



# Lawsuit Claims GE Capital Could Have Stopped Petters' Multi-Billion Ponzi Scheme

<https://melandbudwick.com/2013/08/26/lawsuit-claims-ge-capital-could-have-stopped-petters-multi-billion-ponzi-scheme/>

## Walter Pavlo

According to a complaint filed on behalf of the liquidator of Palm Beach Finance Partners, GE Capital Corporation (GECC) had information that should have led it to believe that Thomas Petters was running a Ponzi Scheme back in 2000. However, GECC, Petters' lender at the time, decided to keep that information to itself .... eight years and \$3.5 billion later, the Feds would shut down Petters' operation and investors (victims) were out billions. Nearly one-third of the amount lost was from Palm Beach Finance (PBF) investors. GECC sought to have the civil complaint dismissed citing statute of limitations (more than 4 years) and it had no duty to tell PBF and that it had discovered any wrongdoing. On Friday, a ruling in the Southern District of Florida concluded that the Plaintiff (Liquidating Trustee for PBF) "sufficiently alleges the elements of a claim for civil conspiracy to commit fraud." In other words, the case against GECC is moving forward on the basis that it entered into a conspiracy with one of the largest Ponzi schemers in U.S. history.

PBF victims felt helpless after the discovery and collapse of Petters' scheme, which was uncovered when an employee of Petters Company Inc. (Minneapolis, MN) went to authorities. Deanna Lynn Coleman walked into the U.S. Attorney's Office in Minneapolis on September 8, 2008 and handed authorities information on a Ponzi Scheme that had been running for over a decade. The feds soon shut down the operation and arrested Petters, but he was not about to give up that easy. Petters claimed that he had run a successful business of buying large blocks of consumer goods and reselling them to large wholesale clubs, like Costco and Sam's Club, only to be duped by Coleman and others. Coleman, who admitted her own role in the fraud, cooperated extensively with the Feds and provided documentation that Petters was the mastermind of it all. His trial in November 2009 ended with a guilty



verdict and Petters was subsequently sentenced to 50 years in prison.

On the first day of the Petters trial, the government called witnesses to establish “when” the fraud had started. Those witnesses included executives who worked at GECC from 1998 through 2000, a time when GECC was providing financing secured by receivables from Petters’ customers. Those first few days of testimony piqued the interest of every victim who had invested in Petters after 2000 ... because, according to the lawsuit, the scheme had been discovered by GECC years before 2008.

Attorney Michael Budwick, who is with the law firm of Meland Budwick, P.A., is representing PBF bankruptcy trustee, Barry Mukamal, whose investors lost over \$1 billion, said that the opening testimony of the Petters trial in 2009 was the first time that anyone had heard of GECC having knowledge that Petters’ fraud (Petters Capital, Inc. ... one of many entities controlled by Petters). The first witness was John Marrone, a GECC associate who oversaw a \$50 million line of credit that was provided to Petters....his supervisor Paul Feehan was also called. They and an executive from Costco told of a deal that went bad, but was never reported to law enforcement authorities.

GECC sales people initially approached Petters in 1997 about a line of credit for his growing business. Petters was eager to get the financing and GECC did its initial due diligence by hiring Kroll & Associates to do a background check on Petters. What it found was as an arrest for forgery and bad checks along with lying to the court in another case. Not a good credit risk and GECC executive in charge of Risk & Underwriting, Catherine Midkiff, said that the company should pass on providing financing on the deal. On March 26, 1998, a \$50 million line of credit was extended to Petters Company by GECC. So, my guess is that she was overruled.

The deal, which carried significant risk, was offset by the significant profit that GECC had structured by collecting interest payments, inventory fees, collateral monitoring fees, fees for unused funds from the line of credit and a percentage of the profits on the success of each “purchase” of merchandise. That deal went so well that GECC gave another of Petters’ businesses, Red Tags, a \$55 million line of credit in 1999 and then in January 2000 a GECC executive, Richard Menczynski, wrote a glowing letter of recommendation to “To Whom It May Concern.” The letter would be splashed about for years to attract investors for Petters ... Menczynski went to work for Petters eight months after writing the recommendation as a vice president of finance at



Red Tags. He received a nice signing bonus and a salary bump in the new position.

By mid-2000, the Petters Company had become delinquent on payments. One of the main provisions of the agreement was that Petters would use a shared lockbox with GECC, a bank account set up to receive customer checks to pay down the line. As payments did dribble in from Petters, they came on company checks from Petters Company and not from “customers,” which was a sign that something was amiss. GECC decided to do a little more checking and it reached out to Costco, who then, according to reports provided to GECC by Petters, owed more than \$52 million from goods sold (collateral for the line of credit). It also appeared to be Petters Company’s only customer. The verification was sent to Petters Company who was to obtain a signature from Costco that they did indeed owe the funds. Petters forged a Costco-signature on the verification request and sent it back to GECC.

Petters continued to miss payments and GECC tired of “the check is in the mail,” excuses. GECC’s Feehan took action to contact Costco directly by phone, without Petters knowing, about the outstanding receivable report to try to get confirmation about amounts due to Petters .... Costco said that not only were the invoices fake but that the amounts due to Petters were just a few thousand dollars, not millions. When Petters found out about the call to Costco, he called Feehan yelling profanities to never contact his customers again. Knowing that Petters had falsified the report and essentially had no customers, Feehan put in motion actions to terminate the line of credit and asked for \$45,891,229 to close the line, which included all its fees ... including the success fee for sharing in the profits of the purchases supposedly made by Petters Company.

Messages began flowing from Petters that he was going to make good on his payments to GECC. Numerous voice messages were left by Petters for Feehan saying that he would make good on the final payment with one message being, Petters told Feehan, “I’ll just have investors pay you out, and you guys will be on your way.” By December of 2000, Petters had made good on his promise and GECC had been paid in full. GECC sent Petters a UCC-3, releasing its lien position on Petters Company receivables, thereby allowing another group of investors to step in .... Palm Beach Financial.

With a “letter of recommendation” from GECC, and a first position lien on the “receivables” PFB became the largest single source of funding for Petters’ scheme.



Up until just before the Feds moved in on Petters, the flow of money to PFB was not only routine but provided an above average return for its investors. When Petters started to come up short on payments, the co-founders of PFB (David Harrold and Bruce Prevost) replaced notes which were about to mature with new notes, and then not telling PFB investors. Both Harrold and Prevost have since pleaded guilty to that crime though both have stated that they knew nothing of the grand Petters Ponzi Scheme.

Deanna Lynn Coleman, who was involved in the scheme with Petters but was instrumental in his prosecution, was sentenced to a year in prison.

GECC's position has been that it had no duty to, or relationship with, PFB to tell them any information about the fraudulent disclosures made by Petters. It does bring up the question as to why PFB did not do its own due diligence as any responsible financial institution would do on behalf of its investors. The Court actually agreed with that stating that, "Whatever GECC knew about Petters' fraud, it came by that knowledge through diligent inquiries that any other lender, including the Palm Beach Funds, could have made."

GECC was in a tough position at the time. Had they gone to authorities suspecting Petters was a fraud, they would have most likely lost their entire investment. By keeping silent, they rolled the dice that Petters would come through ... and it paid off then, maybe not so much now. According to Budwick, "We are pleased with the Court's ruling and are looking forward to presenting PFB's bankruptcy trustee to a Florida jury." According to Budwick, PFB's trustee is looking to recover \$1.1 billion in losses and over 3-times that in damages. That would be a big hit for GE!