partnership and the price per unit was also $97,500. If fully capitalized, there would be a total capitalization of $2.34 million.

[60] Fourteen Type 2 Limited Partnerships were registered on March 20, 1985, except for the S/Y Change of Seasons Limited Partnership and the S/Y Main Event Limited Partnership. These two partnerships were registered on November 8, 1985. The fourteen Type 2 Limited Partnerships were:

1. Autumn Sonata Limited Partnership
2. S/Y Bergman Limited Partnership
3. S/Y Bogart Limited Partnership
4. S/Y Casablanca Limited Partnership
5. Queen of Hearts Limited Partnership
6. Ecstasy Limited Partnership
7. Going My Way Limited Partnership
8. S/Y Great Gatsby Limited Partnership
9. High Sierra Limited Partnership
10. Human Desire Limited Partnership
11. Serenade Limited Partnership
12. S/Y Midnight Kiss Limited Partnership
13. S/Y Change of Seasons Limited Partnership
14. S/Y Main Event Limited Partnership

[61] To subscribe to a 1985 Limited Partnership, the investor provided a down payment ranging from $4,000 to $6,000, as well as two Promissory Notes for the total amount of $93,500. An additional varying amount was also paid in professional fees for the acquisition of a unit. The interest owed for the 1985 subscription year, was also payable.

c) Type 3 Limited Partnerships – 1986 LPs

[62] The 1986 Type 3 Limited Partnerships had a different structure due to OCGC's intentions to grandfather the Limited Partnerships so that they would not fall under the new at-risk rules introduced in the February 26, 1986 federal budget. This effort consisted of OCGC Enterprises Inc. first acquiring all of the units of the Type 3 Limited Partnerships before the February 26, 1986 deadline, and then reselling the partnership units to the investors.

[63] The 25 units per Type 3 Limited Partnership each had a unit price of $116,000. If fully capitalized, each Limited Partnership's total capital was $2,900,000. Units were sold in the following twenty Type 3 Limited Partnerships, all registered on January 27, 1986:

1. Ambrosia Limited Partnership
2. Blue Gardenia Limited Partnership
3. Chasing Rainbows Limited Partnership
4. S/Y Close Encounters Limited Partnership
5. Compassion Limited Partnership
6. Duet In the Sun Limited Partnership
7. Elegance Limited Partnership
8. Forbidden Fruit Limited Partnership
9. Holiday For Lovers Limited Partnership
10. Midnight Lace Limited Partnership

11. Morning Star Limited Partnership
12. Operation Moonlight Limited Partnership
13. Pleasure Seekers Limited Partnership
14. Silvery Moon Limited Partnership
15. Sweet Sensations Limited Partnership
16. Winds of Paradise Limited Partnership
17. Wine & Roses Limited Partnership
18. Evening Star Limited Partnership
19. Opal Mist Limited Partnership
20. You Only Live Once Limited Partnership

[64] To purchase a Type 3 Limited Partnership from OCGC Enterprises Inc., an investor was required to provide a $6,000 down payment, two Promissory Notes for the total amount of $110,000, and varying amounts for professional fees ($9,000 for Mr. Belchetz) related to the acquisition of a Limited Partnership unit. Payment was also required for $9,000 in interest due in 1986, the year of subscription.

2. Investment in a Limited Partnership

[65] An investor in evaluating the investment opportunity or subscribing to a Limited Partnership dealt with a variety of documents.

[66] First, investors were provided with an Offering Memorandum that outlined the investment opportunity, the charter market, financial projections, income tax considerations, the management of the partnership, and other details. While there were some differences between each year's Offering Memoranda based on the distinctions between the Limited Partnership types, the general terms of the investment were quite similar.

[67] Upon deciding to invest, an interested party became a limited partner by signing a Subscription Agreement and agreeing to be bound by a Limited Partnership Agreement that was previously signed by the original limited partner. The original limited partner was either Einar Bellfield (Type 1 and Type 2 Limited Partnerships) or OCG Enterprises (Type 3 Limited Partnerships). Through the subscription agreement, the investor also granted OCGC Power of Attorney and the right to act as an agent for the Limited Partnership for purposes relating to the partnership.

[68] An investor in a Type 1 and Type 2 Limited Partnerships then signed two promissory notes, promising to pay the principal amounts and interest outlined in each note. The exact amounts varied depending on the partnership type. For the Type 3 Limited Partnerships, the financing portion differed in that investors signed an agreement to assume the financing and related interest, charges, and expenses purportedly originally arranged by OCGC for OCG Enterprises. This difference is again based on the intention to grandfather the Type 3 Limited Partnerships by first selling the partnership units to OCG Enterprises and claiming that they were actively carrying on a business on a regular and continuous basis before the at-risk rules came into effect.

[69] A number of other key agreements and documents were part of the investment process. Amongst others, there were:

1) a loan agreement between OCGC and the investor, with OCGC agreeing to loan the amount of the subscription price outstanding after the down payment, if any, and with the promissory notes provided by the investor securing the loan;

2) an agreement that the investor agree to guarantee and indemnify OCGC for his or her share of any expenses incurred on behalf of the Limited Partnerships;

3) a Buy-Back Agreement, signed between OCGC and each investor, or assumed from OCG Enterprises, as was the case for the Type 3 Limited Partnerships. As described in the S/Y Garbo LP, this agreement granted the subscriber the right to force OCGC to buy the unit back pursuant to the conditions set out:

> The Partner has an irrevocable right to sell the Units in the Partnership to OCG on the terms and in accordance with the provisions contained herein and OCG must purchase such unit in accordance with such provisions.[9]

[70] To provide a summarizing illustration, the paragraph below outlines the key components of the investment process. The S/Y Close Encounters LP is used as an example, with some differences due to the intention to avoid the new at-risk rules. The S/Y Close Encounters LP's compliance with the at-risk rules is at issue in this case, however, it is useful to employ it as a model.

[71] An investor subscribed to a unit of the S/Y Close Encounters LP by, *inter alia*:

1. Signing a Subscription Agreement and Power of Attorney Agreement with OCGC (acting on behalf of OCG Enterprises), the owner of 100% of the S/Y Close Encounters LP units included the investor's agreement to the following:

    a) The agreement is bound by the Limited Partnership Agreement, previously signed by the original limited partner, OCG Enterprises, bare trustee.

    b) The investor's assumption of the financing that was originally arranged by OCGC for OCG Enterprises and the assumption of all related obligations to pay interest, charges, and expenses. The purported existing financing amounted to $110,000 of the $116,000 unit price, and was secured by two promissory notes. The first promissory note was in the principal amount of $75,000 and the second promissory note was in the principal amount of $35,000.

    c) The assignment of a Buy-Back Option from OCCG on behalf of OCG Enterprises, to the subscriber.

[9] Exhibit A-44, Tab 7, The S/Y Garbo Limited Partnership Buy Back Agreement.

d) The investor's agreement to grant OCGC Power of Attorney and to appoint OCGC as his agent and true and lawful attorney for purposes in connection with the S/Y Close Encounters LP.

e) The investor's agreement to make the following current and future payments to OCGC:

- $6,000 of the $116,000 total purchase price of the partnership unit to be paid immediately;
- Payments for interest that accrued on the first Promissory Note between January 1, 1986 and the closing date of the unit purchase, with $750 due for each month; and
- Interest payments of $750 from January 31, 1987 to December 31, 1991.

2. Signing a Guarantee or Indemnity Agreement, whereby the investor agreed to indemnify OCGC for his share of any payments made by OCGC on behalf of the S/Y Close Encounters LP in carrying out its agreements with the Limited Partnership.

3. Charter Operations Agreements between the Limited Partnerships and OCGC

[72] In its capacity as general partner, OCGC entered into a number of agreements related to charter operations with each Limited Partnership. The key agreements that OCGC entered into with the Limited Partnerships included:

1) A Limited Partnership Agreement, setting out the general terms of the partnership and the relationship and rights of the limited partner and the general partner;

2) An Agreement of Purchase and Sale between the Limited Partnership and OCGC, in which the Limited Partnership agreed to buy a yacht from OCGC for a purchase price that ranged from $2.34 million to $2.9 million, depending on the partnership year. This was equivalent to the total investment in the Limited Partnership if the limited partnership was fully capitalized;

3) A Management Agreement where OCGC contracted to manage the Limited Partnership's yacht chartering business;

4) An Agreement for Providing a Line of Credit, where OCGC contracted to arrange an operating line of credit for the Limited Partnership to ensure adequate cash flow and cover any deficits that may arise in the course of yacht charter operations.

F: THE FACTUAL SUMMARY

1. Early Days

[73] OCGC was incorporated in May 1984 by Einar Bellfield as the sole director and shareholder. The Appellants describe this vision as follows:

> Mr. Bellfield had a vision (among other ideas) to purchase and/or to design and manufacture luxury sailing yachts, and in addition, to provide management and financial assistance within the yacht charter industry. In this regard, Mr. Bellfield can be considered a pioneer.[10]

According to the testimony of certain individuals, some believed that Mr. Bellfield's luxury yacht charters concept was novel and had the potential to do well and reach a new market.

[74] Initially, from 1984 to August 1985, the OCGC team consisted only of Mr. Bellfield and his wife Tina working out of their condominium den and occasionally using office premises at the TD Business Centre. In August 1985, Osvaldo Minchella joined the OCGC team after meeting Mr. Bellfield at RadioShack. Mr. Minchella was working at RadioShack at the time and sold Mr. Bellfield a computer. It was not

[10] Appellant's Final Submissions, Appendix 1 at page 2.

until May 1986 that OCGC operations moved to its own office on Richmond Street in Toronto.

[75] As noted, Mr. Bellfield incorporated OCGC in May 1984 as the sole director and shareholder. On July 15, 1984, Einar Bellfield received a discharge as a bankrupt, after having filed for bankruptcy on June 3, 1983. Several months after receiving the bankruptcy discharge, Mr. Bellfield was arrested on October 2, 1984 on four fraud charges related to another matter. The S/Y Garbo LP and S/Y Gable Limited Partnership's Offering Memoranda were distributed shortly thereafter in December 1984. After a preliminary inquiry decision committing him to stand trial, Mr. Bellfield was eventually acquitted on those other charges in 1987.

2. Marketing and Sale of Limited Partnerships

[76] Before the incorporation of OCGC in May of 1984, Mr. Bellfield began developing the concept for the luxury yacht chartering Limited Partnerships. The Appellant Mr. Garber first became aware of OCGC through a client. Mr. Bellfield had approached that client with the opportunity to purchase units in the 1984 Limited Partnerships. The client asked Mr. Garber to review the investment documentation that Mr. Bellfield had presented.

[77] Mr. Garber's evaluation of Mr. Bellfield's initial attempt at structuring the Limited Partnerships was that the financial projections were incomplete and the outline of the investment's business potential was brief. Mr. Garber was not prepared to touch the investment at that particular point in time. In his view, there were problems with the transaction's structure and the level of information disclosed to investors. Mr. Garber thought it was a very aggressive tax deal and at that time he advised his clients not to make the investment.

[78] Mr. Garber referred Mr. Bellfield to his accounting partner Stacey Mitchell, a chartered accountant, because the Limited Partnership offerings were more in line with Stacey Mitchell's area of professional focus on cash flow projections. Mr. Mitchell refined the proposal, with the more rigorous product ultimately presented to Mr. Garber. At that point, Mr. Garber decided that it was an interesting opportunity for his partners and his clients. Mr. Garber and two of his accounting firm partners, Mr. Mitchell and Mr. Sugarman, purchased a unit together. A number of their clients also bought units.

[79] The 1984 Limited Partnership units in the S/Y Garbo LP and the S/Y Gable Limited Partnership (the "S/Y Gable LP") were sold by word of mouth, through the accounting firm Moses, Sugarman & Company (i.e. Stacey Mitchell), by lawyers familiar with OCGC, and by Mr. Bellfield himself. At this stage, there was no marketing strategy for the Limited Partnerships. The development of the promotion of the Limited Partnerships was still in the embryonic stage. Each potential investor was provided a variety of documentation including the 1984 Offering Memorandum.

[80] In 1984, only two Limited Partnerships were registered and sold. The sales and promotion of the Limited Partnership units significantly increased the following year however, and units in 14 Limited Partnerships were sold. The 1985 Offering Memoranda were more refined, although they remained substantially similar to the 1984 Offering Memoranda. During this period, efforts to promote the investment opportunity began to spread around a network of promoters and brokers.

[81] The brokers and promoters included lawyers and accountants who knew of Mr. Bellfield or OCGC and were doing work of some kind for them. These lawyers and accountants began to refer clients and received both professional fees from clients and commissions from OCGC. They also purchased some of the units themselves. David Franklin, a lawyer, was one of the key brokers who came on board to peddle the Limited Partnerships after meeting with Mr. Bellfield in the summer of 1985. He was involved in the marketing of the 1985 and 1986 transactions, but by 1987, he was no longer involved.

[82] Mr. Franklin became one of the most significant promoters for OCGC. He prepared an investment proposal that contained information based on the Offering Memoranda. He circulated this investment proposal to prospective buyers, brokers, and promoters. He prepared a template letter that he sent to his various sub-agents who were selling units. The investment proposal solely emphasized the tax benefit as according to him, he and the sub-agents were marketing a tax deal and not a business investment opportunity.

[83] Mr. Franklin testified that although he was a lawyer himself, he relied upon the lawyers and accountants' opinions on the tax issues. As far as an investment from a business point of view, Mr. Franklin thought it was a great business opportunity because the investor would be making money from revenue generated from the

charter business of the yachts. In his opinion, the worst-case scenario was that as long as the Limited Partnership was carrying on the business, the investor could claim any losses. Although Mr. Franklin believed that Mr. Bellfield was acquiring yachts, he believed that even if there was no revenue you could still claim expenses and still benefit from the transaction on a cash basis.

[84] Upon beginning his testimony, Mr. Franklin sought and was granted protection under section 5 of the *Canada Evidence Act* and section 9 of the *Ontario Evidence Act*. His attendance was under subpoena *duces tecum*. In terms of credibility, I note that Mr. Franklin was a very fast talker. He had an explanation for everything and it was clear that he had drunk Mr. Bellfield's Kool-Aid. He did not want to answer the questions presented and made attempts to give a side answer rather than answer a question directly. On many occasions, he did not recall certain information despite his central promotional role. Mr. Franklin blamed everyone else for being responsible for misrepresentations, including the lawyers, accountants, and the CRA. Nonetheless, I assessed that the evidence of Mr. Franklin, which I reference here, is adequately credible to establish the nature of his promotional efforts, the timeframe, and character of certain misrepresentations.

[85] There were numerous lawyers and accountants involved with, acting for, or in concert with Mr. Bellfield, OCGC or the Limited Partnerships at various times. There were also promoters, agents, and subagents, all peddling the units. Some of the lawyers and accountants had multiple clients and professional relationships that would obviously be in conflict. For example, they charged professional fees to investors who were clients while receiving commissions on sales from OCGC. Also, an accounting firm might prepare the financial statements for OCGC on a pro forma basis for a Limited Partnership while at the same time, sell units in a Limited Partnership to its own clients, purchase their own units, and even provide tax opinions for the Offering Memoranda. The lawyers acted similarly, to some extent. This did not occur in every case but there seemed to be an attitude of "what's wrong with that?" Maybe this was not a conflict or something that would cause a professional to hesitate in 1984, but it would certainly raise an eyebrow in the 21st century. Where did this all leave the investor, whether it was in 1986, 2004, or 2013? In reviewing the evidence, one is struck repeatedly by the questions: who was working for whom, and in what capacity? What was the duty owed to whom, when, and what personal or business interest did they have in the activity?

3. Development and Marketing of Yacht Chartering Business

[86] In the planning, development and marketing of the luxury yacht chartering vision there were a number of people who were responsible for or participated in the marketing, sales, and operations of the Limited Partnership from June 1986 to 1990. Steven Leibtag provided sales and marketing advice and was present from December 1985 through to late 1987. Rose Ashworth was present from September 1986 to June or July 1989 as a sales representative for Fantaseas. David Martin was present from March 1988 to 1989 conducting marketing and sales for Fantaseas. Bruce Oekler was involved from December 1985 to December 1986 in developing a product for travel agents in Florida. Helen Fullem was involved from December 1988 to March 1989 in promoting Fantaseas overseas in Europe.

[87] The Fantaseas concept of elegant cruises on large luxury yachts with four separate cabins accommodating upwards of eight people, targeted the high-end market. Starting in late 1986, the development and marketing of the luxury yacht charter profile of Fantaseas was mainly events or activities. Starlight representatives visited travel agencies in Toronto, Ontario. They offered familiarization tours to acquaint travel agents with the Fantaseas product. Starlight attempted to develop a corporate incentive program. Trade shows were attended in New York and Chicago as well as two trade shows in Toronto to promote Fantaseas. An audio-visual presentation was developed and used in office presentations in Toronto. Cold calls were made and brochures were developed and circulated. Itineraries were developed for yacht charters in the Caribbean with particulars for restaurants, departure sail times and dates, activity options, sources of food, etc. A well-known chef named Jacques Pepin and his menus and food were used for promotional purposes. There was also solicitation of market houses in Europe. There was an audio-visual presentation at the Casa Loma in Toronto as well as speakers, which included Mr. Bellfield. This was basically a Q+A session for present investors and to advance the sale of units in Limited Partnerships.

[88] Attempts were made to develop local government relations in St. Lucia and to establish a foothold operational centre in the Rodney Bay Marina. Attempts were made to develop appropriate crew training programs as well as plans for food and beverage procurement and delivery. Attempts were undertaken to obtain media coverage through an article entitled “Ultimate Charter” in May 1986, written by Bruce Kemp, the author who also happened to conduct the feasibility study for OCGC for the luxury yacht charter business proposed.

[89] Professionals produced a video shot in the Caribbean, and travel agents used certain shots from the video. Advertisements were placed in Lifetime magazine and the Globe and Mail. There was also a promotional kit developed for use by the travel agents but it was in short supply and those who were trying to develop contact with the travel agents industry could not obtain sufficient copies needed to market the product.

[90] The development, marketing, and chartering of the Fantaseas concept was not without its problems. None of the individuals retained had any experience in the development of a start-up business of marketing yachts. They had no experience in the design or construction of yachts, the marketing and sales of yachts, or marketing and sales to the high-end niche market they were pursuing. A feasibility study of some four volumes was completed in 1986 for OCGC, with an update completed some two years later. Despite the existence of these studies, Ester Allan (now Ester Palmer and referred to as such from herein), who was overall responsible for the marketing, sale and operations of Starlight and the Fantaseas concept, never read the feasibility studies. Her major sales representatives, Rose Ashworth, David Martin, and Stephen Leibteg were not even aware of the studies.

[91] At a certain point, the marketing efforts were no longer productive because there was no product (i.e. yachts) or an insufficient amount to bring the marketing of the luxury yacht charters to fruition. Despite the 36 yachts promised to the Limited Partnerships, OCGC only ever acquired. The S/Y Garbo was an 80-foot yacht, the S/Y Gable was an 88-foot yacht, and the S/Y First Impressions was a 50-foot yacht. The S/Y Garbo was not available for chartering until the spring of 1987 and the S/Y Gable was not launched until November 1988. The S/Y First Impressions did not meet the Fantaseas concept and was looked upon as a provisioning vessel. The following section provides an overview of the planning, design, construction, and acquisition of yachts by OCGC.

4. Planning, Design, Construction, or Acquisition of Yachts

a) General

[92] The success of the 1984 Limited Partnerships and all successive Limited Partnerships sold was totally dependent upon having a yacht for each Limited Partnership to participate in the luxury yacht chartering business for the purpose of

earning income. Each yacht would be a part of the fleet of yachts used in the Fantaseas concept of elegant cruises on luxury yachts sold on charter with four cabins per yacht.

[93] As mentioned above, OCGC committed to deliver 36 yachts. For the 1984 Limited Partnerships, the S/Y Garbo and S/Y Gable were to be under construction in 1984 and delivered in 1985. For the 1985 Limited Partnerships, 14 additional yachts were due by December 31, 1985, bringing the total number of luxury yachts to be completed by the end of 1985 to 16 vessels. In 1986, OCGC committed to delivering an additional twenty yachts by the final months of 1989 or early 1990.

b) The Yachts

[94] As will be described hereafter, there were really only three yachts ever owned or purportedly owned by OCGC or held by OCGC: the S/Y First Impressions, the S/Y Garbo and the S/Y Gable. Only one of the yachts was available in 1985; the S/Y First Impressions, which was only 50 foot and not suitable for the Fantaseas concept. Neither the S/Y Garbo nor the S/Y Gable were ever legally owned or registered in the names of the Limited Partnerships, nor used to the benefit of the S/Y Gable or S/Y Garbo Limited Partnerships.

c) The S/Y First Impressions

[95] The first yacht acquired by OCGC was the S/Y First Impressions. Mr. Bellfield took possession of the 50-foot yacht, to avoid losing OCGC's deposit paid on the S/Y Garbo. On November 27, 1985, title for the S/Y First Impressions was transferred to OCGC. This yacht did not satisfy OCGC's obligations to deliver large luxury yachts to the Limited Partnerships.

[96] The S/Y First Impressions was purported to be a provisioning yacht for the luxury yacht charters but in November 1985 but there were no yachts to provision. The First Impressions arrived in St. Lucia in March 1986 where there was a dispute over the lack of payment for the crew services rendered in the trans-Atlantic crossing that resulted in the arrest of the S/Y First Impressions. Eventually the ownership of the S/Y First Impressions was transferred to Tina Bellfield on June 26, 1992, and the yacht was located in Toronto, Ontario.

d) The S/Y Garbo

[97] The second yacht acquired by OCGC was the S/Y Garbo, purportedly intended for the S/Y Garbo LP. In February 1985, Mr. Bellfield met the owners of Dynamique Yachts in France and discussed with them the possibility of building luxury yachts. Dynamique was to build the S/Y Garbo for OCGC. Over an extended period of time, Mr. Bellfield failed to arrange financing for the S/Y Garbo, and to meet his financial obligations to Dynamique. Various agreements and memorandums were drafted and payments options rearranged. Repeatedly, Mr. Bellfield did not meet his full financial obligations. A $50,000 deposit was paid, but further payments were not forthcoming for a significant period of time. Mr. Bellfield faced the risk of losing the deposit due to his inability to pay the balance owed on the S/Y Garbo. Upon negotiation, the deposit was ultimately credited towards the acquisition of a smaller yacht, the S/Y First Impressions.

[98] OCGC eventually paid the funds owed and acquired the S/Y Garbo. Dynamique sailed the yacht across the Atlantic to St. Martin and OCGC took possession of the S/Y Garbo on April 4, 1986. As it turned out, the yacht was not up to the standard contemplated by the Fantaseas concept and it suffered extensive structural damage in its maiden voyage that required it go into a dry dock in Florida, U.S.A. for repairs. The S/Y Garbo was not available for charters until April 1987. Even then, there were interior decoration problems, electrical issues, and general ongoing repairs because of the yacht being in a southern climate. There were ongoing requests for OCGC to pay its bills for repairs, etc., and funding was slow if available at all. Title was never registered in the name of the S/Y Garbo LP. Ultimately, in 1988 the S/Y Garbo was sold to Maxi-Yacht International S.A.R.L. as part of financing for the French yacht building company.

e) The Ondine (the S/Y Great Gatsby)

[99] OCGC negotiated the purchase of a racing yacht known as the Ondine that was going to be called the S/Y Great Gatsby. The racing yacht was an 80-foot aluminium yacht that was not suitable for the Fantaseas concept. Notwithstanding the foregoing, OCGC entered the contract to purchase the Ondine for $298,500 on December 24, 1985. Eventually, Mr. Bellfield was once again behind on his payments and legal action was commenced by the owner of the Ondine against OCGC for default of payments and for stripping the yacht. The matter was settled in

April 1988 and the possession of the yacht was transferred back to the original owner.

f) The Med 86

[100] A Med 86 was seen at a yacht show in Miami and it was thought that it could be renovated to suit the Fantaseas concept. An Agreement of Purchase and Sale was executed on January 30, 1987 but the sale did not close. The price of the yacht was $US 1,425,000 with a down payment of $350,000 paid in escrow with the balance payable on closing set for April 1, 1987. The closing was delayed to May 1, 1987 with OCGC agreeing to pay an additional $200,000 in escrow. In the end, the deal did not close and OCGC was put in default. In arbitration with the owner, U.S. Yacht was awarded damages of $367,167 plus accrued interest due to the failure to close.

g) The S/Y Gable

[101] The third yacht purportedly acquired by OCGC was the S/Y Gable. The S/Y Gable was designed by Sparkman Stevens for the S/Y Gable Limited Partnership. It was to be constructed by Michel Dufour, a well-known French builder. The plan was for Mr. Dufour to carry out the construction of yachts and for Mr. Bellfield to provide financing. Negotiations around the design continued from 1986 to 1987. Maxi-Yacht International was created with Mr. Bellfield and Mr. Dufour as shareholders. The Maxi-Yacht boat-building facility was constructed and eventually had three yachts in various stages of construction. The first yacht was the S/Y Gable with two other yachts in the process of construction, one with a deck on, and one with the hull being made. The S/Y Gable was completed, launched, and christened in November 1988 and was the first yacht that was available to be delivered to a Limited Partnership that truly met the Fantaseas concept. Even so, it was never transferred to the S/Y Gable LP or to any other Limited Partnership, nor was it used to the benefit of any Canadian Limited Partnership. Instead, it was sold to Starlight S.A.M., a French entity.

h) Other contracts

[102] The other two yachts constructed at the Maxi-Yacht facility were the Demoiselles des Rochfort and the Rocco Jr. Both were sold to French Limited Partnerships.

[103] In addition, two purchase agreements were signed with Chantier Yachting France for two yachts in March 1985; however, the company went into receivership in July 1985.

5. The CRA Audit and Investigation

[104] The CRA began to look into the affairs of OCGC after an inquiry into a file of an OCGC investor named Steven Mitchell on October 14, 1986. At that time, CRA auditor Karen McCordick was to review the validity of the S/Y Gable LP business losses claimed by Mr. Mitchell. This was followed up with a request for the individual tax returns of Mr. Mitchell and his wife for 1984 and 1985. It turned out that Steven Mitchell was in fact the brother of Stacey Mitchell who had been heavily involved in providing accounting services to OCGC for the Type 1 Limited Partnerships as well as being a promoter and investor in some of the Limited Partnerships.

[105] The review by Ms. McCordick into the business losses of Steven Mitchell led her to the S/Y Gable LP Offering Memorandum and Mr. Bellfield, who was purported to be the keeper of the records of OCGC and the corporate returns of OCGC for 1984 and 1985. Over the next few months, Ms. McCordick pursued the S/Y Gable LP's records and documentation but was unsuccessful. In addition, it was noted that no corporate income tax returns had been filed by OCGC at that time. The file was eventually referred to the Tax Avoidance section and in the spring of 1986 was referred to Special Investigations.

[106] Over a period of many months in 1987, there were numerous attempts by the CRA to have discussions with OCGC and its representatives, in particular with Mr. Bellfield, to obtain information with respect not just to Steven Mitchell's returns but to the overall operations of OCGC and its Limited Partnerships scheme. Some of the information provided was forthcoming and other information was lacking. As it turns out, much of the information requested was being manufactured as the requests were being made.

[107] Special Investigations and Tax Avoidance continued their investigations and enquiries independent of each other but Tax Avoidance took a backseat to Special Investigations. Tax Avoidance apparently investigates the civil side of tax issues while Special Investigations investigates and prepares tax issues for criminal

prosecution. Tax Avoidance formulated their position on OCGC and the Limited Partnership scheme in 1988.

[108] In June 1989, there were search and seizures conducted at OCGC facilities and other locations, as well as various interviews of individuals affiliated with OCGC and investors. The CRA investigations, whether by Tax Avoidance or Special Investigations, were extensive and exhaustive, but were not without problems given that Tax Avoidance was one department of CRA and Special Investigations was another. Furthermore, the RCMP became involved with respect to the investigation of possible criminal activity.

[109] The CRA Tax Avoidance came to the belief that OCGC was engaged in fraudulent activity and was of the view that

(a) There was a premature claim for deductions i.e. capital cost allowance;

(b) OCGC was significantly underfinanced and that there was no financing for yacht construction;

(c) There was no capital contribution by the partners—simply a circulation of loans from OCGC to the partners and back to OCGC. OCGC never had the money to make the loans in the first place;

(d) There was a certain amount of unreasonableness in the expenses and some amounts claimed for expenses were excessive, i.e. the feasibility studies;

(e) Some expenses were never incurred; and

(f) There were significant problems in the actual manufacturing and delivering of the yachts for the Limited Partnerships.

[110] In the end, the Minister disallowed all the losses, interest and professional fees claimed by the investors. As described above, criminal charges were laid against Pierre Rochat, Mr. Bellfield, and Mr. Bellfield's right hand man, Mr. Minchella. Mr. Rochat pled guilty to uttering forged documents. Mr. Bellfield and Mr. Minchella were convicted of two counts of fraud and two counts of uttering forged documents and their convictions were upheld on appeal.

G: MISREPRESENTATIONS: A FRAUD FROM BEGINNING TO END

[111] The Appellants assert that despite the evidence presented of a persistent pattern of OCGC and Mr. Bellfield's lies, there are sufficient indicators of a business because $13–14 million was spent on what the Appellants describe as efforts to establish a yacht chartering business. In Appendix One of the Appellants' Final Submissions, they state:

> 3. Despite the fact that the venture was ultimately unsuccessful, and notwithstanding the evidence of lies and/or misrepresentations proffered by Mr. Bellfield, the fact is, that OCGC **created and established yacht chartering businesses that were both visionary and worldwide in scope**.
>
> [Emphasis in original]

[112] This statement is accurate in part; but should read, "OCGC created and established the illusion of a yacht chartering business". I find that the yacht chartering business was nothing more than an illusion, a fraud from beginning to end. Most certainly there were sufficient indicia present to lend an air of legitimacy. Most certainly there was money spent for the purpose of developing these indicia, but for Mr. Bellfield, they were all for the purpose of perpetuating the fraud on the investors in the Limited Partnerships, the CRA, and many other parties that came into contact with him in this venture.

[113] The evidence shows that the investors were induced with misrepresentations to invest not in genuine Limited Partnerships, but rather in a Ponzi-like scheme orchestrated by Mr. Bellfield. OCGC never had the capital necessary to implement the investment plan, despite its many representations to the contrary. The only source of funds OCGC had available was the investors' interest payments and the small deposits made by investors upon subscription in the Type 2 and Type 3 Limited Partnerships. With a dire lack of capital, Mr. Bellfield had to continue to sell units in Limited Partnerships so that he could keep funds coming in and he could continue to perpetuate the fraud. To maintain the appearance that the investment opportunity was real, Mr. Bellfield had to make an effort to build or acquire yachts and provide indications that a charter business was being developed. These efforts however, were always limited in scope and always suffered from both a lack of yachts to implement any genuine chartering business, and a severe lack of funds. Barely any results were produced when compared to the enormity of the results represented to investors as not only planned, but also to some extent, already achieved. Any yacht building and

charter development efforts by OCGC and its related companies were mere window-dressing. Mr. Bellfield kept his scheme to himself and Mr. Minchella. Investors, promoters, lawyers, accountants, and the staff of OCGC were all kept in the dark.

[114] The documentary evidence shows that the starting point for the fraud began from the time that the first Offering Memoranda were prepared in November 1984, if not earlier. This was before any investors subscribed for any Limited Partnerships units. The fraud continued without stop and grew in scope until the entire scheme unravelled after the CRA and the RCMP began an extensive investigation, and the investors ultimately ceased making their interest payments. The categories of misrepresentations laid out in the section below show how the fraud progressed chronologically and grew in scope and size, including:

1) The fundamental misrepresentations in the Offering Memoranda;

2) The misrepresentations to professionals at closing, including the false documents provided at closing such as
    a) the false certificates,
    b) the false statements regarding OCGC's obligations,
    c) the false solemn declarations,
    d) the false affidavits,
    e) the false hull registration numbers;

3) The misrepresentations in OCGC's materials and public relations campaigns regarding the "fleet of yachts" and the "Gourmet Commissary";

4) Numerous false revenue and expense items listed in the financial statements, with false expenses growing annually;

5) Misrepresentations regarding the provision of financing and goods and services from the foreign entities Starlight S.A. and Neptune Marine;

6) Backdated and false documents, including yacht delivery schedules and Management Agreements;

7) Misrepresentations to various yacht builders or sellers as to the availability of funds to build or purchase yachts;

8) Ongoing misrepresentations to OCGC, Starlight employees and third parties as to the state of charter operations and yacht construction;

9) Ongoing false statements to investors regarding the number of yachts built or under construction, and expected delivery dates;

10) Ongoing misrepresentations regarding the state of charter operations and the number of charters booked; and

11) False loss statements and other documents to defraud the CRA and the investors.

[115] The examples below highlight the numerous instances of misrepresentation by OCGC, beginning with the first misrepresentations that OCGC and Mr. Bellfield made to the 1984 investors in the Offering Memoranda and continuing with the multitude of misrepresentations OCGC continued to make throughout the taxation years in question. The Respondent spent well over one hundred pages in his Final Submissions detailing the extensive misrepresentations. Here, only key falsehoods are reviewed. There are a sufficient number of examples provided to convey the intricate and pervasive nature of the fraud. I have referred extensively to the Respondent's submission on the misrepresentation as I found the Respondent's summary and submission on this area excellent and succinct.

a) The Offering Memoranda

(i) The 1984 Offering Memoranda: Misrepresentations of Material Facts

[116] Both the 1984 Offering Memorandum for the S/Y Garbo and the S/Y Gable are replete with material misrepresentations. They demonstrate that from their very first contact with this investment opportunity, the investors were fraudulently induced

to invest. Material misrepresentations were made to the investors, legal and accounting professionals, those marketing and promoting the LPs and to the tax professionals whose opinions were included in the Offering Memorandum.

[117] Key misrepresentations were made in both the 1984 Offering Memorandum for the S/Y Garbo LP and the Offering Memorandum for the S/Y Gable LP. These documents are substantively the same. The S/Y Garbo LP Offering Memorandum is referred to below by way of example.

[118] When considering the material misrepresentations below, it is important to highlight that Mr. Bellfield certified on November 1, 1984, that the contents of the S/Y Garbo LP Offering Memorandum were true and constituted full disclosure of material facts relating to the investment opportunity, as required by law. The certifying statement said as follows:

> The foregoing constitutes full, true and plain disclosure of all material facts relating to the securities offered by this Offering Memorandum as required by Part XIV of the Securities Act (Ontario) and the regulations thereunder.[11]

Financing and Feasibility Study

[119] The Offering Memorandum states that business start-up costs of $953,200 will be deductible in the first year of operation and that those costs consist mainly of a feasibility study and the costs for arranging financing. The evidence shows, however, that no financing was ever arranged. There was also no feasibility study in the first year of operation. A feasibility study was not commissioned until late 1985 and was only delivered by Bruce Kemp on January 28, 1986, at a cost of $4,000. Further, the evidence showed that Mr. Kemp had no experience in the yacht charter business or in yachting at all—he was a writer. The false assertion that the feasibility study was deductible in the first year of operation is repeated elsewhere in the Offering Memorandum.

Brokers for Management and Bookings

[120] The first page of the Offering Memorandum states: "OCG Corporation has made arrangements with major brokers both for providing management and

[11] Exhibit A-44, The S/Y Garbo Limited Partnership Offering Memorandum at 21.

necessary bookings", but there is no evidence that such arrangements were made at the time that the Offering Memorandum was distributed. In fact, Ester Palmer, Mr. Bellfield's sister-in-law, testified that she did not even begin working for Starlight Charters until approximately January 1986 and only then were efforts made to market the charters and build relationships with various travel agents. Ester Palmer was the first employee of OCGC other than Tina Bellfield and Mr. Minchella and was responsible for the development and marketing of the yacht charter business. I found Ms. Palmer to be somewhat naïve, and a person who took total direction from Mr. Bellfield. For example, no bills approved by Ms. Palmer were paid without Mr. Bellfield's specific authorization. She believed everything he said, notwithstanding documentation that should have told her otherwise. As a witness, she very frequently avoided answering questions by saying "I do not know" or "I don't recall", citing these phrases dozens of times during cross-examination, in fact over 100 times, even on matters that should have been within her knowledge.

[121] For example, in referring to an OCGC brochure, Ester Palmer could not recall who edited the brochure. She had no personal knowledge of who prepared the text, no knowledge as to where some of the information in the brochure came from, she couldn't recall whether there was an international reservation system in place for the yacht charters, she didn't know who was responsible for paying Jacques Pepin, she didn't know if Fabu-D'Or was operating, and on and on. While the length of time that has passed between the events she was testifying about and the trial might explain this lack of memory in part, it does not sufficiently explain how she would have no knowledge or understanding of certain affairs.

[122] Ms. Palmer became an investor in the Forbidden Fruit Limited Partnership in 1986 and claimed losses for a yacht that did not exist. Further, she never paid for the unit nor did she pay any interest on the purchase of the unit. Notwithstanding that Ms. Palmer was basically responsible for the marketing of the yacht chartering business, and was an investor herself, she never read the feasibility studies at any time, even though they were specifically referred to in the Offering Memoranda of the Limited Partnerships. In fact, the feasibility study was never the subject of any discussion during the operations. She appeared to be somewhat truthful in the things she was aware of, but she seemed to be terribly naïve and clearly believed Mr. Bellfield, her brother-in-law, on every aspect of the operation, with significant personal reasons to continue to do so.

Brokerage Fees, Construction Financing, and Acquisition Loans

[123] The Offering Memorandum shows $55,455 in brokerage fees, $1,109,000 in constructing financing, and $66,545 in construction financing interest. There is no evidence, however, that the brokerage fees were based in reality or that OCGC ever arranged construction financing. In fact, all references to financing in the Offering Memorandum, either for investors or for the project, are false. In the tax opinion included in the Offering Memorandum from the law firm Leve & Zeller, a number of assumptions were based on false representations by OCGC, including that loans for $54,166 were available through a chartered bank to each limited partner for their unit acquisition, and that the loan was secured by a letter of credit. These representations were entirely false.

Cutlery, Linen, China, and Utensils

[124] Cutlery, linen, china, and utensils are listed as a deductible expense item for $15,000 when in fact these items were not purchased until Ester Palmer began working with Starlight Charters in 1986.

Marketing and Advertising

[125] The Limited Partnership is described as having $60,000 in deductible expenses for marketing and advertising. The evidence points to the main person working on marketing and advertising of the charter was Ester Palmer, but she testified that she only began at Starlight Charters in 1986. Again, it is not possible that $60,000 in marketing and advertising expenses were deductible as described in the Offering Memorandum as no such expenses could have been incurred until after Ms. Palmer began working at Starlight Charters. The Respondent's Final Submissions accurately summarize why the representations regarding marketing and advertising expenses are false:

> Palmer was in charge of marketing, sales, and operations. Her position was, she said, comparable to that of a general manager. Palmer did not start her employment at Starlight until January 6, 1986. She said Starlight was a start-up business and she was starting from scratch. Minchella confirms the evidence of Palmer on this point. When Minchella joined OCGC in August 1985 the staff consisted of Einar Bellfield, his fiancée, Tina Bellfield and himself. Tina Bellfield was doing administrative work. That was the OCGC team up to December 31, 1985 except for professional advisers like

> Zeiler, Mitchell and David Franklin's assistant, Elizabeth Burrows, who was doing courier work. The representation that the partnership had deductible expenses in the amount of $60,000 for marketing and advertising was false.[12]
>
> [Footnotes removed]

Capital Cost Allowance

[126] Repeatedly throughout the Offering Memorandum, the S/Y Garbo yacht is described in the Offering Memorandum as being acquired or under construction in 1984, with capital cost allowance deductions beginning in that year. The testimony of Loic LeGlatin demonstrates that it is impossible that the S/Y Garbo was acquired in 1984 or that construction even began in 1984.

[127] Mr. LeGlatin was hired by Mr. Bellfield purportedly to find yachts suitable for the Limited Partnerships. Mr. LeGlatin was definitely highly skilled to do this works as he had extensive experience in the yachting field. His testimony showed him to be a credible witness who had nothing to gain from misrepresenting his experience working for OCGC. He was a straightforward, frank, and honest individual who answered questions directly, with the information and knowledge that he had. Mr. LeGlatin was not a person who was going to shade the truth in any way, but simply gave evidence on matters that he had knowledge of, and certainly appeared to be knowledgeable in the areas upon which he was examined and cross-examined. Mr. LeGlatin testified that he personally arranged the order for what would be the S/Y Garbo, with an agreement between OCGC and the yacht-builder Dynamique for one 80-foot yacht signed on February 19, 1985.

[128] Mr. LeGlatin also testified that OCGC's claim that the purchase agreement was executed following a previous letter of intent purportedly signed in November 1984 was false and in fact, impossible. In November 1984, OCGC was still working out of Mr. Bellfield's den in his condominium. Only Tina Bellfield worked for the company, along with a clerical assistant/courier. OCGC's other main persons of contact were accountants and lawyers. It was Mr. LeGlatin who originally connected Mr. Bellfield with the Dynamique yacht-building company and he did not even begin working for OCGC until approximately January 1985. Furthermore, he did not meet with Chantal Jeanneau of Dynamique until February 1985.

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[12] Respondent's Final Submissions at 36.

[129] The S/Y Garbo was not under construction in 1984 nor owned by OCGC. Possession of the S/Y Garbo by OCGC did not actually pass until April 1986. Title to the S/Y Garbo never passed to the S/Y Garbo LP. Mr. Garber, the 1984 investor in this case, testified that his understanding was that a capital cost allowance was deductible in 1984 because the S/Y Garbo was at the very least already under construction. The representation in the Offering Memorandum that a capital cost allowance was deductible in 1984 is false.

[130] These are but some examples of the numerous and significant misrepresentations in the Offering Memoranda. The misrepresentations go to both the tax advantages of the investment and the business venture, and show the ongoing and pervasive nature of the fraud. The material facts that were falsely presented go to the core of the securities being offered to investor and OCGC's failure to ensure that they were carried out as presented is a fundamental breach of its obligations.

[131] Mr. Bellfield through OCGC made these misrepresentations to ensure that a potential investor would find the yacht charter investment attractive. The new 80-foot luxury yacht under construction; the accoutrements necessary for luxury charters such as cutlery, linen, and china being acquired; the appropriate marketing and advertising undertaken; and the individuals retained to manage the business and book the charters all supported by financing and a feasibility study as well as deductibility of the capital cost allowance on the new 80-foot yacht. These were all representations made to create the perception of a legitimate yacht chartering business right from the beginning, and none of these representations were true.

(ii) The 1985 Offering Memoranda: Material Misrepresentations Continue

[132] The substantial nature of OCGC's misrepresentations continued into the Offering Memoranda for the 1985 Type 2 Limited Partnerships, all of which are substantively the same as the Type 1 Limited Partnerships. Mr. Bellfield again certified that these Offering Memoranda represented full and true disclosure of material facts as required by law. Key examples of these misrepresentations are set out in the paragraphs below.

Brokers

[133] On the first page of the 1985 Offering Memoranda, OCGC claims that it has made arrangements with major brokers. Again, this claim is not possible because

Ester Palmer did not begin her work at Starlight Charters until January 1986 and it was only at that point that she began to make arrangements with brokers.

Charter Bases

[134] The first page contains the assertion that charter bases were already established in Monaco and St. Lucia, by one Starlight Charters S.A. of Geneva. This assertion is impossible. The evidence showed Starlight Charter S.A. to be nothing more than a shell company that never provided any goods or services. The first page of the 1985 Offering Memoranda states, with the above-mentioned false assertions underlined:

> The OCG Corporation is an established company with assets in the marine industry. In cooperation with Starlight Charters S. A. of Geneva, OCG has previously established charter bases in Monaco and St. Lucia.
>
> Sail and motor yachts are becoming increasingly popular both by the people who look at it for a vacation and for the people who are only interested in it as a tax investment. Yachts offer generous depreciation possibilities and also a possibility for good return on invested capital.
>
> Although boats are allowed high capital depreciation, the fact remains that they depreciate very little in value, and more than likely will appreciate. The major areas for charter operations are in the Caribbean, the Mediterranean and Tahiti in the Pacific. OCG Corporation has made arrangements with major brokers both for providing management and necessary bookings.
>
> [Emphasis added]

Financing and Feasibility Study

[135] The false representation that business start up costs totalling $953,200 was incurred and deductible in the first year of operation is repeated in the 1985 Offering Memoranda. These costs are again described as mostly relating to a feasibility study and arrangements for financing however, the evidence shows that these claims are false because there was no financing arranged or delivered, and no feasibility study was commissioned until the end of 1985. In addition, the feasibility study was delivered in 1986 and only at a cost of $4,000.

Construction Financing, Construction Brokerage Fees, Investor Loans, Letter of Credit

[136] All of the representations about financing were false. There was no construction financing, no construction brokerage fees, and therefore no construction financing interest that could be owed. No loans were made to investors, and no funds were advanced for the construction of the yacht. The amount of $212,200 listed in the Offering Memoranda as a deductible expense is for arranging a letter of credit that did not exist. The only letter of credit was one that was entirely fraudulent, purportedly arranged with Neptune Marine Resource S.A., a company set-up by Mr. Bellfield that was part of the elaborate fraud perpetrated. The accounting firm Laventhol & Horwath based part of its tax opinion on the false representations that there were loans available and that OCGC had arranged for an operating line of credit to fund operations.

Cutlery, Linen, China, and Utensils

[137] Both the false representations that $15,000 in cutlery, linen, china, and utensils and $60,000 in marketing and advertising expenses had been incurred are repeated in the 1985 Offering Memoranda. The reasons supporting the conclusion that these statements are false are explained in detail above, but to again summarize briefly, Ester Palmer was involved in both the first purchases of cutlery etc. and the first yacht charter marketing and advertising efforts, and she did not begin working with Starlight Charters until January 1986.

Yacht Acquisition

[138] The 1985 Offering Memoranda also contains numerous representations that the 1985 Limited Partnerships would acquire their yachts in 1985, when in fact, construction of the yachts had not even begun and such an acquisition was impossible. This material misrepresentation is highly significant as the acquisition of a yacht was at the core of the securities described in the Offering Memoranda.

[139] These misrepresentations were there to induce investors to become part of a fraudulent scheme in order to provide a continuous flow of funds to maintain the illusion of a legitimate enterprise, all unbeknownst to the investors.

(iii) The 1986 Offering Memoranda: Multiple False Representations, Again

[140] The 1986 Offering Memoranda continued the tradition with a parade of false representations. These are summarized following, using the S/Y Close Encounters

LP as an example. These false representations demonstrate not only that OCGC perpetrated a fraud against the 1986 investors from the beginning by inducing them to invest, but also that the purported grandfathering of the 1986 Limited Partnerships using the vehicle of OCG Enterprises was simply another false representation.

Financing

[141] The S/Y Close Encounters LP Offering Memorandum states that OCGC provided loans to OCG Enterprises to fund the original purchase of all 25 units of the S/Y Close Encounters LP on January 2, 1986, but there is no evidence that such loans were actually provided. The Offering Memorandum also states that OCG Enterprises contributed the original Limited Partnership capital of $2.9 million to the S/Y Close Encounters LP, but there is no evidence that these amounts were actually contributed by OCG Enterprises.

OCG Enterprises' Capital

[142] The Offering Memorandum represented that $1.45 million of the capital purportedly provided by OCG Enterprises to capitalize the yacht "has been used by the Limited Partnership to acquire the Yacht and related services", when in reality the S/Y Close Encounters LP's yacht had not yet been purchased and was not in the process of being built.

Line of Credit

[143] The Offering Memorandum states that a line of credit was established and was available on an annual basis until January 1, 1992, to make loans to the S/Y Close Encounters LP when it faced cash flow deficiencies. It states that the S/Y Close Encounters LP paid a one-time standby fee to OCGC for this arrangement, but in reality, there is no evidence that a line of credit for those purposes was ever established or that OCGC had the means to establish such a line of credit.

Gourmet Dining and Services

[144] The S/Y Close Encounters LP's Offering Memorandum claims that "gourmet dining and attentive service are currently offered" as part of the yacht

chartering business on a "60-foot sailing catamaran or an 80-foot sailing monohull", when in fact, actual charters offered and yachts available were extremely limited in 1986, if available at all. Further comments regarding the lack of yachts and the paucity of actual charters are explored in the sections entitled "Building and Purchasing of Boats" and "Starlight Charter".

Feasibility Study

[145] The Offering Memorandum claimed that OCGC "continuously updates and amends the feasibility study" when there is no evidence that feasibility studies were "continuously" updated. There were only two feasibility studies put into evidence, the first one in 1986, and an update provided in 1988.

Cutlery, Linen, China and Utensils?

[146] The Offering Memorandum also contains the representation, again, that cutlery, linen, china, and utensil expenses had been incurred, this time for the total amount of $65,000. While Ester Palmer testified that she made the first purchase of such items in 1986, they did not go to the S/Y Close Encounters LP; it did not even have a yacht yet and would have no use for such items at that time.

Bond Guarantee

[147] The assertion that OCGC arranged for a completion guarantee for the S/Y Close Encounters LP, and paid $29,000 for this bond guaranteeing that the yacht would be constructed at a fixed price is also false. The statement in the Offering Memorandum that OCGC incurred $72,500 in brokerage fee for construction financing arranged is false. No construction financing was ever arranged, and there was no $150,000 in deductible expenses for money advanced to OCGC for arranged financing for purchasers of the secondary offering.

Inspection and Monitoring Services; and Service, Decorating and Outfitting Equipment

[148] The Offering Memorandum represents that $60,000 was a deductible expense for inspecting the "Yacht under construction" to ensure it was built to the required specifications. The Offering Memorandum also asserts that the S/Y Close Encounters LP incurred $69,000 in deductible expense for "service, decorating and

outfitting equipment". No S/Y Close Encounters yacht was ever built and none was under construction at that time, so both these representations are false.

Starlight Charter S.A. and Neptune Marine

[149] The 1986 Offering Memorandum also contains numerous references to Starlight Charters S.A. (the "Starlight S.A.") and Neptune Marine Resource S.A. (the "Neptune"). While Starlight S.A. is mentioned in previous Offering Memoranda, the 1986 misrepresentations regarding Starlight S.A. and Neptune are numerous and substantial.

[150] These two entities were established by Mr. Bellfield in Switzerland, where corporate law at the time prevented the release of the identities of the individuals behind corporate structures.[13] Mr. Bellfield used these entities to make numerous misrepresentations to the effect that financing was available from Neptune and that Starlight S.A. contracted to provide yacht chartering goods and services. One of the main reasons these entities were employed in the scheme seems to have been as part of a late-game strategy to avoid an originally unanticipated large corporate tax debt.

[151] For the purpose of brevity, an excerpt from the Respondent's Final Submissions below summarizes some of the most significant misrepresentations regarding Starlight S.A. and Neptune that are found in the S/Y Close Encounters LP Offering Memorandum:

> 112. The false representations of fact in the S/Y Close Encounters Limited Partnership and other 1986 limited partnerships included:
>
> a. that certain of the management services under the Management Agreement and the Acquisition Agreement had been subcontracted by OCG Corporation to Starlight Charters S.A. ("Starlight"), which will be responsible for performance thereof. The services were to include but not be limited to construction consultation and inspection, arranging construction and operating financing, guaranteeing completion of construction, provision of a feasibility study, provision of staff, crew and supplies, arranging mooring facilities,

[13] See page 13 of third amended reply, admitted on page 1 of Appellant's Answer.

maintenance of the yacht, carrying out marketing programs and operating the yacht chartering business (p.14)…

b. that most of the initial services had been subcontracted to Starlight Charters S.A. which would be responsible for the performance thereof (p.26).

c. that ongoing services had been subcontracted to Starlight Charters S.A. which would be responsible for the performance thereof with the right of OCGC to retain a 10% administration fee on all amounts invoiced to the limited partnership (p.27).

d. that Starlight Charters S.A. had been engaged to manage the business of the limited partnership by OCGC. (p.33)

e. that Neptune Marine Resource S.A. had provided substantial financial assistance to OCGC in the purchase of the yacht and the Initial Services (p. 33).

f. that a material contract relating to the yacht which have been entered into and remain in full force and effect included a management agreement between OCGC and Starlight Charters S.A. dated January 2, 1986 (p. 35).

…

…that the partnership had incurred deductible expenses of $300,000 in respect to a letter of credit standby fee (p. 25) OCGC never did obtain an operating line of credit. Minchella agreed that the only letter of credit was the one with Neptune. The representation that the partnership had incurred a deductible expense respecting a letter of credit was false.

…

…that OCGC had arranged a completion bond (p.26). Minchella recalled that Forsey told Bellfield that if an agreement called for a performance bond and one didn't exist, that they should make one. The Neptune Marine Resources S.A. Performance Bond was manufactured in a cut and paste session in the offices of OCGC and printed in Toronto by Sibilia & Associates. This representation was false.

…

… that OCGC had arranged a line of credit on behalf of the Limited Partnership (p.27) OCGC never did obtain an operating line of credit. Minchella agreed that the only letter of credit was the Neptune Marine Resources S.A. letter of credit printed by Sibilia and Associates in Toronto. This representation was false.

…

that Starlight Charters S.A. would arrange mooring spaces for the yacht in the Caribbean and Mediterranean, international promotion and marketing and advertising, all for a fixed fee to be paid by OCGC for which OCGC would be entitled to a 10% administration charge (p. 28). Starlight Charters S.A. provided no goods or services to any limited partnership. This representation was false.[14]

[14] Respondent's Final Submissions at 43-49.

[Footnotes omitted]

[152] Despite the numerous material representations to the contrary in the 1986 Offering Memoranda, no funds were actually available from Neptune, nor were any funds available to Starlight S.A. Moreover, Starlight S.A. never actually provided any yacht chartering goods and services. In fact, the evidence shows that many of the services listed above were never provided at all to the Limited Partnerships, by any party.

[153] I again emphasize that these misrepresentations induced investors to become part of the fraudulent scheme that provided a source of cash for Mr. Bellfield. As time progressed, the misrepresentations were repeated and expanded. It is evident that it was necessary to make assertions that would make the fraudulent scheme appear legitimate as the fraud continued to grow.

b) Misrepresentations to Professionals

[154] Much like most other parties involved with Mr. Bellfield and OCGC, accounting and legal professionals were repeatedly provided with false representations. They based their legal or accounting opinions and/or promotional efforts on these false representations. While some of these misrepresentations were addressed above in reference to the tax opinions in the Offering Memoranda, further examples of misrepresentations to professionals are following. Again, the representations were so plentiful that those listed below are only key examples provided for illustrative purposes.

(i) False Closing Documents

[155] A number of false documents and misrepresentations were made at closing to the legal professionals representing investors. These professionals examined and relied upon OCGC's representations through certificates, signed obligations, solemn declarations, and/or affidavits, to support the legitimacy of the investment opportunity and, in representing their clients' interests, to ascertain that the yachts were indeed under construction and third party financing had been obtained.

False Certificates

[156] The misrepresentations made by Mr. Bellfield and OCGC in and around closing to the 1985 investors and the professionals representing some of those investors were egregious, with multiple false certificates signed and affidavits sworn.

[157] Mr. Bellfield signed certificates in the first weeks of December 1985 patently misrepresenting that 13 yachts were under construction and to be delivered by December 31, 1985. The certificates asserted that five 80-foot yachts were under contract for purchase from the yacht builder Dynamique and eight 60-foot catamarans were under contract for purchase from Chantiers Yachting France, and that these yachts were allocated to Limited Partnerships. In fact, none of the 13 yachts were under construction at that time. The contracts to purchase yachts from the yacht builders did not exist as described, and thus, it was impossible for the yachts to have been delivered by December 31, 1985.

[158] The evidence shows that these false certificates and other misrepresentations made by OCGC were relied upon by lawyers representing some of the investors and were considered key documents to complete closing. This included the Appellant Dr. Leckie Morel's S/Y Midnight Kiss LP. As summarized in the Respondent's Final Submissions:

> 142. …In the reporting letter, Kelsey, Melnik & Hendler advised the subscribers that they had examined the Offering Memorandum, Certificates of OCGC, and a contract and telexes between OCGC and Dynamique Yachts providing for the purchase by OCGC of an 80' yacht from the company. The firm also advised that it had relied on certain matters of fact, certificates of the general partner and the opinion of the vendor's solicitor, Leve & Zeiler. In the letter, the Kelsey Melnik & Hendler further advised the subscribers that OCGC had entered into an agreement for the purchase of a completed yacht prior to May 23, 1985 and that one of the yachts ordered from Dynamique Yachts was for the partnership and would be delivered prior to December 31, 1985.
>
> …
>
> 150. In their reporting letters for the 1985 partnerships including the Midnight Kiss, Kelsey, Melnik & Hendler reported that they had, among other things, examined the Offering Memorandum, the Certificate of OCG and a contract and telexes between OCG and Chantiers Yachting France providing for the purchase by OCG of an 80-foot yacht from the company. They also reported that OCG had entered into the agreement for the purchase of the completed yacht and the acquisition of certain assets prior to May 23, 1985. They reported that the yacht was presently under construction and would be delivered prior to December 31, 1985.[15]

[15] Respondent's Final Submissions at 59-60.

[Footnote omitted, emphasis added]

[159] Mr. Minchella signed a similar certificate for the Human Desire Limited Partnership on March 9, 1986, falsely asserting that 13 yachts were under construction and one yacht would be delivered (or, if the delivery dates were true facts, one yacht would already have been delivered) to the Human Desire Limited Partnership by December 31, 1985.

Obligations of OCGC

[160] Both Mr. Bellfield and Mr. Minchella signed on behalf of OCGC, a number of "Obligations of OCGC". In these documents, OCGC falsely represented that as consideration for the investors' subscription in the Limited Partnerships, OCGC had contracted for an 80-foot yacht to be built and delivered by December 31, 1985, that OCGC would sell to the Limited Partnership as outlined in the Agreements of Purchase and Sale. The obligation that OCGC had obtained financing from a third party in order to cover the cost of purchasing the yacht was also misrepresented.

[161] David Franklin testified that he relied on these obligations, and that these same false representations were relied upon by others during closing, including the Appellant Dr. Leckie Morel. Mr. Franklin's evidence on this matter is accurately summarized in the following excerpt from the Respondent's Final Submissions:

> 147. Franklin confirmed that the Obligation of OCGC was given in consideration of the closing of the transaction. He understood the other good and valuable consideration was the giving of the promissory notes by the investors. He said he relied upon the statements in closing and he believed them to be true. Respecting the representation of third party financing in the Obligation of OCGC, Franklin said it was important since he did not want to be called upon to pay cash for the purchase of the yacht. Franklin agreed that the Obligation was being provided during the course of the closing, that it confirmed he was going to get a yacht on a particular date, and that there was third party financing to carry out the commitment. He agreed the same representations had been made to Dr. Leckie, the appellant.[16]

[Footnotes omitted, emphasis added]

Solemn Declarations

[162] David Franklin, in his capacity as a lawyer, took solemn declarations from Mr. Bellfield on December 16, 1985 that the above-described OCGC certificates

[16] Respondent's Final Submissions at 61-62.

were true, and that contracts with Dynamique and Chantiers Yachts France existed and would provide for a total of 13 yachts to be delivered on December 31, 1985. Again, this assertion was impossible and the evidence shows that no such contracts existed as described.

Affidavits

[163] Mr. Bellfield also swore affidavits in November 1985 that contained a number of impossible and false statements, including the assertion that there were no agents or sub-agents making commission on the sales of Limited Partnership units. The evidence shows that these statements were manifestly untrue, with Mr. Franklin already earning commissions and using sub-agents at the time the affidavits were sworn. The affidavit also contained an incomprehensible assertion regarding the source of the yacht for the S/Y Great Gatsby Limited Partnership. As correctly summarized by the Respondent in his Final Submissions:

> 151. In an affidavit sworn in November of 1985, Bellfield represented that OCGC had contracted to purchase yachts from Chantiers Yachting (France) prior to May 21, 1985 and indicated 3 of the 4 yachts were for the Bergman, the Midnight Kiss and the Great Gatsby partnerships. Franklin said he could not explain how it was that Bellfield would be saying in November of 1985 that he had purchased the Great Gatsby from Chantiers Yachting and yet by December 1985 was negotiating for the Great Gatsby as a refurbished yacht. In a further November 1985 affidavits, Bellfield allocated the yachts said to be the subject of contracts with Chantiers Yachting (France) to entirely different partnerships. In fact, Chantiers Yachting (France) had been in receivership since July of 1985. While Franklin could identify Bellfield's signature on the affidavits, he could offer no explanation for the inherently contradictory statements in the affidavits and could not reconcile the statements in the three affidavits.[17]

False Hull Registration Numbers

[164] In another egregious example of his pattern of manufacturing false documents to sustain his fraudulent scheme, Mr. Bellfield arranged to have false hull registration numbers created when he was pressed to provide proof that yachts were indeed under construction. Since hull registration numbers are only available after about a third of the yacht is built and a hull has been constructed, the provision of a hull registration numbers also represents that construction had progressed sufficiently enough to ensure that a yacht was deliverable by a specified date.

[17] Respondent's Final Submissions at 63-64.

[165] John Gartenburg appears to have provided the impetus that led Mr. Bellfield to create false hull registration numbers. Mr. Gartenburg is the lawyer who represented Donald Ubell, a potential Limited Partnership investor in the S/Y Main Event Limited Partnership. Mr. Gartenburg testified the he believed that his due diligence responsibilities to his client required that he obtain the hull registration number that the Agreements of Purchase and Sale between OCGC and the S/Y Main Event Limited Partnership stated would be provided by December 31, 1985. This was to ensure that the 60-foot catamaran promised to the S/Y Main Event was actually being constructed as claimed. Mr. Gartenburg described this as fundamental to the investment. It should be noted that in this regard, Mr. Gartenburg appears to have been the legal professional who was most mindful of his professional obligations in representing potential investors.

[166] A number of witnesses provided evidence in support of the conclusion that the hull registration number provided to Mr. Gartenburg was false. An excerpt from the Respondent's Final Submissions correctly summarizes a portion of this evidence:

> 162. On or about April 30, 1986, Minchella wrote Gartenburg a letter enclosing a copy of the hull registration numbers for Chantiers Yachting France, with only the number for the S/Y Main Event revealed "for [his] use only." When testifying, LeGlatin was shown Minchella's letter to Gartenburg dated April 30, 1986 with an attached letter from Chantiers Yachting France dated April 24, 1985 providing a hull registration number for the Main Event 60' catamaran. LeGlatin testified that in April 1985 Chantiers Yachting France had not built a 60' catamaran, had not laid the hull for one and did not have the mould for a 60' catamaran.
>
> 163. Minchella testified in chief that Zeiler had asked him to send a hull registration number for the Main Event to Gartenburg. Minchella did so, by attaching the April 24, 1985 letter from Chantiers Yachting France showing one hull number for the Main Event to his own letter to Gartenburg of April 30, 1986.
>
> 164. Minchella testified in cross-examination that he now knows that the hull registration number for the Main Event is a fabrication of Einar Bellfield's. Minchella now knows that he sent Gartenburg a false and backdated document.[18]

[167] Ultimately, Mr. Gartenburg advised his client to pull out of the transaction and demanded a return of funds because he was not satisfied with the (false) hull registration number provided after significant delays, and felt that the lack of such a number vitiated the entire transaction. Mr. Ubell went on to pursue a return of his funds by legal action.

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[18] Respondent's Final Submissions at 66-67.

[168] As will be discussed later regarding the Limited Partnerships' financial statements, the fraudulent representation of a false hull number to Mr. Gartenburg was not the only occasion that false hull numbers were used to misrepresent to professionals that yachts were under construction and sufficiently completed to be ready at the date specified.

c) Misrepresentations in OCGC Materials: The "Fleet of Yachts" and the "Gourmet Commissary"

(i) Misrepresentations about the "Fleet of Yachts" Available

[169] OCGC's publicity materials also contained misrepresentations about the state of the yacht chartering activities and the number of yachts that made up the Fantaseas "fleet". Below are a few representative examples.

[170] Frequent misrepresentations were made by OCGC and Mr. Bellfield about the number of yachts that were available and performing charters. The Respondent provides a selection of such representations that were made during 1986 and 1987, excerpted in part below:

> Throughout 1986 and 1987 OCGC's outward display was of a fleet of yachts:
>
> a. Business Plan Presented to St. Lucia National Development Corporation, August 1, 1986: "Starlight Charters Ltd. consists of the most exclusive fleet of charter yachts in the world".
>
> …
>
> d. Investor Newsletter, Dec. 5, 1986: "The fleet is comprised of the largest and most supremely comfortable charter maxi yachts in the world, unparalleled in design, comfort and luxury".
>
> [footnotes omitted]

[171] Despite the representations above, during the 1986 and 1987 years, there was no "fleet" of yachts of eighty feet or more. At that time, there were only two boats. First, the 50-foot S/Y First Impressions that OCGC took title to in November 1985 and arrived in St. Lucia in March 1986, but was not suitable to the Fantaseas concept. Second, the 80-foot S/Y Garbo that also did not conform to the Fantaseas brand, and was only briefly available for charters as of April 1987. Further examples of the

misrepresentation regarding chartering activities and yachts available can be found in the section below detailing examples of the misrepresentations regarding Starlight Charter's activities.

(ii) Misrepresentations about the Commissary

[172] Fabu D'Or was a company 100% owned by Mr. Bellfield. It was supposed to be a commissary whose purported purpose was to provide high quality food to Starlight cruises as well as to other potential customers. One document describing Fabu D'Or stated: "Fabu D'Or produces and retails food" and "every course is prepared here from start to fabulous finish". Despite these representations made in the present tense, Fabu D'Or was not in fact producing and retailing food at the time. The marketing plan for Fabu D'Or similarly contained misrepresentations, including that a kitchen facility was complete and in use for testing food, despite it not in fact being complete.

[173] An OCGC brochure also contained misrepresentations about Fabu D'Or, stating that the commissary's "sumptuous delicacies temp guests" and that "every morsel is prepared at the Fabu D'Or commissary". This was impossible because evidence showed that the commissary facility was not operational at that time.

[174] The financial statements for Fabu D'Or ending October 31, 1987, help illustrate the level of misrepresentation about Fabu D'Or, and Mr. Bellfield's incessant pattern of deceit. They state that there was $68,362 in equipment and $82,298 in leasehold improvements, but a letter to investors claimed that there was $500,000 in equipment. Evidence at the trial shows that up until October 1986 only $250 was spent on actual food for the commissary. Mary Crocco testified to the effect that this was a misrepresentation. Ms. Crocco was a sister-in-law to Mr. Bellfield and believed everything that Mr. Bellfield said. In her testimony, she gave the obvious answers to obvious questions, but she appeared confused about several things and could not always recall or explain certain evidence.

[175] It is also important to note that Fabu D'Or was not held out as being created solely for the purposes of providing commissary services to the yacht chartering Limited Partnerships. Its vision was much wider in scope, according to its documents. As accurately summarized by the Respondent in his Final Submissions at page 176:

> 548. The whole concept for Fabu D'Or was not only to provide food for the cruises, but also to provide food to other charters, to airlines and stores like Marks and Spencer and Loblaws. The concept also included a bakery and a delicatessen restaurant that would also retail foods at the same location. These concepts were discussed but never got running.

[176] Many Fabu D'Or "start-up" expenses are included in the list of expenses that the Appellants claim make up the $13 to $14 million, despite the intention that Fabu D'Or would have wider, non-yacht chartering purposes. The Respondent appropriately summarized a portion of Mr. Minchella's testimony on Fabu D'Or's multiple purposes at page 177 of his Final Submissions:

> 550. Minchella said the limited partners would only have known as much about the Commissary as his 1987 document "The Charter Market and Competition" told them. Minchella doesn't know if the limited partners would have understood that their money was going towards building a facility to be owned by OCGC which was to include a restaurant and intended to supply baked products to chain stores like Loblaws.

d) Financial Statements for Limited Partnerships

[177] The yacht chartering limited partnerships' financial statements were filled with false information regarding expenses incurred, revenues earned, and when or if the promised asset of a yacht had been acquired. These financial statements were represented to the investors as providing the true state of the finances of the Limited Partnerships that they invested in. The investors, in turn, entirely relied on the truthfulness of the financial statements as the basis for their losses claimed in their yearly income tax returns when they were provided annually with a Schedule of Losses per unit.

[178] The sections following describe examples of key misrepresentations in the financial statements of each of the Limited Partnership types. Although the Appellants' yacht chartering limited partnerships are used as illustrative examples, the misrepresentations are substantively the same across all the Limited Partnership financial statements of the same type.

(i)Financial Statements for the Type 1 Limited Partnerships

[179] The S/Y Garbo LP financial statements for the years 1984 to 1989 inclusively were created by the accounting firm Hattin, Moses, Sugarman & Company as part of a review engagement. No audits were performed.

[180] Hattin, Moses, Sugarman & Company played several different roles with both the S/Y Garbo LP and the S/Y Gable LP. The firm helped design the tax aspects of the investment, marketed and sold the investment opportunity to some of its clients and received commissions for doing so, and prepared the Limited Partnerships' financial statements. Some members of the firm were also investors, with Mr. Garber (the Appellant), who worked with the firm, co-owning the unit in the S/Y Garbo LP with fellow firm members Mr. Mitchell, and Mr. Sugarman.

[181] The evidence shows that the S/Y Garbo LP financial statements and the S/Y Gable LP financial statements were replete with false amounts for expenses and revenues that had no basis in reality. Key examples of the false statements, found throughout the balance sheets, income statements, and notes, are set out following.

[182] There are numerous false statements regarding the S/Y Garbo and the S/Y Gable including a yacht and accessories valued at $1,095,236 listed in the balance sheet ending December 31, 1984 for both Limited Partnerships. Depreciation is taken against the assets on both balance sheets even though the assets did not exist and were not under construction at that time.

[183] The 1985 to 1989 financial statements also falsely list the S/Y Garbo LP and the S/Y Gable LP as having yachts during those financial years and record depreciation being taken on the asset.

[184] The evidence shows that possession of the S/Y Garbo was only acquired by OCGC in April 1986, before being sold to finance Maxi-Yacht International S.A.R.L. in February 1988. There is no evidence that the S/Y Garbo LP itself ever acquired title to the yacht. While OCGC was entitled to acquire title on behalf of the partnership, such acts had to be done for the benefit of the Limited Partnership. Sale of the yacht could only be done by special resolution of the Limited Partners, as outlined in the Limited Partnership Agreement. There is no trace of a sale or mortgage of the yacht on the financial statements of the S/Y Garbo LP. In an example of the pervasive and material nature of the fraud perpetrated against the

investors, the S/Y Garbo is simply listed continuously as an asset through to 1989 with depreciation taken.

[185] The misrepresentations regarding the S/Y Gable are similar. Despite being listed on the balance sheet in the year ending December 31, 1984, and as an asset in the years from 1985 to 1989 inclusively, the S/Y Gable was still under construction in August 1988. The yacht was only delivered to OCGC in October 1988 and christened in Monaco in November 1988. Shortly after its christening, the S/Y Gable yacht was sold to a French entity, Starlight S.A.M. Just like the S/Y Garbo LP, the sale is not reflected anywhere on the S/Y Gable LP financial statements, which highlights the fraudulent misrepresentation that the yacht was owned by the S/Y Gable LP beginning in 1984 through 1989.

[186] Fictional charter revenue amounts also appear on income statements for both the S/Y Garbo LP and the S/Y Gable LP beginning in the 1986, 1987, and 1988 financial years. The evidence shows that these amounts are not based in reality and appear to have been made up.

[187] For the 1986 year, it was impossible that there was any charter revenue earned by the S/Y Garbo LP. The yacht was acquired in April 1986 and was not available for charter until April 1987 because it was undergoing intensive repairs in a dry-dock. For the 1987 year, the evidence shows that it was not possible for the S/Y Garbo LP to have obtained charter revenues as high as the $123,000 listed, considering that the S/Y Garbo was in a dry-dock until April 1987. Any actual charters conducted in the remainder of the year earned minimal revenues. The charter revenues recorded as earned by the Limited Partnership on the 1988 statement of income are also false, as the S/Y Garbo was sold to finance Maxi-Yacht International S.A.R.L. in February 1988.

[188] Revenues listed as earned from chartering the S/Y Gable in 1986, 1987, and 1988 years are similarly unsubstantiated. The S/Y Gable was only finished and (very briefly) acquired by OCGC in 1988 and was then almost immediately sold to the related French entity.

[189] The December 31, 1984 year-end Statement of Income for the S/Y Garbo LP is full of additional false amounts, including expense amounts for a feasibility study,

marketing and advertising, and linen, cutlery, china, and utensils, none of which were acquired or commissioned before 1986.

[190] While the Appellant Mr. Garber is still claiming the expenses listed in the previous paragraphs, at mid-trial he dropped his claim for the following expenses that were listed on the 1984 Statement of Income: construction financing brokerage fees, construction financing interest, brokerage fees, letter of credit standby fees, and office expenses. The evidence at trial, including Mr. Minchella's testimony, shows that any reflections of these amounts in the financial statements are fictitious. For example, regarding the office expenses listed in the 1984 year, almost all OCGC work occurred in Mr. Bellfield's den, and no other space was used until December 1984. Rent, if any, was at such a small costs; rendering the amounts listed for office expenses highly disproportionate. And in considering that the amount is surrounded by other false amounts, it is highly unlikely to have a factual basis.

[191] The following comments are not meant as a consideration of expenses that the Appellant no longer puts before the Court; rather they are only considered as part of an effort to evaluate the veracity of the financial statements as a document. The full picture demonstrates the inherent dishonesty of the financial statements for the Type 1 Limited Partnerships. Again, it was upon these financial statements that the investors relied on in representing to the CRA that they were entitled to claim losses.

(ii) Financial Statements for the Type 2 Limited Partnerships

[192] The financial statements from the Type 2 Limited Partnerships are similarly false. Here, the S/Y Midnight Kiss LP is used as an example, but the misrepresentations are substantively the same for all Type 2 Limited Partnerships.

[193] Initially the financial statements for several of the Type 2 Limited Partnerships were to be prepared by the accounting firm Laventhol & Horwarth, but ultimately they were prepared by Orenstein & Partners. The mandate of both of these accounting firms was limited to undertaking a review. No audit was conducted.

False Hull Registration Numbers Provided to Financial Statement Preparers

[194] From January to April 1986, Harvey Taraday, a junior accountant at Laventhol & Horwarth was doing the field work in preparing the financial

statements. This witness appeared reliable, speaking with respect to factual matters only, and his evidence was limited strictly to the brief period of time in which he acted on the file. As part of the review he was conducting, Mr. Taraday requested substantiation that the yachts were under construction through the provision of hull registration numbers. He understood that these numbers could only be obtained once the hull of a yacht was built. Mr. Franklin confirmed in his testimony that he too was looking for hull registration numbers in order to confirm whether capital cost allowance could be claimed.

[195] Mr. Taraday also testified that OCGC asked Laventhol & Horwath to use the S/Y Garbo LP's financial statements as a model that, contained misrepresentation about the existence of a yacht asset and depreciation claims.

[196] Mr. Taraday testified that Mr. Minchella provided a list of hull registration numbers for seven Type 2 Limited Partnerships: the S/Y Main Event, the S/Y Bogart, the S/Y Bergman, the S/Y Change of Seasons, the S/Y Casablanca, the S/Y Autumn Sonata, and the S/Y Midnight Kiss. These same hull registration numbers appeared in the letter forwarded by Mr. Minchella to a partner at Laventhol & Horwath. Mr. Minchella introduced the numbers as relating to yachts "which were built".[19]

[197] A letter was also sent by Mr. Minchella to Mr. Franklin on April 7, 1986 that listed the hull registration numbers of "yachts which were built by Chantiers Yachting France" and "yachts which were built by Dynamique". This list contained 18 purported Hull Registration Numbers. Mr. Minchella testified that he included three Limited Partnerships in that list that were never actually subscribed to by any investors.[20]

[198] During his testimony, Mr. Minchella conceded that he now knows the hull registration numbers were false. The statements that any yachts were built by Chantier Yachting France and Dynamique were not true, and the yachts listed as having hull registration numbers in the letters to Laventhol & Horwath and to Mr. Franklin were in fact never under construction. He claimed, however, that he was unaware at the time that the numbers were false, and that while he put together the lists and forwarded them as per Mr. Bellfield's instructions, it must have been Mr.

[19] Exhibit A-5, Tab 11 or Exhibit R-15, Tab 82.
[20] Exhibit A-5, Tab 11 or Exhibit R-15, Tab 82.

Bellfield himself who provided the false numbers. Mr. Franklin also testified that he later found out that the hull registration numbers provided were false.

[199] The evidence indeed shows that none of the yachts for which hull registration numbers were provided were ever constructed. Chantiers Yachting France went into receivership in July 1985 and never built any yachts for OCGC. The statement in a letter to Mr. Franklin on April 7, 1986 that Hull Registration Numbers existed for 13 yachts "which were built by Chantier Yachting France" is therefore impossible and entirely false. Dynamique only built two yachts that were ultimately acquired by OCGC. No other 80-foot yachts were acquired by OCGC from Dynamique for the Limited Partnerships. The statement in Mr. Minchella's letter to Mr. Franklin that the S/Y Gable, the S/Y Queen of Hearts, the S/Y High Sierra, and the S/Y Change of Seasons were built by Dynamique is therefore also false. Part of the evidence on this subject is accurately summarized by the Respondent at page 81 of their Final Submissions:

> 219. When LeGlatin first met with the Jeanneaus at Dynamique in January 1985 they were finishing the mould for the construction of the new 80' boat. By July 1985 the hull would have been completed. Between February 1985 and April 1986 LeGlatin made frequent trips to the Dynamique yard in La Rochelle. He never saw more than one Dynamique 80. Naval architect, Michel Joubert, the designer of the Dynamique 80 said that Dynamique had commenced building the hull for the first Dynamique 80 by February 1985 and he was advised in July 1986 that the first Dynamique 80 had been sold and that he was to receive a royalty payment. Construction on a second Dynamique 80 commenced sometime in 1986 and that boat was sold by December 1986. Joubert says that it is impossible that five Dynamique 80' boats could have been built by April 1986.
>
> 220. When LeGlatin and Bellfield visited Chantiers Yachting France on February 20, 1985, before its bankruptcy, LeGlatin saw that all that Chantiers Yachting France had in its yard were moulds for smaller boats and the mould for the Lacoste 42. At that point Chantiers could only build one boat at a time and had no experience in building larger boats.
>
> [Footnotes omitted]

[200] An expert opinion prepared for the Respondent by Eric Ogden, a naval architect and yacht surveyor, further substantiates the falseness of the hull registration numbers provided to Laventhol & Horwarth in the course of their mandate to create financial statements for the 1985 Limited Partnerships.[21] Mr. Ogden's opinion also provides further evidence that the hull registration number given to Mr. Gartenburg at closing in his capacity as a lawyer representing Donald Ubell, and the hull

[21] Exhibit R-144, Expert witness report prepared for the Department of Justice, Canada by Eric A. Ogden.

registration numbers in the lengthy list provided to Mr. Franklin were false. Mr. Ogden concluded that none of the hull registration numbers conformed to the style used by either French yacht building company, and more generally, was not consistent with the official format of French hull registration numbers.

Misrepresentations in the Financial Statements

[201] After the mandate with Laventhol & Horwath was terminated by OCGC, the accounting firm Orenstein & Partners went on to do eight of the Financial Statements for the Type 2 Limited Partnerships. This was but one of many different capacities that Peter Browning and his firm acted in for the Limited Partnerships and OCGC. Mr. Browning's accounting firm had initially provided tax opinions on the reasonableness of the expenses to be claimed by the Limited Partnerships as described in the Offering Memoranda. His firm then prepared financial statements for some of the Limited Partnerships. The firm also became a sales agent and active promoter for OCGC, as well an advocate on behalf of OCGC and the Limited Partnership to the CRA. Lastly, the firm, at a later date, conducted an audit of OCGC's financing.

[202] Mr. Browning is an avid sailor, a chartered accountant by training, and most recently, an investment banker. In his testimony, Mr. Browning was protective of the yacht chartering investment scheme, which he described as a "tax gimmick". He consistently chose his words very carefully and had a tendency to only accept the obvious when it was presented to him. He frequently put forth other explanations or alternative descriptions in order to support his individual theory of the case.

[203] Mr. Browning testified that in preparing the financial statements for the eight Type 2 Limited Partnerships, including the S/Y Midnight Kiss LP, only a review was conducted, with no verification or substantiation of the existence of assets or the truthfulness of claimed transactions. The firm fully relied on the management's representations.

[204] Mr. Browning testified that he prepared the financial statements for the 1985 taxation year with the understanding that capital cost allowance was deductible because a yacht was delivered to the Limited Partnerships by December 31, 1985. He came to this understanding based on the provision by OCGC of its invoices for the yacht to the Limited Partnerships and by the hull registration numbers provided. None of the Type 2 Limited Partnerships that Mr. Browning prepared financial

statements for even had yachts under construction at that time, including the S/Y Midnight Kiss. The capital cost allowance claims were false. In the S/Y Midnight Kiss LP's 1986 financial statements prepared by another member of Mr. Browning's firm, no capital cost allowance was claimed.

[205] Mr. Browning also testified that he prepared the financial statements for the 1985 taxation year in part by relying on invoices provided by OCGC. Mr. Minchella testified that these invoices were prepared for both the Type 1 and Type 2 Limited Partnerships in March 1986, obviously in preparation for creating the financial Statements. Mr. Minchella testified that he relied on the Offering Memoranda to source the numbers listed in the invoices, and they were not in any way related to whether the services or goods were actually provided by OCGC to the Limited Partnerships.

[206] Much like the financial statements for the Type 1 Limited Partnerships, the S/Y Midnight Kiss and other Type 2 Limited Partnerships' financial statements were filled with falsehoods. The Respondent accurately summarized the broad nature of the misrepresentations in his Final Submissions:

> 241. The balance sheet and related notes to the financial statements of the Midnight Kiss for the year ended December 31, 1985 are false.
>
> 242. The balance sheet for the year ended December 31, 1985 for the S/Y Midnight Kiss Limited Partnership describes Fixed Assets totalling $1,284,800. Notes 1 and 2 to the financial statement describe the depreciation policy and the fact of depreciation being taken against the asset. The Fixed Assets are described in Note 3 as a Yacht and cutlery, linen, china and utensils. Note 3 states that "No depreciation was claimed as the assets were not put into operation during this period."
>
> 243. There was no Midnight Kiss yacht in 1985 or ever. The balance sheet of the Midnight Kiss for the year ended December 31, 1985 was false.
>
> 244. The statement of income for the S/Y Midnight Kiss Limited Partnership for year ended December 31, 1985 discloses expenses of a $100,000 for a feasibility study, $60,000 for marketing and advertising costs, $212,200 for a letter of credit standby fee, $66,545 for construction financing interest, and $55,455 for construction financing brokerage fees. No feasibility study was even commissioned until late 1985 or delivered until 1986, no marketing and advertising was provided before 1986 and, no financing was ever provided to the Midnight Kiss.
>
> 245. The statement of income for the S/Y Midnight Kiss Limited Partnership for year ended December 31, 1985 is false.

246. The statements of income for the S/Y Midnight Kiss Limited Partnership for years ended December 31, 1986, 1987, 1988 and 1989 are also false. The income statements in these years variously make false claims respecting moorage arranging fees, moorage fees, feasibility study fees, interest on line of credit, letter of credit standby fees, construction financing interest, and construction financing brokerage fees.

247. The statements of income for the S/Y Midnight Kiss Limited Partnership for each of the years 1985, 1986, 1987, 1988, and 1989 are false.

(iii) Financial Statements for the Type 3 Limited Partnerships

[207] The Type 3 Limited Partnerships' financial statements similarly list fictitious expenses. In this section, the S/Y Close Encounters LP's financial statements are used as an example, but the misrepresentations are substantively the same for the other Type 3 Limited Partnerships.

[208] Amounts of $116,000 appear in the 1986, 1987, and 1988 year statements that seem to correspond with the same amount listed in the Offering Memorandum for a purported completion guarantee fee. An additional $29,000 is listed in 1986 for arranging the completion guarantee. The evidence shows that no such completion guarantee existed or was arranged.

[209] The Construction Financing Fee listed in the 1986 Statement of Income and the amounts of $50,000 listed for a letter of credit standby fee in the 1986, 1987, and 1988 financial years are false. No such financing was ever obtained, despite the fact that evidence highlighted how crucial this financing would have been to make OCGC's investment proposal feasible and attractive to investors. Nor was an operating line of credit obtained for the Type 3 Limited Partnerships, despite the $11,675 fee listed as an interest expense in the 1987 Statement of Income.

[210] The $60,000 listed as an expense for the inspection of the building of the yacht is not based in reality. There was no yacht being built for the S/Y Close Encounters LP for 1986, 1987 and 1988. While the claim that the inspection of previous yachts might benefit later Limited Partnerships might carry some weight in a different set of facts, the prevalent nature of the fraud in this case makes this a weak argument in supporting the veracity of this expense. Similarly, the 1987 expense for $100,000 and $59,000 in 1988 for moorage arranging fees is not based in reality. No yacht was under construction and at the rate of construction of yachts generally, it was not plausible that mooring needed to be arranged in advance. The 1987 expense

of $25,000 for the further feasibility study is also false, as described above regarding expenses for feasibility studies by other Limited Partnership types.

e) Misrepresentations regarding Foreign Entities

[211] The Appellants argue that much of the fraud perpetrated was related to Mr. Bellfield's realization that OCGC would have a considerable corporate tax liability. In response to this, the Appellants claim that Mr. Bellfield, along with others, created a trail of false documents to reduce the corporation's taxable income. The Appellants' theory is summarized at page 26 of their Final Submissions, stating:

> OCGC as a supplier of goods and services to Limited Partnerships had significant taxable income by virtue of the invoices it delivered to the Limited Partnerships. In order to reduce its taxable income, it created false relationships and documents, including the creation of false transactions between itself and certain Swiss foreign entities, Neptune Marine Resources Ltd. and Starlight SA.

[212] The fraudulent misrepresentations and false documents created to give the illusion of a relationship with the foreign entities Neptune and Starlight S.A. are but one part of the grand fraud perpetrated by Mr. Bellfield. They cannot be parceled out, as the Appellants argue, to be treated as the separate relationship of OCGC and its tax affairs, because, as I have repeated, there was never any business and the entire scheme was a fraud from beginning to end. The fraudulent documents pertaining to Starlight S.A. and Neptune help establish that OCGC never had any access to financing, but constantly misrepresented that it did and that it was providing such financing as part of its contractual obligations to the Limited Partnerships. The false documents also help illustrate the massive scale of the fraud perpetrated. Examples of these false documents are described in broad strokes following.

[213] As discussed above, Mr. Bellfield established two entities in Switzerland and fraudulently held these entities out as offering financing and/or goods and services to OCGC and the Limited Partnerships. In support of these fraudulent claims, Mr. Bellfield and his co-conspirators Mr. Minchella and Mr. Pierre Rochat cooperated to create false agreements, invoices, account statements and other documents, which were given to the CRA by OCGC. This purportedly showed that Neptune made loans to Starlight S.A. and OCGC. These documents included a Yacht Financing Agreement, a Guarantee or Indemnity Agreement, an Agreement for providing Line

of Operating Credit, and invoices and account statements between S/Y Close Encounter LP and Neptune from January 1, 1986 to January 31, 1987.

[214] False invoices and other documents were also created and presented to the CRA purportedly showing that Starlight S.A. provided yacht chartering goods and services. This included a Management Agreement between OCGC and Starlight Charters S.A., an invoice from Starlight Charters S.A. to OCGC dated January 1, 1986 for consultation fees, feasibility study, update study, et cetera, and so on. These are only a few examples.

[215] One of the most egregious examples of misrepresenting the financing available from Neptune involved the creation of false performance bonds. The Respondent accurately summarized the evidence regarding these performance bonds at page 135 of his Final Submissions:

> 388. Exhibit R-77 is a binder of Performance Bonds.
>
> a. Tab 1 is the Neptune Marine Resources S.A Performance Bond for $1,450,000 with Neptune as the surety, Maxi Yacht as principal and OCGC as obligee. The Bond is for the Gable and refers to a written contract between Maxi Yacht and OCGC dated Nov. 1, 1984 for the building of one luxury 86 foot sail yacht of Sparkman and Stephens design. Minchella said there was no such contract.
>
> b. Tab 2 is the Neptune Marine Resources S.A Performance Bond for $1,450,000 with Neptune as the surety, Maxi Yacht as principal and OCGC as obligee. The Bond is for the Garbo and refers to a written contract between Maxi Yacht and OCGC dated Nov. 1, 1984 for the building of one luxury 86 foot sail yacht of Sparkman and Stephens design. Minchella said there was no such contract.
>
> c. Minchella pointed out another flaw with the Garbo Performance Bond which indicates it was signed January 2, 1986. He said that could not have happened either. Minchella explained that it was Forsey who noticed there weren't Performance Bonds, although the documentation required them and Forsey wasn't at the company on January 2, 1986. Minchella thought the flawed signature date was found on all the Performance Bonds.
>
> d. Minchella found another reason to identify backdating in the Performance Bonds. The Performance Bonds for the 1985 partnerships were all for $1.45 million which value comes from the amending agreements which weren't signed until April 1987.
>
> [Footnotes omitted]

[216] From the evidence, it appears that the fraudulent performance bonds were created in a cut and paste effort by OCGC people and were printed by Sibilia and

Associates. OCGC was invoiced for these expenses and for expenses relating to false documents regarding Starlight S.A. and Neptune. These expenses for documents perpetrating the fraud are included in the Appellants' summaries of funds that they claim were spent on the yacht chartering business.

[217] All of the Neptune and Starlight S.A. documents were false. Neptune never provided any financing, and Starlight S.A. never provided any goods and services.

f) More False or Backdated Documents

(i) Yacht Delivery Schedules

[218] Multiple yacht delivery schedules provided by OCGC and/or Mr. Bellfield were referred to and produced as evidence throughout the trial. All of these contained misrepresentations of when yachts would be delivered.

(ii) Management Agreements

[219] Numerous false and backdated management agreements were created by OCGC. Amongst these were management agreements purportedly entered into with "Louic LeGlatin" in trust for a corporation to be incorporated in the Channel Islands, or witnessed by an individual by the same name. Mr. *Loic* LeGlatin testified that he did not enter into these agreements nor did he recognize them, and that his name was misspelt. He further testified to the impossibility of his entering into an agreement *in trust* for the corporation listed in the agreement, and the fact that the agreements were backdated to a date prior to his first encounter with Mr. Bellfield. Mr. LeGlatin also explained that he only introduced Mr. Bellfield to Pierre Rochat in February 1985, and as such, agreements purportedly between Mr. Rochat and OCGC entered into in November 1984 and January 1985 were false.

g) Further Misrepresentations to Investors

[220] As stated previously, it is unnecessary to list all the false representations made by OCGC and Mr. Bellfield. The effort here is to provide sufficient examples to illustrate the pervasive and all-encompassing nature of the fraud. To that end, the excerpt from the Respondent's Final Submissions at page 119–124 serves to provide further examples of Mr. Bellfield and OCGC's continuous fundamental misrepresentations to investors. The first excerpt reads:

> 347. On June 24, 1985 Einar Bellfield sent a letter to Larry Magelonsky [*sic*] announcing the completion and delivery of the Garbo by the end of July 1985 and the completion of the Gable by the end of 1985 and the start of Gable charters in January 1986.
>
> [Footnotes omitted]

[221] This representation is false, as described further in the next section regarding the building and purchasing of yachts. OCGC only acquired possession of the S/Y Garbo in April 1986. The S/Y Gable was only launched in November 1988.

[222] The second excerpt reads:

> 349. The Stafford party charter took place on the leased Med. 86 between Feb. 22, 1987 and March 1, 1987. The Staffords were limited partnership investors. Dorothy Louie testified that Bellfield didn't want the clients to know that the leased Med 86 was not their yacht; Bellfield instructed them to say that it was one of OCGC's yachts. On page 4 (#0360000093) of her report she wrote:
>
> > I can see that his concerns are valid, especially when we are instructed to give the impressions that the Med 86 is our yacht and that we have had charters all winter. In the course of conversation and sometimes under questioning by the clients, the truth would slip out and can become a source of embarrassment not only to the crew but to the Company as well.
>
> 350. Both the captain, Hugues Chiffoleau and Louie had received these instructions from Einar Bellfield as to what they were to say to the clients. They were instructed to give the impression that the Med 86 was their yacht, which was not true. They were also instructed to say that they had had charters all winter, even though she knew that this was only their second charter. They were instructed to say things that were not true in order to give the clients a false impression. From speaking with other crew on the boat the clients found out that the boat was leased and this was only the second charter. The clients questioned her; she had to do a cover-up which was very uncomfortable for her.
>
> > As in this case, Bill let the cat out of the bag by telling the clients that the yacht did not belong to Starlight Charters and that we had in fact charter the Med 86 from US Yachts. Also, that this has only been our second charter. I was questioned on both issues, and covered up by saying that we had in fact bought two Med 86 which was being refurbished in Florida, and being behind schedule, could not make it to the Caribbean in time for their charter, and the owner of US Yacht, feeling responsible, had loan us his personal yacht.
> >
> > About the other charters, again because of the yachts being behind schedule, we had to cancel most of our bookings but because we did not want to spoil their planned vacation, had arranged to have this yacht at their disposal. They accepted the

> explanations, but being investors, I can see where they have grounds for being annoyed for not being told the truth. With the next charter coming up in April and yachts not being available, it should be made very clear what should be related to the clients so that we are not put in an awkward position again. We cannot force the crew to lie so perhaps in the interest of all concerned, it would be better to explain the situation to the clients prior to the charter.
>
> [Footnotes omitted, emphasis added]

[223] As can be seen from the post-charter report written by Ms. Dorothy Louie, OCGC employees were involved in various ways in perpetrating the fraud. Some of them became concerned, but most were not aware of the massive fraud in which they were involved. I found Ms. Louie to be a fairly credible witness. She answered the questions presented to her concisely and to the point. It was obvious she believed what she had been told at the beginning, but as time progressed, she ran into relationship issues and began to recognize Mr. Bellfield's deceit. For example when they were taking charters out on the Med 86, she had been given the impression that the Med 86 was OCGC's yacht. They were not told that the yacht was leased. Einar Bellfield gave instructions to tell the guests that the yacht was owned by OCGC. It slipped out that the yacht was not owned by OCGC, and this was only on the second charter. Ms. Louie said she had to do her best to cover up the untruths she was told.

[224] As summarized accurately by the Respondent, the misrepresentations to the investors continued flagrantly, including:

> 351. At other times, investors were told:
>
> a. March 10/11, 1987 letter: "The purpose of the meeting is to ratify certain changes made by OCG in the design and construction of the Yacht and to update some of the management and operating costs to reflect current conditions"…"To ratify and confirm amendments made by the General Partner in the various operating agreements with Overseas Credit and Guarantee Corporation and Starlight Charters S.A. to reflect increased costs and enhanced operations".
>
> b. Feb. 22, 1988 letter: "During the month of January OCGC has been involved in lengthy meeting with Neptune Marine Resources in Geneva to obtain the required documentation from Financial Institutions"
>
> c. March 15, 1988 letter: "We would like to bring to your attention that Overseas Credit and Guaranty Corporation is doing everything within its powers to obtain the third party documents from Europe to satisfy Revenue Canada's request".

d. Sept. 7, 1988 letter: "At that meeting it was established that Revenue Canada's only serious problem lay in their understanding of the financing mechanisms put in place by Overseas Credit and Guaranty Corporation".

e. […]"It is partially correct in that OCGC has used the $750 per month from investors to build boats. However, most of these funds have been used to build tooling and to get the production going to a point where construction financing can be drawn on. At the same time construction financing has been arranged through Neptune Marine Resources S.A. evidence of which is on hand at the OCGC office. Further, Maxi Yacht (France) makes frequent draws on the construction financing arranged by Neptune and will continue to do so in the future". --- "OCGC can not demonstrate that they have paid for these services [Starlight Charters S.A.] because these services were paid for on OCGC's behalf by Neptune Marine Resources S.A. (OCGC thus owes Neptune for these services). Bank confirmations of these payments have been presented to Revenue Canada".--- "OCGC has used the investors' promissory notes to secure financing to provide the variety of services".--- "Starlight Charters S.A. is a Swiss service company controlled by persons other than Mr. E. Bellfield…and has provided Revenue Canada with a letter ..and a sworn affidavit from Mr. E. Bellfield that he does not control Starlight".---"Neptune Marine Resources provide the construction financing for Maxi and has paid for the services provided by Starlight to OCGC on behalf of the Limited Partnerships… Mr. E. Bellfield does not control Neptune and is prepared to put witnesses on the stand to testify to that effect".

f. Dec. 6, 1988 Convention Centre minutes: "Blond with glasses ---Where is the money that our notes secure?---Mr. Bellfield replied: that is collateral security for funds raised in Europe". ---"We have spent our cash flow partially for the standby line of credit that we need".---"One more yacht will be completed within two or three months and from there on every two months. In 1989 – one every month".[534]

g. Feb. 3, 1989 letter: "…OCGC has prepared an information package which addresses a number of questions raised by investors with respect to their yacht investment. This package, which is enclosed contains…ii) Limited Partnership Statement of Source and Application of Funds".

h. August 30, 1989 Annual General Meeting Business Update: "Improvements were made to the second and third boats…the fourth boat also experienced similar delay problems…It is also interesting to realize that there are currently two boats in the water that are active in chartering. However Revenue Canada is still attacking these two Limited Partnerships on the same basis. Our third boat was placed in the water, as of April 1989, the fourth will be in at the beginning of August".

i. Sept. 28, 1990 Browning letter to investors: "Our engagement was to assist Mr. Scace to assess whether the financing transactions with Neptune Marine Resources S.A. in connection with the manufacturing of yachts and the provision of services relating to the yacht chartering/luxury cruise business had, in fact, taken place. This financing structure had

> been described by Mr. Bellfield and reflected in his hand-written schematic diagram previously referred to".
>
> j. March 28, 1991 letter: "This is to formally notify you that Overseas Credit has complied with the security agreement with Neptune Marine Resources S.A. and accordingly has assigned your outstanding debt to 937325 Ontario Inc."
>
> [Footnotes omitted]

[225] As discussed above, all representations regarding Starlight Charters S.A. and Neptune were false. OCGC's representations quoted above regarding the number of yachts under construction, available for charter, and to be acquired by Limited Partnerships were not a true representation of the state of affairs, as will be illustrated in the section that follows.

h) Building and Purchasing Yachts

(i) Overview

[226] Over the course of the fraud masterminded by Mr. Bellfield, several different yacht building and acquisition strategies were employed. As will be seen following, most possibilities that Mr. Bellfield explored were short-lived, usually because OCGC lacked the funds to carry out its contractual obligations.

[227] As previously stated, OCGC committed to delivering 36 yachts. For the 1984 Limited Partnerships, the S/Y Garbo and the S/Y Gable were supposed to be under construction in 1984 and delivered by the end of 1985. For the Type 2 Limited Partnerships, 14 additional yachts were due by December 31, 1985, bringing the total number of luxury yachts that should have been completed by the end of 1985 to 16 yachts. None were delivered by that date. In 1986, OCGC committed to delivering an additional 20 yachts by the final months of 1989 or early 1990.

[228] The evidence at trial demonstrated repeatedly that OCGC did not have the capital required to fund the acquisition of the yachts. The Respondent noted that to meet its obligations to acquire the 16 yachts due before December 31, 1985, OCGC would have needed at least 16 million dollars. It would have needed an additional $20 million minimum for the other 20 yachts promised to the remaining Limited Partnerships. This amount does not even begin to account for any soft costs related to acquiring the yacht assets or **any of the extensive ongoing expenses** of setting up a

luxury yacht chartering as OCGC was obligated to do as the general partner under the terms of its Limited Partnership Agreements. With no source of financing, OCGC relied entirely on investor deposits and interest payments. As the Respondent noted, OCGC did not even receive 16 million dollars in total from all investors by the end of 1988. The Respondent correctly summarized the impossibility of OCGC delivering on its yacht delivery promises because of its lack of funds:

> The approximate cost of a Fantaseas yacht has been described in the evidence. Robert Forsey, at Bellfield's request, advised Bellfield by letter dated August 28, 1986 that the cost of building such a yacht would be in the range of $1,300,000 to $1,500,000. In OCGC's October 31, 1985 financial statements, OCGC represents at Note 5 that the company had arranged for financing the construction of the 16 charter vessels for $16,800,000 or $1,050,000 on each charter vessel. On January 30, 1987, U.S. Yacht and OCGC entered into a purchase and sale agreement for one Med 86 for US$1,425,000. In seeking bridge financing for Picton from the CIBC, OCGC told Robert Callander that OCGC estimated the cost for the construction of each yacht to be $1,450,000 (but were not seeking financing from the CIBC).
>
> OCGC therefore needed between $16,000,000 and $24,000,000 prior to December 31, 1985 just to pay for the costs of 16 yachts, with no allowance for soft costs at all. OCGC did not even receive this amount from its investors by the end of 1988 by which point it had promised to provide 36 yachts.[22]
>
> [Footnotes omitted]

[229] In total, OCGC only ever took possession of three yachts despite promising 36 luxury yachts by 1990. The particulars of the circumstances of the possession of these three yachts have already been reviewed (see paragraphs [94] through [101]).

(ii) Dynamique: The S/Y Garbo and the First Impressions

[230] It was Loic LeGlatin, hired by Mr. Bellfield to assist with yacht acquisition for OCGC based on his extensive knowledge of the yachting world, who introduced Mr. Bellfield to Chantal and Yann Jeanneau of Dynamique in February 1985 to discuss the possibility of building of luxury yachts. Chantal Jeanneau was the main contact person at Dynamique. Mr. LeGlatin coordinated negotiation of contract between Mr. Bellfield and Dynamique, and acted as the technical advisor to Mr. Bellfield. Dynamique was involved in the building of two yachts for OCGC, the S/Y Garbo, and the S/Y First Impression.

---

[22] Respondent's Final Submissions at 137.

The S/Y Garbo

[231] The first contract for the S/Y Garbo was signed between OCGC and Dynamique on February 19, 1985. As discussed above, despite misrepresentations to the contrary, OCGC's representations that the S/Y Garbo or the S/Y Gable was under construction in 1984 were false since the first encounter with Dynamique only occurred in 1985.

[232] By March 6, 1985, Dynamique had become nervous because Mr. Bellfield had not arranged for a letter of credit required for the down payment. Less than ten days later, Mr. Bellfield ordered two more yachts from Dynamique despite having not yet come up with a down payment for the first yacht. Mr. LeGlatin testified that this was a trick in order to increase Dynamique's patience.

[233] Dynamique again contacted Mr. Bellfield on April 17, 1985 regarding the down payment required under the original contract for the S/Y Garbo. In May 1985, Dynamique contacted Mr. LeGlatin to inform him that the down payment had still not been received and they were attempting to ascertain whether the down payment would ever be forthcoming or if the contract was annulled due to failure to meet this condition. Mr. LeGlatin testified that he spent several months in France until July 1985, frequently calling and waiting to hear from Mr. Bellfield regarding the down payment for Dynamique. Dynamique continued to construct the 80-foot yacht but assumed that Mr. Bellfield was not able to purchase it. Dynamique completed the hull in July 1985. Again, it should be noted that it is only after hulls are completed that a hull registration number can be obtained on application and assigned to a specific yacht.

[234] The evidence shows that another draft contract was proposed in September 1985. The contract required a down payment and OCGC needed to pay the remaining balance by October 1985 before title would be transferred. Mr. LeGlatin testified that at the time, he was no longer receiving funds for his own wages, and OCGC continued to fail to pay any funds to Dynamique. His personal financial situation became so dire that Mr. LeGlatin testified that he needed to borrow money from Chantal Jeanneau to buy a plane ticket home.

[235] Mr. LeGlatin, Ms. Jeanneau, and Mr. Bellfield met together in October 1985 at the Annapolis Boat Show in Annapolis, Maryland, where Mr. Bellfield was still

pursuing the yacht under construction despite not having paid any funds. Mr. Bellfield proposed that he rent the yacht for a few months first before paying for it. A memo of agreement was drafted with payment options, including an option that would require Mr. Bellfield to follow a payment schedule. This schedule called for payment of $100,000 by October 15, 1985, but once again, Mr. Bellfield did not meet this obligation. He did eventually pay a down payment of $US 50,000 on November 1985.

The S/Y First Impressions

[236] Dynamique was done with negotiating with Mr. Bellfield. The question then became whether Mr. Bellfield would lose the $50,000 he had paid to Dynamique thus far. Mr. LeGlatin testified that he suggested that Mr. Bellfield take a 50-foot yacht as an alternative to losing the deposit. The $US 50,000 deposit for Dynamique was used to purchase the 50-foot instead, with the bill of sale dated November 27, 1985. Title for the S/Y First Impressions, a yacht that would not satisfy OCGC's obligations to the Limited Partnerships, passed to OCGC some 8 months after the initial contract for the S/Y Garbo. At this point, it was one month before all 16 yachts promised to the Type 1 and Type 2 Limited Partnerships were due for delivery. OCGC had only managed to pay $50,000 at that time and clearly had difficulty even paying its employee, Mr. LeGlatin.

[237] Ester Palmer testified that the S/Y First Impression was supposed to be used as a provisioning boat for the luxury yacht charters, but in November 1985, there were no yachts to provision. The boat arrived in St. Lucia in March 1986. Mr. Steven Leibtag, Operations Manager at Starlight Canada, testified that he visited the St. Lucia base of operation around that time. He testified that there was a significant dispute with the S/Y First Impressions crew over a lack of payment for their services rendered in the transatlantic crossing. Mr. Leibtab was an experienced salesperson who appeared to answer accurately the questions directed to him. He said that the reason he left OCGC was that they did not need his expertise since they did not have any yachts. A similar frustration was expressed by others who later left OCGC, such as Bruce Oekler.

[238] Until March 1986, the S/Y First Impression was the only boat available and even though it did not fit within the Fantaseas brand, the boat was used to conduct limited charters in the Caribbean. None of the charters benefited any of the Limited Partnerships. These efforts were simply part of continued efforts at window-dressing

and demonstrating to investors that OCGC had yacht chartering capabilities. Eventually the ownership of the S/Y First Impressions was transferred to Mr. Bellfield's wife on June 26, 1992, and located in Toronto, where Mr. Jack Moles later saw it. Mr. Moles was an employee of OCGC and supervised the repair work on the S/Y Garbo in Florida. David Martin also testified that he knew that the yacht was in Ontario throughout his employment, but he considered the S/Y First Impressions to be outside of the Fantaseas operations. David Martin had been an employee of Starlight from Canada from March, 1988 to 1989 conducting marketing and sales for Fantaseas. I found that Mr. Martin presented well as a witness, appeared to be knowledgeable on the questions asked, and was direct, and honest.

The S/Y Garbo, continued

[239] On December 15, 1985, yet another contract was created between Dynamique and OCGC; this time with OCGC acting as the trustee for the S/Y Garbo. Mr. LeGlatin testified that once again he was in France contacting Mr. Bellfield and OCGC frequently looking for the funds to pay for the 80-foot yacht, and again they were not forthcoming. Dynamique ultimately sailed the yacht across the Atlantic to St. Martin. The documentary evidences shows an invoice and bill of sale from Dynamique to OCGC, amongst other documents, with the S/Y Garbo finally sold to OCGC on April 4, 1986.

[240] At that point, there was <u>one</u> Limited Partnership yacht, with fifteen more yachts outstanding and no funds or ability to build these other yachts. There were also two problems with the one "Fantaseas" yacht that had finally come into OCGC's possession.

[241] First, the S/Y Garbo was not up to standards. Ester Palmer, Vice-President Operations of Starlight Canada, described the S/Y Garbo as a very sleek and beautiful yacht. She explained, however, that the S/Y Garbo did not fit the Fantaseas concept because it did not have the four equal cabins and therefore charters could not be sold on an equal basis. David Martin, General Manager of Starlight Canada, also described the S/Y Garbo as not complying with the Fantaseas concept.

[242] Second, the S/Y Garbo suffered extensive structural damage on its maiden voyage, and had to be in a shipyard in Florida to undergo significant repairs. This meant that there was no 80-foot yacht available for charters. Again, the only yacht that could go on charters until the S/Y Garbo left the dry dock in April 1987 was the

S/Y First Impressions, which was not a Limited Partnership yacht and smaller than required for the Fantaseas concept. In fall 1986, Bruce Oekler, a travel consultant in Miami who worked on marketing and sales for Starlight Canada, testified that he had to delay his marketing efforts because the S/Y Garbo was still not in the water.

[243] Jack Moles came on as Project Supervisor in October 1986 to supervise the yacht repairs on the S/Y Garbo in the Guy Couach Boatyard in Florida. He attempted to speed them up because work was proceeding very slowly. Mr. Moles appeared very knowledgeable about the areas upon which he testified. He was straightforward, professional, and he answered questions fairly. Mr. Moles testified that there were serious structural problems with the S/Y Garbo due to the yacht's design. He also testified that one of his priorities was to address late payments for repair work that was slowing down the completion of work. He established a local bank account as an effort to ensure work was paid for in a timely manner and to ensure the yacht could leave the yard as soon as possible.

[244] Mr. Moles testified that there was some tension between him and OCGC from time to time because there was difficulty in getting money from OCGC. He was trying to get the S/Y Garbo out of the yard, and pay the interior decorator. The rules were that people had to be paid before the yacht could leave the yard. At a time when OCGC was already supposed to have delivered 16 yachts, OCGC was having trouble paying for repairs on its very first Limited Partnership yacht. To emphasize, OCGC could not afford repairs on one yacht when it had represented itself as having at least 16 million dollars to acquire the yachts to be delivered by December 31, 1985.

[245] The S/Y Garbo finally left the yacht yard in Florida and went to St. Lucia to start chartering on April 6, 1987. The first charter on the S/Y Garbo occurred in April 1987. After that time, Mr. Moles heard regularly from Eraldo Marcolongo, Operations Manager with Starlight Canada, who was based in St. Lucia. Mr. Marcolongo was often in contact with Mr. Moles, looking for materials or parts for the S/Y Garbo. There were interior decoration problems with the S/Y Garbo, electrical problems and general ongoing repairs as a result of the yacht being in a southern climate. In an ever-repeating pattern in the story of the OCGC fraud, Mr. Marcolongo had to repeatedly request funds to pay the bills. He regularly complained about the problem of getting regular funding on a timely basis, and he was looking for a maintenance budget.

[246] Despite the S/Y Garbo not being available for charter until April 1987, the S/Y Garbo 1986 financial statements list charter fees and false representations about the S/Y Garbo's availability for charter. The number of actual charters that the S/Y Garbo undertook was limited, and many of the passengers who spent time aboard the S/Y Garbo did so at reduced investor rates or were complimentary. This was in the interest of Mr. Bellfield's to keep up the smoke and mirrors of the luxury yacht charter fraud. David Martin, General Manager of Starlight Canada, testified that the S/Y Garbo was out of service for the summer of 1988. The S/Y Garbo ultimately went to St. Martin and then to boat shows to market the Fantaseas concept. A sailing schedule in evidence shows the S/Y Garbo at charter shows in the Virgin Islands, St Thomas, Antigua, and on one cruise in the fall of 1988.

[247] In 1988, the S/Y Garbo was sold to Maxi-Yacht International S.A.R.L. as part of the financing of that yacht-building company. The sale of the S/Y Garbo asset to Maxi-Yacht does not appear in any of the Limited Partnerships financial statements.

(iii) The S/Y Great Gatsby

[248] The S/Y Great Gatsby was one of several yachts that OCGC negotiated about potentially purchasing but ultimately did not. Under its contracts with the S/Y Great Gatsby Limited Partnership, a Type 2 Limited Partnership, OCGC was to deliver the S/Y Great Gatsby yacht by December 31, 1985.

[249] Originally a racing yacht known as the "Ondine", the S/Y Great Gatsby was an 80-foot aluminium yacht described by several witnesses as being in terrible condition. To bring it up to specifications for the Fantaseas purpose would have been very difficult, if not impossible. Nonetheless, OCGC had a contract to purchase the ex-race boat. Mr. Moles testified that the S/Y Great Gatsby was quite unsuitable for the Fantaseas concept. It did not meet the vision and standard. In terms of the issues with the yacht, Mr. Moles also testified that the aluminium required a total rebuild and there was an electrolysis issue. Jack Moles' assessment, based on an auto-gauge inspection to determine the thickness of the hull, was that the yacht would only be satisfactory for a day-cruiser. Mr. LeGlatin also noted the yacht's deficiencies when he conducted a survey of the ex-racing yacht. The cost to bring the S/Y Great Gatsby up to standard was not reasonable. Bruce Oekler testified that he was aware of the Ondine ("the S/Y Great Gatsby"), but that he understood it to be an incomplete shell

with no rigging. Clearly, the S/Y Great Gatsby could not meet the standards of a Fantaseas yacht.

[250] Regardless of the clear deficiencies of the ex-racer, OCGC contracted to purchase the Ondine on December 24, 1985 for US $298,500, with an initial payment followed by the balance monthly instalments for 24 months with no guarantees whatsoever on the yacht's condition. It was to become the S/Y Great Gatsby Limited Partnership's yacht. Various protracted negotiations followed, with assorted legalities to determine. However, once again, OCGC (Mr. Bellfield) was behind on payments. This led to the non-completion of the deal because US $12,652 was still required for the closing to be completed. The owner of the Ondine actually filed action against OCGC in September 1987 for default of payments and for stripping the yacht. The matter was finally settled by Mr. Bellfield on April 29, 1988, and possession of the yacht was transferred back to the owner.

[251] Despite the fact the yacht did not qualify, was ultimately never acquired, nor used for the chartering, the S/Y Great Gatsby was listed as an asset on the S/Y Great Gatsby Limited Partnership financial statements for the year ending on December 31, 1985.

(iv) The Med 86 (the First Gable)

[252] Two different yachts had the potential of becoming the yacht for the S/Y Gable LP. The first one was a "Med 86" to be purchased from U.S. Yacht. Again, this deal did not close due to OCGC's failure to pay the funds required to complete the purchase. The second Gable was eventually acquired by OCGC, but OCGC's title to the yacht was only held briefly.

[253] Mr. Moles saw the Med 86 Gable at a Miami boat show and arranged for a survey of the yacht to be conducted. He believed that the Med 86 cabin could be renovated to create four cabins adequate to suit the Fantaseas concept. In the end, despite the redesign proposed by Mr. Moles, and an agreement of purchase and sale dated January 30, 1987, the purchase did not close. The price for the yacht was US $1,425,000, with a down payment of US $350,000 being required, paid in escrow before closing, and balance paid on closing. The date for closing was set for April 1, 1987. A further agreement was made delaying that closing date to May 15, 1987, with OCGC agreeing to pay an additional US $200,000 in escrow. Despite this arrangement, OCGC never did close the deal and was put in default.

[254] OCGC demanded arbitration with U.S. Yacht, with various complaints exchanged. The arbitration's findings, however, underlined the true nature of OCGC's problems. The problem was the same recurrent issue of a lack of capital. The arbitrator found that OCGC suffered from a lack of sufficient cash flow to pay the amount owed on May 15, 1987, and awarded U.S. Yacht a considerable amount of damages, totalling more than $379,167. OCGC only received $162,298 in refund of the amount paid into escrow.

(v) Chantier Yachting France

[255] Purchase agreements were signed with Chantier Yachting France for two yachts in March 1985, however, the company informed OCGC that it had gone into receivership in July 1985. No yachts were actually built by Chantier Yachting France for OCGC. As described above, subsequent to Chantier Yachting France entering into receivership, OCGC made numerous fraudulent misrepresentations regarding purportedly valid purchase agreements with the company, as well as hull registration numbers for yachts built or under construction by Chantier Yachting France despite the impossibility of these facts.

(vi) Maxi-Yacht

[256] The second Gable was built in France, based on a designed by Sparkman and Stevens, a highly respected naval architect firm, and constructed by Michel Dufour, an acclaimed French boat builder. The arrangement was actually for a number of yachts to be built, with Mr. Bellfield providing the funds to finance the manufacturer in France while Mr. Dufour carried out the construction. Negotiations around the design continued, running from as early as January 1, 1986 through September 30, 1987. A number of other individuals were also involved in discussions concerning the yacht design, with an Italian designer working on the interior, as well as consulting with OCGC people such as Mary Crocco as to the appropriate kitchen appliances, et cetera.

[257] Mr. Moles traveled to France several times, acting as OCGC's technical liaison. He saw the Maxi-Yacht facility's new building and described the facilities as having three yachts on the floor at various stages of construction. The first yacht (the S/Y Gable) had a deck on it. The second yacht had a completed interior with the deck ready to go on, and the third yacht he described as being laminated in the mould.

[258] Mr. Martin also visited the Maxi-Yacht facility in France in August 1988. He met with Michel Dufour, the Italian designers, and the house representatives in Europe. His impression of the Maxi-Yacht facility was that it was a first class facility. Mr. Moles testified that the Maxi-Yacht facility in France appeared to be purpose built, the operations seemed to run smoothly and the plant was workable for the volume of yachts planned. Photos were entered into evidence of the Maxi-Yacht facility with yachts under construction.

[259] There is no doubt based on the evidence that the architect, builder, designer, and technical advisor involved with the Maxi-Yacht had great expertise. The plant clearly created a beautiful product. This does not change the fact though, that the product was merely used in an attempt to perpetuate and continue the elaborate fraud. By the time the S/Y Gable was completed and christened in 1988, this Limited Partnership yacht was long overdue, as were many other yachts owed to the Limited Partnerships. Worse, the S/Y Gable LP's financial statements list the yacht as a fully owned asset, when the actual Gable was only built, completed, and delivered by Maxi-Yacht in October 1988.

[260] The S/Y Gable is the only yacht that was (briefly) delivered that can truly be described as meeting the Fantaseas standards. Ms. Palmer was on the S/Y Gable to take photos for marketing purposes, and as a guest to evaluate the guest experience. She described the yacht as a beautiful yacht, with service and cuisine that was consistent with the Fantaseas concept. Mr. Moles also saw the S/Y Gable under construction in France at the Maxi-Yacht facility. In October 1988, he was in France for sea trials of the S/Y Gable. Mr. Moles described the S/Y Gable as a large, sleek, racehorse type of yacht that met the Fantaseas concept, and gave a generally good impression. Mr. Martin, General Manager of Starlight Canada from March 1988–1989, also described the S/Y Gable at the time as a spectacular vessel.

[261] OCGC took great pains to make sure the christening of the S/Y Gable was a large attention-grabbing event. This was particularly important to OCGC because at the time, an extensive audit was underway by the CRA, and it wanted to emphasize strongly the growing nature of its "successful" venture. The christening even included the presence of Prince Albert of Monaco. It was, essentially, an elegant example of the smoke and mirrors OCGC continuously employed to provide just enough indications of a genuine business to attempt to keep suspicions that the entire investment scheme was a fraud at bay.

[262] Shortly after the launch, the ownership of the S/Y Gable was transferred to Starlight S.A.M., a related French entity.

[263] The Maxi-Yacht plant created two other yachts, the Demoiselles des Rochefort and the Rocco Jr. These appear to have been the two yachts that Mr. Moles saw on at the Maxi-Yacht plant. Both of these yachts were sold to French partnerships in December 1988 and were not used to meet any of the contractual obligations to the Canadian Limited Partnerships.

(viii) Picton

[264] Picton was the site of a warehouse that OCGC entered into a purchase and sales agreement for in August 1986, and where, despite numerous representations to the contrary, OCGC did very little. For example, in one instance in the evidence (March 1987 "Overseas Credit and Guaranty Corporation Proposal for Establishing Credit Arrangements"), Picton is falsely described as follows:

> The [Picton] plant is 25,000 square feet in size and moulds have been developed for a 75' catamaran, also designed for the ultimate cruise experience. This plant in full operation is scheduled to produce 12 vessels per year and production will commence in the spring of 1987.
>
> [Footnotes removed]

[265] The plant was not in fact in operation, or anywhere near operational. Ross Price was hired as an employee of OCGC to work at the Picton site, which was purchased by OCGC from his family. Mr. Price was a witness who I found to be forthright and candid, and he remembered the required details of his evidence quite clearly. I found him to be quite credible.

[266] Mr. Price was the on-site manager of the Picton facility for about a year, from fall 1987 to spring 1988. His responsibility was basically to be the site manager, to clean the property up and to get it on the road to serving as a production facility. The property was poorly lit and dirty, with minor electrical work done. Second-hand catamaran moulds were put in the building and assembled, but otherwise, nothing else was done. Mr. Price set-up some accounts with local suppliers, but as time progressed, the suppliers never were paid. The Picton facility was a warehouse only. It needed significant upgrades including lighting, air systems, glass shop specialities, electrical supply, a compressor system, wood shop, and a mechanical shop. In

essence, the building was a shell without the capacity for any production, and it remained that way. The building was merely a warehouse with used moulds in it. These used moulds had spent a significant time outdoors exposed to the weather and were in such a state of disrepair that they could not be used. Between August 1986 when the property was sold and spring 1988, only the second hand moulds were delivered. As summarized by the Respondent regarding the mould in his Final Submissions:

> 490. Bellfield purchased a disassembled used travel lift from the Prices in October 1986 for $38,000 to be assembled by Ross Price inside the warehouse.
>
> 491. Bellfield purchased 60' catamaran moulds from Andrews Trucking for $40,000 and had them moved to Picton in January 1987.
>
> 492. Ross Price was hired by OCGC to work in the Picton warehouse in the spring of 1988, did some clean up, pulled the moulds in the yard into the warehouse and bolted them together and tried to get a set of lines off the moulds because there were no drawings for them. Then Bellfield wanted to sell the property so they moved the moulds and travel lift outside into a field. Price stayed with OCGC through the winter of 1989 but by October 1989 he was no longer an employee. The Picton facility never produced any catamarans while Price was involved.
>
> 493. In October 1986 British catamaran designer Derek Kelsall provided a preliminary design for a 75' catamaran to OCGC for $3000. In March 1987 Kelsall visited Picton Ontario and examined the 63' catamaran moulds which were sitting in the yard. He was not impressed by them. Kelsall provided a written assessment of the moulds and the possibility of incorporating them into a 75' design and was paid $2000. He had no further exchanges of correspondence with OCGC, the design work did not proceed and Kelsall had no further involvement with OCGC or Maxi Yacht.

[267] Mr. Price testified that an investor, George Ward, showed up at the facility to see what was going on. Mr. Ward thought something was wrong with the Limited Partnership investment, and he went to the Securities Exchange Commission in Toronto with his concerns. Mr. Price also testified that he felt that some of the facts in the OCGC brochure distributed were simply not correct.

[268] Mr. Moles also testified regarding his involvement with the Picton plant. Overall, his impressions of the plant were poor and he felt that to make it operational it would have required considerable expense and effort. Even if it was operational, only one catamaran could have been built at the time given the limited space. In a report he produced in July 1987, he predicted that the earliest the first catamaran

could be produced at the Picton facility, if his extensive recommendations were implemented, would be in 1989. A 1988 business plan described the facility as operational beginning in fall of 1988 and that Mr. Moles was moving to the area to coordinate the operation's start-up. Mr. Moles testified that the business plan did not follow his recommendations, and that he never intended to move to Picton.

[269] Further misrepresentations made by OCGC regarding the Picton facility are accurately summarized by the Respondent in his Final Submissions at pages 160–162 as follows:

> 494. Contrary to the claim on page 10 of the OCGC corporate brochure, Kelsall was not the project leader in the construction and design of OCGC's maxi-catamarans. Kelsall was not aware of the use of his picture and name in the brochure, and to his knowledge his technology was not used in the claimed construction and design of OCGC's maxi-catamarans.
>
> …
>
> 503. The forecast of boats on the water by 1990 which was attached to Robert Forsey's Feb. 24, 1987 memo to Bellfield showed one 75' catamaran, the Main Event, being completed in 1987, four catamarans being produced in 1988 and more in 1989. To Mole's knowledge no such boats were ever produced.
>
> 504. Minchella received a copy of Forsey's "Delivery Schedule For Boats" memorandum to Bellfield of Feb. 24, 1987 with its attached "Forecast of Boats on Water by the Year 1990" (Exhibit R14-Tab 173) which showed ten catamarans to be built by Maxi Yacht International at its Picton plant. Minchella said he was not in charge of that project so could not say where construction financing for the catamarans would come from. However, Minchella did know that at March 1987 OCGC did not have any bank or other external financing available to it for the construction of the yachts besides the investors' interest payments and the investors' notes.
>
> 505. Minchella was shown page 10 of the OCGC brochure at Exhibit A22-Tab 5 which features a picture of Derek Kelsall, describes him as project leader, and states that his technology is being used in the construction and design of the OCGC catamarans. Minchella said he was not involved in the production of the brochure but, having seen the facts relating to Kelsall, that the brochure misstates both Kelsall's position and involvement and further misrepresents that there was manufacturing going on at Picton, which never happened with anyone's catamaran technology.
>
> 506. In 1989 Loïc LeGlatin, who by then had his own business building catamarans, saw an ad in the paper about a former boat building plant in Picton, Ontario so he drove there to take a look. He met someone there who may have been the former owner and had the keys, so could show him around. He saw a very old design catamaran mould sitting there and it was damaged. He followed up and received a letter from Stephen Sobot of OCGC dated December 21, 1989 which included a drawing of the catamaran which he recognized as the Derek Kelsall design LeGlatin had showed Bellfield in 1985. LeGlatin knew the drawing did not match the moulds

> that he had seen. Once he realized that it was OCGC that he was dealing with he stopped all discussion.
>
> [Footnotes removed]

i) Starlight Charters

(i) Starlight Canada

[270] Starlight Canada was incorporated in 1986, and Ester Palmer came on board shortly thereafter. It was only once she joined the organization that any marketing efforts occurred. Her evidence shows that a significant portion of her work for Starlight Charters consisted of marketing the luxury yacht chartering investment opportunity to potential Limited Partnership investors. This was done either by selling the concept through audio-visual presentations, or after they invested, arranging for investors to enjoy yacht charters at reduced rates.

[271] It was clear from Ms. Palmer's evidence that she was not aware of the enormity of the fraudulent scheme she was involved in. She carried out some efforts that at first glance may appear to be genuine expenses incurred to establish a yacht chartering business. Ms. Palmer attempted to market the yacht charters to various travel agents and to partake in promotional opportunities such as boat shows, contests, and magazine articles. None of these efforts amounted to anywhere near the scale that would have been required to create a genuine luxury yacht chartering venture, and it seems Ms. Palmer lacked the experience to know the extent to which she was being used by Mr. Bellfield to aid him in providing an air of legitimacy to his fraudulent operations. For example, a Fantaseas presentation video, an expense that was invoiced to Starlight Canada, was frequently used to market the yacht chartering Limited Partnership investment. It was a key part of the presentation to seduce potential investors.

[272] The evidence shows that the operations of Starlight Canada, while unbeknownst to many of the individuals involved, were undertaken primarily to market the sale of Limited Partnership units, and to provide the illusion of legitimacy to the fraud. This reality did become clear to certain individuals involved in marketing efforts for Starlight Charters. For example, Bruce Oekler testified that a lack of available yachts made it impossible for him to continue to market the product. Bruce Oekler had contacted approximately 200 travel agents about the Fantaseas

concept; he testified that after he left Starlight Charters in December 1986, none of these agents were contacted about the luxury yacht charters.

[273] All of Starlight Charters' marketing efforts required making fraudulent misrepresentations as to the number of yachts it had available and the state of its operations. These were generally based on trusting Mr. Bellfield's representations. Several brief examples are highlighted following, but only serve to represent a much wider body of evidence.

[274] In May 1986, Starlight Canada coordinated a promotional magazine article by a sailing enthusiast who wrote enthusiastically about his stay on a yacht in April 1986, and referred to the fact that ten yachts would be available. This fact was obviously false and impossible given the state of yacht acquirement at the time. The article only served to promote the venture and provide it with airs of further legitimacy.

[275] On a number of occasions, Starlight Canada misrepresented itself as having a fleet of yachts and a yacht chartering operation at the ready, including the following examples, as summarized in the Respondent's submissions at page 125:

> Sept. 25, 1986 letter from Ashworth to Sears Travel: 'The Fantaseas fleet, operated by Starlight Charters Ltd., is comprised of the largest and most supremely comfortable charter maxi yachts in the world".
>
> Oct. 14, 1986 letter from Ashworth to Tour Desk One Inc.: "It's the perfect way for your 'hard to please clients' to relax, close their eyes and be pampered aboard the world's most supremely luxurious fleet of charter yachts".
>
> January 9, 1987 letter from Ashworth to Jack Haughton of Osler, Wills & Bickle: "The Fantaseas fleet, operated by Starlight Charters Ltd., is comprised of the largest and most supremely comfortable charter maxi yachts in the world, all eighty feet or greater."
>
> February 20, 1987 letter to Don McLeod, Ashworth wrote: "The Fantaseas fleet, operated by Starlight Charters Ltd., is comprised of the largest and most supremely comfortable charter maxi yachts in the world, all eighty feet or greater."
>
> May 22, 1987 letter to an incentive house, Ashworth wrote: "The Fantaseas fleet, operated by Starlight Charters Ltd., is comprised of the largest and most supremely comfortable charter

> maxi yachts in the world, all eighty feet or greater. We take great pride in our personalized service"

[276] Starlight Charters' main purpose, was to market the fraudulent scheme to potential Limited Partners and to maintain the illusion of the scheme's legitimacy. The expenses it incurred should be regarded as having been not for the Limited Partnerships' benefit, but for the purpose of carrying out and maintaining the fraud.

(ii) Caribbean Operations

[277] The evidence clearly revealed that the entire OCGC operations and the Fantaseas concept was an undercapitalized operation from the beginning. As indicated earlier, it is my view that OCGC operations and the Fantaseas concept had all the hallmarks of a Ponzi-like scheme. With no capital from the beginning, there was an inability to fund the operations of the Caribbean base. This included the charter operations, a cornerstone in its marketing efforts, and the location where the product marketed was to be delivered (the high end cruises).

[278] A successful long-term business requires significant start-up costs. Here, there was a need for an infrastructure for the Caribbean operations of the Starlight Charters concept, as promised to the Limited Partnerships. This infrastructure would have included the Caribbean base with an office, marina, vessels, trained crew, provisioning and services, in order to meet the expected demand of the market in the high-end yacht chartering service. Delivery of the service was a problem from the beginning because of inadequate funding, i.e. no cash flow for even the most basic parts of delivery for the promises advanced to Limited Partnerships. As noted, there was some marketing carried out in order to develop interest in the Starlight Charters high end yacht service, but it is my finding that this marketing was not done for the benefit of the Limited Partnerships, but rather to advance the Ponzi-like scheme. This was not a smash and grab robbery; this was a long term fraud that was growing in size and scope over a long period of time to the benefit of Mr. Bellfield, and to the long term disadvantage of the Limited Partnership investors.

[279] According to the Caribbean Operations Manager, Mr. Marcolongo, very early on in the establishment of operations there was not enough money for its operations, and on some occasions there was no money at all. There are numerous examples of the inadequate levels of funding. There was insufficient or no money for safety and yacht repairs. There was an inability to meet rent obligations. There was

not even adequate money to provision charters that were going to be contras. There was an inadequate amount of money to obtain and train a crew, pay marina fees, pay for a telephone and telex, and according to Mr. Marcolongo, they could not even afford to buy deck shoes. He even stole power from a local restaurant. Mr. Marcolongo made inquiries to see if they could sell some of their equipment to pay for some of their operations, but in the end, Mr. Marcolongo had to use his own money to fund the operations.

[280] This was the situation that existed before the first yacht that came close to meeting the Fantaseas concept was even acquired. This continued onward even after the S/Y Garbo was acquired and made seaworthy. It is difficult to conclude otherwise than that the operational aspects of Starlight Charters and the Fantaseas concept were anything more than window-dressing, when the basic operational expenses of the Starlight Charters Marina in the Caribbean for only one yacht that did not meet the Fantaseas concept could not be met. The simple reason for the failure of the success of the operations in the Caribbean was that there was no capital and no financing; there was none of what was promised to the investors. All there was were interest payments and small down payments on the sale of Limited Partnerships unit, which were used by the OCGC head office to perpetuate the fraud. This included acquiring a vessel or vessels that would meet the Fantaseas concept and thereby allow for the sales of more partnerships, and in turn, create a greater cash flow to meet the ongoing obligations of the entire fraudulent scheme.

[281] The argument of the Appellants in part relies on expenses paid towards the provision and operation of certain charters taken from 1986–1990 as indications that this had to be a legitimate operation. The purported charters can be broken down into five varieties. First, there appeared to be approximately 25 charters in total. Of these 25, there were approximately five contras, which were charters offered in lieu of payment of bills or expenses incurred by OCGC. There were eight investor charters taken by investors in the Limited Partnerships at discounted rates. There were four familiarization charters, for the purpose of promoting the product. There were three charters that were terminated in whole or in part because the customers were unhappy with the product. This left approximately five charters that were actual paid charters over a period of five years.

[282] Of those 25 charters, it appears that approximately four were in the S/Y First Impressions, two were in the Med 86, 15 were in the S/Y Garbo, four were in the S/Y Gable, and one was in a French Limited Partnership yacht, the Demoiselle de

Rochefort. Of the S/Y Garbo cruises, there were four familiarization tours, two contras, and four investor trips. Of the S/Y Gable there were approximately two contras, and the two others were unhappy customers. Separate and apart from the 25 charters that reportedly took place, there were 14 others that were reportedly cancelled. Ten were cancelled for technical reasons, crew problems, or maintenance issues, and two were investor cancellations.

[283] What is particularly startling about the analysis of the purported charters and the cancellations between 1986 and 1990 is that there was no real improvement over time in terms of ability to deliver on the service marketed for the benefit of the Limited Partnerships—if anything it simply got worse. To the point that in 1990, they were in effect no charters and if there was a charter, it was conducted by a non-Canadian Limited Partnership yacht.

[284] A significant majority of the charters were contras, investors, or familiarization tours. These were conducted for the purpose of a) satisfying investors so as to develop more investors, and b) to promote the product to writers or people providing services to the company, again for the purpose of getting more investors that would lead to getting more money that would lead to a greater fraud.

[285] A fraud of this proportion requires a significant amount of smoke and mirrors to keep the fraud advancing forward. More Limited Partnerships had to be sold all the time in order to perpetuate the fraud. In order to advance these sales, there had to be promotion by word of mouth as well as more general legitimization through the use of various parties including travel agents. The mere participation by a number of legitimate members of the travel field does not a true business make; Mr. Bellfield needed the operation to attain a level of presumed legitimacy. Just like many other well-know Ponzi schemes, this involved the use of various unsuspecting legitimate actors who, unbeknownst to them, aided in promoting the fraud as if it were a genuine operation. The expenses of running the Caribbean operations, were expenses incurred to perpetuate the fraud. The expenses did not constitute true business expenses that can flow through as eligible expenses for the Limited Partnerships.

j) Other OCGC Businesses

[286] Once OCGC was incorporated in May 1984, it was quickly followed by the incorporation and establishment of a variety of other businesses. Some of these entities formed an integrated part of OCGC, some were peripheral and some had nothing to do with integral OCGC operations, but they were all entities where Einar Bellfield was the operating mind. The OCGC related entities included the following:

1) OCG Financial Holdings Ltd.: a holding corporation;

2) Overseas Credit and Guaranty (Alberta) Corporation: formed to move capital assets of OCGC to Alberta to get a better tax advantage;

3) OCGC Enterprises Inc.: a company in which Mr. Minchella was the secretary and the treasurer and that was the initial limited partner of all of the Type 3 Limited Partnerships;

4) Overseas Mortgage Corporation;

5) OCG Investments Alberta;

6) The Baron Group;

    a) Baron Securities: an entity that sold investments which were not the yacht chartering Limited Partnerships, whose offices were at Yonge and Finch, not at the Richmond Street location of OCGC;
    b) Baron Insurance Agencies Inc.;
    c) Baron Investment Services Inc.;
    d) Baron National Securities Inc.;

7) The American Diversified Realty Group;

    a) American Diversified Realty Fund: sold units in a realty fund in which Mr. Minchella and his wife had signing authorities with Mr. Bellfield;
    b) American Diversified Realty Inc.: Mr. Minchella was Vice-President. This was an operating company for American Diversified Realty Fund;
    c) ADR Management and Construction Inc.: a company that was to oversee construction of a new project;

8) 780807 Ontario Ltd.;

9) 750070 Ont. Ltd.;

10) Starlight Group;

    1) Starlight Charters Ltd.: based in Toronto and established to produce and market the Fantaseas program for the OCGC Limited Partnerships;
    2) Starlight St. Martin S.A.R.L.;

11) Brock Yacht Charter Inc.: Jill Brock's company, who was originally hired to do marketing and consulting for Starlight Charters but in the end, sold the company;

12) Maxi Yacht International Ltd.: a company to acquire and build yachts in Ontario, in which Mr. Minchella was the Secretary-Treasurer;

13) Maxi Yacht International Inc.: a Florida company to repair and service yachts that came into operation such as the S/Y Garbo;

14) Superior Group;

    1) Superior Salmon Farms Limited: Einar Bellfield and his brother Jelleto opened a salmon farm in eastern Canada, and purchased small salmon from the government to grow and then sell for a profit. Lawyers who did work for this particular company then billed OCGC;
    2) Superior Cumberland Bay Limited: a subsidiary of Superior Salmon Farms;

15) 780315 Ontario Limited;

16) Lauderdale Marina (1988) Ltd.: a marina purchased in Orillia, Ontario in Mr. Minchella's name in trust in 1988. A houseboat was bought in 1984, was transferred to this company and then rented at Lauderdale Marina;

17) Coastal Cruisers Inc.: operated a cruiser co-owned by Mr. Minchella and Mr. Bellfield at fifty percent each;

18) Fabu D'Or Cuisine Incorporated: a commissary that OCGC purportedly commenced that was to be used for the purpose of production of food and meals for the Limited Partnership charters and commercially;

19) Lease Invest Ltd.: a company to sell a financial product that involved investing in leases, for example to lease equipment to Fabu D'Or, with Mr. Minchella as Secretary-Treasurer; and

20) Marine Indemnity Fund.

[287] Of all of these entities, only OCGC Enterprises Inc., Starlight Charters, Maxi-Yacht International Limited, and Fabu D'Or Cuisine Inc. had anything to do with the sale of yacht chartering Limited Partnerships, and establishing the Limited Partnerships scheme. There was no evidence before the Court indicating that the other entities were involved in the luxury yacht chartering scheme. The only involvement the entitles had was that some of the money claimed by the Appellants to have been spent by OCGC to acquire goods and services for the Limited Partnerships, were in fact spent on acquiring goods and services for those companies.

[288] Three OCGC-related ventures that were not within the domain of the luxury yacht chartering business are highlighted following because their circumstances are particularly insightful. The first, American Diversified, requires mention because of the findings of an Ontario Securities Commission decision relating to its activities. It also provides an illustrative example of how good and services that the Appellants claim were acquired for the yacht chartering Limited Partnerships were actually used for a variety of Mr. Bellfield's other ventures. The second and third examples, Lauderdale Marina and Coastal Cruises, illustrate the same.

(i) American Diversified

[289] The American Diversified Realty Fund Limited Partnership was the subject of an investigation and hearing by the Ontario Securities Commission. The Commission's findings that the American Diversified venture was a mere sham betray a similar pattern to the findings regarding OCGC's yacht chartering scheme made by this Court. As correctly summarized by the Respondent at page 7 of his Final Submissions, the Ontario Securities Commission concluded as follows:

> 5. On February 5, 1991 the Ontario Securities Commission released its decision on a Securities Act investigation and hearing into American Diversified Realty Fund Limited Partnership, American Diversified Realty Inc., OCGC, OCGC Financial Holdings Ltd., OCGC (Alberta) Corporation, Baron Securities Inc, Einar Bellfield and Paul Brooks, imposing trading bans on all respondents.[1]
>
> 6. On February 11, 1991, the Globe and Mail reported on the outcome of the Ontario Securities Commission investigation into American Diversified Realty, a business Minchella had been very involved with. Minchella believed that because some yacht limited partnership investors were also ADR investors that they were aware of the investigation, the trading bans, and ADR being shut down. The article was called "Real Estate Firm Shut Down for Sham Financing Scheme" and after reporting on the 8 year trading ban imposed on the scheme's chief architect, Einar Bellfield, it summarized the Ontario Securities Commissions findings regarding the sham financing scheme as follows:
>
> a. The scheme had the money going around in a circle;
>
> b. The company that was supposed to make the real estate investments ended up holding notes that were not backed by assets;
>
> c. The company that was supposed to make the real estate investments had no money to make the investments;
>
> d. The investors ended up paying a half per cent interest on their own money.
>
> (footnotes removed)

[290] The American Diversified Realty Fund Limited Partnership provides another example of expenses that are included in the Appellants' claim that $13–14 million was spent on yacht chartering activities. Payments to the individual acting as the Chief Operating Officer of the American Diversified Realty Fund Limited Partnership are included in the calculations leading to those total amounts. In addition, based on the evidence, Mr. Minchella appears to have done considerable work on American Diversified Realty Fund-related matters from 1985 through 1989, amongst his work on other non-yacht chartering Limited Partnership matters. Payments to Mr. Minchella are also included in the $13–$14 million the Appellant claimed was spent on establishing a legitimate yacht chartering business. Mr. Minchella, as can be seen from the list of ventures above and in the example provided below, acted in numerous capacities in Mr. Bellfield's ventures unrelated to the yacht chartering Limited Partnerships.

(ii) Lauderdale Marina and Coastal Cruisers

[291] Lauderdale Marina was another operation of OCGC that was unrelated to the luxury yacht chartering activities. Also related to Lauderdale Marina was Coastal Cruises that OCGC described as a houseboat rental operator. Mary Crocco's ex-husband, Rick Crocco, was Manager of Lauderdale Marina.

[292] Ms. Crocco claimed to have worked at the Lauderdale Marina for approximately three weeks but some of the evidence contradicts this claim. There is evidence showing that she worked to obtain insurance for Lauderdale Marina while at OCGC. There is also evidence of her working on Lauderdale Marina's kitchen while working at Fabu D'Or, and evidence of her assisting with obtaining a roof contract for Lauderdale Marina. There were also a number of instances where Ms. Crocco's corporate credit card was shown as being used for Lauderdale Marina, including an auto rental at Midland Ontario, dining in Gravenhurst, and petrol expenses. In addition, in a letter from Mary Crocco to all OCGC staff, Ms. Crocco bore the title "General Manager, Coastal Cruisers", and advised staff to keep the Coastal Cruisers reservation line free.

[293] Ms. Crocco asserted in her testimony that she spent 90% of her time working for OCGC on Fabu D'Or. It is questionable if this is a fair representation of her time allocation. The evidence shows that the percentage of time that her duties were spent on OCGC activities unrelated to yacht chartering operations was likely higher. Indeed, the evidence shows that Ms. Crocco was not unlike other OCGC employees whose time was preoccupied with a variety of OCGC schemes and ventures, such as marketing and promotion of the Limited Partnerships, and most significantly, the development of the (illusion of) yacht chartering operations.

[294] Regarding Coastal Cruisers, this is another example of non-yacht chartering Limited Partnership-related work that Mr. Minchella did, but was not excluded from the Appellants' calculations of the $13–$14 million that they claim was spent on establishing a yacht chartering business. For example, Mr. Minchella spent some of his work time acquiring a houseboat with Mr. Bellfield, that they both co-owned and was used by Coastal Cruisers.

H: RELEVANT LAW AND ANALYSIS

1. Did the three Limited Partnerships constitute a source of income pursuant to sections 3 and 4 of the Income Tax Act and capable of suffering a loss under sections 3, subsection 9(2), and section 96?

a) Is there a Source of Income for the Purposes of the Income Tax Act?

[295] The Appellants claim that their Limited Partnerships were engaged in business and constitute a source of income for the purposes of the *Act*. They argue that separate and apart from any fraudulent activities perpetrated by Mr. Bellfield et al. in relation to OCGC, the yacht chartering business itself was not a fraud. The Appellants contend that of approximately $15 million of funds that the investors provided to OCGC, $13–14 million were spent on goods and services for the purposes of creating a yacht chartering business. As stated by the Appellants in their Final Submissions:

> 158. In the present appeals, the rights of the Limited Partnerships with respect to OCGC were, at least in part, respected. The Limited Partnerships entered into agreements whereby they were entitled to various goods and services which were to be provided by OCGC, and they received many of these services, including all of the goods and services described in Appendix 1 hereto. The Appellants, in other words, … received, at least in part, what they bargained for.
>
> 159. […] the Appellants in the present Appeals were a part of a business that undertook significant efforts in order to generate a profit. While no profit ever materialized, the fact that the process was started is sufficient. In other words, the fact that the majority of partnerships never received a boat is not determinative of whether or not the losses were incurred while a business was being carried on.
>
> 160. Significant money was paid to arms-length third parties in order to begin establishing the appropriate infrastructure required for the yacht chartering business.
>
> …
>
> 162. Similarly, significant money was also spent on the hiring and training of staff to operate OCGC, the Starlight Charters office in Toronto, the bases in St. Lucia and Monte Carlo and the OCGC owned yacht manufacturing factory in Rochefort, France for the production of the yachts themselves. Fantaseas was marketed at tradeshows, in magazines, in newspapers, and to individuals who visited Starlight Charters' Toronto office.
>
> 163. As explained above, there is no revenue benchmark that OCGC had to satisfy in order for its business to be legally recognized. Further, that the company failed to earn a profit is immaterial when determining whether the Limited Partnerships were ever in business, or whether the business commenced despite fraudulent conduct.

[296] The Appellants also assert that the Limited Partnerships should be evaluated on the basis that they employed a franchise business model. OCGC's activities and expertise developed over the period of time in question, and the development of certain goods and services accrued to the benefit of all the Limited Partnerships, who in essence had bargained for the development of substantively the same yacht chartering-related goods and services.

[297] The Appellants further argue that the Respondent has the onus to prove that the yacht chartering business was a fraud from beginning to end because that assumption was not made by the Minister during the assessment period. The Appellants' position on this matter is that the CRA simply concluded that because Mr. Bellfield committed a fraud, it followed that the Limited Partnerships were a fraud. The Appellants assert that the CRA never considered whether the Limited Partnerships themselves operated a business, separate and apart from the fraud, or in co-existence with the fraud. They claim that the CRA never evaluated the 13 to 14 million dollars spent on building a yacht chartering business, nor interviewed third party suppliers and subcontractors because the tax authorities always maintained the position that the Limited Partnerships were merely a fraud. This was done in order to be consistent with the criminal charges pursued against Mr. Bellfield et al. The Appellants emphasize that because the assumption was not made on assessment, the Minister has the burden to prove that there was a fraud from beginning to end, and has not done so.

[298] The Respondent argues that the Limited Partnerships were a fraud from beginning to end, and as such, cannot constitute a business and thus, are not a source of income under the *Act*. They assert that the evidence shows overwhelmingly that from day one, the Appellants were fraudulently induced to invest in the Limited Partnerships based on material misrepresentations, and the Limited Partnerships never amounted to anything more than a fraud throughout their existence.

(i) The Law

The Source Doctrine

[299] For the purposes of the *Act*, in order for income to be taxable it must come from a source.[23]

[300] Section 9 of the *Act* describes the computation rules to determine what constitutes a taxpayer's income or loss from a business or property, as follows:

> 9. (1) Subject to this Part, a taxpayer's income for a taxation year from a business or property is the taxpayer's profit from that business or property for the year.
>
> (2) […] a taxpayer's loss for a taxation year from a business or property is the amount of the taxpayer's loss, if any, for the taxation year from that source computed by applying the provisions of this Act respecting computation of income from that source with such modifications as the circumstances require.

[301] A business is defined broadly under subsection 248(1) of the *Act*, which simply states that a business includes "a profession, calling, trade, manufacture or undertaking of any kind whatever and, […] an adventure or concern in the nature of trade" and excluded from that definition is income from an office or employment. This definition is not exhaustive and it is therefore necessary to also refer to the case law.

[302] In *Stewart*, the Supreme Court rejected the reasonable expectation of profit test and adopted a common law definition of business. The Court explained the hallmark features needed to identity a source of business income under the *Act*, as follows:

> [50] It is clear that in order to apply s. 9, the taxpayer must first determine whether he or she has a source of either business or property income. As has been pointed out, a commercial activity which falls short of being a business, may nevertheless be a source of property income […]
>
> [51] Equating "source of income" with an activity undertaken "in pursuit of profit" accords with the traditional common law definition of "business", i.e., "anything which occupies the time and attention and labour of a man for the purpose of profit": *Smith*, *supra*, at p. 258; *Terminal Dock*, *supra*. As well, business income is generally distinguished from property income on the basis that a business requires an additional level of taxpayer activity: see Krishna, *supra*, at p. 240. As such, it is logical to conclude that an activity undertaken in pursuit of profit, regardless of the level of taxpayer activity, will be either a business or property source of income.
>
> …

[23] See section 3 of the *Act*.

[303] The question, therefore, in analyzing whether a source of business income exists, is to determine whether the activity is undertaken in pursuit of profit. If there is a sufficient level of clearly commercial activity, it constitutes a source of business income. If the level of activity is less than that associated with a business, it may still qualify as a source of property income. The inquiry is best summarized in the following excerpt from *Stewart*:

> [61] … whether or not a taxpayer has a source of income from a particular activity is determined by considering whether the taxpayer intends to carry on the activity for profit, and whether there is evidence to support that intention. As well, where an activity is clearly commercial and lacks any personal element, there is no need to search further. Such activities are sources of income.

Can a Fraud Constitute a Source of Income/Business?

[304] In *Hammill v. Canada*,[24] the Federal Court of Appeal considered the deductibility of expenses that the taxpayer paid to an agent in efforts to sell certain precious gems. The Tax Court judge had concluded that the expenses were not deductible under paragraph 18(1)(*a*) because the taxpayer was "the victim of a fraud, from beginning to end",[25] and as such, the expenses could not be found to relate to a business under the *Act*. The Tax Court also went on to find that the expenses claimed were not reasonable in the circumstances, within the meaning of section 67 of the *Act*.

[305] In affirming the Tax Court of Canada's decision, the Federal Court of Appeal emphasized the trial judge's factual finding that the fraud began from the very inception of the transactions in question. Justice Noël, writing for himself, Justice Létourneau, and Justice Nadon, summarized the key factual findings at trial, a portion of which is excerpted below:

> [26] At the very beginning of his analysis, the Tax Court Judge makes a finding of fact which has gone largely uncontested and which, in my view, is fatal to the appellant's case on the first issue. He said (paragraphs 114 and 115):
>
> > [114] As far as the Court is concerned there is no question that the Appellant was the victim of a substantial fraud from the beginning to the end. The Court is satisfied that this fraud commenced when the Appellant was contacted about profits to be made from buying and selling gems and this fraud continued with the purported efforts of the perpetrators to sell the gems. …

[24] *Hammill v. Canada*, 2005 FCA 252 [*Hammill*].
[25] *Hammill v. Canada*, 2004 TCC 595 [*Hammill*] at 15.

...

> The Tax Court Judge later reiterated that "... the whole transaction was a fraud from its inception" (paragraph 127).
>
> [Emphasis in original]

[306] The Federal Court of Appeal went on to affirm that, so long as the evidence supported the conclusion that there was a fraud from beginning to end, it is not possible for a business to exist, and there is therefore no source from which expenses can be deducted for tax purposes. The Court stated:

> [27] This finding by the Tax Court Judge that the appellant was the victim of a fraud from beginning to end, if supported by the evidence, is incompatible with the existence of a business under the Act. This is not a case where the Court must have regard to the taxpayer's state of mind, or the extent of a personal element in order to determine whether a certain activity gives rise to a source of income under the Act (*Stewart, supra, Tonn v. The Queen, 96 DTC 6001 etc.*). Nor is this a defalcation case of the type described in *Parkland Operations, supra*; *Cassidy's Limited, supra*; *Agnew, supra*; and IT-185R, where a business is defrauded by an employee or a third party, and the issue becomes whether the resulting loss is reasonably incidental to the income-earning activities.
>
> [28] A fraudulent scheme from beginning to end or a sting operation, if that be the case, cannot give rise to a source of income from the victim's point of view and hence cannot be considered as a business under any definition […]
>
> [Emphasis added]

[307] In the year following the *Hammill* decision, the Federal Court of Appeal again had the opportunity to consider the deductibility of certain expenses in the context of fraudulent activity in *Vankerk v. The Queen*.[26] In that case, the taxpayers claimed deductions relating to their investments in partnerships whose business would be the production of sound recordings.

[308] Before the Tax Court of Canada,[27] the parties filed a Statement of Agreed Facts that characterized the partnerships as entirely fraudulent. Key agreed facts summarized by Justice Little included:

> [2] […]

[26] *Vankerk v. The Queen*, 2006 FCA 96 [*Vankerk*].
[27] *Vankerk v. The Queen*, 2005 TCC 292.

a) Commencing in 1987, Mark Allan Eizenga and at a later date, James Sylvester hatched a scheme to defraud investors and the Government of Canada of millions of dollars.

b) The scheme involved the creation of multiple putative "partnerships". These "partnerships" were not genuine partnerships because neither Eizenga nor Sylvester as the principles of the managing general partner operating as Advanced Business Opportunities ever had the intention to carry on business in common with the investors. Rather, the intention of Eizenga and Sylvester was to defraud the investors and the Government of Canada of money.

c) Eizenga, Sylvester and others represented to the investors that the "partnerships" would carry on the business of producing sound recordings, records and the like. This representation was false and known by Eizenga and Sylvester to be false.

d) In fact, the bulk of the monies collected as investments in the various partnerships were simply re-routed into the pockets of Eizenga, Sylvester, their companies and nominees. The small amount of money which was not diverted to Eizenga, Sylvester and others was spent on window-dressing to give the appearance of business activities by the partnership when there, in fact, was none.

e) Eizenga and Sylvester marketed the "partnerships" as vehicles, which would produce substantial tax savings. Eizenga and Sylvester also promoted the "partnerships" as high-risk record production businesses.

f) Much of the investment in the "partnerships" was done through obligations to make cash payments and enter into promissory notes, which obligations were either not honoured or where (*sic*) only when tax refunds were generated.

g) The tax refunds of the investors were generated by the fraudulent statements generated by Eizenga, Sylvester and their nominees to create an apparent entitlement to the deduction of losses and accrued interest by the investors.

h) The refunds thus generated were then re-circulated to Eizenga, Sylvester, their companies and nominees or pocketed by the investors.

i) The Minister later disallowed the various deductions claimed by the investors on the basis that, inter alia, the amounts claimed had not been incurred for the purpose of earning income from a business or property.

...

v) None of the so-called partnerships carried on their designated business and none was capable of carrying on their designated business. To the extent any activity was carried on by the so-called partnerships, the activity or activities were designed as window-dressing to disguise and conceal the sham activities and intentions of Eizenga, Sylvester and their corporations. None of these activities were for the benefit of the unit holders. Quite the contrary, the activities were solely for the benefit of Eizenga, Sylvester and their corporations.

[309] Justice Little went on to conclude that the only activity associated with the "partnerships" was the fraudulent activity carried out by the masterminds of the scheme. There was no business carried out in common, no view to profit, and therefore no valid partnerships as defined under section 2 of the *Partnerships Act of Ontario.*[28] Justice Little noted that the parties both conceded as much in the Statement of Agreed Facts.

[310] Justice Little considered whether the Appellants were involved in a business within the meaning of the *Act* that would give rise to the ability to deduct their expenses pursuant to paragraph 18(1)(*a*). The Court noted, amongst other pertinent facts, that the partnerships were never formed, and that the amounts claimed, relied on fraudulent statements made by the perpetrators. In concluding that no business existed but rather an entirely fraudulent scheme, the Court stated, in part:

> [26] On the facts contained in the Statement of Agreed Facts and on the facts presented to the Court I have concluded that the expenses that were claimed were not expenses within the meaning of paragraph 18(1)(*a*) of the *Act* because the so-called expenses were "window dressing", "phony or fictitious expenses".
>
> [27] I have therefore concluded that on these facts there was no business being carried on. This was nothing more than a fraudulent scheme perpetrated by Eizenga and Sylvester.
>
> [28] In reaching this conclusion, I have referred to the following Court decisions:
>
> In *Tonn et al. v. R.*, 96 DTC 6001 the Federal Court said that there must be a possibility of earning income or the expense is not deductible.
>
> In *Moloney, Young, Russell and Fullard v. The Queen*, 89 DTC 5099 the Federal Court said that a scheme has no real business purpose behind it if it consists of nothing more than the circular movement of paper and return generated solely from income tax deductions. (Note - This decision was affirmed by the Federal Court of Appeal in *Moloney v. The Queen*, 92 DTC 6570.
>
> In *Stewart v. Canada*, 2002 SCC 46 (CanLII), [2002] 2 S.C.R. 645 the Supreme Court of Canada said at page 679:
>
> > ...whether or not a taxpayer has a source of income from a particular activity is determined by considering whether the taxpayer intends to carry on the activity for profit, and whether there is evidence to support that intention.
>
> [29] In this situation there was no business activity carried on by any of the three Partnerships.

[28] *Partnerships Act of Ontario*, R.S.O. 1980, c. 370, s. 2.

[Emphasis in original]

[311] Finally, Justice Little went on to conclude that the $280,087 and $344,003 in interest expenses claimed by each of the Appellants respectively were based on amounts paid for "so-called promissory notes".[29] The claims were not deductible under paragraph 20(1)(*c*) of the *Act* because there was no evidence that the interest was actually paid, and there was no business related to the interest expenses claimed as required under paragraph 20(1)(*c*). Finally, Justice Little concluded that pursuant to section 67 of the *Act*, the losses claimed were not reasonable in the circumstances, stating:

> [35] In this situation Willem Vankerk paid cash of $92,275.00 and claimed losses of $899,066.00 plus interest of $344,004.00. Elsbeth Vankerk paid cash of $109,650.00 and claimed losses of $750,060.00 plus interest of $280,087.00. The magnitude of the cash paid compared to the losses that were claimed is not reasonable in the circumstances.

[312] In upholding Justice Little's decision on appeal, the Federal Court of Appeal noted that all parties agreed that the appellants were victims of a fraud. Justice Sharlow, writing for herself, Justice Evans, and Justice Malone, went on to emphasize that the key fact was that there was no business and where there is no business, there can be no deductible business expenses. Justice Sharlow wrote, in part:

> [2] It is common ground that the appellants were defrauded, and that none of the putative partnerships carried on any business. There are only trails of fictitious documents created by Mark Allan Eizenga and James Sylvester to make it appear that the partnerships existed and made business expenditures, when in fact they did not. It is argued for the appellants that they honestly believed that they had invested in partnerships that were carrying on business, that they were presented with business plans that appeared to be reasonable, and that they relied reasonably on reputable lawyers, accountants, investment advisers and bankers. It is also argued that the appellants are innocent victims of a scheme that was intended to defraud them as well as the Government of Canada, and that it is not fair that they should bear all the loss.
>
> [3] All of these arguments miss the point. This is not a case in which the deductibility of a loss can be saved by evidence that the appellants acted with due diligence. This is not a case of a business that suffered losses because it was ill conceived or poorly managed, and the tax authorities are second guessing the business acumen of a taxpayer. This is a case where, in fact, there was no business. There were no business expenses. There is no factual foundation for any of the deductions claimed by the appellants. These appeals will be dismissed with costs.

[Emphasis added]

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[29] *Vankerk* at para 31.

[313] A number of cases after the Federal Court of Appeal's decisions in *Vankerk* and *Hammill* cited the legal principle that if taxpayers are the victim of a fraud from beginning to end, their expense claims are barred from deductibility because there is no source under the *Act*. For example, in *Lefebvre v. The Queen*,[30] Justice Lamarre asserted that expenses used to finance a tax scheme are not deductible under the *Act*. The Court determined, amongst other conclusions, that the rental losses in question were not deductible because they related to expenses that were never incurred to earn income, but rather to finance the scheme. Justice Lamarre wrote:

> [9] Moreover, the tax refund turned over to Mr. Avard cannot be a deductible expense for the Appellants, as their agent is claiming. The sum handed over by the Appellants to Mr. Avard was not used to earn income from a property; it was used to finance the tax scheme organized by Mr. Avard. Such an expense cannot be deductible, even if the Appellants were victims of tax fraud (see *Vankerk v. The Queen*, … 2006 FCA 96, [2006] F.C.J. No. 371 (QL)).

[314] By way of another example, in *Heppner v. The Queen*,[31] Justice Woods identified the legal principle that losses are not deductible if they were paid and lost in a fraudulent scheme. She stated:

> [4] The position of the Crown is that there is no source of income from which the appellant can claim a deduction because the money was lost in a fraudulent scheme.
>
> [5] The legal principle that the Crown relies on is not in dispute, and has been articulated by the Federal Court of Appeal in several recent decisions: *Hammill v. The Queen*, 2005 D.T.C. 5397; *Vankerk v. Canada*, 2006 FCA 96… and *The Queen v. Nunn*, 2007 D.T.C. 5111.

Justice Woods went on to conclude that the evidence pointed to the entire transactions being a scam, and therefore, without a sufficient connection between a genuine business and the losses claimed, the losses were barred from deductibility.

The Co-Existence of a Fraud and a Business

[315] The Appellants argue that even if it is found that there was fraud, a fraud and a business can co-exist and still constitute a source. Key examples of the case law

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[30] *Lefebvre v. The Queen*, 2006 TCC 247.
[31] *Heppner v. The Queen*, 2007 TCC 667.

that the Appellant cites in support of this argument are examined below, with the grounds upon which the Court came to its conclusion emphasized.

[316] In *Agnew v. The Queen*,[32] Justice O'Connor heard appeals that were representative of approximately 138 appeals by taxpayers whose investments provided virtually identical fact sets. The promoter of the tax advantageous investments, as well as the service provider in the investment opportunity misappropriated funds. Despite these misappropriations, Justice O'Connor allowed the taxpayers' appeals because there was evidence that sufficient commercial activity was carried out. The Court summarized the main reasons for allowing the appeals as follows:

> [123] In my opinion the appeals are to be allowed with costs for the following principal reasons:
>
> (1) There was clearly a commercial activity being carried on. Embryos were being bought, imported and transferred into host cows with a view to producing calves having the same meat quality as that of the donors of the embryos. Were it not for the defalcations the bulk of the evidence is that the plan would have succeeded.
>
> (2) There was an operating farm where activities took place. The activities may not have been, on the grand scale contemplated in the OM but there is no doubt the activities were carried out.
>
> (3) The investors relied on the personalities involved namely, the lawyer Kennedy, who had a good reputation, Ernst & Young, the Coles, the putting forth of the plan by Costello, a well-known investment counsellor, the involvement of AIC. Although the involvement of these various entities and persons may not have been as extensive as it should have been it appears however that the investors were impressed by the persons involved. It is also a fact that at least Watters carried out extensive research on the concept and made inquiries of several bodies which even Betteridge stated were the correct bodies to review. Watters apparently decided that, at first, he did not like the investment but consequently he changed his mind and went ahead with it.
>
> (4) The Appellants paid for their investment with their own monies. Even though the monies were borrowed from National Trust Company they were borrowed on the security which the Appellants placed on their homes or some other assets. Thus, effectively, they were putting up their own assets/cash to make the investment.
>
> (5) The operation was to be carried out without any financing by the partnership or the corporations later involved.
>
> (6) The plan was carried out over a long term, was extensive and thorough and included eight material contracts. It attracted 135 investors. It was not "fly by night".

[32] *Agnew v. The Queen*, 2002 CanLII 1030 (TCC).

> (7) It is well established that a desire to obtain a tax advantage or loss does not automatically stigmatize the investment and thus render it simply as a tax evasion scheme even though a business is contemplated.
>
> (8) Most importantly there was no personal benefit or element involved in the investment. In *Stewart v. Canada*, [2002] S.C.J. No. 46, a decision of the Supreme Court of Canada issued after the hearing of these appeals, a thorough analysis is made of the concept of reasonable expectation of profit.
>
> [Emphasis added]

[317] As can be seen from the excerpts above, considerable weight was placed by the trial judge on the existence of commercial activity that would have led to a successful enterprise but for the misappropriations of funds. In addition, the Tax Court of Canada also emphasized, amongst other factors, the existence of an operational site where the activities took place, the appellants' provision of funds secured by their own assets, and the fact that no financing was to be offered by the partnership or corporations.

[318] In *Hayter v. Canada*,[33] the Appellant invested in a plan involving the purchases of a large volume of laptops that would then be resold. Ultimately the laptops were not delivered and the taxpayer was a victim of fraud. The Tax Court of Canada rejected the Minister's argument that there was no business, with the Court emphasizing that although the laptops were never delivered, they were purchased. Justice Pizzitelli distinguished the facts in *Hayter* from those in the *Vankerk* as follows:

> [27] The Respondent has taken the position that since the transaction was never completed, i.e., the laptops were never delivered, that same is evidence there was no business and relies on *Vankerk v. Canada*, 2006 FCA 96 […] In that case, however, the investors purchased units in partnerships that were found not to have carried on any business activity, with their investments siphoned off by the two individuals who perpetrated a scheme to defraud investors and Government by soliciting investments in fake partnerships. In paragraph 3 of the appeal, Sharlow J.A. stated:
>
> > 3 … This is a case where, in fact, there was no business. There were no business expenses. There is no factual foundation for any of the deductions claimed by the appellants. …
>
> [28] In the case at hand, the funds were not being used to invest in a purportedly existing partnership. There was no partnership with SCQ or those behind it. The funds were

[33] *Hayter v. Canada*, 2010 TCC 255.

> advanced to a joint venture partner who paid the funds for the acquisition of laptops and did not misappropriate them.

[319] Justice Pizzitelli went on to further distinguish the facts before him from another case, *Kleinfelder v. The Minister of National Revenue*.[34] He emphasized that in the laptop investment, unlike the investment scheme in *Kleinfelder*, the funds were used to purchase the asset that was at the core of the investment scheme, whereas in *Kleinfelder*, the automobiles were never purchased. The Tax Court stated:

> [29] The Respondent also relied on *Kleinfelder v. The Minister of National Revenue*, 91 DTC 913, where the Appellant, who was in the business of buying and selling real estate, agreed to participate in a joint venture with a party and advanced funds to start a business of buying Mercedes automobiles from estates and reselling them at a profit, to be split 50-50. In paragraph 28 thereof, Hamlyn J. stated:
>
> > 28 The transaction of buying the automobiles never took place, marketing never took place and the evidence about how the actual business was to be carried on was vague and imprecise. The infusion of capital by the appellant was to start the business but that business operation never started. The moneys were not expended by the partnership for the purpose of gaining or producing income in that, the other partner Mr. Gee misdirected the funds.
>
> [30] This case is distinguishable from the *Kleinfelder* case above in that the funds advanced to the joint venture were in fact paid towards the purchase price of the laptop computers and were not misdirected by Mr. Solleveld. The joint venture, in fact, took all steps to meet its obligations to acquire the laptop computers and the only misappropriation was by the Seller or its underlying principals. There was also correspondence and agreements evidencing the terms of the purchase, notwithstanding that they changed from time to time as part of the Seller's scheme to extract a higher and higher purchase price.
>
> [Emphasis added]

[320] In *Johnston v. Canada*,[35] the taxpayer claimed losses amounting to over $230,000 relating to his attempts to start yacht charter operation in the Virgin Islands. The Appellants emphasize that "the efforts undertaken by the appellant in the *Johnston* case pale in comparison to the activities undertaken by OCGC on behalf of the Limited Partnerships".[36] In *Johnston*, however, the taxpayer was found to be a credible witness who purchased a yacht and signed a charter management agreement with a Virgin Islands company, amongst other substantial efforts. Justice Bell rejected the Minister's arguments that the Appellant had no reasonable expectation of

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[34] *Kleinfelder v. The Minister of National Revenue*, 91 DTC 913.
[35] *Johnston v. Canada*, [1998] T.C.J. No. 63.
[36] Respondent's Final Submissions at para. 157.

profit, and determined that the taxpayer undertook extensive efforts and was a victim of bad circumstances. In concluding that the losses were deductible, the Court stated:

> [26] The Appellant was a wholly credible witness. I accept his evidence. He has been and is an entrepreneur who believes in instituting business enterprises and pursuing them or abandoning them in the absence of a conviction that they will succeed. The evidence supports this entrepreneurial spirit and activity. It points clearly to his success in establishing and continuing Custom.
>
> [27] It is hard to imagine that he could have done more to ensure not only a reasonable but a thorough examination of the yacht business he was seeking to enter. The evidence is clear that he consulted with experts with respect to the boat and with respect to the type of operation and with respect to other matters where he turned to experience for assistance. It does not militate against his business acumen that he encountered difficulties in an environment where it appears that not only were business ethics ignored but fraud was practiced. He encountered problems both from man and from nature which could not be foreseen. It might be said that he was extremely unfortunate with regard to a number of the events described above. However, it is clear to me that this man set out in the yacht charter business with the purpose of succeeding in turning it to account in an economic way. The Reply to the Notice of Appeal stated that the Appellant, before starting the "Activity ... prepared no business plan to determine if it would be profitable." That is clearly incorrect as palpably demonstrated by the Appellant's evidence and the admissions of the tax department's auditor.

The Federal Court of Appeal in *Johnson*

[321] In *Canada v. Johnson*,[37] the Federal Court of Appeal recently had the opportunity to reconsider the appropriate tax treatment in the context of a fraud. Ms. Johnson had invested in what turned out to be a Ponzi scheme. Unlike many of the other investors however, she profited from her investment without knowing that the proceeds she collected came from the funds provided by the many other investors who ultimately lost their funds. The Tax Court of Canada determined that the income was not taxable in her hands because, based on *Hammill*, a fraudulent scheme cannot constitute a source of income.

[322] Justice Woods' decision was overturned on appeal. The Federal Court of Appeal held that because Ms. Johnson's contractual rights were respected, her income constituted a source, regardless of whether the funds provided to her came from other investors, and whether she was aware of the source of the funds or not. In concluding that Ms. Johnson's income was taxable, Justice Sharlow, writing for

[37] 2012 FCA 253, leave to appeal dismissed in 2013 CanLII 14327 (SCC), [*Johnson*].

herself, Chief Justice Blais, and Justice Trudel, reviewed *Hammill* and then detailed when a Ponzi scheme may still give rise to an income source, stating in part:

> [43] I do not quarrel with the proposition that a Ponzi scheme involves the shuffling of money and that it will collapse at some point. However, for income tax purposes, income is calculated on an annual basis, not over the entire life of an enterprise. A Ponzi scheme may well be a source of income for some participants during some part of its existence. This case suggests how that could be so. Hypothetically, if Ms. Johnson had made her payments to Mr. Lech knowing that he would use the money to operate a Ponzi scheme, she would have profited exactly as she did in the years in issue in this case, 2002 and 2003.
>
> ...
>
> [46] There are two difficulties with Ms. Johnson's position. The first difficulty is that it is based on a mischaracterization of the basis upon which Ms. Johnson is being taxed. She is not being taxed because she profited innocently from a Ponzi scheme. She is being taxed because she entered into a series of agreements with Mr. Lech to receive a profit on her investments with him, and she received what she bargained for. The fact that Mr. Lech funded her payments with the proceeds of a Ponzi scheme is irrelevant.
>
> [47] The second difficulty with Ms. Johnson's argument is that it is based on an incorrect understanding of the statutory scheme for determining income for income tax purposes. The question as to whether a Ponzi scheme is a source of income to a particular person, whether innocent or not, is a question that must be answered on the basis of the facts relating to that person. In principle, a person who participates in a Ponzi scheme, either as the main operator or in association with others, may be engaged in an undertaking that would be recognized for income tax purposes as a business, even if the business is unlawful. Such a person is taxable on any profits derived from the Ponzi scheme and, depending upon the specific circumstances, may be permitted to deduct any related losses.
>
> [48] It may well be that a victim of a Ponzi scheme is unable to claim any tax relief for the resulting loss. That would be the case if, for example, the circumstances are analogous to those in *Hammill v. Canada*, 2005 FCA 252 (CanLII), 2005 FCA 252. Mr. Hammill was induced to purchase gems for eventual resale, and accumulated a significant inventory. When he decided it was time to sell the gems, he paid a substantial sum of money to a person who promised to facilitate the sale. The promises were never kept, and the gems were stolen. Mr. Hammill claimed a deduction for the amounts paid to facilitate the sale, on the basis that the purpose of the expenditures had been to sell his gems at a profit. It was determined at trial, however, that Mr. Hammill was the victim of a fraud that commenced when he was contacted about the profits to be made from buying and selling gems, and continued with the purported efforts of the perpetrators to sell the gems. This Court confirmed that his expenditures were not deductible because they were not connected to any source of income – or in other words, there was in fact no business even though Mr. Hammill honestly believed that there was. Justice Noël, writing for the Court, summarized this conclusion as follows at paragraph 28 of the reasons:

> A fraudulent scheme from beginning to end or a sting operation, if that be the case, cannot give rise to a source of income from the victim's point of view and hence cannot be considered as a business under any definition
>
> [49] However, the principle upon which Mr. Hammill was precluded from claiming tax relief for his losses is not applicable to Ms. Johnson. Their circumstances are entirely different, not because she profited from her transactions with Mr. Lech, but because her contractual rights were respected. As a matter of law, the fact that Mr. Lech used the proceeds of his unlawful Ponzi scheme to fund the profits he was contractually obliged to pay to Ms. Johnson is not relevant in determining the income tax consequences to Ms. Johnson of her transactions with Mr. Lech.
>
> [Emphasis added]

[323] As set out in *Johnson*, whether a Ponzi scheme gives rise to a source of income is a question determined on its facts, for each taxation year in question. The mere fact that income is earned from a Ponzi scheme, either knowingly or unknowingly, does not preclude the existence of a source. Moreover, a taxpayer who operates a successful Ponzi scheme is likely to earn income, albeit illegally, sourced from the fraudulent activities he or she perpetuates. The key, according to the Federal Court of Appeal, is to determine whether the taxpayer's contractual rights were respected, and whether the taxpayer got what they bargained for.

The Definition of Fraud

[324] For the purposes of those reasons, it is helpful to refer to several definitions of fraud. According to *Black's Law Dictionary*, a fraud is:

1) A knowing misrepresentation of the truth or concealment of a material fact to induce another to act to his or her detriment…

2) A misrepresentation made recklessly without belief in its truth to induce another person to act.

3) A tort arising from a knowing misrepresentation, concealment of material fact, or reckless misrepresentation made to induce another to act to his or her detriment…

4) Unconscionable dealing, esp., in contract law…[38]

[325] *The Dictionary of Canadian Law* defines a fraud as: "[t]he essential elements of fraud are dishonesty, which can include nondisclosure of important fact, and deprivation or risk of deprivation..."[39]

[326] *Black's Law Dictionary* describes a fraudulent misrepresentation as:

> A false statement that is known to be false or is made recklessly – without knowing or caring whether it is true or false- and that is intended to induce a party to detrimentally rely on it. – Also termed fraudulent representation; deceit.[40]

[327] The Respondent also sets out a number of authorities that provide a definition of a fraud in civil matters. They are excerpted in part below:

> 599. The constitutive elements of civil fraud were first laid out in *Pasley v. Freeman*, incorporated into Canadian law in 1909 by the Privy Council's decision in *United Shoe Machinery*, and succinctly summarized by the Alberta Court of Appeal in *Kelemen v. El-Homeira*:
>
> > (1) there must be a false representation of fact;
> > (2) the representation must be made with knowledge of its falsity;
> > (3) it must be made with the intention that it should be acted on by the plaintiff ... in a manner which resulted in damage to him;
> > (4) it must be proved that the plaintiff has acted upon the false statement, and has sustained damage by doing so.
>
> 600. The second element's source in English law is *Derry v. Peek*[829], where negligent misrepresentation (then not actionable) was distinguished from the higher threshold of fraudulent misrepresentation, which constitutes the tort of deceit:
>
> > […] fraud is proved when it is shown that a false representation has been made (1) knowingly, or (2) without belief in its truth, or (3) recklessly, careless whether it be true or false.
>
> 601. *Derry v. Peek* was followed and applied by Canadian case law, most recently by the Supreme Court of Canada in *BG Checo International Ltd.*[830] which also reiterated that

[38] *Black's Law Dictionary*, 9th ed., s.v. "fraud".
[39] *The Dictionary of Canadian Law*, 3d ed., s.v. "fraud".
[40] *Black's Law Dictionary*, 9th ed., s.v. "fraudulent misrepresentation".

> fraudulent misrepresentations could be simultaneously actionable in tort and for breach of contract.[41]

[328] In *Motkoski Holdings Ltd. v. Yellowhead (County)*,[42] the Alberta Court of Appeal referred to some of the citations offered by the Respondent in providing the following summary of the definition of fraud:

> [57] The legal definition of fraud is well established: *Derry v. Peek* (1889), 14 A.C. 337; *BG Checo International Ltd. v. British Columbia Hydro and Power Authority*, 1993 CanLII 145 (SCC), [1993] 1 S.C.R. 12 at pp. 22, 54, 74-5; *TWT Enterprises Ltd. v. Westgreen Developments*1992 ABCA 211 (CanLII), (1992), 3 Alta. L.R. (3d) 124, 127 A.R. 353 (C.A.). There are two branches to it. Both branches are built on a finding that a false or inaccurate statement was made. Under the first branch, fraud is established if the defendant "knew" that the statement was false, and made it with the knowledge or intention that the plaintiff would rely on it.
>
> [58] Under the second branch, it is sufficient if the defendant did not actually know the statement was false, so long as the statement was made recklessly. "Recklessly" in this context means that the statement was made "without caring whether it was true or false". "Recklessly" does not just mean the statement was made with "very great negligence", nor that it was made in a highly risky context, such that the probability of someone relying on the statement to their detriment was enhanced. As Lord Herschell said in *Derry v. Peek* at p. 375, "making a false statement through want of care falls far short of, and is a very different thing from, fraud, and the same may be said of a false representation honestly believed though on insufficient grounds". Under neither branch of the test is it sufficient that the defendant "should have known" the truth, or should have been more careful and made further inquiries; actual knowledge or actual indifference to the truth is required.

(ii) Analysis

A Fraud from Beginning to End

[329] I conclude that the OCGC yacht chartering business was a fraudulent scheme from beginning to end throughout which the investors' contractual rights were not respected. As such, per the Federal Court of Appeal in *Johnson* and *Hammill*, it cannot give rise to a source of income from the Appellant's point of view and cannot be considered a business under any definition. The Appellants argue that the burden regarding certain assumptions is on the Respondent. It is not necessary, however, for this Court to enter into an intricate analysis of whom the burden falls upon to prove or destroy any assumptions that the Limited Partnerships were a fraud from

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[41] Respondent's Final Submissions at 191-192.
[42] *Motkoski Holdings Ltd. v. Yellowhead (County)*, 2010 ABCA 72.

beginning to end. If the onus was upon the Appellants, they have failed to meet it, and if the burden was indeed the Respondent's, she has proven on a balance of probabilities that the contractual rights of the investors were not respected and the Limited Partnerships were a fraud through and through.

[330] The evidence has shown that, within the meaning of the definitions of fraud set out above, the OCGC yacht chartering business was a fraudulent scheme. From the start, Mr. Bellfield and OCGC induced investors to subscribe in the Limited Partnerships by knowingly misrepresenting multiple material facts. Throughout the taxation years in question, Mr. Bellfield and OCGC fraudulently misrepresented the state of the yacht chartering business, the availability of capital and access to financing, the number of yachts under construction, and yacht delivery dates. Dishonesty infiltrated all levels of OCGC's interactions, from its relationship with the investors to its relationships with professionals as well as third parties. These misrepresentations are found in a wide span of OCGC activities and materials, including the yacht chartering promotion material, certificates and representations made to investors, accounting and legal professionals, information provided to banks, newsletters distributed to investors, financial statements upon which the investors relied to claim their losses, the information provided to the CRA, and most importantly, from the beginning, the Offering Memoranda. It is not a situation where a venture morphed into a fraud over time—the fraud was present when the Offering Memoranda was conceived.

[331] OCGC, as the vendor of the Limited Partnership units and as the general partner of each of the 36 Limited Partnerships, and Mr. Bellfield as the sole shareholder, director, and president of OCGC, had complete control of all aspects of the scheme and persistently and repeatedly made material misrepresentations. These falsehoods were of such significance that they go to the very core of OCGC's contractual obligations to the parties involved with the corporation, including obligations undertaken towards investors and yacht builders, as well as assertions made to legal and accounting professionals.

The Amount of Funds Spent

[332] The mere fact that a significant amount of money was spent is not surprising given the enormous scope of the scheme, which originally brought in over 600 investors. A considerable amount of smoke and mirrors are necessary to continue a fraud of such a large scale, aimed at high net worth individuals, and purported to be

creating a luxury yacht chartering business at the highest end of a not yet accessed charter market. In fact, spending much of the investor money coming in to perpetrate the illusion of a successful business is the hallmark of a Ponzi scheme.

[333] Further, the evidence does not show that the cited $13–14 million was in fact spent on activities relating specifically to a yacht chartering business. Some of those funds were spent on OCGC activities that were not related to the Limited Partnerships, such as payments to employees who also worked on other OCGC endeavours. Most of those funds were spent by OCGC on marketing and promoting the Limited Partnerships as tax shelter investment opportunities and creating the smoke and mirrors necessary to do so. Such expenses were not incurred for the purpose of building a yacht chartering business but rather in this case were the costs of perpetuating the fraud. Other portions of the funds were used by Mr. Bellfield for his personal benefit, including the eventual transfer of the title for the S/Y First Impressions from OCGC to Tina Bellfield.

[334] Having professionally appointed offices and premises to impress investors or to utilize the same presentations to investors are all part of the back-drop and scenery to perpetuate a Ponzi-like scheme. The entire Fantaseas concept was all part and parcel of the ever-growing factual background necessary to attract and convince investors to buy into the tax gimmick presented and sold by Mr. Bellfield. This included the establishment and operations in the Caribbean, the development and establishment of manufacturing facilities, including prototypes, the establishment of the commissary concept and the promotional activities. Furthermore, the attempts to utilize prominent individuals for promotional activities were carried out for the purpose of maintaining the illusion of legitimacy. Examples include: a) Sparkman & Stephens for yacht design; b) yacht manufacturers such as Mr. Dufour at Maxi-Yacht, Chantier Yacht France and Dynamique; c) Jacques Pepin as the designer and developer of menus (at a certain point, against his will); and d) having the S/Y Gable christened by Prince Albert of Monaco. Mr. Bellfield used professionals to develop fraudulent financial statements and prospectuses, all for the purpose of gaining the air of legitimacy. Most professionals were caught up in the whole concept because they were making professional fees and commissions on sale of units in the Limited Partnerships.

[335] As was explained above in identifying OCGC's many misrepresentations, at least $16 million would have been required merely to buy the yachts promised to the 16 Limited Partnership by the end of 1985. An additional minimum of $20 million

would have been needed for the yachts owed to the remaining Limited Partnerships in which units were purchased, making a total of $36 million required merely for the acquisition of yachts. This figure does not include any soft costs related to yacht acquisition. More significantly, this $36 million estimate does not include the millions of dollars that would have been required to set up, market, and manage the genuine yacht chartering business promised by OCGC. The scope of the fraud perpetuated here was so extensive that the number of yachts actually delivered and charters actually undertaken are strikingly trivial in their proportional insignificance. Based on the evidence before the Court, it is indisputable that the portion of the $13–14 million actually spent on Limited Partnership related activities was anything more than money spent on elaborate window-dressing to perpetuate the fraud.

[336] The Appellants state that the sheer magnitude of the expenses can only signify that the Limited Partnerships reached the state of being in business. I regret to have to repeat myself, but this was not a smash and grab robbery; this was a sophisticated, planned, and well-orchestrated Ponzi-like scheme which grew in size and scope as more people were duped by the illusion of the legitimacy of OCGC's operations. No doubt there would have come a point in time that the Ponzi-like scheme would have collapsed, but the money spent was necessary for Mr. Bellfield to maintain the illusion of legitimacy. Without spending this money, the illusion of legitimacy would have disappeared rapidly and the Ponzi-like scheme would have collapsed.

Mr. Bellfield Benefited from Fraud

[337] Certain funds cannot be traced but it appears reasonable to conclude from the evidence that Mr. Bellfield appropriated some funds for his own benefit. For example, The S/Y Garbo was sold as part of financing Maxi-Yacht International, which constructed three yachts for OCGC: the S/Y Gable, the Demoiselle, and Rocco Jr. None of these three yachts were ever acquired by a Canadian Limited Partnership. Michel Dufour's affidavit evidence states that two of the yachts, the Demoiselle and Rocco Jr, were sold to French Limited Partnerships. As a result of the sale, OCGC France received commissions of approximately 10,000,000 FF. He further states that Mr. Bellfield as the majority shareholder controlled OCGC France directly or indirectly, and that most of the funds used to build the Demoiselle and Rocco Jr. yachts came from OCGC in Toronto. While Mr. Dufour was never cross-examined on this evidence because he is deceased, I found his evidence to be sufficiently reliable and necessary for admission at trial in affidavit form, under the principled exception to hearsay. With regards to Mr. Dufour's evidence, I believe it to be

reliable and have probative value. First, the evidence was given by videotape, second, it was under affirmation, and third, there was no apparent reason or motive for Mr. Dufour to give evidence of anything that was less than truthful. In addition, Mr. Dufour was an integral part of the purported construction of the Fantaseas concept yachts, and was certainly in a position to speak to the issues at which his evidence was directed. His evidence appears to be corroborated to some extent by the evidence that is before the Court, albeit on a collateral or indirect basis. Having said the foregoing, I accept Mr. Dufour's evidence on his interactions with Mr. Bellfield and OCGC, as well as the operations of Maxi-Yacht. There was no counter-evidence provided as to any points of his evidence that may have been questioned by the Appellants, in particular where the funds of those were directed.

[338] The Appellants argue that Mr. Bellfield must have had the intention for at least a portion of the business to be genuine, because he spent almost all of the investor money coming in, and much of it on Limited Partnership related activities. Repeated and persistent material misrepresentations and the failure to meet contractual obligations do not cease to be categorized as fraud merely because the scheme may not have left the fraud artist(s) with a lot of cash in pocket after paying all the expenses to maintain the fraud. It is also clear from the evidence that various contractual obligations undertaken with third parties in furthering the illusion of a yacht chartering business were undertaken without regard to cost nor long-term ability to pay. It is apparent that in this case, Mr. Bellfield likely hoped to keep the scheme going for significantly longer than it did.

[339] This is most definitely not a story of a businessperson with a great vision whose failings led him to perpetuate some fraudulent acts while still attempting to build a genuine business. The misrepresentations are too significant early on; the falsehoods too constant and prevalent. Mr. Bellfield was a fraud artist from the start.

Mr. Bellfield was a mastermind

[340] Mr. Bellfield used his personality, communication skills, and ability to convince others. He traded favours with lawyers, accountants, promoters, and prominent persons to create this illusion. Once he created the foundation for the establishment of the Limited Partnerships and the incentive for persons who would have the wherewithal to bring on investors, i.e. accountants, lawyers, and individuals

such as Mr. Franklin, the scheme took on a life of its own because of the attractive nature of the investment as a tax gimmick.

[341] According to the Appellants, from 1984 to 1991, Mr. Bellfield employed at least 68 individuals excluding independent contractors and outside individuals at a cost of $1.6 million. It was acknowledged that some were working on other OCGC interests, but the Appellants assert that the majority were working on creating the luxury yacht chartering business. I have found that the modus operandi of Mr. Bellfield was to commit a fraud from beginning to end. This fraud began with only two people—Mr. Bellfield, and his wife Tina. Later, it included Mr. Minchella and Mr. Bellfield's sister-in-law, Ester Palmer. As time went on, more Limited Partnerships were marketed, more Limited Partnership were developed, more investors subscribed, more promises and commitments were made and larger operations were necessary. All of this led to more personnel being required. Some of the personnel recognized the fraudulent nature of the activities and no longer wanted to be involved, i.e. Mr. LeGlatin and Mr. Garthson. Others did not have the capacity to recognize the fraud either because of their lack of work experience and/or their close relationship to Mr. Bellfield. There is no doubt that the witnesses who felt that the endeavour was a genuine business were clear as to what they believed, but unfortunately, they were duped into participating in an illusion created by Mr. Bellfield. The entire enterprise was a fraud *ab initio*.

[342] Einar Bellfield was a master of deceit and manipulation. The evidence clearly shows that no one other than himself and eventually Mr. Minchella, were fully aware of the scope and magnitude of the Ponzi-like scheme perpetuated. Mr. Bellfield was extremely careful about having employees and associates of OCGC operate in silos, and conducted its affairs on a need-to-know basis. Almost all of the employees operated in their own sphere of work endeavours without knowledge of the endeavours of others. For example, Ester Palmer was primarily focused on marketing and promotion. Mr. Dufour was focused on the development and manufacturer of the yachts. Mr. Marcolongo was focused on Caribbean operations. Jack Moles was focused on acquiring and adapting yachts to the Fantaseas concept. Mr. LeGlatin was much the same as Mr. Moles but in the European context. The only ones really working together were some of the marketing people—Ester Palmer, Stephen Leibtag, David Martin, and Rose Ashworth and they did not even all work together at the same time. On the commissary side, there was Dorothy Louis and Mary Crocco. On the side selling Limited Partnership units, there was David Franklin and Peter Browning, amongst others. None of these individuals had much knowledge of the activities of the other. Only Mr. Bellfield knew how the puzzle fit together, and

he ensured that the containment continued until the very end. Even with regard to his own right hand man Mr. Minchella, he kept him in the dark with lies and deceit.

Claims regarding the CRA's Behaviour

[343] The Appellants throughout the trial made numerous suggestions or innuendos about a variety of aggressive or inappropriate behaviour by members of the CRA. My task is not to assess the conduct of the CRA, but rather to determine whether or not the expenses claimed in these appeals are legitimate. This is not a criminal prosecution. As stated in *Ereiser v. Canada*:[43]

> [31] […] the role of the Tax Court of Canada in an appeal of an income tax assessment is to determine the validity and correctness of the assessment based on the relevant provisions of the *Income Tax Act* and the facts giving rise to the taxpayer's statutory liability. Logically, the conduct of a tax official who authorizes an assessment is not relevant to the determination of that statutory liability. It is axiomatic that the wrongful conduct by an income tax official is not relevant to the determination of the validity or correctness of an assessment.

[344] As I stated, the entire Ponzi-like scheme was set to collapse eventually. The conduct or intervention of the CRA did not turn this Ponzi-like scheme, a fraud from beginning to end, into a genuine business. All the intervention did was instigate the lifting of the veil to reveal the prevalent nature of the fraud.

Lack of Capital and Access to Capital

[345] The Appellants attempted to address the lack of capital or access to capital by arguing that OCGC could have mortgaged the yachts to obtain additional financing. Several witnesses also testified to this effect. While this right might have been available to OCGC, it was seriously limited. The mere existence of a right to mortgage the yachts as the general partner does not vitiate the many misrepresentations that OCGC made to multiple parties that it had capital and access to capital. In addition, any mortgaging of a Limited Partnership yacht could only take place if it was in the best interest of the Limited Partnership. The partners could not sell a yacht without a special resolution. The evidence did not demonstrate that the

[43] *Ereiser v. Canada*, 2013 FCA 20.

Limited Partnerships had any interest in having their yachts mortgaged. Their interest was in having the yacht asset delivered and operational with a yacht chartering business established so that it could offer charters. The investors' tax interests were also in having the yacht delivered so that they could begin claiming capital cost allowance, and in having the expenses charged to the Limited Partnerships, so the tax benefits could flow down to them.

[346] No evidence was provided of yachts being mortgaged or sold in order to access capital in a way that benefited the Limited Partnerships. For example, when the S/Y Garbo was sold to finance a French yacht builder, no information was presented to the S/Y Garbo Limited Partnership about the sale and the proceeds of the sale were not put towards the benefit of the partnership. The Limited Partnership did not allow the sale or disposition of all or substantially all of the Limited Partnerships assets, i.e. yacht, by a special resolution by the Limited Partnership, as required in the Limited Partnership Agreement. The S/Y Garbo was sold because—as was the perpetual pattern of OCGC—capital was needed to meet OCGC's obligations to deliver yachts to Limited Partnerships, and the corporation did not have enough money. The corporation's source for funds was limited to incoming interest payments and small deposits of investors. OCGC sold the S/Y Garbo to a French yacht builder in a scramble to finance an effort to keep the scheme going. Further, there were only three yachts actually built, of which at least one was not suitable for chartering purposes. Mortgaging the few yachts that did exist would have done little to address OCGC's fundamental lack of capital.

Analyzing the Purported "Business Indicia"

[347] The Appellants focused their case on the business indicia, and argued strongly that the presence of business indicia which grew over time showed that they were "in business and continued in business throughout the years under appeal". In a vacuum, the argument is very strong. However, it does not stand to scrutiny.

[348] In order to perpetuate this long-term fraudulent scheme, business indicia had to be developed, presented, and maintained to give the perception of legitimacy. The perception of legitimacy and tax attractiveness appealed to innocent investors and led to upwards of approximately $460,000 per month in cash flow to Mr. Bellfield. Of the business indicia, much of the indicia were short term. For example, besides Mr. Minchella and family members, all employees of OCGC involved were short term employees most of whom were with OCGC for six months to a year. The retaining of

professionals was a similar story, switching accounting and law firms, or using one firm for one transaction and another for a different transaction, so that nobody would really know what was going on. Virtually all contracts for the acquisition or construction of yachts were disasters, except the S/Y Gable, with none of them resulting in title to any yacht passing to any of the 36 Limited Partnerships.

[349] Legitimacy required a corporation in the front end: OCGC. It required an Offering Memorandum, but one without fraudulent material misrepresentations. There was no feasibility study in the front end, no market assessment, no professional workup of an Offering Memorandum, and no capitalization. These are all things that OCGC represented that it had done when contracting with investors. All efforts at building a yacht chartering business could only go so far without a product.

[350] The $13 to 14 million sounds significant and it is significant, however it is not so significant when it is considered in the context of the scale of this fraud. There were 36 Limited Partnerships subscribed, capitalized at approximately $2.5 million each, for a total capitalization of $90 million. By December 31, 1985, commitments had been made to deliver 16 yachts at a minimum cost of a million dollars each. By that date, none had been built and it was not until over a year and a half later that a single yacht was even available for chartering. In order to keep the fraud going, to keep investors coming, and maintain the cash flow, which at one time or another was $460,000 per month plus, money had to be spent on the illusion of a legitimate business.

[351] As time went on, it would take more money to continue the illusion, but the money was not there in the amounts necessary to hold up the fraud. Again, OCGC needed at least $16 million just to build the 16 yachts owed to the first 16 Limited Partnerships by December 31, 1985—this is without consideration of the millions of dollars it would have taken to actually establish, develop, and maintain a head office for a genuine yacht chartering business, develop and promote marketing and advertising to sell the product, keep accounting and legal requirements up to speed, pay commissions, train a full staff for the alleged fleet of 36 yachts, build a genuine functioning commissary, and so on. The monohulls were going to be built in France and the catamarans were going to be built in Picton. All of this was to be done without one nickel of capitalization on the front end, and without any capitalization or funding at any point in time except for the cash deposits by the investors and their monthly interest payments.

[352] The business indicia that the Appellants refer to are simply the window-dressing necessary to perpetuate the fraud from beginning to end on everyone that Mr. Bellfield came into contact with. There is no evidence that supports the intention to carry on any activity for profit as required by the Supreme Court of Canada decision in *Stewart*. This is not a case similar to the Tax Court decisions referred to previously in *Johnston v. Canada*,[44] and *Agnew v. The Queen*,[45] in which sufficient genuine business activities were undertaken. This is a case more akin to *Vankeerk*. In *Vankeerk*, a Statement of Agreed Facts established the fraudulent nature of the scheme and the fact that the Limited Partnerships were not genuine. In this case, the fraudulent nature of the entire scheme is established by the facts set out in the many examples of misrepresentations above.

OCGC bore the Hallmarks of a Ponzi-like Scheme

[353] Separate and apart from being a fraud from beginning to end, the evidence reveals that OCGC's yacht chartering investment was effectively a Ponzi-like scheme with the essential and hallmark characteristics of a Ponzi-like scheme.

[354] The planning and development of the yacht chartering business—whether it was a novel or entrepreneurial or business-like idea or investment—was undercapitalized and underfinanced from the incorporation of OCGC in May 1984. In fact, I would go so far as to say it was never financed and it was never capitalized.

[355] *Black's Law Dictionary* defines a Ponzi scheme as follows:

> A fraudulent investment scheme in which money contributed by later investors generates artificially high dividends or returns for the original investors, whose example attracts even larger investments. · Money from the new investors is used directly to repay or pay interest to earlier investors, usually without any operation or revenue-producing activity other than the continual raising of new funds. The scheme takes its name from Charles Ponzi, who in the late 1920s was convicted for fraudulent schemes he conducted in Boston.[46]

[356] While the yacht chartering business was a modified Ponzi scheme in the sense that it was a Ponzi-like scheme oriented towards creating the illusion of

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[44] *Johnston v. Canada*, [1998] T.C.J. No. 63.
[45] *Agnew v. The Queen*, 2002 CanLII 1030 (T.C.C.).
[46] *Black's Law Dictionary*, 9th ed., s.v. "Ponzi scheme".

substantial tax losses instead of high returns, it was still a Ponzi-like scheme. The investors' funds were the only source of funds, and they were not used to pay returns or repay early investors, but rather, to maintain the illusion of a business so that investors would continue to subscribe, attracted by the opportunity to claim significant losses for tax purposes without investing substantial funds. Just like most Ponzi schemes, the yacht chartering business never had any access to capital, nor consisted of any true operations or revenue-producing activity beyond those required for window-dressing to maintain an appearance of legitimacy.

[357] I make reference to the Respondent's Memorandum of Fact and Law, paragraphs 82–92, which substantiate with the references therein, the fact that the only source of revenue for the yacht chartering businesses were the investors' monthly interest payments and small down payments from some of the investors:

> 82. Minchella claimed that building the boats with investors' interest payments had been the deal right from the beginning.
>
> 83. Bellfield was able to pay Dynamique for the 1984 partnership yacht Garbo on April 4, 1986 because he had the cash inflow from the 1985 investors who were sending in their money at the end of December 1985 and the first few months of this purchase and any additional purchases were predicated on the success of our marketing and sales efforts."
>
> 90. Minchella said another source of funds for Maxi Yachts construction of the Gable was a mortgage put on the Garbo after OCGC sold the Garbo to Maxi Yacht. He agreed that money from one partnership had to be used to meet promises to another partnership but Minchella claimed that OCGC had the right to mortgage the boats.
>
> 91. Minchella claimed that it was the defaults in payments in the 1986 limited partnerships which represented approximately 70% of all of the receivables of OCGC's that kept the 1985 partnerships from getting their yachts.
>
> 92. In fact, investor defaults in later years had nothing to do with OCGC's failure to honour its commitment to even one 1985 limited partnership. OCGC committed in the Offering Memoranda to the construction and delivery in 1985 to the 1985 partnership yachts. Bellfield's Ponzi scheme and his absence of capital from the outset explain OCGC's failure to meet its 1985 commitments, not events occurring after the fact.

[358] In the course of evidence in the trial, during the cross-examination of John Garthson, there was a review of the financing options available to OCGC. They included:

1) Vendor-take back financing;

2) A lending institution advancing money to the investors who would then use the money to buy the units;

3) Pledging of investors' promissory notes to a financial institution;

4) Obtaining third party financing of delivery of goods and services;

5) Manufacturer take on the obligation to fund the construction pending the yacht sales;

6) A combination of options 1 to 5; and

7) OCGC self-finance the yacht development based on interest payments received from the investors, and the mortgage the yachts.

[359] There could be no vendor-take back financing because the vendor was OCGC and the evidence shows that they never had any access to financing nor could they have reasonably expected to have such access. OCGC did not have the credit-worthiness for:

a) Vendor take back financing; and

b) Third party financing.

Manufacturers could not take on the obligation of financing construction because OCGC never met their financial obligations to the manufacturers, or manufacturers went into receivership. The manufacturers in the end were substantially owned, in whole or in part by Mr. Bellfield. Lending institutions could advance money to the lenders to buy the units, but that was an individual investor-by-investor process. The banks would not provide OCGC with financing. The banks instead invited OCGC to

refer investors to them for this purpose. In addition, there was no evidence of pledging promissory notes to financial institutions, but there was evidence of attempts to obtain financing from financial institutions, which was largely unsuccessful.

[360] The evidence discloses that none of the foregoing actions took place, save and except for a) the monthly interest payments by the investors and b) sale of the S/Y Garbo that was only used for the limited purpose of financing Maxi-Yacht International. The bottom line is that there was no financing. Any attempt to obtain financing through *bona fide* financial institutions was a failure at best and the other alleged financing were simply on paper, from companies that Mr. Bellfield controlled.

[361] It is my view that from the beginning, the entire scheme was a fraud upon the Appellants and other investors and as it turned out, a fraud on the CRA. Crucial to perpetrating the fraud in the magnitude carried out by Mr. Bellfield and others in concert with him was having innocent investors on his side. How did Mr. Bellfield achieve getting investors on side? He did so by taking three classic actions in a fraud of this nature:

> 1) The development of a product that was attractive to a target market;
>
> 2) By making representations and commitments to investors in the target market to gain their confidence and investment; and
>
> 3) By concluding contractual relationships with investors to ensure a continuous flow of funds.

He then repeated the foregoing over and over again to new and innocent, hopeful investors.

[362] A review of the evidence clearly shows all of the foregoing:

1) Evidence of the nature of a product and its attractiveness to gullible, hopeful, and innocent investors who might even be considered greedy, i.e. Offering Memoranda;

2) Evidence of representations and commitments to gullible, hopeful, and innocent potential investors. Representations and commitments are fundamental enticements to the development of a contractual relationship with the investors, i.e. false documents provided prior to and at closing;

3) Evidence of a contractual relationship created with each individual investor with all the appropriate documentation to establish what at first glance would appear to be a solid contractual relationship but in essence is smoke and mirrors for a game of masquerade with the investors and to all who might enquire or look into the bona fides of the scheme, i.e. all the subscription-related documents;

4) Evidence of the financial aspects of each Limited Partnership, namely the losses of each individual partnership and how those losses were shown in the Limited Partnerships. The loss statements were then used to claim losses, as in the financial statements and related documents;

5) Information flow to investors and the public and the creation of indicia of a legitimate of a business operation of each Limited Partnership i.e. the window dressing of Starlight Charters and the Commissary;

6) The development and distribution of information on the exclusivity and opportunity the product presents to the target market. This included information to capture the imagination of innocent investors such as the luxurious nature of the cruises in sunny climates with sumptuous meals and state of the art accommodations all without financial risk to the investor and attractive cash returns through a tax gimmick.

[363] The evidence of misrepresentations presented at trial was enough to convince me of all of the foregoing. In fact, the volume of evidence is so overwhelming, voluminous, and uncontradicted, that when one looks at the evidence in its totality,

one cannot come to any other conclusion other than that this was a fraud from beginning to end perpetrated by the mastermind Mr. Bellfield. He showed no mercy in terms of duping the public, the investors, the CRA, his own staff, and others, in his attempts to further his own personal interests and those of his family members. There was no genuine business carried on and I therefore conclude that the Appellants did not have a source of income from which they could deduct expenses or losses.

b) Were the Limited Partnerships Genuine Partnerships Carrying on a Business in Common with a View to Profit?

[364] The Respondent argues that the Limited Partnerships do not constitute genuine partnerships because they were merely part of a fraud perpetuated upon the investors. He asserts that there was no common purpose of carrying on a business with the investors, stating at page 218 of his Final Submissions:

> 695. … the evidence does not establish that the S/Y Garbo, Midnight Kiss or Close Encounters were genuine "partnerships." OCGC, while carrying on a fraud business *at the expense of* the investors, was not carrying on business *in common* with the investors.
>
> [Emphasis in original]

[365] The Appellants assert that the Limited Partnerships were in fact carrying on a yacht chartering business, in which substantial start-up costs were anticipated. The Appellants emphasize that even where a yacht was not ultimately delivered, and the business was unsuccessful, other goods and services that were acquired as part of the $13 to 14 million spent were related to the yacht chartering business. They assert that it is not the place of the Minister or the Court to second-guess the business acumen of taxpayers; but rather simply to evaluate if sufficient indicators of commerciality are present.

[366] In evaluating whether the Limited Partnerships were engaged in a business, the Appellants argue that the focus of the inquiry should be on the Limited Partnerships themselves, rather than on other relationships where fraud or misrepresentations were present. They assert that the focus of the inquiry should not be on the relationship between OCGC and the CRA regarding OCGC's corporate taxes, in which OCGC perpetuated a fraud to evade a significant corporate tax liability. The Appellants further assert that the inquiry should also not focus on the relationship between OCGC as a vendor and the investors as purchasers of units in the Limited Partnerships in which various misrepresentations were present in the sale

transactions. Instead, the Appellants argue, the only relevant determination is whether the Limited Partnerships had sufficient business indicia to demonstrate that they were a genuine business. The Appellants state at page 30 of their Final Submissions that the focus of the Court should be as follows:

> 74. In order to determine whether the Limited Partnerships were in business, one must look at what the Limited Partnerships paid for and what they received in exchange for those payments by way of goods and services as part of the start-up of their respective businesses.

(i) The Law

The Taxation of Partnerships

[367] While a partnership is not considered a taxpayer under the *Act*, subsection 96(1) instructs that partnership income or losses should be calculated at the partnership level as if the partnership was a separate entity, and then allocated proportionately amongst the individual partners in accordance with their partnership share. The relevant portions of the provision read:

> 96. (1) Where a taxpayer is a member of a partnership, the taxpayer's income, non-capital loss, net capital loss, restricted farm loss and farm loss, if any, for a taxation year, or the taxpayer's taxable income earned in Canada for a taxation year, as the case may be, shall be computed as if
>
> (a) the partnership were a separate person resident in Canada;
>
> (b) the taxation year of the partnership were its fiscal period;
>
> (c) each partnership activity (including the ownership of property) were carried on by the partnership as a separate person, and a computation were made of the amount of
>
> (i) each taxable capital gain and allowable capital loss of the partnership from the disposition of property, and
>
> (ii) each income and loss of the partnership from each other source or from sources in a particular place, for each taxation year of the partnership[…]
>
> …
>
> (f) the amount of the income of the partnership for a taxation year from any source or from sources in a particular place were the income of the taxpayer from that source or from sources in that particular place, as the case may be, for the taxation year of the taxpayer in which the partnership's taxation year ends, to the extent of the taxpayer's share thereof; and

> (g) the amount of the loss of the partnership for a taxation year from any source or from sources in a particular place were the loss of the taxpayer from that source or from sources in that particular place, as the case may be, for the taxation year of the taxpayer in which the partnership's taxation year ends, to the extent of the taxpayer's share thereof.

The Essential Ingredients of a Valid Partnership

[368] Partnership losses are only deductible under the *Act* if it is established that a valid partnership existed. Ontario's *Partnerships Act*[47] defines a partnership as follows:

> 2. Partnership is the relation that subsists between persons carrying on a business in common with a view to profit […]

[369] The essential ingredients required for a genuine partnership were outlined by Justice Bastarache, writing in dissent in *Continental Bank Leasing Corp. v. Canada*.[48] In essence, a genuine partnership will be found where the parties were:

1) carrying on a business;
2) in common; and
3) with a view to profit.

[370] Justice Bastarache's three essential ingredients for a partnership were adopted by the Supreme Court of Canada in two subsequent cases, *Backman v. Canada*,[49] and *Spire Freezers Ltd. v. Canada*.[50] Both cases apply the legislative definition found in Ontario's *Partnerships Act* and most common law partnership statutes.

[371] In undertaking a factual inquiry required to assess whether a partnership existed, the parties' intentions will be considered, as will various other indicia such as, the parties' contributions to the effort, the existence of a joint interest in property, whether income or losses are shared, whether there was shared management and

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[47] *Partnerships Act*, RSO 1990, c P.5.
[48] *Continental Bank Leasing Corp. v. Canada* [1998] 2 SCR 298.
[49] *Backman v. Canada*, 2001 SCC 10 at para. 17-18 [*Backman*].
[50] *Spire Freezers Ltd. v. Canada*, 2001 SCC 11 at para. 14-16, [*Spire Freezers Ltd.*].

control, and if the parties shared a bank account. Justice Bastarache described the factual inquiry required to evaluate if a partnership existed as follows:

> [23] The existence of a partnership is dependent on the facts and circumstances of each particular case. It is also determined by what the parties actually intended. As stated in *Lindley & Banks on Partnership* (17th ed. 1995), at p. 73: "in determining the existence of a partnership . . . regard must be paid to the true contract and intention of the parties as appearing from the whole facts of the case".
>
> [24] The Partnerships Act does not set out the criteria for determining when a partnership exists. But since most of the case law dealing with partnerships results from disputes where one of the parties claims that a partnership does not exist, a number of criteria that indicate the existence of a partnership have been judicially recognized. The indicia of a partnership include the contribution by the parties of money, property, effort, knowledge, skill or other assets to a common undertaking, a joint property interest in the subject-matter of the adventure, the sharing of profits and losses, a mutual right of control or management of the enterprise, the filing of income tax returns as a partnership and joint bank accounts.

Ingredient One: Carrying on a Business

[372] In considering how to analyze the first ingredient, "carrying on a business", the Supreme Court of Canada in *Backman* clarified that in the context of the partnership test, a business does not necessarily need to be new, nor does the business need to be carried on for a significant amount of time. In fact, one transaction may be sufficient to ground a finding that the parties were carrying on a business, so long as the purported partnership does not amount to an "empty shell". As stated by the Supreme Court of Canada:

> 19 In law, the meaning of "carrying on a business" may differ depending on the context in which it is used. Provincial partnership acts typically define "business" as including "every trade, occupation and profession". The kinds of factors that may be relevant to determining whether there is a business are contained in the existing legal definitions. One simple definition of "carrying on trade or business" is given in Black's Law Dictionary (6th ed. 1990), at p. 214: "To hold one's self out to others as engaged in the selling of goods or services." Another definition requires at least three elements to be present: (1) the occupation of time, attention and labour; (2) the incurring of liabilities to other persons; and (3) the purpose of a livelihood or profit: see *Gordon v. The Queen*, [1961] S.C.R. 592, per Cartwright J., dissenting but not on this point, at p. 603.

> 20 The existence of a valid partnership does not depend on the creation of a new business because it is sufficient that an existing business was continued. Partnerships may be formed where two parties agree to carry on the existing business of one of them. It is not necessary to show that the partners carried on a business for a long period of time. A partnership may be formed for a single transaction. As was noted by this Court in *Continental Bank*, supra, at para. 48, "[a]s long as the parties do not create what amounts to an empty shell that does not in fact carry on business, the fact that the partnership was created for a single transaction is of no consequence." Furthermore, to establish the carrying on of a business, it is not necessary to show that the parties held meetings, entered into new transactions, or made decisions: Continental Bank, supra, at paras. 31-33. A business may be established even in circumstances where the sole business activity is the passive receipt of rent, as was noted by L'Heureux-Dubé J. in *Hickman Motors Ltd. v. Canada*, [1997] 2 S.C.R. 336, at para. 46 […]

Ingredient Two: "In Common"

[373] In *Backman*, the Supreme Court of Canada went on to analyze the meaning of carrying the business out "in common". The Court reiterated that the fact that only one partner carries out the management and control of the partnership does not preclude a finding that the business is carried out in common. The Court also noted that the finding that a partnership existed might be based in part on a valid contractual agreement between partners, but the existence of a contractual agreement is not sufficient to decide the issue. All three criteria for a valid partnership must be met. The Court went on to summarize other factors that may be relevant in considering whether the parties had the intention to carry on a business "in common", stating:

> 21 In determining whether a business is carried on "in common", it should be kept in mind that partnerships arise out of contract. The common purpose required for establishing a partnership will usually exist where the parties entered into a valid partnership agreement setting out their respective rights and obligations as partners. As was noted in *Continental Bank*, supra, at paras. 34-35, a recognition of the authority of any partner to bind the partnership is relevant, but the fact that the management of a partnership rests with a single partner does not mandate the conclusion that the business was not carried on in common. […] It may be relevant if the parties held themselves out to third parties as partners, but it is also relevant if the parties did not hold themselves out to third parties as being partners. Other evidence consistent with an intention to carry on business in common includes: the contribution of skill, knowledge or assets to a common undertaking, a joint property interest in the subject-matter of the adventure, the sharing of profits and losses, the filing of income tax returns as a partnership, financial statements and joint bank accounts, as well as correspondence with third parties: see *Continental Bank*, supra, at paras. 24 and 36.
>
> …

> 27 In the case at bar, taken by themselves, the partnership agreement and other documentation indicate an intention to form a partnership. But that is not sufficient because the fundamental criteria of a valid partnership must still be met.

[374] In *Teelucksingh v. Canada*,[51] the Tax Court of Canada noted that the approach to the partnership test differs in the context of Limited Partnerships, which by their very nature require that management and control only be exercised by the general partner. Justice Miller stated:

> [68] […]Obviously, with respect to a limited partnership, the question of control and management is somewhat different and it is only the general partner who would exercise such control and management.

Ingredient Three: A View to Profit

[375] Regarding the third ingredient, "a view to profit", the Supreme Court of Canada in *Backman* emphasized that the intentions of the parties will be the key consideration. Tax motivations for participating in the partnership will not affect the validity of a partnership, so long as an ancillary intention to make a profit also exists. As stated by the Supreme Court:

> 22 A determination of whether there exists a "view to profit" requires an inquiry into the intentions of the parties entering into an alleged partnership. At the outset, it is important to distinguish between motivation and intention. Motivation is that which stimulates a person to act, while intention is a person's objective or purpose in acting. This Court has repeatedly held that a tax motivation does not derogate from the validity of transactions for tax purposes: *Shell Canada Ltd. v. Canada*, [1999] 3 S.C.R. 622; *Canada v. Antosko*, [1994] 2 S.C.R. 312; *Stubart Investments Ltd. v. The Queen*, [1984] 1 S.C.R. 536, at p. 540. Similarly, a tax motivation will not derogate from the validity of a partnership where the essential ingredients of a partnership are otherwise present: *Continental Bank, supra*, at paras. 50-52. The question at this stage is whether the taxpayer can establish an intention to make a profit, whether or not he was motivated by tax considerations. For further discussion, see D. Nathanson, "Tax Motive Kills Partnership: Spire Freezers (cf. Continental Bank)" (1999), 7 *Tax Litigation* 458.
>
> 23 Moreover, in *Continental Bank*, *supra*, this Court held that a taxpayer's overriding intention is not determinative of whether the essential ingredient of "view to profit" is present. It will be sufficient for a taxpayer to show that there was an ancillary profit-making purpose. This flows from the following

[51] *Teelucksingh v. Canada*, 2011 TCC 22 [*Teelucksingh*].

observation made in *Lindley & Banks on Partnership*, *supra*, at pp. 10-11, and adopted in *Continental Bank*, *supra*, at para. 43:

> . . . if a partnership is formed with some other predominant motive [other than the acquisition of profit],*e.g.*, tax avoidance, but there is also a real, albeit ancillary, profit element, it may be permissible to infer that the business is being carried on "with a view of profit." If, however, it could be shown that the sole reason for the creation of a partnership was to give a particular partner the "benefit" of, say, a tax loss, when there was no contemplation in the parties' minds that a profit . . . would be derived from carrying on the relevant business, the partnership could not in any real sense be said to have been formed "with a view of profit".

> 24 An ancillary purpose is by definition a lesser or subordinate purpose. In determining whether there is a view to profit courts should not adopt or employ a purely quantitative analysis. The amount of the expected profit is only one of several factors to consider. The law of partnership does not require a net gain over a determined period in order to establish that an activity is with a view to profit. For example, a partnership may incur initial losses during the start up phase of its enterprise. That does not mean that the relationship is not one of partnership, so long as the enterprise is carried on with a view to profit in the future. Therefore, where a partnership is formed with the predominant motive of acquiring a tax loss, it is not necessary to show an intention to profit by the amount necessary to recoup the acquired losses or produce a net gain.

[376] *Spire Freezers Ltd*. also emphasized that a tax motivation, or the fact that a business would incur significant losses initially, was not sufficient to find that there was no view to profit so long as an ancillary profit making intention existed. The Court stated:

> 25 […] the fact that the appellants admitted that they principally entered into the transactions to reduce their Canadian income tax liability by gaining access to the losses does not prevent a finding of partnership.

> 26 The majority of the Court of Appeal also rejected the notion that there was a view to profit because the parties did not contemplate recouping the initial loss. However, the determination of the existence of a view to profit is not a matter of strictly quantitative analysis. The quantum of the initial loss compared to the anticipated profit does not negate the holding of partnership in this case. The law of partnership does not require a net gain over a determined period in order to establish that an activity is with a view to profit. For example, a partnership may incur initial losses during the start-up phase of its enterprise. That does not mean that the relationship is not one of partnership, so long as the enterprise is carried on with a view to profit in the future. […]

[377] It is not sufficient, however, to ground a finding that there was "a view to profit" if the parties' singular intention was to access significant tax benefits, without any actual business being carried out in common with a view to profit. Such was the determination in *Rouleau v. The Queen*,[52] and *McKeown v. The Queen*.[53] As stated by Justice Archambault in *Rouleau*:

> [25] In light of the findings of fact set out above, I will adopt, in very large part, the approach of the late Chief Judge Garon in *McKeown*. There, the Chief Judge asked the following initial question: was Cablotel a partnership? He answered this question in the negative, because "the investors in question were merely seeking substantial tax benefits and never demonstrated any intention of working together to undertake scientific research and experimental development activities. In short, they had no intention of forming a genuine partnership." (paragraph 393 of his reasons). In my opinion, this question requires greater thought before I can decide it. However, as Chief Judge Garon held at paragraphs 394 *et seq*., I find that Cablotel did not carry on any business:
>
> > [394] In addition, no business was carried on either by the appellant or by Commu-Sys Enr. and Cablotel Enr. in relation to the carrying out of the research work. This case is similar to *Bendall v. The Queen*, *supra*, in which Judge Bonner stated the following:
> >
> > The issue here is whether the appellant carried on a "business" within the meaning of the *Income Tax Act*("Act"). That word is to be given its ordinary meaning and that meaning does not include a tax avoidance scheme which is nothing more than a pale imitation of a business. The appellant was not involved in a commercial activity either directly or through Omni as his agent. The objective evidence regarding the manner in which the scheme operated and the actions and inaction of the parties point clearly to a conclusion that both the appellant and the promoters of the scheme were indifferent to the marketing of the speed reading course and to the earning of profits from that activity. There can be no doubt that what was sought was a tax deduction which would result in a refund part of which was to go to enrich the promoters of this scheme and the remainder of which was to go to the appellant.
> >
> > [Footnote omitted.]
> >
> > [395] In the case at bar, no steps or requests whatsoever were taken or made to ensure that the project would be profitable. I cannot find anything suggesting that the groups in question could have been profitable. No market research survey had been done. No marketing

[52] *Rouleau v. The Queen*, 2007 TCC 338 [*Rouleau*].
[53] *McKeown v. The Queen*, [2001] 4 CTC 2197 [*McKeown*].

> plan had been developed. Moreover, the structure put in place was set up solely for tax purposes, as shown by the "participation program" that was established only to create the illusion that the government's criteria were being met.

[378] As stated in *Teelucksingh*, the view to profit is not necessarily limited to when the business is in partnership form:

> 74 […] a view to profit is a view to profit from the business or enterprise, not strictly from the particular form of legal entity.
>
> 75 […] The fact that no profit was made while in the partnership form is not sufficient to deny this form of arrangement its legitimacy. This was a cleverly crafted investment vehicle, premised on the existence of a real business.

The Proper Approach to the Partnership Inquiry

[379] The Supreme Court of Canada in *Backman* provided guidance as to how the partnership inquiry should be conducted, emphasizing the need to identify the true contract between the parties and their intentions within the factual context of each case. The Court stated:

> 25 As adopted in *Continental Bank*, *supra*, at para. 23, and stated in *Lindley & Banks on Partnership*, *supra*, at p. 73: "in determining the existence of a partnership . . . regard must be paid to the true contract and intention of the parties as appearing from the whole facts of the case". In other words, to ascertain the existence of a partnership the courts must inquire into whether the objective, documentary evidence and the surrounding facts, including what the parties actually did, are consistent with a subjective intention to carry on business in common with a view to profit.
>
> 26 Courts must be pragmatic in their approach to the three essential ingredients of partnership. Whether a partnership has been established in a particular case will depend on an analysis and weighing of the relevant factors in the context of all the surrounding circumstances. That the alleged partnership must be considered in the totality of the circumstances prevents the mechanical application of a checklist or a test with more precisely defined parameters.

[380] In *Rezek v. Canada*,[54] the Federal Court of Appeal also discussed the role of intention and documentation in the partnership inquiry and emphasized that regardless of whether an agreement exists, the focus will always be on whether the facts at hand show that the three essential elements for a partnership are met:

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[54] *Rezek v. Canada*, 2005 FCA 227 [*Rezek*].

> [80] A declared intention of the parties that there is no partnership relationship will carry little or no weight. *Lindley & Banks* at paragraph 5-05 quote Cozens-Hardy M.R.'s more forceful statement in *Weiner v. Harris*, [1910] 1 K.B. 285:
>
> > Two parties enter into a transaction and say "It is hereby declared there is no partnership between us." The Court pays no regard to that. The Court looks at the transaction and says, "Is this, in point of law, really a partnership?". It is not in the least conclusive that the parties have used a term or language intended to indicate that the transaction is not that which in law it is.
>
> [81] Nor will the existence or non-existence of a partnership agreement be sufficient to decide the issue. In *Backman v. The Queen*, 2001 SCC 10 (CanLII), [2001] 1 S.C.R. 367 at paragraph 27, Iacobucci and Bastarache JJ. determined that, even in the face of a partnership agreement and other formal documentation, there was no partnership because the fundamental criteria for a valid partnership were not met.
>
> [82] Sophisticated parties may have elaborate documentation. Unsophisticated parties may not and may also not be aware of the law of partnership. The question is always whether there is a business carried on in common with a view to profit. If there is, a partnership subsists at law, irrespective of the parties' stated intention, the existence or non-existence of a partnership agreement or the parties' understanding of the law.

(ii) Analysis

[381] The appropriate question then, in applying the partnerships test to the extensive evidence presented in this case, is whether the yacht chartering Limited Partnerships were carrying on a business in common with a view to profit. With the numerous misrepresentations made by Mr. Bellfield et al, did the parties have a shared intention to carry out the Limited Partnership's business in common with a view to profit such that the Limited Partnerships constitute valid partnerships? Focusing on the evidence regarding the intention of the parties, with OCGC as the general partner, and the investors as the limited partners, and on the fundamental contractual nature of a partnership, was there a meeting of the minds between the parties?

[382] In addition to my conclusion that the yacht chartering business was a fraud from beginning to end and bore all the hallmarks of a Ponzi scheme, I also conclude that the Limited Partnerships were not genuine partnerships in law. The three elements required to meet the partnership test are not met. The numerous misrepresentations provided by way of examples in the factual summary above demonstrate the all-encompassing nature of OCGC and Mr. Bellfield's misrepresentations, and how they were vitiated any shared intention to enter into and carry on a partnership relationship. I apply the three partnership factors below.

[383] There was no "business carried on". There was merely a fraud perpetuated by Mr. Bellfield. This was a fraud from beginning to end, regardless of whether some of the investors still believe that there was a genuine yacht chartering business. The only business that existed was the business of the fraud perpetuated by Mr. Bellfield and his vehicle for the fraud, OCGC. The purpose of the business was to defraud the investors and the CRA. The evidence discloses that fundamental misrepresentations were made to investors right from the beginning in the founding documents of each Limited Partnership. The misrepresentations were so significant that the Offering Memoranda was fundamentally misleading so as to render it impossible for the investors to have a meeting of the minds with the perpetrator of the fraud. Briefly, one need only refer to the evidence of Mr. Belchetz, who admitted that had he known that the things purportedly done in the Offering Memorandum had not been done, he probably would not have made the investment.

[384] There was no business "in common", despite the existence of partnership contracts. These documents, and all the documents relating to the Limited Partnerships, were riddled with fraudulent misrepresentations. They were part of the window dressing—part of the fiction. I query how there could be a meeting of the minds when the two parties had different motives—Mr. Bellfield to perpetrate a fraud, and the investors to get the benefits of a tax gimmick with a longer term ancillary view to invest in a yacht chartering venture. How could there be a meeting of the minds when the foundation of the scheme is fraudulent yet the investors are not aware of or are ignorant of the fraud perpetrated on them. There can be no intention of carrying on a business "in common" on the facts of this case.

[385] As for the "view to profit", there was no view to profit for the Limited Partnerships. As stated by the Respondent, the evidence establishes that Mr. Bellfield had the intention to profit *at the expense* of the Limited Partnerships. Mr. Bellfield never had the intention to actually pursue a venture in common with the investors that would result in the Limited Partnerships themselves or the investors making a profit. The number of misrepresentations he made are too prevalent and the level of fraud too pervasive to determine otherwise. The yacht chartering activities were so drastically under-funded, the activities so limited and unsuccessful, the yachts so delayed and limited compared to the number contracted for, the extensive luxury yacht chartering business promised so large and the activities actually carried out so skeleton thin, that I can only conclude that the sole activities pursued by OCGC were merely attempts to create the illusion of an operating business.

2. If the Limited Partnerships are determined to constitute an income source, did they actually suffer the losses claimed by the Appellants?

(i) The Law

The Test under Subsection 18(1)

[386] Subsection 18(1) of the *Act* sets out the requirement that for expenses to be deductible, they must have been incurred by the taxpayer for the purpose of gaining or producing business or property income. The provision states:

> 18. (1) In computing the income of a taxpayer from a business or property no deduction shall be made in respect of
>
> (a) an outlay or expense except to the extent that it was made or incurred by the taxpayer for the purpose of gaining or producing income from the business or property

[387] Justice Iacobucci, writing for the majority in *Symes v. Canada*[55] after canvassing the relevant jurisprudence, concluded that a *purpose* test, based on the language of paragraph 18(1)(*a*), was the most appropriate test to apply when evaluating whether an expense is deductible under subsection 18(1). The Court stated:

> Upon reflection, therefore, no test has been proposed which improves upon or which substantially modifies a test derived directly from the language of s. 18(1)(*a*). The analytical trail leads back to its source, and I simply ask the following: did the appellant incur child care expenses for the purpose of gaining or producing income from a business?[56]

[388] The applicable test therefore, is the following: were the expenses incurred for the purpose of gaining or producing income for the Limited Partnerships.

(ii) Analysis

[389] If I erred in determining that the Limited Partnerships did not carry on a genuine business which constituted a source, I conclude in the alternative that the expenses claimed were not incurred for the purpose of operating the Limited Partnerships' yacht chartering business and therefore are not deductible pursuant to subsection 18(1). Fundamental to Mr. Bellfield's fraudulent scheme was the creation of a documentary trail to attempt to legitimize an otherwise illegitimate, illegal, and

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[55] *Symes v. Canada*, [1993] 4 SCR 695.
[56] *Ibid*. at 48.

fraudulent presentation of expenses, and losses, all for the purpose of advancing on the fraud to allow himself and others to sell the Limited Partnership units.

[390] Mr. Bellfield had to create losses in order to perpetuate the sale of Limited Partnerships as tax advantageous. Given that he was not actually incurring the expenses necessary to legitimize these losses, he had to create expenses that were never incurred in the year in which they were represented to have incurred. Or if they were incurred, they were incurred for the mere purpose of maintaining the illusion of a genuine business capable of delivering 36 yachts and operating a luxury chartering business for that fleet of yachts. The expenses were a fiction!

[391] As part of the evidence with respect to the misinformation and the misrepresentations circulated by Mr. Bellfield and others, a reference will be made to the financial statements developed and massaged by Mr. Bellfield for the individual partnerships and used by the investors as the cornerstone for their losses. Buttressed by undisputed facts as to: a) the existence of yachts for each individual Limited Partnership; b) the availability of yachts for use by individual Limited Partnerships' in the charter business; and c) the expenses allegedly incurred and invoiced yet never actually paid for or incurred show that most expenses were not incurred or if they were incurred, were never actually paid for because OCGC lacked the resources to pay for these expenses.

[392] Certainly, there were some expenses incurred and some expenses paid for, but similar to *Vankerk*, expenses that were not fictitious or phony were incurred as window dressing for the purpose of perpetuating a fraudulent scheme. The purpose of those expenses was to continue Mr. Bellfield's fraudulent scheme and not to earn or produce income. The expenses were paid for with the interest payments of the investors or were never paid for.

[393] Although not the mastermind behind this massive fraud, but someone who played a key role in maintaining and expanding it, Mr. Minchella was of the view that as long as you had a paper trail to show that the expense was incurred or paid, that was all that was required to justify and support the financial statements and losses claimed. This he learned at the knee of the mastermind, Mr. Bellfield. In preparing financial statements for the Limited Partnerships, Mr. Minchella would go to respective Limited Partnerships' Offering Memoranda, copy down the expenses shown on the pro-forma statements, and insert the expenses in the draft financial

statements. The fact that these expenses were never incurred, was not a requirement as far as Mr. Minchella was concerned, in order to be listed in the financial statements.

[394] The conclusions above are more than sufficient to dispense with these appeals. I ground my finding first in the fundamental determination that the Limited Partnerships constituted a fraud from beginning to end and that the fraud bore the hallmarks of a Ponzi scheme; second that Limited Partnerships were not genuine partnerships in law; and finally, the alternative conclusion that the purpose of those expenses—if incurred—was not to earn or produce income but rather to provide window-dressing to the fraud.

[395] Given the lengthy nature of this trial, the number of parties affected by this decision, and the efforts put in by counsel, several of the Respondent's other alternative arguments are also briefly canvassed below.

3. If the Limited Partnerships actually suffered the losses claimed, did they properly compute the timing of partnership expenses claimed for the taxation years in question?

a) The Law

(i) The Test under 18(9)

[396] Subsection 18(9) of the *Act* requires that a taxpayer match in a reasonable manner any prepaid expenses for services, interest, taxes, rent, royalty, or insurance to the year in which those expenses relate. The provision states in part:

> 18. (9) Notwithstanding any other provision of this *Act*,
>
> (a) in computing a taxpayer's income for a taxation year from a business or property […], no deduction shall be made in respect of an outlay or expense to the extent that it can reasonably be regarded as having been made or incurred
>
> (i) as consideration for services to be rendered after the end of the year
>
> (ii) as, on account of, in lieu of payment of or in satisfaction of, interest, taxes (other than taxes imposed on insurance premiums), rent or royalties in respect of a period that is after the end of the year, or

(iii) as consideration for insurance in respect of a period after the end of the year[…]

(b) such portion of each outlay or expense (other than an outlay or expense of a corporation, partnership or trust as, on account of, in lieu of payment of or in satisfaction of, interest) made or incurred as would, but for paragraph 18(9)(*a*), be deductible in computing a taxpayer's income for a taxation year shall be deductible in computing the taxpayer's income for the subsequent year to which it can reasonably be considered to relate.

b) Analysis

[397] As previously described, the documentary trail created by Mr. Bellfield to justify the tax losses claimed had little relation to actual expenses incurred, nor to the timing of the expenses incurred purportedly for yacht chartering purposes, and are therefore, also precluded from deductibility pursuant to subsection 18(9).

4. If there was a source with genuine losses taken at the correct times, what is the amount of capital cost allowance, if any, that the S/Y Garbo Limited Partnership is entitled to take?

a) The Law

[398] The Respondent argues that even if the Limited Partnerships were found to constitute sources of income that incurred genuine losses taken at the correct time, capital cost allowance would not be available in respect of the S/Y Garbo because the S/Y Garbo LP never acquired the yacht.

[399] In *Hewlett Packard (Canada) Ltd. v. R.*,[57] the Federal Court of Appeal affirmed that the "classic test of acquisition" is the one articulated by Justice Cattanach in *Minister of National Revenue v. Wardean Drilling Ltd*.:

> ... it is my opinion that a purchaser has acquired assets of a class in Schedule B when title has passed, assuming that the assets exist at that time, or when the purchaser has all the incidents of title, such as possession, use and risk, although legal title may remain in the vendor as security for the purchase price as is the commercial practice under conditional sales agreements. In my view the foregoing is the proper test to determine the acquisition of property described in Schedule B to the *Income Tax Regulations*.[58]

[57] *Hewlett Packard (Canada) Ltd. v. R.*, 2004 FCA 240.
[58] *Minister of National Revenue v. Wardean Drilling Ltd*. (1969), 69 D.T.C. 5194 (Can. Ex. Ct.) at p. 5198.

[400] Capital cost allowance may be deducted pursuant to paragraph 20(1)(*a*) of the *Act*, with the portion of the capital cost deductible prescribed by the *Income Tax Regulations*. Regulation 1102(1) excludes from deductibility property that was not acquired for an income gaining or producing purpose.

b) Analysis

[401] The evidence discloses that as a key part of marketing the Limited Partnerships, capital cost allowance was held out to be deductible right from the beginning. Albeit, when Mr. Bellfield was caught in this misrepresentation, he had to retract but then created other deductions to allow the losses to be substantiated.

[402] Specifically relating to the capital cost allowance claimed for the S/Y Garbo, the yacht was purportedly delivered in the spring of 1986 but had to go to a dry dock for a full year. The S/Y Garbo was not available for charters until the spring of 1987, at which point its primary charter function was to impress investors and others. No evidence was presented that title to the S/Y Garbo was ever acquired by the S/Y Garbo LP. While OCGC was allowed to hold title to the S/Y Garbo, this had to be done in the interest of the S/Y Garbo LP. It was not. I conclude that even if I erred in determining that there was no source, the capital cost allowance claimed by the Appellant for the S/Y Garbo is not deductible pursuant to Regulation 1102(1)(*c*). The yacht was only used by OCGC as window-dressing to perpetuate the fraud and was never acquired by the S/Y Garbo LP for income gaining or earning purposes.

5. Did each of the Appellants incur the interest expenses claimed pursuant to paragraphs 18(1)(a) and 20(1)(c) of the Income Tax Act?

a) The Law

[403] A taxpayer can deduct certain interest expenses from their income on an accrual basis under paragraphs 18(1)(*a*) and 20(1)(*c*) of the *Act*. Under subparagraph 20(1)(*c*)(i), the amount must be for interest paid or payable for borrowed money used to earn business or property income. Subparagraph 20(1)(*c*)(ii) allows a deduction for interest payable for property acquired for the purpose of gaining or producing business or property income. For amounts to qualify under both subparagraphs, the interest amounts must be reasonable and paid or payable that year in fulfilment of a legal obligation to pay the interest. The provision states in part:

> 20. (1) Notwithstanding paragraphs 18(1)(a), 18(1)(b) and 18(1)(h), in computing a taxpayer's income for a taxation year from a business or property, there may be deducted such of the following amounts as are wholly applicable to that source or such part of the following amounts as may reasonably be regarded as applicable thereto […]
>
> > (c) an amount paid in the year or payable in respect of the year (depending on the method regularly followed by the taxpayer in computing the taxpayer's income), pursuant to a legal obligation to pay interest on
> >
> > > (i) borrowed money used for the purpose of earning income from a business or property (other than borrowed money used to acquire property the income from which would be exempt or to acquire a life insurance policy),
> > >
> > > (ii) an amount payable for property acquired for the purpose of gaining or producing income from the property or for the purpose of gaining or producing income from a business (other than property the income from which would be exempt or property that is an interest in a life insurance policy), […]
> >
> > or a reasonable amount in respect thereof, whichever is the lesser;

[404] The Supreme Court of Canada considered the deductibility of interest under subparagraph 20(1)(*c*)(i) in *Shell Canada Ltd. v. Canada*,[59] and summarized the qualification requirements as follows:

> [28] Section 20(1)(c)(i) allows taxpayers to deduct from their income interest payments on borrowed money that is used for the purpose of earning income from a business or property. It is an exception to s. 9 and s. 18(1)(b), which would otherwise prohibit the deduction of amounts expended on account of capital, i.e., interest on borrowed funds used to produce income. […] The provision has four elements: (1) the amount must be paid in the year or be payable in the year in which it is sought to be deducted; (2) the amount must be paid pursuant to a legal obligation to pay interest on borrowed money; (3) the borrowed money must be used for the purpose of earning non-exempt income from a business or property; and (4) the amount must be reasonable, as assessed by reference to the first three requirements.

[405] In *Ludco Enterprises Ltd. v. Canada*,[60] the Supreme Court of Canada considered the proper inquiry for the income-earning purpose test under subparagraph 20(1)(*c*)(i). After canvassing a number of approaches, the Court concluded that the question to pose was whether the taxpayer had a reasonable expectation of income in making the investment for which the money was borrowed. The Court stated:

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[59] *Shell Canada Ltd. v. Canada*, [1999] 3 SCR 622 [*Shell*].
[60] *Ludco Enterprises Ltd. v. Canada*, 2001 SCC 62.

> [50] With respect to the plain meaning of s. 20(1)(*c*)(i), the only express requirement related to "purpose" is that borrowed money must have been "used for the purpose of earning income". Apart from the use of the definite article "the", which on closer analysis is hardly conclusive of the issue before us, nothing in the text of the provision indicates that the requisite purpose must be the exclusive, primary or dominant purpose, or that multiple purposes are to be somehow ranked in importance in order to determine the taxpayer's "real" purpose. Therefore, it is perfectly consistent with the language of s. 20(1)(*c*)(i) that a taxpayer who uses borrowed money to make an investment for more than one purpose may be entitled to deduct interest charges provided that one of those purposes is to earn income.
>
> ...
>
> [54] Having determined that an ancillary purpose to earn income can provide the requisite purpose for interest deductibility, the question still remains as to how courts should go about identifying whether the requisite purpose of earning income is present. What standard should be applied? In the interpretation of the Act, as in other areas of law, where purpose or intention behind actions is to be ascertained, courts should objectively determine the nature of the purpose, guided by both subjective and objective manifestations of purpose: see *Symes*, *supra*, at p. 736; *Continental Bank*, *supra*, at para. 45; *Backman*, *supra*, at para. 25; *Spire Freezers*, *supra*, at para. 27. In the result, the requisite test to determine the purpose for interest deductibility under s. 20(1)(*c*)(i) is whether, considering all the circumstances, the taxpayer had a reasonable expectation of income at the time the investment was made.
>
> [Emphasis added]

[406] The distinction between subparagraph 20(1)(*c*)(i) and subparagraph 20(1)(*c*)(ii) is explained in the Tax Court of Canada decision, *Penn Ventilator Canada Ltd. v. The Queen*.[61] Justice Lamarre Proulx concluding that based on the Supreme Court of Canada determination in *Minister of National Revenue v. TE McCool Ltd.*,[62] that a promissory note does not constitute borrowed money, subparagraph 20(1)(*c*)(i) could not apply to interest paid on a promissory note. Justice Lamarre Proulx then went on to hold that subparagraph 20(1)(*c*)(ii) applied in that case so as to make the interest on the promissory note deductible.

[407] *Shell* is also frequently cited to express the principle that a taxpayer's legal relationship must be respected except where otherwise required by a provision of the *Act* or where the legal relationships are a sham. As stated by the Supreme Court of Canada:

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[61] *Penn Ventilator Canada Ltd. v. The Queen*, 2002 CanLII 871.
[62] *M.N.R. v. TE McCool Ltd*, [1949] C.T.C. 395.

> [39] This Court has repeatedly held that courts must be sensitive to the economic realities of a particular transaction, rather than being bound to what first appears to be its legal form: *Bronfman Trust*, *supra*, at pp. 52-53, *per* Dickson C.J.;*Tennant*, *supra*, at para. 26, *per* Iacobucci J. But there are at least two *caveats* to this rule. First, this Court has never held that the economic realities of a situation can be used to recharacterize a taxpayer's *bona fide* legal relationships. To the contrary, we have held that, absent a specific provision of the Act to the contrary or a finding that they are a sham, the taxpayer's legal relationships must be respected in tax cases. Recharacterization is only permissible if the label attached by the taxpayer to the particular transaction does not properly reflect its actual legal effect: *Continental Bank Leasing Corp. v. Canada*, [1998] 2 S.C.R. 298, at para. 21, *per* Bastarache J.

b) Analysis

[408] I next consider the Respondent's alternative argument regarding the deductibility of the Appellants' claimed interest expenses under subparagraph 20(1)(*c*)(ii). To qualify under subparagraph 20(1)(*c*)(ii), the interest must meet the same four elements cited above from *Shell*: 1) the amount must paid or payable in the year the deduction is sought; 2) there must be a legal obligation to pay interest on the amount paid or payable; 3) the amount must be incurred for a non-exempt income earning purpose; and 4) the amount must be reasonable. There is a slight modification required to the purpose test for the interest amount to qualify under subparagraph 20(1)(*c*)(ii). The question to be asked is: was there a reasonable expectation of income *at the time* the property was acquired for business or property (non-exempt) income-earning purposes? As explained in *Ludco*, income-earning does not need to be the primary or dominant purpose of the investment.

[409] I determine that only three out of four parts of the test are met. First, the amounts claimed as interest relate to the year in which the deductions are sought. Second, as asserted above, I conclude that there was no source of business income because the investors were defrauded from beginning to end. The Supreme Court of Canada in *Ludco* directs my inquiry to the objective and subjective manifestations of the taxpayers' intentions *at the time* the investment was made. I determine that despite the fact that the Appellants' were defrauded of their interest payments, they had a reasonable expectation of income *at the time* of their investment as required under subparagraph 20(1)(*c*)(ii) and outlined in *Ludco*. The Appellants' expectation of income was only in the long-term and was an ancillary purpose of an otherwise tax-motivated investment, but it nonetheless qualifies under the statute. Third, I conclude that the interest amounts were reasonable.

[410] Ultimately, however, I conclude that the fourth requirement is not met. The interest expenses are not deductible under subparagraph 20(1)(*c*)(ii) because there was no legal obligation to pay interest. The promissory notes are based on the fundamental misrepresentation that they were to act as security for loans purportedly arranged by OCGC. OCGC claimed that these purported loans were to finance the purchase price of a Limited Partnership unit, which in turn would be used by OCGC to capitalize each Limited Partnership and finance its operations. No such loans existed, and the Limited Partnerships were never capitalized. The Appellants entered into the promissory notes based on fraudulent misrepresentations, and any contractual obligation to pay interest amounts is vitiated by fraud.

6. Other Issues

a) The At-Risk Rules and the S/Y Close Encounters Limited Partnership:

(i) The Law

[411] The S/Y Close Encounters LP, along with the other partnerships of the same type, attempted to circumvent the at-risk rules introduced as of February 25, 1986. Subsection 96(2.1) limited the deductibility of a partner's losses to the amount of capital that partner invested, subject to certain adjustments. The provision states in part:

> 96.(2.1) Notwithstanding subsection (1), where a taxpayer is, at any time in a taxation year, a limited partner of a partnership, the amount, if any, by which
>
> (a) the total of all amounts each of which is the taxpayer's share of the amount of any loss of the partnership, determined in accordance with subsection 96(1), for a fiscal period of the partnership ending in the taxation year from a business (other than a farming business) or from property
>
> exceeds
>
> (b) the amount, if any, by which
>
> (i) the taxpayer's at-risk amount in respect of the partnership at the end of the fiscal period […]
>
> shall
>
> (c) not be deducted in computing the taxpayer's income for the year,
>
> (d) not be included in computing the taxpayer's non-capital loss for the year, and
>
> (e) be deemed to be the taxpayer's limited partnership loss in respect of the partnership for the year.

[412] The grandfathering provisions that the S/Y Close Encounters LP and other Type 3 Limited Partnerships rely on are found in subsection 96(2.5). The requirement

that must be met to avoid the at-risk rules is that the partnership needs to have been "actively carrying on business on a regular and continuous basis immediately before February 25, 1986 and continuously thereafter".

[413] In *Goren v. R.*,[63] Justice Bowman (as he then was) determined that a Limited Partnership was not exempt from the at-risk rule because it did not meet the grandfathering requirement. The Court stated:

> 9 I have great difficulty in seeing how THCLP can be said to have been regularly carrying on the business of operating a health care centre on February 26, 1986 when construction of the facility was not completed on that date and it was not the owner of it. THCLP had not received the money to acquire the home and in fact it was still owned by Medi-Villas. There of course have been cases such as *Minister of National Revenue v. M.P. Drilling Ltd.* (1976), 76 D.T.C. 6028 (Fed. C.A.) and *Gartry v. R. (1994), 94 D.T.C. 1947 (T.C.C.)* where it was held that a business had been commenced before the operation started to generate revenues, but in such cases the activities of the taxpayer including the expenditures of moneys, the acquisition of assets and the creation of a business structure had advanced to the point at which, as a matter of commercial reality, it could be said that it had commenced the process of operating a profit making entity.
>
> 10 None of these factors existed here on the relevant date of February 26, 1986. True, subscription forms had been received but the partnership was essentially only a shell with no capital but anticipation that it would acquire a nursing home that it intended to operate**.** It is difficult to see how Parliament could have made its intention any clearer that for the members of a limited partnership to avoid the application of the at-risk rules the partnership had to be actively engaged in the business that was expected to generate the income. While cases such as *MP Drilling* and *Gartry* may hold that a business may commence at a date before the income producing activities start, the words "actively" and "on a regular and a continuous basis" connote (indeed, denote) a degree of commercial activity that it is impossible to find here.
>
> [Emphasis added]

(ii) Analysis

[414] The evidence demonstrates that regardless of all other conclusions, the Type 3 Limited Partnerships were not carrying on a business on a regular and continuous basis before the at-risk rules were introduced on February 26, 1986. As described in *Goren*, it takes more than simply the subscription of units in a Limited Partnership to carry on a business on a regular and continuous basis. All that occurred before February 1986 with respect to the Type 3 Limited Partnerships, was the subscription of units by an entity operating and controlled by Mr. Bellfield. None of the expenses

[63] *Goren v. R.*, [1997] 3 C.T.C. 2025, 98 D.T.C. 1963 [*Goren*].

incurred prior to the grandfathering date were incurred for the purpose of the Type 3 Limited Partnerships earning or gaining income. This is simply another example of papering the file in an attempt to legitimize the fraudulent scheme and allow Mr. Bellfield another year of selling Limited Partnerships to continue the Ponzi scheme despite the introduction of new tax rules.

b) Section 67:

(i) The Law

[415] Section 67 of the *Act* provides a general limitation on the deductibility of expenses or outlays that are otherwise deductible under the *Act*, requiring that the expenses be reasonable in circumstances. The provision states:

> 67. In computing income, no deduction shall be made in respect of an outlay or expense in respect of which any amount is otherwise deductible under this Act, except to the extent that the outlay or expense was reasonable in the circumstances.

[416] The Appellants accurately summarized the law on this issue at page 35–36 of their Final Submissions:

> In a leading case on the section, the Court in *Gabco Limited v. Canada (Minister of National Revenue - M.N.R.)* concluded:
>
> > It is not a question of the Minister or this Court substituting its judgment for what is a reasonable amount to pay, but rather a case of the Minister or the Court coming to the conclusion that no reasonable business man would have contracted to pay such an amount having only the business consideration of the appellant in mind.
>
> Reasonableness measures the expense in terms of its magnitude or quantum. While there may be a subjective element on the part of the trier of fact, there should be a search for the objective component.
>
> > *Mohammad v. Canada*, [1997] F.C.J. No. 1020 (F.C.A.)at para. 28, […]
>
> The determination of whether an expense is "reasonable" should be made as of the time the expenditure was made and not with the benefit of hindsight. Further, reasonableness is an open-ended concept that requires the judgment and common sense of an objective and knowledgeable observer with reference to the open marketplace.
>
> > *Williams v. Canada*, 2009 TCC 93 at para. 16, [Williams] […]

Safety Boss Ltd. v. Canada, [2000] T.C.J. No. 18 (T.C.C.) at para. 27 […]

Simply paying more than fair market value for a product is not necessarily unreasonable. On this point, the Federal Court of Appeal has concluded:

> While it may be true, as suggested in *Mohammad*, that paying fair market value for something is prima facie reasonable, I am unable to agree with the Crown that it necessarily follows that paying more than fair market value for something is unreasonable. There may be circumstances in which a decision to pay more than fair market value for something is a reasonable decision. [emphasis added]

Petro-Canada v. Canada, 2004 FCA 158 at para. 64, [Petro] […]

…

It is trite law that it is not the court's position to second guess the business judgment of taxpayers. Often dubbed the Business Judgment Rule, errors in business judgment, unless the Act stipulates otherwise, do not prohibit one from claiming deductions for losses arising from those errors.

Tonn v. Canada, [1995] F.C.J. No. 1635 (C.A.) at para. 39 […]

Similarly, section 67 is not a mechanism to reduce expenses based on poor business judgement. Accordingly, expenses will not be denied simply because a person, with the benefit of hindsight, made a poor business decision.

Hammill v. Canada, [2005] F.C.J. No. 1197 (F.C.A.) at paras. 52-53, [*Hammill*], […] *Williams*, supra at para. 16 […]

[417] The Respondent in turn, amongst other arguments, referred to the oft-cited quote by the Federal Court of Appeal in *Hammill* regarding the application of section 67:

> 53. The choice of words (reduce or eliminate) is not accidental. The Supreme Court was setting-up section 67 as the proper means of testing the reasonableness of an expense once a business has been found to exist. It was doing so after having explained that at the first level of inquiry (i.e. the existence of a source of income and the relationship between an expense and that source) courts ought not to second guess the business judgment of the taxpayer (Stewart, supra, paragraphs 55, 56 and 57). Section 67 was identified as the statutory authority pursuant to which an inquiry could be made as to the reasonableness of an expense. In my view, the Supreme Court in Stewart acknowledged that there is no inherent limit to the application of section 67, and that in the appropriate circumstances, it can be used to deny the whole of an expense, if it is shown to be unreasonable.

(ii) Analysis

[418] By any measure of common sensibility, the expenses allegedly incurred were not reasonable in the circumstances and are barred from deductibility under section 67 because many of them were not incurred in whole or in part, or if they were incurred, were not incurred for a profit motive other than for a profit to Mr. Bellfield. All in all, the expenses were not reasonable in the circumstances in consideration of the entire scheme. In terms of the expenses themselves, recorded on the financial statements and relied upon by the investors in claiming their losses, there was no regard on Mr. Bellfield or OCGC's part as to a) whether they were legitimate or b) if they were reasonable in quantum for services rendered, if they were rendered at all. Many of the amounts claimed appeared to be entirely manufactured and had no basis in reality.

I: CONCLUSION

[419] I decline to address every alternative argument raised by the Respondent. My canvassing of the legal issues herein and my resulting conclusions, namely the lack of a source of income, the non-existence of genuine Limited Partnerships, the further determination that the expenses, when incurred, were not incurred for business purposes, as well as the alternative arguments I addressed briefly, are more than sufficient to dispose of this appeal. For the reasons outlined, the four appeals are dismissed.

J: COSTS

[420] The Court will receive submissions on costs in writing within 45 days of the date of this decision with written submissions limited to fifteen pages of text. Costs submissions should address the following issues: a) should either party be entitled to costs; b) if the answer to the first question is in the affirmative, what type of costs? That is, costs based on the Tariff, or some costs award other than the Tariff based on Rule 147 including consideration of settlement offers, if any. Any evidence on the issue of costs should be by way of affidavit with each party entitled to put in a response affidavit within 15 days of receiving the other party's cost submissions. If the parties want to be heard orally on the issue of costs, please advise the Court in

writing, in addition to written submissions, at the time of filing the written submissions and the Court will advise if it will entertain oral submissions.

Signed at Ottawa, Ontario, this 7th day of January, 2014.

"E.P. Rossiter"

Rossiter A.C.J.

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REASONS FOR JUDGMENT BY:	Associate Chief Justice E.P. Rossiter
DATE OF JUDGMENT:	January 7, 2014

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