

**UNITED STATES DISTRICT COURT
DISTRICT OF MINNESOTA**

United States of America,

Plaintiff,

Civil No. 08-05348 ADM/JSM

v.

Thomas Joseph Petters; Petters Company,
Inc., a/k/a PCI; Petters Group Worldwide, LLC;
Deanna Coleman, a/k/a Deanna Munson;
Robert White;
James Wehmhoff;
Larry Reynolds, and/or dba Nationwide International
Resources, aka NIR;
Michael Catain and/or dba Enchanted
Family Buying Company;
Frank E. Vennes, Jr., and/or dba Metro Gem
Finance, Metro Gem, Inc., Grace Offerings
Of Florida, LLC, Metro Property Financing,
LLC, 38 E. Robinson, LLC, 55 E. Pine, LLC,
Orlando Rental Pool, LLC, 100 Pine Street
Property, LLC, Orange Street Tower, LLC,
Cornerstone Rental Pool, LLC, 2 South
Orange Avenue, LLC, Hope Commons, LLC,
Metro Gold, Inc.,

Defendants,

Douglas A. Kelley,

Receiver,

Gary Hansen,

Receiver.

**MEMORANDUM OF LAW IN SUPPORT OF THE MOTION TO APPROVE
THE COORDINATION AGREEMENT AMONG PLAINTIFF UNITED STATES
OF AMERICA, THE RECEIVER, THE CHAPTER 11 TRUSTEE OF PETERS
COMPANY, INC., ET AL., AND THE CHAPTER 7 TRUSTEE OF POLAROID
CORPORATION, ET AL. N/K/A PBE CORPORATION, ET AL.**

Douglas A. Kelley, by and through his counsel, respectfully submits this memorandum of law in support of his motion to approve the Coordination Agreement among Plaintiff United States of America, the Receiver, the Chapter 11 Trustee of Petters Company Inc., et al., and the Chapter 7 Trustee of Polaroid Corporation, et al. n/k/a PBE Corporation, et al. (the “Coordination Agreement”). Capitalized terms used, but not defined herein, shall have the meaning ascribed to them in the Coordination Agreement.

BACKGROUND AND ARGUMENT

1. On October 6, 2008, this Court issued an Order for Entry of Preliminary Injunction, Order Appointing Receiver and Other Equitable Relief, [Docket No. 12], as subsequently amended on October 14, 2008 [Docket No. 43], October 22, 2008 [Docket No. 70] and December 8, 2008 [Docket No. 127] (collectively, the “Receivership Order”) and appointed Douglas A. Kelley as Receiver (the “Receiver”) for Petters, PCI and PGW, as well as certain entities owned and controlled 100% by such entities.

2. Pursuant to the Receivership Order, “the Receiver is authorized to take exclusive immediate custody, control, and possession of all the property, assets, and estates belonging to or in the possession, custody, or under the control of Defendants, wherever situated ... divert mail and to sue for, collect, receive, take in possession, hold, liquidate or sell and manage all assets of Defendants and other persons or entities whose interests are now held by or under the direction, possession, custody, or control of

Defendants.” Receivership Order, Section IV, ¶ B1. Furthermore, “[t]he Receiver shall have the power and authority to perform any other act necessary or desirable to accomplish any of the foregoing.” Receivership Order, Section IV, ¶ B9.

3. On December 1, 2008, and through the Superseding Indictment entered June 3, 2009, Petters, PCI and PGW were indicted by a federal grand jury on charges of (i) mail fraud, (ii) wire fraud, (iii) conspiracy to commit mail fraud and wire fraud, and (iv) conspiracy to commit money laundering, in violation of 18 U.S.C. §§ 371, 1343, 1956 and 1957. *See* Indictment, Doc. No. 75 and Superseding Indictment, Doc. No. 196, *United States of America v. Petters et al.*, Case No. 08-cr-00364 (RHK-AJB) (D. Minn.) (the “Criminal Fraud Case”). Petters was also indicted on charges of money laundering. *Id.* The Honorable Richard H. Kyle was assigned to the case. The indictment alleges that Petters and the Individual Defendants used PCI and PGW, as well as their subsidiary entities, to orchestrate a massive Ponzi scheme to defraud investors out of more than \$3 billion.

4. On December 2, 2009, a jury in the United States District Court of the District of Minnesota found Petters guilty of all 20 counts charged in the Indictment and Superseding Indictment. On April 8, 2010, Petters was sentenced to 50 years in prison for his crimes. The Individual Defendants are currently awaiting sentencing. Pursuant to the Court’s *Preliminary Order of Forfeiture*, Case No. 08-cr-00364, Doc. No. 395, certain property, including real property, proceeds from the sale of real property and accounts were forfeited to the United States pursuant to 18 U.S.C. § 981(a)(1)(C) and 28 U.S.C. § 2461(c). *Id.* at ¶¶ 1 & 2. A general money judgment was also entered against

Petters in the amount of \$3,522,880,614.10 in favor of the United States. *Id.* at ¶3. As a result of Petters' conviction, the United States asserts the right to forfeit all proceeds of the criminal acts conducted as part of this fraudulent scheme, including all assets of PCI and PGW and their subsidiary entities, including PBE Corporation and its subsidiaries.

5. Pursuant to an order entered on June 3, 2010, Judge Kyle held that "determining complex issues of fact related to the amount of the victims' losses would both complicate and prolong the sentencing process to such a degree that the need to provide restitution is outweighed by the burden it would impose" and declined to order restitution. *Order*, at p. 10-11, Doc. No. 459 in the Criminal Fraud Case.

6. For the reasons stated herein, the Receiver believes it is in the best interest of these estates to compromise and resolve their respective claims to property subject to the Preliminary Order of Forfeiture. This proposed resolution will preserve property of the receivership and property of the PCI Estates, PGW Estate and the PBE Estates in order to maximize recovery to legitimate victims and creditors of the massive Ponzi Scheme. Through the coordination of the efforts of the United States, the Receiver, the Trustee and Stoebner, the ongoing expenses of administration of these various entities and estates will be materially reduced, thereby maximizing any resulting recovery for victims and creditors.

7. On August 16, 2010 the United States, the Receiver, the Trustee and Stoebner, after several months of intense negotiations, entered into and executed a Coordination Agreement, a true and correct copy of which is attached to the Declaration of Daryle Uphoff as Exhibit A.

8. The Coordination Agreement accomplishes several goals. First, the Coordination Agreement equitably and efficiently allocates assets and causes of action among the Receiver, the Trustee, Stoebner, the Receiver and the United States, and removes the risk of forfeiture of substantially all of the assets of the PCI Estates, PGW Estate, the PBE Estates, the Petters Capital Estate, the Petters Aviation Estate and each of their subsidiary entities. Second, the Coordination Agreement accounts for and allocates among the several bankruptcy estates expenses incurred for their respective benefit and allocates such expenses relating to actual or potential third party litigation commenced or to be commenced by the Trustee, Stoebner or the Receiver. Ex. A at Section III. Third, the Coordination Agreement resolves the criminal liability of PCI and PGW and the important consequences of such corporate criminal liability and the potential divestiture of estate assets through forfeiture by the United States of corporate assets which are currently administered by the Trustee and Stoebner in their respective bankruptcy cases. Ex. A at Section II. Lastly, it provides for a material wind-down of the Receivership with respect to the Individual Defendants. Ex. A at Section I.

9. This case involves an intersection and collision of laws, involving cases flowing independently of each other consisting of a federal civil receivership, federal criminal proceedings and a multitude of bankruptcy cases. Each body of law suggests a method of resolving the different and competing claims a victim or creditor may have to the same property. Each body of law concurrently has, as its intended purpose, a different result or remedy each was enacted to promote. The rights and duties of all of the constituent parties necessary to reach legally mandated ends can and do conflict while

attempting to reach the same ultimate purpose, to efficiently maximize the recovery for the victims and creditors of this massive fraud.

10. In every possible instance, the absence of coordination among the various parties in these cases will diminish the recovery of the victims and creditors of this fraud. As a result and to the credit of all of the parties involved, this Coordination Agreement is presented to the Court as the best possible way to proceed in these cases to maximize any available recovery to victims and creditors.

11. Fraudulent schemes, and particularly Ponzi schemes, pit victim against victim because, in most instances, the funds recovered are not sufficient to satisfy the claims of all of the numerous creditors and victims. The same is true here. Additionally, many of the victims and creditors of the Petters Ponzi Scheme are making claims before both the Bankruptcy Court and in multiple proceedings in the District Court, with resolution of such claims requiring consideration of both bankruptcy and criminal law with each having a comprehensive means for collecting and distributing assets. These multi-faceted approaches to claims, however, would strain already limited resources and cause the Trustee, Stoenner, the Receiver and the United States to expend significant resources competing against each other for many of the same assets in order to distribute such assets to predominantly the same creditors or victims.

12. The United States, the Receiver, the Trustee and Stoenner believe that by entering into this Coordination Agreement they will maximize the recovery of assets and distributions to creditors and victims while minimizing the risks, costs and expenses of administering the receivership and bankruptcy estates.

13. In addition to resolving issues and claims regarding assets of Petters and the Individual Defendants, the Coordination Agreement also resolves outstanding criminal charges against PCI and PGW. PCI and PGW, as corporations, are civilly and criminally liable for the acts of their officers, agents and employees. The evidence presented at Petters' trial and the guilty pleas of the Individual Defendants demonstrate that PCI and PGW were the legal entities through which Petters and the Individual Defendants committed their crimes. The additional investigation conducted by the Trustee and his professionals bear this out as well. The Individual Defendants utilized PCI and PGW to fraudulently obtain and launder billions of dollars from individuals, investment groups, institutional investors and hedge funds. Through PCI and PGW, Petters and the Individual Defendants induced investments through the use of forged documents, false financial reports and data and meaningless security agreements and other pledges of assets. Petters and the Individual Defendants caused investors to invest funds in both PCI and PGW that were simply used to repay prior investors in the Ponzi Scheme and support their lavish lifestyles.

14. Therefore, there is little doubt that the United States could seek to forfeit or execute on the tangible or intangible assets of both the PCI Estates and the PGW Estate and their respective subsidiaries. Such actions by the United States would very likely divest the PCI Estates and the PGW Estate of substantially all estate assets, greatly diminishing the potential recovery to creditors and victims, as pursuit of claims would be materially impaired or claims would not be pursued and administration of the PCI Estates and the PGW Estate could be brought to a halt. In exchange for guilty pleas, the

Coordination Agreement preserves the property of the PCI Estates and the PGW Estate through the agreement of the United States not to seek forfeiture or otherwise execute on assets of the PCI Estates, the PGW Estate and their respective subsidiaries.

15. Since the commencement of the Civil and Criminal Fraud Cases, the Receiver, Trustee and Stoebner have incurred expenses that have provided benefit to the Receivership and each of the respective bankruptcy cases, particularly the costs and expenses of the forensic accounting work necessary to examine and assess the hundreds of bank accounts, tens of thousands of transactions and tens of billions of dollars of transactions that comprise the Petters Ponzi Scheme.

16. The Receiver retained PwC to perform the forensic accounting analysis involving the entire Petters organization, including inter-company transfers throughout that organization and transfers to and from third parties. It would be incredibly inefficient, if not impossible, in a case of this magnitude involving what may be one of the most complex Ponzi schemes in history (and thereby necessitating one of, if not the most complex forensic projects ever undertaken) to have each one of over 100 entities owned directly and indirectly by Petters separately hire a forensic accountant for each entity to compile and analyze the underlying data and produce a report, when each transaction often involved multiple entities through which funds passed. It is for that reason, as combined with the experience and resources of PwC, that PwC was retained by the Receiver to do the forensic work on behalf of all entities. The Receiver has also advanced certain funds to the Petters Estates since the Petition Dates to cover operational expenses and otherwise allow for the administration of these estates for the benefit of

victims and creditors. The Coordination Agreement obviates the need for litigation to resolve the allocation of such costs and expenses among the Receiver, the Trustee and Stoebner and will provide demonstrable benefit to each of these estates. The Parties to the Coordination Agreement recognize and agree that forensic work performed by PwC has benefited non-receivership entities.

17. The Parties have extensively negotiated the terms of the Coordination Agreement for several months and have resolved the significant issues described herein in light of the risks associated with litigating such matters, and in order to avoid fact-intensive, protracted and costly litigation. The Coordination Agreement will avoid actual and imminent uncertainties regarding the intersection of these conflicting bodies of bankruptcy, federal equity receiver law and criminal law and will allow all parties to move forward in a unified and coordinated manner to maximize the recovery of assets for the benefit of victims and creditors. Absent such agreement, the United States, through its power of criminal and civil forfeiture, likely would seek to forfeit all assets attributable to criminal activity, including those of the Petters Estates.

18. As Judge Rakoff observed in *United States v. Dreier*, 682 F. Supp. 2d 417 (S.D.N.Y. 2010), “[a]n under-appreciated evil of substantial frauds ... is how they pit their victims against one another.” *Id.* at 418.

Where, as here, the funds remaining after the fraud is uncovered are insufficient to make whole ... numerous victims and creditors, these unfortunates are left to squabble over who should get what ... In this case, moreover, resolution of these competing claims involves consideration of three bodies of law-criminal law, securities law, and bankruptcy law-that cannot always be reconciled without some friction. For some time now, it has been evident to this Court in presiding over the criminal action against Dreier, and to the judges presiding over the civil

enforcement action brought against Dreier by the Securities and Exchange Commission and the bankruptcy proceedings involving the estates of Dreier and his law firm, Dreier LLP, that these inherent tensions are best addressed through coordination and cooperation by all concerned.

Id.

19. Judge Rakoff's words are as applicable in these instant cases as they were in the Dreier Ponzi scheme case. The Bankruptcy Code is a finely-tuned mechanism for the "comprehensive means of collecting and distributing assets." *United States v. Frykholm*, 362 F.3d 413, 417 (7th Cir. 2004) (Easterbrook, J.). The Parties recognize and agree that while forfeiture is an effective means to recover assets, the Bankruptcy Code "provide[s] a superior way to marshal ... assets and distribute them to creditors." *Id.*

20. The Coordination Agreement is in the nature of a pre-emptive settlement agreement outlining the rights and responsibilities of the parties before any need for litigation arises. "Settlement agreements are generally encouraged and favored by the courts ... [i]n the absence of mistake or fraud, a settlement agreement will not be lightly set aside." *Justine Realty Co. v. American Nat'l Can Co.*, 976 F.2d 385, 391 (8th Cir. 1992). "The general principle that the law favors settlement agreements has been recognized for over 100 years." *Liddell by Liddell v. Bd. of Educ. of City of St. Louis*, 126 F.3d 1049, 1056 n. 9 (8th Cir. 1997) (citing *Williams v. First Nat'l Bank*, 216 U.S. 582, 595, 30 S.Ct. 441, 445, 54 L.Ed. 625 (1910) (compromises of disputed claims are favored by the courts) (citing *Hennessy v. Bacon*, 137 U.S. 78, 11 S.Ct. 17, 34 L.Ed. 605 (1890))). "The law strongly favors settlements. Courts should hospitably receive them ... [a]s a practical matter, a remedy that everyone agrees to is a lot more likely to succeed than one to which the defendants must be dragged kicking and screaming." *Liddell by Liddell v.*

Bd. of Educ. of City of St. Louis, 126 F.3d 1049, 1056 (8th Cir. 1997) (quoting *Little Rock Sch. Dist. v. Pulaski County Special Sch. Dist. No. 1*, 921 F.2d 1371, 1383 (8th Cir. 1990)).

21. The Coordination Agreement will avoid actual and imminent uncertainties regarding the intersection of conflicting bodies of law and will allow all parties involved to move forward in a unified and coordinated manner to maximize the recovery of assets for the benefit of victims and creditors.

CONCLUSION

For the foregoing reasons, the Receiver respectfully requests the Court to issue its Order Approving the Coordination Agreement.

DATED: August 18 , 2010

LINDQUIST & VENNUM P.L.L.P.

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