

UNITED STATES BANKRUPTCY COURT  
SOUTHERN DISTRICT OF FLORIDA  
WEST PALM BEACH DIVISION  
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In re:

Chapter 11

PALM BEACH FINANCE PARTNERS,  
L.P., a Delaware limited partnership, *et al.*,<sup>1</sup>

Case No. 09-36379-BKC-PGH  
(Jointly Administered)

Debtors.

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PALM BEACH FINANCE PARTNERS, L.P.,  
a Delaware limited partnership, and PALM  
BEACH FINANCE II, L.P., a Delaware  
limited partnership,

Adv. Pro. No. \_\_\_\_\_

Plaintiffs,

v.

US BANK, N.A., a national banking  
association, and M&I MARSHALL & ILSLEY  
BANK, a Wisconsin banking corporation,

Defendants.

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**COMPLAINT**

Palm Beach Finance Partners, LP and Palm Beach Finance II, LP (collectively, “Plaintiffs” or “Palm Beach”) hereby sue defendants US Bank, N.A. (“US Bank”) and M&I Marshall & Ilsley Bank (“M&I Bank”) and allege as follows:

**INTRODUCTION**

1. Banks have a unique perspective: they see where all the money comes from and where it all goes. Banks also have a unique responsibility: by law, they are required to know the

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<sup>1</sup> The address and last four digits of the taxpayer identification number for each of the Debtors follows in parenthesis: (i) Palm Beach Finance Partners, L.P., 3601 PGA Blvd, Suite 301, Palm Beach Gardens, FL 33410 (TIN 9943); and (ii) Palm Beach Finance II, L.P., 3601 PGA Blvd, Suite 301, Palm Beach Gardens, FL 33410 (TIN 0680).

purpose of the money flowing in and out of their accounts. US Bank and M&I Bank took on the specific responsibility to Plaintiffs to know that the over \$22 billion dollars flowing through their institutions for a single client were for legitimate transactions. That client was Thomas Petters and his companies (collectively, “Petters”) and Petters paid the Defendant banks substantial fees for the privilege of running a massive multi-billion dollar fraud through those very same accounts at US Bank and M&I Bank.

2. The fraud was simple and complete: every transaction was fake; there were no legitimate documents to support the transactions; and, with the exception of the investors like Plaintiffs, everyone who sent or received funds from Petters’ US Bank and M&I Bank accounts was in on the fraud. Thus, had the banks ever done what they are supposed to do by law and specifically told Plaintiffs they were doing—verified the legitimacy of the billions of dollars worth of transactions in their Petters’ accounts—the fraud would have been discovered. Instead, the Defendants apparently accepted Petters’ word over 22 billion times.

3. When every one of the transactions Defendants said was real turned out to be fake, Plaintiffs lost over \$1 billion dollars.

### **JURISDICTION AND VENUE**

4. This Court has subject-matter jurisdiction over this Adversary Proceeding, which relates to cases under title 11, United States Code, in the United States Bankruptcy Court for the Southern District of Florida, Case No. 09-36379-BKC-PGH, pursuant to 28 U.S.C. § 1334(b).

5. This Adversary Proceeding is a non-core “related” matter pursuant to which the Bankruptcy Court is authorized to issue proposed findings of fact and conclusions of law and submit them to the District Court for issuance of a final judgment pursuant to 28 U.S.C. § 157(c)(1).

6. Venue of this Adversary Proceeding is proper in the Southern District of Florida pursuant to 28 U.S.C. § 1409(a).

### **PARTIES**

7. Plaintiff Palm Beach Finance Partners, LP (“PBF”) is a limited partnership organized under the laws of the State of Delaware, with its principal place of business located at Palm Beach Gardens, Florida.

8. Plaintiff Palm Beach Finance II, LP (“PBF II”) is a limited partnership organized under the laws of the State of Delaware, with its principal place of business located at Palm Beach Gardens, Florida.

9. Defendant US Bank is a division of US Bancorp, a holding company headquartered in Minneapolis, Minnesota with nationwide operations.

10. Defendant M&I Marshall & Ilsley Bank is a Wisconsin banking corporation and is a subsidiary of Marshall & Ilsley Corporation, a financial services company headquartered in Milwaukee, Wisconsin with operations in Florida.

### **STATEMENT OF FACTS**

#### **A. Palm Beach’s Investment with Petters**

11. Palm Beach are two hedge funds based in Palm Beach Gardens, Florida whose investors include individuals, retirement plans, trusts and other hedge funds (the “Palm Beach Investors”).

12. The primary investment that the Palm Beach funds made was in asset-backed financing and in particular “closeout” sales – the transactions by which retailers or wholesalers get rid of slow-moving, excess inventory. Palm Beach only funded closeout sales brought to it by one broker: Thomas Petters.

13. Petters created a special purpose vehicle to issue promissory notes to Palm Beach: Palm Beach Holdings, Inc. f/k/a Petters Capital, Inc. (“Petters Capital”). Petters Capital sold promissory notes to Palm Beach and promised that the proceeds from the notes would be used to finance the purchase of consumer electronics which would be resold to retailers such as Costco. The collateral for the notes was supposed to be the consumer electronics bought with the proceeds of the notes.

14. Collectively Palm Beach invested in excess of \$1 billion with Petters. PBF I invested approximately \$225 million in funds contributed by its limited partners in exchange for secured, short-term promissory notes issued by Petters Capital. PBF II invested approximately \$850 million in funds contributed by its limited partners and investors in the Palm Beach offshore funds in exchange for secured, short term promissory notes issued by Petters Capital.

**B. Petters’ Ponzi Scheme**

15. In the fall of 2008, Petters’ massive fraudulent Ponzi scheme was discovered. Instead of purchasing closeout inventory, once Petters obtained funds from investors those funds would be transferred to sham vendors who would return the money back to Petters. Petters used that money for his own purposes and the remainder went to pay purported returns to investors to keep the scheme going.

16. The scheme is alleged to have started as early as 1995. Between 2002 and 2008 alone over \$22 billion dollars was transferred from Petters to the sham vendors and back to Petters again. That \$22 billion flowed through accounts at US Bank and M&I Bank.

**C. The Banks’ Role**

17. The Defendant banks were supposed to play a critical role in Palm Beach’s investment with Petters. Indeed, both US Bank and M&I Bank earned substantial fees on the

billions of dollars that flowed through their accounts as part of the Petters Ponzi scheme. Blowing the whistle on Petters would have meant a significant loss of income for the Defendant banks.

18. A typical transaction was supposed to work as follows. As the broker, Petters purported to negotiate the purchase and resale of new, high end merchandise (usually consumer electronics). Petters then purported to negotiate the terms of each exchange, and entered into a purchase contract with the vendor and a sale contract with the end purchaser, who typically was represented to be Costco.

19. Upon finalizing agreements for purchase and resale, Petters presented the deal to Palm Beach for financing to obtain the cash flow necessary to execute the purchase of the excess inventory and pay the vendor. If Palm Beach agreed, it would fund the deal in exchange for a promissory note issue by Petters Capital which allegedly would be repaid – at a premium and with fees – from the proceeds of the ultimate sale to an end purchaser, Costco. The notes were generally 180 days in duration and paid annualized interest of 15% or even higher.

20. As an assurance against fraud, Palm Beach required a series of checks to be completed before any investor money was released to Petters. Two of the most important safeguards were US Bank and M&I Bank.

21. All of the money Palm Beach invested in Petters—approximately \$1 billion—was transferred through PBFP's account at US Bank. All of the funds Petters transferred to Palm Beach came from either Petters' US Bank or M&I Bank accounts. This amounted to thousands upon thousands of transfers in both US Bank and M&I Bank.

22. This was no accident. Palm Beach was referred to US Bank and M&I Bank by associates of Petters. US Bank and M&I Bank bragged of their substantial relationship with

Petters and their sophistication and experience with these Petters transactions. In reliance on these representations, Palm Beach agreed to do business with US Bank and M&I Bank.

23. By law, every bank must “know their customer” and that includes knowing where the money flowing into the account is coming from and why and where it is going and why. This is particularly true if the amounts flowing in and out the account are sizable, as was the case with Petters where many transactions were in the millions of dollars. The purpose of these requirements is to detect and prevent crime and the banks have been made responsible for this duty for one simple reason: only the banks have the ability to see all the money and know its origin and destination. Both US Bank and M&I Bank had this duty with respect to the Petters accounts under common law due care standards.

24. Most significant to Plaintiffs, however, were the representations made by both banks about the due diligence and monitoring they did on the underlying Petters transactions—all of which must have been false because the transactions the banks approved were all fake.

**D. US Bank**

25. US Bank was a key gatekeeper for Palm Beach. US Bank was the Custodian on PBFB’s “Holdings” account which was the account used to transfer funds from Palm Beach to Petters to pay the vendors selling Petters the closeout inventory.

26. Once Palm Beach agreed to the deal, it would transfer the necessary funds to PBFB’s “Holdings” account at US Bank. As Custodian, US Bank, before releasing the Palm Beach funds to Petters, was supposed to verify the purchase by requiring and examining a sales confirmation, a purchase order, requisite insurance and a UCC-1 filing. US Bank represented to Palm Beach that no funds would be released for a Petters transaction unless the transaction had

been confirmed as real. Palm Beach relied on US Bank to perform this critical confirmation function as a safeguard against fraud.

27. As direct evidence of this reliance, Palm Beach touted US Bank's role as custodian to its own investors as a reason to invest in the Palm Beach funds that invested in Petters. Specifically, Palm Beach represented to investors that no funds would be released unless the purchase and resale orders had been executed, and Palm Beach had obtained title to and a UCC-1 secured interest in the goods, general casualty insurance on the goods, and creditor insurance on the end purchaser. Palm Beach confirmed in its Confidential Memoranda that it required these protections as a precondition to any lending. It was US Bank's job to make sure each of those safeguards was in place.

28. Instead of verifying the transactions as legitimate—which could not have happened because they were all fake—US Bank allowed the transfer of \$1 billion of Palm Beach Investors' money to a fraudster.

29. In addition to being the bank for PBFP, Petters also had an account at US Bank and Palm Beach drew substantial comfort knowing that US Bank therefore had knowledge of all sides of Petters' business including on how entire Petters operations was funded and was operating.

#### **E. M&I Bank**

30. In addition to the assurances of US Bank that it would verify each and every transaction, Palm Beach also had the assurances of M&I Bank, the other bank Petters used to both receive payments from the retailers and repay Palm Beach on the notes. Most importantly, the money into M&I Bank should have come from the retailers purchasing the purported goods. Instead, the money came from Petters or his affiliates. This was a bright red flag that should

have led M&I Bank not to approve the transaction. Nonetheless, M&I Bank approved each and every fraudulent transfer.

31. M&I Bank's purpose was to be another safeguard against fraud. Thus, the money for a transaction was to come into M&I Bank first and could only be released to US Bank if the money came from a retailer and the transaction otherwise was verified. By failing its stated purpose, M&I Bank failed Palm Beach.

32. The purported inventory purchase and sale transactions did not exist and the documents evidencing those transactions were fabricated. Petters was operating a Ponzi scheme where he used Palm Beach's funds to pay off other investors. Palm Beach alone lost \$1 billion dollars because the very transactions US Bank and M&I Bank confirmed as real were all fake.

**F. Additional Fraudulent Transactions**

33. In addition to the fraudulent transactions approved by the Defendant Banks that led to the release and ultimate loss of over \$1 billion of Palm Beach Investors' funds, the Defendant Banks also had knowledge of another red flag that should have alerted the Banks to the massive fraud: the roundtripping of funds between Petters and Lancelot Investment Management. ("Lancelot"). Lancelot was another hedge fund that invested in Petters and its principal, Gregory Bell, was a participant in the fraud and has been indicted.

34. Part of Lancelot and Bell's participation in the Ponzi scheme were roundtripping transfers where funds were transferred from Lancelot to Petters and from Petters back to Lancelot—in almost identical amount—in order to make it look like Petters was paying down notes. These transfers were in huge sums—\$20 million dollars, for example—and the roundtripping would be complete within hours. Between February 2008 and June 2008 alone, the amount of these roundtrip transactions totaled over \$1 billion dollars..



35. Although the nature and the amount of these transactions should have set off alarm bells in the Banks, the Banks remained silent. Despite knowing the significant business PBFP did with Petters, US Bank never told PBFP that its other customer Petters had these kinds of suspicious transactions in its accounts. To the contrary, the Banks continued to be cheerleaders for Petters. Had the Bank said something, given the volume and speed in which these transactions would occur, Palm Beach would have questioned the veracity of the Petters operations.

**FIRST CAUSE OF ACTION**

(Negligence Against US Bank)

36. Palm Beach repeats and realleges paragraphs 1-34 above as though fully set out in this claim.

37. US Bank owed a duty of care to Palm Beach, a duty not only inherent in its relationship to Palm Beach, but also as a result of its communications with Palm Beach regarding Palm Beach's investment.

38. US Bank breached its duties of care and did so with the knowledge that the injury from that breach would occur in Florida where Palm Beach is located.

39. As a direct and proximate cause of US Bank's breach, Palm Beach has been damaged in an amount to be proven at trial.

**SECOND CAUSE OF ACTION**

(Negligence Against M&I Bank)

40. Palm Beach repeats and realleges paragraphs 1-38 above as though fully set out in this claim.

41. M&I Bank owed a duty of care to Palm Beach, a duty not only inherent in its relationship to Palm Beach, but also as a result of its communications with Palm Beach regarding Palm Beach's investment.

42. M&I Bank breached its duties of care and did so with the knowledge that the injury from that breach would occur in Florida where Palm Beach is located.

43. As a direct and proximate cause of M&I Bank's breach, Palm Beach has been damaged in an amount to be proven at trial.

### **THIRD CAUSE OF ACTION**

(Breach of Contract Against US Bank)

44. Palm Beach repeats and realleges paragraphs 1-42 above as though fully set out in this claim.

45. US Bank had a contract with Palm Beach for valuable consideration.

46. Palm Beach duly performed under that contract, or its performance was excused.

47. US Bank materially breached its contract with Palm Beach.

48. The breaches by US Bank proximately caused damage to Palm Beach.

### **FOURTH CAUSE OF ACTION**

(Breach of Contract Against M&I Bank)

49. Palm Beach repeats and realleges paragraphs 1-47 above as though fully set out in this claim.

50. M&I Bank had a contract with Palm Beach for valuable consideration.

51. Palm Beach duly performed under that contract, or its performance was excused.

52. M&I Bank materially breached its contract with Palm Beach.

53. The breaches by M&I Bank proximately caused damage to Palm Beach.

**PRAYER FOR RELIEF**

WHEREFORE, Plaintiffs respectfully request judgment against Defendants, under all applicable causes of action, as follows:

1. actual compensatory, consequential, incidental, special and exemplary damages in an amount to be proven at trial;
2. punitive damages;
3. such civil penalties as allowed by law;
4. attorney's fees and costs of this suit as allowed by law;
5. pre-judgment and post-judgment interest as allowed by law; and
6. such other and further legal and equitable relief as the Court deems just and proper.

**DEMAND FOR JURY TRIAL**

Plaintiffs hereby demand a trial by jury on all claims.

Dated: December 21, 2009

Respectfully submitted,

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