

**UNITED STATES BANKRUPTCY COURT
DISTRICT OF MINNESOTA**

In re:

**Jointly Administered under
Case No. 08-45257**

Petters Company, Inc. et al.,

Court File No. 08-45257

Debtors.

Court File Nos.:

(includes:

Petters Group Worldwide, LLC;

08-45258(GFK)

PC Funding, LLC

08-45326(GFK)

Thousand Lakes, LLC;

08-45327(GFK)

SPF Funding, LLC;

08-45328(GFK)

PL Ltd., Inc.;

08-45329(GFK)

Edge One LLC;

08-45330(GFK)

MGC Finance, Inc.;

08-45331(GFK)

PAC Funding, LLC;

08-45371(GFK)

Palm Beach Finance Holdings, Inc.)

08-45392(GFK)

Chapter 11 cases
Judge Gregory F. Kishel

**GREENWICH INSURANCE COMPANY'S AND XL SPECIALTY INSURANCE
COMPANY'S MOTION FOR RELIEF FROM AUTOMATIC STAY, IF APPLICABLE,
TO ALLOW PAYMENT OF CERTAIN DEFENSE EXPENSES**

1. Greenwich Insurance Company ("Greenwich") and XL Specialty Insurance Company ("XL Specialty"), by and through undersigned counsel, hereby enter a limited appearance solely for the purpose of moving this Court, pursuant to Rules 4001(a) and 9014 of the Federal Rules of Bankruptcy Procedure, and 11 U.S.C. § 362(d), for relief from the automatic stay, to the extent applicable, to advance certain legal fees and expenses: (1) to Petters Group Worldwide LLC ("PGW") under a Private Company Reimbursement Insurance Policy issued to PGW by Greenwich (the "PGW Policy"); and (2) to Thomas Petters under the PGW Policy and under a Private Company Insurance Policy issued to Petters Company Inc. ("PCI") by XL

Specialty (the “XL Policy”). (The PGW Policy and PCI Policy are referred to collectively herein as the “Policies”, and PGW and PCI are referred to collectively as the “Debtors.”) This Court has jurisdiction over this motion pursuant to 28 U.S.C. §§ 1334 and 157(a), Local Rule 1070-1, Fed. R. Bankr. P. 5005 and applicable rules. This is a core proceeding.

2. The Court will hold a hearing on this motion at 10:30 o’clock a.m., on April 7, 2009, before the Honorable Gregory F. Kishel, Courtroom 2-A, Second Floor, 316 North Robert Street, St. Paul, MN 55101, or as soon thereafter as counsel may be heard.

3. Any response to this motion must be filed and delivered not later than April 2, 2009, which is three days before the time set for the hearing (excluding Saturdays, Sundays and holidays), or filed and served by mail not later than March 27, 2009, which is seven days before the date set for the hearing (excluding Saturdays, Sundays and holidays). **UNLESS A RESPONSE OPPOSING THE MOTION IS TIMELY FILED, THE COURT MAY GRANT THE MOTION WITHOUT A HEARING.**

4. Thomas Petters, the sole owner and former Chairman and Chief Executive Officer of PGW and the sole owner and former President of PCI, currently stands accused of orchestrating one of the largest Ponzi schemes in U.S. history. In the months following the federal government’s announcement of its investigation into alleged fraud by Mr. Petters and several of his business associates, all but one of those business associates have pleaded guilty to criminal charges, and all of those who have pleaded guilty claim that Mr. Petters was the mastermind behind and primary beneficiary of the fraudulent scheme. Mr. Petters, who was arrested on October 3, 2008 and is being held without bail, continues to proclaim his innocence and is mounting a defense for the criminal trial, which is currently slated to begin June 9, 2009. Mr. Petters and PGW, which also has been indicted for its alleged role in the Ponzi scheme, have

provided XL with notice of the criminal proceeding, as well as with notice of several civil actions filed against them, and have requested payment of defense expenses they incur in connection with the lawsuits. XL has reserved all of its rights under the Policies and applicable law. In addition, XL informed Mr. Petters and PGW that, although it believes the automatic stay is not applicable to such payments, out of an abundance of caution, and in light of the unusual circumstances and serious coverage issues raised by this matter, XL would need to obtain approval from this Court to begin making payments under the Policies. In order to grant XL's Motion, this Court is not required to determine whether or not the proceeds of the Policies are property of the Debtors' estates; rather, the Court is simply asked to grant XL relief from the stay for the purposes of paying reasonable fees, costs, and expenses. Any payments made would be subject to a full reservation of all of XL's rights under the Policies and applicable law.

5. On September 24, 2008, federal agents executed a search warrant on the headquarters of PGW and the personal residence of Mr. Petters. A few days later, Mr. Petters resigned from his positions with PCI and PGW. On October 2, 2008, the federal government filed a criminal complaint in the United States District Court for the District of Minnesota against Mr. Petters in a case captioned, *United States of America v. Thomas Petters and Larry Reynolds*, Case Number 08-MJ-364(FLN). That same day, the government also filed a Complaint for Permanent Injunction and Other Equitable Relief against PCI, Mr. Petters, and several of his business associates in a case captioned, *United States of America v. Thomas Joseph Petters, et al.*, Case No. 08-CV-5348 (D. Minn.) (the "Freeze of Assets Action"). On October 6, 2008, the federal government filed an amended complaint, adding PGW as a defendant.

6. An affidavit prepared by Special Agent Eileen Rice, and filed in connection with the Freeze of Assets Action, asserted that the FBI's investigation revealed that Mr. Petters,

Deanna Coleman (PCI's former Vice President of Operations), Robert White (PCI's former Chief Financial Officer and subsequent consultant to PCI), Enchanted Family Buying ("Enchanted"), Michael Catain (who allegedly controlled Enchanted), Nationwide International Resources, Inc. ("NIR") and Larry Reynolds (who allegedly controlled NIR) had engaged in a massive, fraudulent scheme pursuant to which investors were convinced to invest billions of dollars in PCI based on misrepresentations and false documents. Specifically, the affidavit asserted that investors were induced to invest money based on false purchase orders which purported to show PCI's purchase of goods and merchandise from Enchanted and NIR and the subsequent sale of those same goods and merchandise by PCI to well known stores like B.J.'s Wholesale Club, Sam's Club, Costco and Boscovs.

7. Within less than a month after the filing of the Freeze of Assets Action, Ms. Coleman and Messrs White, Catain and Reynolds entered guilty pleas in connection with charges levied against them. In their plea agreements, Ms. Coleman and Mr. White claim that, at the direction of Mr. Petters, they created the false purchase orders which purported to show the purchase of nonexistent goods and merchandise from Enchanted and NRI. They admit that they received millions of dollars for their participation in the fraud but further claim that the vast majority of the proceeds of the fraud went to Mr. Petters and PCI.

8. In their plea agreements, Mr. Catain and Mr. Reynolds agreed to plead guilty to one count of money laundering, claiming that since 2002, they had conspired with Mr. Petters to launder the proceeds of the fraud. Both Mr. Catain and Mr. Reynolds admit that the companies they controlled – Enchanted and NIR, respectively – were shell corporations with no real assets. Messrs. Catain and Reynolds further claim that, at the request of Mr. Petters, they accepted wire transfers from PCI's investors who thought their funds were being loaned to PCI to purchase

electronic goods from Enchanted or NIR. Instead of applying those funds towards the purchase of goods, Mr. Catain and Mr. Reynolds reportedly kept a small commission of between .025 and .05 percent of the funds and then transferred the remaining balance to PCI's bank account.

Between 2002 and September 2008, approximately \$12 billion reportedly was routed through the Enchanted account and another approximately \$12 billion was routed through NIR's account.

9. On December 1, 2008, a grand jury returned a 20-count indictment against Mr. Petters, PCI and PGW. Among other things, the indictment alleges that Mr. Petters, PCI, PGW, Ms. Coleman and Mr. White created false purchase orders, invoices, and financial statements in order to trick investors into lending funds to PCI. The indictment further alleges that funds provided by the investors were secured by promissory notes and security agreements that purported to pledge as collateral the nonexistent goods and merchandise referenced in the fake documents and/or fictitious accounts receivable. Consistent with the guilty pleas entered by Mr. Catain and Mr. Reynolds, the indictment asserts that, in furtherance of the scheme, Messrs. Reynolds and Catain entered into an agreement with the defendants pursuant to which they accepted "tens of billions of dollars" as payments from investors for the nonexistent merchandise and then forwarded those funds, minus a commission for their participation in the fraud, to accounts controlled by Mr. Petters, PCI and PGW. The indictment further asserts that, instead of using the investments to purchase the referenced goods and merchandise, Mr. Petters, PCI and PGW used the funds to make lulling payments to investors, to make large payments, sometimes exceeding millions of dollars, to individuals who assisted in the scheme, to fund businesses owned or controlled by the defendants, and to fund Mr. Petters' extravagant lifestyle. The indictment alleges the defendants have violated 18 U.S.C. §§ 371, 1341, 1343, 1956, and 1957, and charges Mr. Petters with two counts of conspiracy and 18 counts of mail fraud and money

laundering. PCI and PGW are named in the two conspiracy counts and in 10 of the counts alleging mail fraud and money laundering.

10. A few weeks after Mr. Petters was indicted, another one of his former colleagues, James Wehmhoff, PGW's former Executive Vice President – Finance, Tax and Treasury, agreed to plead guilty to one count of conspiracy to commit tax evasion and one count of aiding and assisting tax fraud. According to the plea agreement, Mr. Wehmhoff has acknowledged that he conspired with Mr. Petters and other employees of businesses owned by Mr. Petters to mischaracterize approximately \$60 million in payments made to or on behalf of Mr. Petters as loans when they should have been reported as income and to mischaracterize millions of dollars in payments to employees as gifts when they should have been reported as income. The plea agreement further asserts that Mr. Wehmhoff prepared personal tax returns for Mr. Petters and for employees of business entities owned by Mr. Petters, which he knew falsely underreported income. In addition, Mr. Wehmhoff's plea agreement states that he knowingly prepared false financial statements for Mr. Petters.

11. In the few weeks preceding and the weeks following the federal government's disclosure of its investigation, several civil lawsuits were filed against PCI, PGW, Mr. Petters, Ms. Coleman and Messrs. White, Catain and Reynolds, including *AI Plus, Inc., et al. v. Petters Group Worldwide, et al.*, Case No. 08-CV-5456 (D. Minn.); *Mars Hill Media v. Petters Group Worldwide, et al.*, Case No. 08-CV-5410 (D. Minn.); *Apriven Partners, LP, et al. v. Petters Group Worldwide, LLC, et al.*, Case No. 08-CV-5373 (D. Minn.); *Lancelot Investors Fund, LP, et al. v. Thomas Joseph Petters, et al.*, Case No. 08-CV-5399 (D. Minn.); *Interlachen Harriet Investments Limited v. Petters Group Worldwide, LLC, et al.*, Case No. 08-CV-5312 (D. Minn.); *Apriven Partners, LP v. Thomas J. Petters*, Case No. 08-CV-01760-M (N.D. Tex); *Acorn*

Capital Group, LLC v. Thomas J. Petters, Case No. 08 CIV. 7236 (S.D.N.Y.); *Ritchie Capital Management, LLC, et al. v. Thomas J. Petters, et al.*, Case No. 2008 L 51021 (Cir. Ct, Cook Cty, IL); and *LG Electronics, Inc. v. Petters Group Worldwide, LLC, et al.* (S.D. Tex), Case No. 08-cv-163. (These lawsuits are collectively referred to herein as the “Civil Actions.”)

12. PCI, PGW, Messrs. Petters, White, Reynolds, Catain and Wehmhoff and Ms. Coleman (collectively, the “Receivership defendants”) eventually entered into stipulations with the federal government in the Freeze of Assets Action pursuant to which Douglas A. Kelley was appointed as their Receiver. On October 22, 2008, the Honorable Ann D. Montgomery, United States District Court for the District of Minnesota, entered an order staying civil litigation against the Receivership defendants. On December 8, 2008, Judge Montgomery entered an amended order, which among other things, continues to stay actions against the Receivership defendants, although it carves out criminal actions; actions or proceedings by a governmental unit to enforce such governmental unit’s police or regulatory power; the enforcement of a judgment, other than a money judgment, obtained in an action or proceeding by a governmental unit to enforce such governmental unit’s police or regulatory power; or participation by creditors or other interested parties in ongoing bankruptcy proceedings filed by the Receiver. Thus, for now, the Civil Actions are subject to Judge Montgomery’s stay order.

13. Greenwich issued Private Company Reimbursement Insurance Policy No. ELU105480 to PGW for the policy period June 25, 2008 to June 25, 2009. Subject to all of its terms and conditions, the Policy provides a \$10,000,000 maximum aggregate limit of liability, inclusive of Defense Expenses,¹ for all Loss resulting from Claims under the Management

¹ Unless defined in this Motion, capitalized terms are defined in the Policies. A copy of each policy is attached as Exhibit 1 and Exhibit 2 to the Declaration of Kristine Tejano Rickard.

Liability and Company Reimbursement Coverage Part (“MLCRC Part”)² first made during the Policy Period against PGW and/or its Insured Persons for Wrongful Acts. *See* Exhibit A, Declaration of Kristine Tejano Rickard, Ex. 1, PGW Policy, Declarations, Item 3; MLCRC Part, § I. This is part of, and not in addition to, the \$10,000,000 maximum aggregate Limit of Liability provided for all Claims made under the PGW Policy during the Policy Period. *See id.*, PGW Policy Declarations, Item 3(d); General Terms and Conditions (“GTC”), § III(A)(1).

14. XL Specialty issued Private Company Insurance Policy No. ELU105060 to PCI for the policy period June 1, 2008 to June 1, 2009. Subject to all of its terms and conditions, the PCI Policy provides a maximum aggregate Limit of Liability of \$5,000,000, inclusive of Defense Expenses, for all Claims made against PCI and/or its Insured Persons during the Policy Period under its MLCRC Part.³ *See* Exhibit A, Declaration of Kristine Tejano Rickard, Ex. 2, PCI Policy, Declarations, Item 3; MLCRC Part, § I. This is part of, and not in addition to, the \$6,000,000 maximum aggregate Limit of Liability provided for all Claims made under the PCI Policy during the Policy Period. *See id.*, PCI Policy Declarations, Item 3(d); GTC, § III.A.1.

15. Each of the Policies contains two insuring agreements. Insuring Agreement I(A) of the PGW Policy provides coverage for Loss (which includes Defense Expenses) resulting from a Claim made against PGW Insured Persons if such Loss is not permitted or required to be paid by PGW as indemnification, while Insuring Agreement I.A of the PCI Policy provides

² Because the MLCRC Part appears to be the only coverage part of the PGW Policy that currently is implicated, XL limits its discussion of the applicable Policy provisions to the MLCRC Part. Other coverage parts of the PGW Policy may be implicated in the future in other actions or claims. Similar bases for relief from the stay, if applicable, would apply to such other coverage parts of the PGW Policy.

³ As with the PGW Policy, because the MLCRC Part appears to be the only coverage part of the PCI Policy currently implicated, XL limits its discussion to the MLCRC Part. Other coverage parts of the PCI Policy may be implicated in the future in other actions or claims. Similar bases for relief from the stay, if applicable, would apply to such other coverage parts of the PCI Policy.

similar coverage for Insured Persons of PCI. Insuring Agreement B of the Policies provides coverage (1) to the extent that the Insured Company indemnifies any of its Insured Persons for covered Loss in connection with claims made against them, or (2) for covered Loss from a Claim made against the Insured Company. *See id.*, PGW Policy, MLCRC Part, § I and PCI Policy MLCRC Part, § I

16. Coverage under the Policies is subject to satisfaction of the applicable retention amount. With regard to the PGW Policy, there is a \$0 retention with respect to Insuring Agreement I(A) and \$50,000 with respect to Insuring Agreement I(B). *See id.*, PGW Policy, Declarations, Item 4. With respect to the PCI Policy, there is a \$0 retention under Insuring Agreement I.A and \$100,000 under Insuring Agreement I.B. *See id.*, PCI Policy, Declarations, Item 5. Each of the Policies further provides that, in the event of the Insured Company's financial insolvency, the retention amount applicable to Insuring Agreement A shall apply. *See id.*, PGW Policy, MLCRC Part, § IV(C) and PCI Policy, MLCRC Part, § IV.C.

17. Under each of the Policies, it is the duty of the Insureds, and not of XL, to defend any Claim asserted against them. *Id.*, PGW Policy, Endorsement No. 30 and PCI Policy, Endorsement No. 11. Loss potentially covered under the Policies, however, includes Defenses Expenses, which is defined by the Policies as "reasonable legal fees and expenses incurred in the defense of any Claim." *Id.*, PGW Policy, GTC, § II(E) and PCI Policy, GTC, § II.E.

18. Each of the Policies also contains a Tie In Limits Endorsement which provides, among other things, that the premiums for the PGW Policy, PCI Policy and a policy issued to another of Mr. Petters' companies, Thomas Petters, Inc. (the "TPI Policy"), were "negotiated with the understanding that all policies would have shared limits of liability." *Id.*, PGW Policy, Endorsement No. 24, and PCI Policy, Endorsement No. 19. The endorsement further provides

that XL's maximum aggregate limit of liability for all Loss from all Common Claims shall be \$10,000,000, which amount shall be part of and not in addition to XL's maximum aggregate Limit of Liability for all Loss from all Claims under the respective Policies. *Id.* Any payment of Loss, including Defense Expenses, for Common Claims under the PGW Policy, PCI Policy, or TPI Policy reduces the Limit of Liability available under the other policies for Common Claims. *Id.*

19. Coverage under the Policies is limited by certain, terms, conditions and exclusions. Endorsement No. 13 to the PCI Policy, for example, provides:

The Insured represents that the statements and particulars contained in the Applications are true, accurate and complete, and agree that this Policy is issued in reliance on the truth of that representation, and that such particulars and statements, which are deemed to be incorporated into and constitute a part of this Policy, are the basis of this Policy. No knowledge or information possessed by any Insured will be imputed to any other Insured. With respect to the Company only, no knowledge or information possessed by any Insured other than the President, Chief Executive Officer, Chief Financial Officer, Chairman of the Board, General Counsel (and Human Resources Director if Employment Practices Liability is purchased) of the Company will be imputed to the Company. In the event that any of the particulars or statements in the Application are untrue, this Policy will be void with respect to any Insured who knew of such untruth or to whom such knowledge is imputed.

See Exhibit A, Declaration of Kristine Tejano Rickard, Ex. 2, PCI Policy, Endorsement No. 13.

“Application,” as defined by the PCI Policy, includes “the application attached to and forming part of this Policy” and “any materials submitted therewith, which shall be retained on file by the Insurer and shall be deemed to be physically attached to this Policy.” *Id.*, PCI Policy, GTC, § II.A.

20. Mr. Petters signed the renewal application, dated April 8, 2008, submitted for the PCI Policy. *See* Exhibit A, Declaration of Kristine Tejano Rickard. PCI 's "Combined Balance Sheet, September 30, 2007 and 2006," also was submitted in connection with the renewal application. *Id.* The Combined Balance Sheet included "current liabilities" and "current accounts receivable" and, according to Special Agent Rice's affidavit, Ms. Coleman has admitted that "current accounts receivable" included on similar financial statements prepared by PCI were based on PCI's false documents and invoices.

21. Endorsement No. 29 to the PGW Policy provides:

The Insured represents that the statements and particulars contained in the Application, as well as the statements and particulars contained in all prior applications, if any, previously submitted to the Insurer, are true, accurate and complete, and the Insured agrees that such statements and particulars, which are deemed to be incorporated into and to constitute a part of this Policy, are material to the risk assumed and form the basis of this Policy. No knowledge or information possessed by any Insured will be imputed to any other Insured. In the event that any of the statements and particulars contained in the Application or in any prior application previously submitted to the Insurer is untrue, this Policy will be void only with respect to any Insured who knew of such untruth.

See Exhibit A, Declaration of Kristine Tejano Rickard, Ex. 1, PGW Policy, Endorsement No. 29. "Application" is defined by the PGW Policy as "the application attached to and forming part of this Policy" and "any materials submitted therewith, which shall be retained on file by the Insurer and shall be deemed to be physically attached to this Policy." *Id.*, PGW Policy, GTC, § II(A).

22. Mr. Petters signed the renewal application, dated May 2, 2008, submitted in connection with the PGW Policy. *See* Exhibit A, Declaration of Kristine Tejano Rickard. In connection with the renewal application, as well as in connection with the applications submitted

for the prior policy years, PGW submitted Combined Balance Sheets, which appear to have incorporated, among other things, the financial information of PCI. *Id.*

23. The Policies also contain a Fraudulent/Criminal Acts exclusion, which excludes coverage for a Claim:

brought about or contributed to in fact by:

- (1) any intentionally dishonest, fraudulent or criminal act or omission or any willful violation of any statute, rule or law; or
- (2) any profit or remuneration gained by any Insured to which such Insured is not legally entitled;

as determined by a final adjudication in the underlying action. Each Insured agrees that, if the Insurer has no liability to an Insured for Loss as a result of a Claim by reason of this Exclusion (A), such Insured will repay the Insurer upon demand all Defense Expenses paid on behalf of such Insured in connection with such Claim.

See Exhibit A, Declaration of Kristine Tejano Rickard, Ex. 1, PGW Policy, MLCRC Part, § III(A), as amended by Endorsement No. 20, and Ex. 2, PCI Policy, MLCRC Part, § III.A., as amended by Endorsement No. 10.

24. PGW and Mr. Petters have requested coverage under the PGW Policy for Loss, including Defense Expenses, they incur in connection with the Criminal Action, the Freeze of Assets Action and the Civil Actions (collectively, the “Actions”). Mr. Petters, as a former director and officer of PCI, also has requested coverage for the Actions under the PCI Policy.

25. In separate correspondence to Mr. Petters and PGW, XL acknowledged receipt of the notices, reserved all of its rights under the Policies and applicable law, and identified certain policy terms, conditions and exclusions, including, but not limited to, the ones set forth above,

which may limit or preclude coverage for the Actions.⁴ With respect to the Policies' representations clauses, XL noted its particular concern that Ms. Coleman's statements to the FBI indicate that the financial information submitted to XL may be false; that all of the individuals who have been charged with crimes relating to the alleged fraud have agreed to plead guilty and claim that Mr. Petters was the central figure in the fraud; and that the FBI claims to have numerous tape recordings in which Mr. Petters admits his culpability and further claims that he admitted culpability when interviewed by FBI agents on September 24, 2008.

26. XL's correspondence also noted that, since Mr. Petters is an insured under the PCI Policy and PGW Policy, the Tie In Limits endorsements are implicated by this matter, thus meaning that XL's maximum liability for all Loss, including Defense Expenses, incurred in connection with the Actions is \$10,000,000. In addition, XL informed Mr. Petters and PGW that, in order to avoid any inadvertent violation of the automatic stay, and in light of the unusual circumstances and serious coverage issues raised by this matter, XL must obtain approval of this Court to make payment for Defense Expenses.⁵

⁴ XL's letters also identified certain exclusions that preclude coverage for a few of the Civil Actions in their entirety. Because XL has determined that there is no coverage for those lawsuits, this Motion does not address Mr. Petters' and PGW's requests for payment of costs and fees incurred in those lawsuits.

⁵ Although Mr. Petters and PGW have requested coverage for the Actions, they have not submitted invoices for legal fees and expenses incurred in connection with any of the Actions, including the Criminal Action. XL is aware of an order entered by Judge Montgomery on December 22, 2008 in which she authorized payment of approximately \$1.9 million in legal fees and expenses incurred by the Receiver defendants and further authorized the Receiver to seek reimbursement for those amounts under applicable insurance policies, including directors' and officers' liability policies maintained by PCI and PGW. To date, XL has not received any request related to that Order and has no way of knowing at this point what, if any, amount of the fees and expenses referenced in that Order qualify as covered Defense Expenses incurred by PGW or Mr. Petters.

27. With regard to the automatic stay, each of the Policies provides that, in the event the insured company files for Chapter 11 bankruptcy protection, the Insureds:

(a) waive and release any automatic stay or injunction to the extent it may apply in such proceeding to the proceeds of this Policy under such Bankruptcy Laws; and

(b) agree not to oppose or object to any efforts by the Insurer or any Insured to obtain relief from the stay or injunction applicable to the proceeds of this Policy as a result of the commencement of such liquidation or reorganization proceeding.

See id., PGW Policy, Endorsement No. 3 and PCI Policy, GTC, § III.Q.

WHEREFORE, XL respectfully requests that the Court enter an order authorizing XL to advance payments under the Policies for Defense Expenses incurred by PGW and Mr. Petters in connection with the Actions. Such payments would be made subject to a full reservation of XL's rights under the Policies and applicable law to deny or limit coverage.

March 16, 2009

Respectfully submitted,

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One of Its Attorneys

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**GREENWICH INSURANCE COMPANY'S AND XL SPECIALTY
INSURANCE COMPANY'S MEMORANDUM IN SUPPORT OF THEIR
MOTION FOR RELIEF FROM AUTOMATIC STAY, IF APPLICABLE,
TO ALLOW PAYMENT OF CERTAIN DEFENSE EXPENSES**

Greenwich Insurance Company ("Greenwich") and XL Specialty Insurance Company ("XL Specialty") respectfully submit this Memorandum in Support of their Motion for Relief from Automatic Stay, if Applicable, to Allow Payment of Certain Defense Expenses (Greenwich and XL Specialty are referred to herein as "XL").

FACTS

The factual support for this memorandum is set forth in the attached Motion and is incorporated as if fully set forth herein.

LEGAL ARGUMENT

I. THE LAW IS NOT SETTLED AS TO WHETHER THE PROCEEDS OF A DIRECTORS AND OFFICERS-TYPE POLICY ARE PROPERTY OF THE BANKRUPTCY ESTATE

Because there is no clearly established rule as to whether the proceeds of a directors and officers-type policy, such as the PGW Policy and the PCI Policy, are property of a debtor's estate under 11 U.S.C. § 541 and, therefore, are subject to the automatic stay contained in 11 U.S.C. § 362, XL has brought its Motion out of an abundance of caution so as to avoid violating the stay. Although XL takes no position in its motion on whether the proceeds of the Policies are property of the estate, XL seeks entry of an order granting relief from the stay, to the extent applicable, for the purposes of paying reasonable and necessary Defense Expenses incurred and to be incurred by PGW and Mr. Petters in connection with the Actions. In light of the fact that the Policies may be void with respect to Mr. Petters and PGW pursuant to the Policies' respective representation clauses, as well as the fact that coverage will be precluded under the Policies if they are convicted or enter guilty pleas, XL understands that, even if the Court grants XL's Motion, it may decide, as other courts have, to place certain conditions or limitations on the payment of Defense Expenses.

The Eight Circuit has not directly addressed the issue of whether the proceeds of a directors and officers liability policy are property of a debtor's estate under 11 U.S.C. § 541. Although courts in other jurisdictions generally hold that a directors and officers *policy* is considered property of the debtor's estate, whether the *proceeds* of the policy also are property of the estate is not settled. *See, e.g., Pintlar Corp. v. Fidelity & Casualty Co. (In re Pintlar Corp.)*, 124 F.3d 1310, 1313 (9th Cir. 1997) (debtor corporation does not have an interest in insurance proceeds owed to its former directors and officers under a directors and officers insurance policy); *In re Minoco Group of Cos.*, 799 F.2d 517, 519 (9th Cir. 1986) (property held by the

debtor for the benefit of another does not constitute property of the estate); *In re Stevens*, 130 F.3d 1027, 1029 (11th Cir. 1997) (“the fact that the insurance policy is property of the bankruptcy estate, however, does not necessarily mean that the proceeds from that policy are also property of the estate. In some circumstances, a creditor or beneficiary other than the debtor may be entitled to proceeds distributed pursuant to an insurance policy that is property of a bankruptcy estate.”); *Reliance Ins. Co. v. Weis, et al.*, 148 B.R. 575, 581 (Bankr. E.D. Mo. 1992) (“As regards insurance policies, directors’ and officers’ liability (DOL) policies or otherwise, some courts have found that the policies are part of the estate, although the proceeds may not be.”); *In re First Cent. Fin. Corp.*, 238 B.R. 9, 16 (Bankr. E.D.N.Y. 1999) (“While a majority of courts consider a [D&O] policy estate property, there is an increasing view that a distinction should be drawn when considering treatment of proceeds arising under such policies”) (citations omitted); *In re Continental Airlines*, 203 F.3d 203, 216-17 (3d Cir. 2000) (the “proceeds from [an] insurance policy should be evaluated separately from the debtor’s interest in the policy itself”).

II. EVEN IF THE POLICY PROCEEDS ARE DETERMINED TO BE PROPERTY OF THE ESTATE, THE COURT MAY GRANT RELIEF FROM THE STAY TO ALLOW PAYMENT OF DEFENSE EXPENSES

Even if the Court concludes that the proceeds of the Policy are property of the Debtors’ estate, the Court can find that “cause” exists under 11 U.S.C. § 362(d) for relief from the stay for the purpose of permitting XL to advance reasonable and necessary Defense Expenses incurred by Mr. Petters and PGW in defense of the Actions. Section 362(d) provides that, upon the request of a party in interest, the Court may grant relief from the automatic stay by terminating, annulling, modifying, or conditioning such stay “for cause.” 11 U.S.C. § 362(d). The determination of “cause” for purposes of this section is determined on a case-by-case basis and is left to the sound discretion of the bankruptcy judge. *See Pursifull v. Eakin*, 814 F.2d 1501, 1504,

1506 (10th Cir. 1987). *See also In re Wilson*, 116 F.3d 87, 90 (3d Cir. 1997) (court must determine “what constitutes cause based on the totality of the circumstances in each particular case”).

In *Nat'l Union Fire Ins. Co. v. Titan Energy, Inc. (In re Titan Energy, Inc.)*, 837 F.2d 325 (1988), for example, the Eighth Circuit, citing in part to the Ninth Circuit's reasoning in *In re Minoco Group of Cos.*, held that certain third-party liability policies issued to the debtor were property of the debtor's estate because the estate was worth more with them than without them. The court further noted, however, that it would be appropriate for the bankruptcy court to lift the stay in order to allow a claimant to pursue its state court action against the debtor's insurer, National Union Fire Insurance Company of Pittsburgh, PA (“National Union”). National Union had filed an action in the insured's Chapter 7 bankruptcy proceeding, seeking, among other things, to rescind the policies and to stay an action previously filed by the claimant against National Union in Louisiana state court under Louisiana's direct action statute. The Eighth Circuit held that, although the bankruptcy court erred in dismissing the case for lack of jurisdiction, on remand, the lower court should refrain from proceeding on National Union's claims based on abstention grounds. *In re Titan Energy, Inc.*, 837 F.2d at 333. In addition, the Eighth Circuit noted that, because the policies were property of the debtor's estate, the state court action was subject to the automatic stay. *Id.* at 334, fn. 15. The court further noted, however, that 11 U.S.C. § 362(d) allows the bankruptcy court to lift a stay and stated that, in light of the circumstances in the particular case – which included, among others, the fact that the insured's Chapter 11 proceeding had been converted to a Chapter 7 proceeding and that there was no evidence that any of the insured's other creditors had made a claim to the policies' proceeds – the court would find it “entirely appropriate” for the bankruptcy court to grant any subsequently

filed motion to lift the stay so that the claimant could pursue its action in Louisiana state court.

Id.

In this case, sufficient “cause” exists to warrant granting relief from the stay to permit XL to pay Mr. Petters’ and PGW’s reasonable and necessary Defense Expenses under the Policies. As noted above, the Policies contain a provision pursuant to which the Insureds agreed that, in the event of a Chapter 11 bankruptcy proceeding, they (1) would waive and release any automatic stay to the extent it might apply to the Policies’ proceeds and (2) would not raise any objections to any attempt by XL or another Insured to obtain relief from any automatic stay. XL understands, however, that this Court must balance the request for advancement against the need to preserve the Debtors’ assets and against the fact that, in light of the allegations asserted by those who have already pleaded guilty, the information submitted in connection with the Policies, the Policies’ respective Representation Clauses and the Fraudulent/Criminal Acts exclusions, Mr. Petters and PGW ultimately may not be entitled to coverage under the Policies. *See In re Chari*, 262 B.R. 734, 737 (Bankr. S.D. Ohio 2001) (analysis of whether to lift stay requires a balancing of the relative harms to the debtor’s estate, if the stay is lifted, against the harms to other interested parties, should the stay remain in place); *see also In re Indian Palms Assocs., Ltd.*, 61 F.3d 197, 206 (3d Cir. 1995) (“Section 362(d) is . . . intended to balance the interests of the creditors and the debtor”). XL further understands that the Court may find that these factors constitute compelling reasons not to lift the stay or may decide, like other courts have, to lift the stay subject to a cap on Defense Expenses or subject to certain conditions. *See, e.g., Eastern Refra. Co. Inc. v. Forty Eight Insul. Inc.*, 157 F.3d 169, 172 (2d Cir 1998) (bankruptcy courts have power to modify or condition an automatic stay so as to fashion the appropriate scope of relief); *In re Vast Solutions, Inc.*, No. 01-32953 (SAF) (Bankr. N.D. Tex.

Apr. 14, 2003) (granting relief from stay, to extent applicable, to allow insurer to pay up to \$150,000 in defense costs); *In re InMold, Inc.*, No. 00-58067 (WS) (Bankr. E.D. Mich. April 21, 2003) (authorizing directors' and officer's liability insurer to advance defense costs subject to a cap of \$200,000); *Executive Risk Indem., Inc. v. Boston Reg'l Med. Ctr., Inc. (In re Boston Reg'l Med. Ctr., Inc.)*, 285 B.R. 87 (Bankr. D. Mass. 2002) (granting relief from the stay in order to permit use of the D&O policy proceeds for payment of defense costs subject to a cap); *In re Adelpia Communications Corp.*, 298 B.R. 49 (S.D.N.Y. 2003) (reversing bankruptcy court's finding that policy proceeds were property of debtor's estate but noting for consideration on remand that court imposed cap of \$300,000 per-insured for defense costs might be appropriate under 11 U.S.C. § 105(a), which allows bankruptcy courts to issue orders, processes or judgments necessary or appropriate to carry out provisions of the bankruptcy code); *In re Arter & Hadden, L.L.P.*, 335 B.R. 666, 674 (Bankr. N.D. Ohio 2005) (permitting directors' and officers' liability insurer to advance defense costs, conditioned upon insureds' filing applications for compensation or reimbursement with the Court as provided by Federal Rule of Bankruptcy Procedure 2016); *In re Laminate Kingdom, LLC*, Case No. 07-10279-BKC-AJC, 2008 Bankr. LEXIS 1594 (Bankr. S.D. Fla 2008) (granting relief from stay, to the extent applicable, but conditioning payment of attorney's fees upon approval by Court following filing of application for compensation or reimbursement with Court.)¹

¹ Copies of the *In re Vast Solutions, Inc.* and *In re InMold, Inc.* decisions are attached as Exhibits A and B.

CONCLUSION

For the foregoing reasons, XL respectfully requests that the Court enter an order authorizing XL to advance payments under the Policies for Defense Expenses incurred by PGW and Mr. Petters in connection with the Actions. Such payments would be subject to any conditions or cap, if any, imposed by the Court and would be made subject to a full reservation of XL's rights under the Policies and applicable law to deny or limit coverage.

March 16, 2009

Respectfully submitted,

FOLEY & MANSFIELD, PLLP

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By /e/ Thomas J. Lallier
One of Its Attorneys

Exhibit A

**UNITED STATES BANKRUPTCY COURT
DISTRICT OF MINNESOTA**

In re:

**Jointly Administered under
Case No. 08-45257**

Petters Company, Inc. et al.,

Court File No. 08-45257

Debtors.

Court File Nos.:

(includes:

Petters Group Worldwide, LLC;

08-45258(GFK)

PC Funding, LLC

08-45326(GFK)

Thousand Lakes, LLC;

08-45327(GFK)

SPF Funding, LLC;

08-45328(GFK)

PL Ltd., Inc.;

08-45329(GFK)

Edge One LLC;

08-45330(GFK)

MGC Finance, Inc.;

08-45331(GFK)

PAC Funding, LLC;

08-45371(GFK)

Palm Beach Finance Holdings, Inc.)

08-45392(GFK)

Chapter 11 cases
Judge Gregory F. Kishel

DECLARATION OF KRISTINE TEJANO RICKARD

I, Kristine Tejano Rickard, declare and state as follows:

1. I am currently employed as Vice President of XL Professional Insurance Company (“XL”), which is an entity related to Greenwich Insurance Company (“Greenwich”) and XL Specialty Insurance Company (“XL Specialty”) and handles claims for Greenwich and XL Specialty.
2. I submit this Declaration in support of Greenwich’s and XL Specialty’s contemporaneously filed Motion for Relief from Automatic Stay and Memorandum of Point and Authorities in Support of Motion for Relief from Automatic Stay, if Applicable, to Allow Greenwich and XL Specialty to Pay Certain Defense Expenses.

3. I am one of the persons who has custody and control of Greenwich's and XL Specialty's business records concerning Petters Group Worldwide LLC ("PGW") and Petters Company Inc. ("PCI"). These records are kept in the ordinary course of Greenwich's and XL Specialty's regularly conducted business activities, which is Greenwich's and XL Specialty's customary practice. I have reviewed Greenwich's and XL Specialty's files on this matter, which leads me to the summary set forth below. All facts set forth herein are either (a) facts of which I have personal knowledge or (b) an accurate summary of Greenwich's and XL Specialty's business records as set forth above.
4. The document attached hereto as Exhibit 1 is a true and correct copy of Private Company Reimbursement Insurance Policy No. ELU105480, issued to PGW for the policy period June 25, 2008 to June 25, 2009 (the "PGW Policy").
5. The document attached hereto as Exhibit 2 is a true and correct copy of Private Company Insurance Policy No. ELU105060, issued to PCI for the policy period June 1, 2008 to June 1, 2009 (the "PCI Policy").
6. I have reviewed Greenwich's underwriting file for the PGW Policy which contains, among other things, a renewal application, signed by Mr. Petters and dated May 2, 2008, and certain Combined Balance Sheets, which appear to have incorporated financial information of certain other entities owned and/or controlled by Mr. Petters, including PCI.
7. I also have reviewed XL Specialty's underwriting file for the PCI Policy which contains, among other things, a renewal application, signed by Mr. Petters and dated April 8, 2008, and PCI's Combined Balance Sheet, September 30, 2007 and 2006.

8. The documents attached hereto as Exhibit 3 are true and correct examples of the notice letters, without attachments, that PGW and Mr. Petters have sent to Greenwich and XL Specialty.
9. XL acknowledged receipt of the notices, reserved all of Greenwich's and XL Specialty's rights under the Policies and applicable law, and identified certain policy terms, conditions and exclusions that may limit or preclude coverage for the noticed matters. In addition, XL informed Mr. Petters and PGW that, in order to avoid any inadvertent violation of the automatic stay, and in light of the unusual circumstances and serious coverage issues raised by this matter, XL must obtain approval of this Court to make payment for Defense Expenses.
10. Pursuant to 28 U.S.C. § 1746, I declare under penalty of perjury that the foregoing is true and correct.

This 13 day of March, 2009


Kristine Tejano Rickard
Kristine Tejano Rickard

**UNITED STATES BANKRUPTCY COURT
DISTRICT OF MINNESOTA**

In re:

**Jointly Administered under
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PAC Funding, LLC;

08-45371(GFK)

Palm Beach Finance Holdings, Inc.)

08-45392(GFK)

Chapter 11 cases

Judge Gregory F. Kishel

I hereby certify that on March 16, 2009, I electronically filed the **Greenwich Insurance Company's and XL Specialty Insurance Company's Motion for Relief from Automatic Stay, if Applicable, to Allow Payment of Certain Defense Experts** with the clerk of the court by using the CM/ECF system, which will send a notice of electronic filing to:

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I further certify that I mailed the foregoing documents on March 16, 2009, to the following parties:

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MN Department of Revenue
Collections Division- Unit 550 Bky. Sec.
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**UNITED STATES BANKRUPTCY COURT
DISTRICT OF MINNESOTA**

In re:

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PAC Funding, LLC;

08-45371(GFK)

Palm Beach Finance Holdings, Inc.)

08-45392(GFK)

Chapter 11 cases
Judge Gregory F. Kishel

**ORDER GRANTING GREENWICH INSURANCE COMPANY'S AND
XL SPECIALTY INSURANCE COMPANY'S MOTION FOR RELIEF FROM
AUTOMATIC STAY, TO THE EXTENT APPLICABLE,
TO ALLOW PAYMENT OF CERTAIN DEFENSE EXPENSES**

This case came before the Court on March ____, 2009, on the Motion of Greenwich Insurance Company and XL Specialty Insurance Company, for Relief from the Automatic Stay, to the Extent Applicable, to Allow Payment of Certain Defense Expenses of Petters Group Worldwide LLC and Thomas Petters under the PGW Policy and PCI Policy (capitalized terms shall have the meaning ascribed thereto in the Motion, unless the context clearly requires otherwise). Appearances are noted on the record. Based on the arguments of counsel, moving documents and the record made at the hearing,

IT IS HEREBY ORDERED:

1. The automatic stay, to the extent applicable, is lifted to allow XL to pay covered Defense Expenses incurred in the Actions by PGW and Mr. Petters under the PGW Policy and PCI Policy, subject to a full reservation of all of XL's rights under the Policies and applicable law, including the right to deny or limit coverage for the Actions.

2. Nothing in this Order shall modify or alter the contractual rights and obligations provided for under the terms of the Policies.

3. Nothing in this Order shall be construed as an express or implied finding by the Court that the Policies and/or their proceeds are property of the Debtors' bankruptcy estates pursuant to 11 U.S.C. § 541 or that the automatic stay, 11 U.S.C. § 362, applies to the Policies and/or their proceeds.

4. This Order shall take effect immediately upon entry.

DATED: _____, 2009

UNITED STATES BANKRUPTCY JUDGE

Gregory F. Kishel