

**UNITED STATES DISTRICT COURT
DISTRICT OF MINNESOTA**

UNITED STATES OF AMERICA,

Case No. 08-cv-5348 ADM/JSM

Plaintiff,

v.

THOMAS J. PETTERS, et al.,

**SECOND REPORT OF THE
RECEIVER**

Defendants.

Douglas A. Kelley (hereinafter the “Receiver”) respectively submits his second report to the Court summarizing major activities during the second 60 days of the receivership.

I. POLAROID CORPORATION BANKRUPTCY FILING

The principal development in the Receivership since the first report was the filing of Chapter 11 Petitions for Polaroid Corporation (“Polaroid”) and nine of its affiliated entities in December 2008. Bankruptcy filings for Polaroid and its affiliates were necessitated by several factors. First, Polaroid had significant operating losses in 2008 exceeding \$100,000,000. Before it sought bankruptcy protection, Polaroid sustained cash losses of approximately three to four million dollars a month. Second, sale or refinancing of Polaroid could only be accomplished in a bankruptcy context given Polaroid’s relationship with other entities owned or controlled by Thomas J. Petters.

Motions were filed to permit Polaroid and its related entities to continue to operate in the normal course of business. The use of cash collateral was authorized by the Bankruptcy Court.

II. PROPOSED SALE OF POLAROID

On January 24, 2009, Polaroid signed an agreement, subject to Bankruptcy Court approval, to sell substantially all of its assets, except cash, to PHC Acquisitions, LLC for \$42,000,000. The agreement was reached after Polaroid's investment banker, Houlihan, Lokey, Howard & Zukin ("Houlihan Lokey"), conducted a world-wide search for potential purchasers and received bids from five interested parties. PHC's bid was selected since it provided the greatest value to Polaroid's creditors. A motion to approve the bidding procedures and set a date for auction of Polaroid's assets was heard on February 18, 2009 and approved by the Bankruptcy Court. The auction will be held in March 2009.

III. LITIGATION FILED TO SET ASIDE POLAROID SECURITY INTERESTS

On February 12, 2009, Polaroid filed adversary proceedings against hedge funds Acorn Capital Group ("Acorn") and Ritchie Management ("Ritchie"). The actions seek to set aside security interests that Acorn and Ritchie obtained in Polaroid's assets in 2008. Acorn's security interest purports to secure an alleged indebtedness of approximately \$281,000,000. Ritchie's security purports to secure an alleged indebtedness of about \$260,000,000. Polaroid seeks to have the security interests invalidated as fraudulent conveyances.

IV. APPOINTMENT OF DOUGLAS A. KELLEY AS TRUSTEE FOR BANKRUPT COMPANIES

In December 2008, the Office of the United States Trustee for the District of Minnesota (“U.S. Trustee”) filed a motion requesting the appointment of a Chapter 11 Trustee in the Petters Group Worldwide (“PGW”) and Petters Company, Inc. (“PCI”) bankruptcies. The U.S. Trustee subsequently appointed Douglas A. Kelley as the Chapter 11 Trustee for PGW and PCI. Ritchie objected to Kelley’s appointment, and a hearing was held before the Bankruptcy Court in January 2009. No decision has yet been issued.

V. ACTIVITIES OF PROFESSIONALS RETAINED BY RECEIVER

A. Lindquist & Vennum P.L.L.P.

Lindquist & Vennum has performed the following services on behalf of the Receiver:

1. Prepared and filed Chapter 11 petitions and schedules for Polaroid and nine affiliated entities.
2. Negotiated the asset purchase agreement between PHC Acquisitions and Polaroid.
3. Prepared and filed a motion to approve bidding procedures and establish an auction date for the Polaroid sale.
4. Prepared and filed responses to objections to the bidding procedures filed by Acorn, Ritchie, and the unsecured creditor committees of PGW, PCI and Polaroid.
5. Prepared and filed memoranda on behalf of the Receiver to the motion by the United States Trustee to appoint a Chapter 11 Trustee and to the objections filed by Ritchie to the appointment of Douglas A. Kelley as Chapter 11 Trustee.

6. Compiled and filed bankruptcy schedules and related statements in the Bankruptcy Court for PGW and ten of its affiliated entities and PCI and eight of its affiliated entities.
7. Represented the Receiver in negotiations between and among Sun Country Airlines, Elite Landings and Petters Aviation Leasing on issues involving airplane leases with CIT and sale of aircraft.
8. Analyzed security interests given by Polaroid to Acorn and Ritchie, and prepared and filed adversary proceedings against Acorn and Ritchie in Polaroid's Chapter 11 case seeking to void the transfer of those security interests as fraudulent conveyances and preferences.
9. Represented the Receiver in rejecting PGW's lease for the corporate headquarters and in negotiating new leases at the premises for PGW and Polaroid. Sought and received approval to transfer PGW's membership interest in the building to the owner and landlord of the premises at 4400 Baker Road. Prepared and filed motions, affidavits, a stipulation and proposed order seeking approval for all these transactions from the Bankruptcy Court.
10. Analyzed Polaroid's interest in a joint venture to develop Polaroid's former corporate campus site into a retail/office complex, and, after determining that no value existed, prepared and filed a motion to reject Polaroid's lease of that property, which was approved by the Bankruptcy Court.
11. Obtained this Court's approval for Petters Real Estate Group LLC to enter into a voluntary foreclosure agreement with Home Federal Bank after determining that property mortgaged to the bank lacked any equity.
12. Assisted in negotiating listing agreements for real estate owned by a Petters' affiliate in Summit County, Colorado and in seeking approval to sell a residence of Tom Petters in Keystone, Colorado.

B. PricewaterhouseCoopers, LLP ("PwC")

PwC provided the following services to the Receiver during the period covered by this report:

1. Tracing Sources and Uses of Funds - PwC requested and received bank account transactional data and supporting documentation from 2002-2008 for certain PCI and PGW entities as well as for Enchanted Family Buying

Company and Nationwide International Resources. PwC is compiling a list of open and closed bank accounts for these entities. Additional bank account transactional data necessary for forensic analyses has been identified and requested.

PwC is analyzing and categorizing cash flows in and out of the bank account data received to date. For each bank account, PwC is identifying, categorizing, and summarizing cash flows for payors and payees.

PwC is compiling an inventory of notes payable that PCI and certain PGW entities entered into with investors. PwC is matching each note's activity to the bank account transactional data. PwC will use these analyses to summarize the amount of principal and interest paid to each investor by year, and to determine each investor's outstanding principal and interest.

2. Electronic Discovery - PwC worked with PGW and Polaroid IT employees to identify and preserve electronically stored information pertaining to certain current and former employees.
3. Asset Searches - PwC performed investigative research to identify information concerning receivership defendants Thomas Petters, Deanna Coleman, James Wehmhoff, Bob White, Michael Catain, and Larry Reynolds, as well as their business associates and other former PCI/PGW employees.
4. PwC's efforts included searching for and identifying real property ownership and related mortgages and/or liens, personal corporate interests, additional corporations affiliated with PCI/PGW, civil litigation histories, Uniform Commercial Code filings (UCC) and other possible business associates of the receivership defendants.

C. FTI Consulting Inc.

FTI Consulting Inc. provided these services during the reporting period:

1. Documented assets held by PGW and PCI for the Receiver.
2. Provided business-related advice to enable the Receiver to make informed decisions regarding Polaroid, Welsh Baker Road LLC, SPB Development Company Ltd, PFG Aspen Walk LLC, patents, trademarks, domain names, Central America Holdings, Broad Sign, Juice Media Worldwide, Business Impact Group, Acton & Mohave Limited Partnerships of Larry Reynolds, miscellaneous receivables, and various minority stock investments.

D. PwC – Corporate Advisory and Restructuring (“PwC-Car”)

PwC-Car provided these services:

1. Advised and assisted the Receiver to analyze multiple alternatives for debtor-in-possession financing for MN Airlines LLC (Sun Country). Analysis included meetings and discussion with Sun Country’s management, its bankruptcy counsel, its outside financial advisor, counsel for the unsecured creditor committee, and its financial advisor. Identified various options for financing as well as proposals to purchase Sun Country.
2. Advised and assisted the Receiver in analyzing proposals to terminate certain aircraft leases between CIT and Sun Country; advised and assisted the Receiver in reviewing a proposed transaction involving two aircraft financing leases with Petters Aircraft Leasing; analyzed Sun Country’s weekly cash flow forecast.
3. Advised and assisted the Receiver in analyzing multiple offers to purchase assets of Polaroid.

VI. INDIVIDUAL DEFENDANTS

A. Tom Petters

Assets Liquidated/Other Deposits to the Receivership Account	\$178,533.24
Less: Paid Asset Preservation and Approved Personal Living Expenses	<u>(\$146,478.72)</u>
Receiver Account Balance as of February 13, 2009	<u>\$ 32,054.52</u>

Personal bank account balances have been transferred to the Receiver’s Account, except where Petters pledged the bank accounts as collateral for loans. The Receiver is investigating certain lenders “setoff” of some bank account balances against loans.

As noted in a Special Report of the Receiver filed on January 22, 2009, the Receiver learned that Tom Petters failed to disclose a \$50,000 withdrawal from Tam O’Shanter Lodge and Convention Center shortly before the receivership order. Petters

directed payments from these funds to friends and relatives and used money to pay for personal expenditures and telephone calls from jail. The Receiver has recovered \$26,804.35 of the remaining funds and has deposited those monies into the Receiver's Account.

The Receiver has paid utilities and maintenance expense to preserve value of Mr. Petters' assets. There currently is not sufficient money in Mr. Petters' personal receiver account to service his mortgages or pay taxes on the real property.

Child support authorized by the Court was paid to Tracy Mixon in December 2008. Payments for January 2009 and February 2009 remain pending while the Receiver investigates Ms. Mixon's receipt of funds from the Tam O'Shanter operating account. Nanny compensation and child care expenses are being paid.

A purchase offer has been received for the personal residence in Keystone, CO. Court approval for the sale will be requested. Two other parcels of land in Summit County, CO are also listed for sale.

The Manalapan, FL and Wayzata, MN residences have been listed for sale, with listing prices of \$11,900,000 and \$8,250,000, respectively. Market appraisals have been obtained for the Plymouth, MN and Winter Park, FL residences, but those properties have not yet been listed for sale.

A detailed inventory of personal property was prepared for the residences in Keystone, Manalapan, and Wayzata. Personal property belonging to others that was left in these homes has been, or is being, returned. The remaining property will be sold with the residences, or will be sold at auction or by consignment.

Four offers have been received to purchase Mr. Petters' fleet of luxury automobiles. Court approval for a sale is being requested.

A purchase offer has been received for Petters' 2004 Tiara 2900 Coronet boat. Court approval for the sale is being requested. Mr. Petters also owns a 1999 Tiara S2 boat, currently docked in Florida. The Receiver is obtaining a market valuation of that boat.

B. Deanna Coleman

Assets Liquidated/Deposits to Receivership Account:	\$3,363,230.92
Asset Preservation and living expenses paid:	(<u>36,068.77</u>)
Receiver account balance as of February 11, 2009	<u>\$3,327,162.15</u>

Bank and investment accounts owed by Deanna Coleman have been liquidated by the Receiver. Additional assets including Timberwolves' season tickets were identified, surrendered to the Receiver, and sold.

The Receiver participated in additional interviews with Ms. Coleman regarding her assets. Coleman provided the Receiver with an updated list of assets including the proceeds from a closed bank account and the sale of a boat. Ms. Coleman voluntarily turned over those proceeds to the Receiver.

During her interviews, Ms. Coleman identified certain properties she gave to third parties. The United States Attorney's Office has served a copy of the Receivership Order on recipients of Ms. Coleman's assets. All were informed that they may not accept, transfer or dissipate the Coleman assets without the prior approval of the Receiver. In addition, they are to fully disclose and identify their holdings to the Receiver.

Ms. Coleman's home has been videotaped and inventoried. The Receiver and Ms. Coleman have entered into an occupancy agreement for the Plymouth residence. A real estate broker has been identified and the home is being offered for sale.

C. Robert White

Assets Liquidated/Deposits to Receivership Account	\$ 3,004,886.36
Asset Preservation and living expenses paid:	(<u>213,223.58</u>)
Receiver account balance as of February 11, 2009	<u>\$ 2,791,662.78</u>

Bank accounts owned by Robert White have been or are being liquidated by the Receiver. Mr. White closed a previously unidentified account with Forex.com Inc and voluntarily turned over the liquidated funds to the Receiver.

Mr. White's home has been videotaped and inventoried. An appraisal confirms that liens against the property leave little or no equity in the home. The Receiver will be working with lienholders and Mr. White's attorney to determine how to avoid expending additional Receiver funds on the property.

Robert and Robyn White were married on February 22, 2008. Mrs. White provided the Receiver with receipts, a copy of her prior divorce decree, and other documentation to prove her pre-marital interest in her home in Orono and personal property, including some furnishings in the White's Excelsior home, and her Volvo automobile. The Receiver has not been expending any funds towards these items and will release pre-marital assets to Mrs. White upon Court approval.

Personal property, including four boats owned by Mr. White, is being appraised and equity determined. The Receiver learned about a 26 foot Pace Ship Sailboat which

had not previously been identified by Mr. White as an asset. Preliminary appraisals of this and other boats confirm little or no equity. Appraisal of the vessel “Spirit”, a 65 foot 1987 Kanter sailboat, suggests some equity. That boat is being offered for sale by the Receiver.

The Receiver is obtaining an appraisal and will be selling a Porsche owned by Mr. White.

D. Jim Wehmhoff

Assets Liquidated/Deposits to Receivership Account	\$ 1,273,028.96
Asset Preservation and living expenses paid:	(<u>90,251.53</u>)
Receiver account balance as of February 11, 2009	<u>\$1,182,777.43</u>

Mr. Wehmhoff’s bank accounts have been liquidated by the Receiver. Financial investment accounts and IRAs are in the process of being liquidated.

Mr. Wehmhoff’s home and lake cabin have been inventoried and videotaped. Photographs documenting the current condition and the condition at the time of purchase were provided by Mr. Wehmhoff for the two homes owned by his company, Intrepid Investment, LLC., that were purchased with Mr. Wehmhoff’s personal funds. Appraisals of the home, cabin, and two Intrepid properties are being obtained by the Receiver to determine equity and guide sale decisions.

A 2002 Lund boat, 1999 Wreves boat, 2004 Polaris 500 ATV, and 2003 Gem Electric car are being appraised. These items appear to have equity and will be sold by the Receiver.

E. Michael Catain

Assets Liquidated/Other deposits to receivership account	\$ 210,077.55
Asset preservation and personal expenses paid:	<u>(\$ 56,750.00)</u>
Receiver Account Balance as of February 11, 2009	<u>\$153,327.55</u>

Michael Catain does not appear to have accumulated significant wealth in bank or stock accounts. Only a few small bank accounts have been identified. Each was liquidated by the Receiver with the funds placed into the Receivership Account. Mr. Catain's assets lie in real estate and other business operations. One of his more successful business operations was the Bay Car Wash located in Excelsior, Minnesota.

The Court has authorized the sale of the Bay Car Wash and that sale is near closing. In early January 2009, the Receiver found that Catain was taking cash receipts from the car wash business and not depositing them into the bank account. The Receiver noted his findings in a Special Report filed with the Court.

Mr. Catain owned a Bentley Azure automobile which has been sold for \$175,000. A diamond ring and two watches were sold for \$32,100.

Mr. Catain also owns four record companies whose assets consist primarily of the rights to various music catalogs and/or recordings. The Receiver has hired a consultant to ascertain the present market value of these assets.

The Receiver is attempting to sell real estate including Mr. Catain's homes on Lake Minnetonka and in Costa Rica. A listing agreement for the Lake Minnetonka home expired December 31, 2008. The Receiver is selecting a new realtor and having this property appraised for sale.

F. Larry Reynolds

Assets Liquidated/Total deposits to receivership account	\$1,491,110.41
Asset preservation and personal expenses paid:	<u>(\$98,127.15)</u>
Receiver Account Balance as of February 11, 2009	<u>\$ 1,392,983.26</u>

The Receiver has liquidated checking and savings accounts, a money market account and stock accounts.

Since the last report, the Receiver sold both of Larry Reynolds' automobiles, a 2007 Bentley and a 2004 Ferrari, for \$225,000. His Las Vegas home is offered for sale.

Mr. Reynolds has three safe deposit boxes. One is located at the Bellagio Hotel Casino and the other two are at California banks. The FBI has been provided keys to these three boxes and will be converting all currency into cashiers checks, which will be deposited into the Receivership Account. Other items will be photographed and inventoried and returned to the boxes to be dealt with at a later time.

Reynolds also holds interests in real estate limited partnerships. The market for this real estate has been affected by the economy and the Receiver has hired a consultant to determine if additional funds in the form of capital calls should be expended.

Dated: 2/19/09

Respectfully submitted,

s/ Douglas A. Kelley

Douglas A. Kelley, Receiver

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