UNITED STATES DISTRICT COURT
FOR THE DISTRICT OF MINNESOTA

UNITED STATES SECURITIES AND EXCHANGE COMMISSION,	:	
Plaintiff,	:	
v.	:	**CIVIL ACTION FILE NO.**
BRUCE F. PRÉVOST, DAVID W. HARROLD, PALM BEACH CAPITAL MANAGEMENT LP, and PALM BEACH CAPITAL MANAGEMENT LLC	:	
Defendants.	:	

COMPLAINT

Plaintiff United States Securities and Exchange Commission ("Commission") alleges as follows:

NATURE OF THE ACTION

1. This is a securities fraud case concerning investment fund managers who funneled more than a billion dollars of their clients' money into a multi-billion dollar Ponzi scheme perpetrated by Thomas J. Petters ("Petters").

2. The Defendants in this case are Bruce F. Prévost ("Prévost"), David W. Harrold ("Harrold"), and their management and investment advisory firms,

Palm Beach Capital Management LP ("PB Management") and Palm Beach Capital Management LLC ("PB Adviser").

3. From as early as 1995 through September 2008, Petters perpetrated a massive Ponzi scheme through the sale of promissory notes (the "Notes") to investors. Petters, a prominent Minnesota businessman who controlled an empire of companies, including Polaroid Corporation, Fingerhut Direct Marketing, and Sun Country Airlines, promised investors that Note proceeds would be used to finance the purchase of vast amounts of consumer electronics by certain vendors. The vendors would then resell the merchandise to certain "Big Box" retailers, including such well-known chains as Wal-Mart and Costco. Over the years, Petters raised billions through the sale of the Notes.

4. But in reality, there were no purchases and resales of consumer electronics. The vendors were shell companies acting in concert with Petters and no retailers participated in the purported transactions. Instead, Petters diverted billions of dollars to his own purposes and paid purported profits to investors with money raised from the sales of new Notes. Petters's purported inventory finance operation was nothing but a Ponzi scheme.

5. Petters raised much of his money by selling Notes to several large feeder-funds. Among the feeder-funds that bought Notes from Petters were two funds controlled by Prévost, Harrold, PB Management, and PB Adviser: Palm Beach Finance Partners, LP ("PBFP") and Palm Beach Finance II, LP ("PBFII" or, together with PBFP, the "Palm Beach Funds" or the "Funds"). The difference

between the two funds was that PBFII was a leveraged fund and PBFP was not. PBFII derived additional purchasing power above and beyond the monies contributed by its investors by borrowing money from two Cayman Islands funds that were also established by Prévost and Harrold: Palm Beach Offshore, Ltd. ("PBO") and Palm Beach Offshore II, Ltd. ("PBOII" and, together with PBO, the "Offshore Funds").

6. From 2004 through at least as late June 2008, the defendants funneled money into the Petters Ponzi scheme by selling interests in the Palm Beach Funds to investors throughout the United States. Investors in the Palm Beach Funds included individuals, foundations, family trusts and other hedge funds. The Funds invested all investor contributions into the Petters Ponzi scheme. Of the approximately $3.65 billion invested in the Petters Ponzi scheme at the time of its collapse, the Palm Beach Funds accounted for more than $1 billion.

7. During the same time period, Prévost, Harrold, PB Management, and PB Adviser earned more than $58 million in fees under their agreements with the Funds and the Offshore Funds.

8. Prévost, Harrold, PB Management, and PB Adviser defrauded the funds and investors in the funds. Prévost and Harrold (individually and through PB Management and PB Adviser) made false representations to investors in the Funds and the Offshore Funds regarding the safeguards purportedly provided by certain bank accounts (the "Collateral Accounts") held by the Funds. Prévost and Harrold told investors that they would use the Collateral Accounts to pay money

for the purchase of Notes directly to vendors and that money for the repayment of notes would come into the Collateral Accounts directly from the retailers. This arrangement purported to protect investors inasmuch as Note proceeds would not be paid to Petters and the role of the retailers in each transaction would ostensibly be verified by the direct, transparent receipt of their payments into the Collateral Accounts. This arrangement was especially important given that Prévost and Harrold did not intend to – and never did – inspect any of the merchandise underlying the Note transactions. But in reality, money for the repayment of Notes held by the Funds always came directly from Petters and never came from any retailers. Prévost and Harrold did not disclose this material fact to investors in the Funds and instead continued to disseminate their false representations regarding the Collateral Accounts.

9. Also, beginning in or about February 2008, after Petters had become unable to repay certain of the Notes held by the Funds, Prévost and Harrold (in their individual capacities and through PB Management and PB Adviser) and Petters acted together to concoct a series of bogus note exchange transactions to conceal Petters's inability to pay. Pursuant to the scheme, when Petters became unable to pay the principal and accrued interest on mature Notes, the Palm Beach Funds, on multiple occasions, exchanged groups of mature Notes that were due to be repaid on or about the date of the exchange for newly-issued Notes that were not due to be paid for six months and that purported to be collateralized by different merchandise. Instead of receiving cash payments and then reinvesting

that cash in new Notes as they had done in the past, Prévost and Harrold simply began exchanging old IOUs for new ones. At the same time, they continued to falsely report, in monthly communications to investors, that the funds were generating the same steady profits that they had generated from their inceptions. These overstated rates of return, in turn, resulted in the payment of excessive management fees and performance allocations to Prévost, Harrold, PB Management, and PB Adviser.

10. As a result of the foregoing, Defendants Prévost, Harrold, PB Management, and PB Adviser, directly and indirectly, have engaged in and, unless enjoined, will continue to engage in transactions, acts, practices and courses of business that violate Section 17(a) of the Securities Act of 1933 (the "Securities Act") [15 U.S.C. §77(q)(a)], Section 10(b) of the Securities Exchange Act of 1934 (the "Exchange Act") [15 U.S.C. §78j(b)] and Rule 10b-5 [17 C.F.R. §240.10b-5] promulgated thereunder, and Sections 206(1), 206(2) and 206(4) of the Investment Advisers Act of 1940 (the "Advisers Act") [15 U.S.C. §§ 80b-6(1), 80b-6(2), and 80b-6(4)] and Rule 206-4(8) [17 C.F.R. § 275.206-4(8)] thereunder.

11. As a result of the foregoing, Defendants Prévost and Harrold, directly or indirectly, have aided and abetted violations by PB Management and PB Adviser of Sections 206(1), 206(2), and 206(4) of the Advisers Act [15 U.S.C. §§ 80b-6(1), 80b-6(2), and 80b-6(4)] and Rule 206-4(8) [17 C.F.R. § 275.206-4(8)] thereunder.

12. The Commission brings this lawsuit to hold the Defendants accountable for their flagrant and repeated violations of the federal securities laws and to prevent further harm to investors.

JURISDICTION AND VENUE

13. The Commission brings this action pursuant to Section 20(b) of the Securities Act [15 U.S.C. §77t(b)], Sections 21(d) and 21(e) of the Exchange Act [15 U.S.C. §§78u(d) and 78u(e)], and Section 209(d) of the Advisers Act [15 U.S.C. § 80b-9(d)].

14. This Court has jurisdiction over this action pursuant to Section 22 of the Securities Act [15 U.S.C. § 77v], Section 27 of the Exchange Act [15 U.S.C. § 78aa], and Section 214 of the Advisers Act [15 U.S.C. § 80b-14], and 28 U.S.C. § 1331.

15. Venue is proper in this Court pursuant to Section 27 of the Exchange Act [15 U.S.C. § 78aa].

16. Acts, practices and courses of business constituting violations alleged herein have occurred within the jurisdiction of the United States District Court for the District of Minnesota and elsewhere.

17. Prévost, Harrold, PB Management, and PB Adviser, directly and indirectly, made use of the means and instrumentalities of interstate commerce and of the mails in connection with the acts, practices, and courses of business alleged herein.

18. Prévost, Harrold, PB Management, and PB Adviser will, unless enjoined, continue to engage in the acts, practices and courses of business set forth in this complaint, and acts, practices and courses of business of similar purport and object.

DEFENDANTS

19. **Bruce F. Prévost** is 50 years old and resides in Palm Beach Gardens, Florida. Prévost, along with David Harrold, is a co-founder of the Palm Beach Funds and is a co-founder and co-owner of Palm Beach Capital Management, LP and Palm Beach Capital Management, LLC.

20. **David W. Harrold** is 51 years old and resides in Del Ray Beach, Florida. Along with Prévost, Harrold is a co-founder of the Palm Beach Funds and is a co-founder and co-owner of Palm Beach Capital Management, LP and Palm Beach Capital Management, LLC.

21. **Palm Beach Capital Management, LP** ("PB Management") is a Delaware Limited Partnership organized on December 18, 2000. PB Management served as the general partner of the Funds. Prévost and Harrold are the only limited partners of PB Management.

22. **Palm Beach Capital Management, LLC** ("PB Adviser") is a Florida limited liability company co-founded by Prévost and Harrold in December of 2000. PB Adviser served as the investment adviser for the Funds and the Offshore Funds. Prévost and Harrold are PB Adviser's controlling owners and only executive officers. As such, Prévost and Harrold had sole responsibility for

management of the investment portfolios of the Palm Beach Funds and the Offshore Funds through PB Adviser.

OTHER RELATED ENTITIES AND INDIVIDUALS

23. **Thomas J. Petters** ("Petters") is 53 years old and is currently serving a 50-year prison sentence for mail and wire fraud in connection with the sale of securities. 1n 1988, Petters founded what became Petters Co., Inc., which purported to finance the fictitious inventory transactions addressed in this Complaint. Petters began selling merchandise online in 1998 and in 2001 jointly with direct mail merchandiser Fingerhut Companies, Inc. Petters bought controlling interests in Fingerhut in 2002, uBid in 2003, Polaroid in 2005, and Sun Country Airlines in 2006. He managed all of these businesses under the umbrella company Petters Group Worldwide, LLC ("Petters Group").

24. **Petters Co., Inc.** ("Petters Co.") is a Minnesota corporation founded by Petters. Petters used Petters Co. to sell the promissory notes that were at the core of his Ponzi scheme.

25. **Petters Group Worldwide, LLC**, ("Petters Group") headquartered in Minnetonka, Minnesota, is the umbrella company through which Petters oversaw the diversified group of approximately 60 companies in which he invested funds derived from his Ponzi scheme.

26. **Palm Beach Finance Partners, L.P.** ("PBFP") is a hedge fund established by Prévost and Harrold. PBFP's objective was to achieve consistent rates of return through the purchase of secured notes relating to transaction

financing of new, in-the-box, pre-sold, name-brand products. PBFP filed for bankruptcy protection on November 30, 2009 in a bankruptcy proceeding entitled In re Palm Beach Finance Partners, L.P., Case No. 90BK36379 (Bankr. S.D. Fl.).

27. **Palm Beach Finance Partners II, L.P.** ("PBFII") is a hedge fund established by Prévost and Harrold. PBFII's objective was the same as PBFP's except that PBFII used leverage provided by the Offshore Funds to increase net returns for its investors by increasing the number of Notes the fund was able to purchase from PCI. PBFII filed for bankruptcy protection on November 30, 2009 in a bankruptcy proceeding entitled In re, Palm Beach Finance II L.P., Case No. 09BK36396 (Bankr. S.D. Fl.).

28. **Palm Beach Offshore, Ltd.** ("PBO") is a Cayman Islands fund established by Prévost and Harrold. PBO's objective was to generate returns for investors via the issuance of promissory notes to PBFII. The Grand Court of the Cayman Islands has ordered that PBO be wound up and, as a result, PBO is in Official Liquidation proceedings in that court.

29. **Palm Beach Offshore II, Ltd.** ("PBOII") is a Cayman Islands fund established by Prévost and Harrold. PBOII's objective was to generate returns for investors via the issuance of promissory notes to PBFII. The Grand Court of the Cayman Islands has ordered that PBOII be wound up and, as a result, PBOII is in Official Liquidation proceedings in that court.

PETTERS RAN A MULTI-BILLION DOLLAR PONZI SCHEME THROUGH THE PUBLIC OFFER AND SALE OF NOTES

30. Beginning in approximately 1995, Petters began raising money by offering and selling Notes issued by Petters Co. to members of the public.

31. Petters offered and sold the Petters Co. Notes to members of the public, including several feeder funds which in turn raised their investment capital from hundreds of private investors located throughout the United States and numerous foreign countries. The Palm Beach Funds were among the feeder-funds to which Petters offered and sold Petters Co. Notes.

32. In offering and selling Petters Co. Notes, Petters represented to investors and potential investors that the proceeds from the sale of the Notes would be used to finance what he described as an purchase order inventory financing operation conducted by Petters Co.

33. Petters represented to investors and potential investors that the purchase order inventory financing operation consisted of transactions in which Petters Co. brokered the sale and delivery of end runs or overstock merchandise, primarily consumer electronics, from manufacturers to certain "Big Box" retailers, including well known firms such as Sam's Club and BJ's Wholesale Club ("Retailers").

34. Petters represented that the manufacturers demanded payment up front while the Retailers did not pay until the merchandise was delivered. Petters represented to investors and potential investors that Petters Co. used investors'

money to finance these transactions for the period between when the Retailers placed their orders and when they paid for the merchandise upon delivery.

35. Petters further represented that these transactions generally took about 90 days to complete but could sometimes take as long as 180 days to complete. Accordingly, Petters structured the Petters Co. Notes to specify a due date 90 days after the issue date, but also to allow for a maximum maturity date of 182 days after issuance.

36. Petters represented to investors and potential investors that they would receive high rates of return on the Petters Co. Notes; in the specific case of the Palm Beach Funds, the annual rate of return on the Notes was 15%.

37. Petters represented to investors and potential investors that the Petters Co. Notes entailed minimal risk, because each Note was secured by the underlying merchandise being financed by the Note.

38. Petters represented that he did business with two companies, Enchanted Family Buying Co. ("Enchanted") and Nationwide International Resources, Inc. ("Nationwide") (collectively, the "Vendors"), that bought the consumer electronics from manufacturers and then resold the merchandise to Retailers.

39. For each transaction Petters, or others at his direction, provided a series of documents to investors, including a funding request from Petters Co. for the amount of money needed to purchase the underlying merchandise, executed note documents reflecting the investment and guaranteeing a specified rate of

return not later than 182 days after issuance, purported purchase orders from a Retailer, purported bills of sale from manufacturers to the Vendors, and documents assigning a security interest in the underlying merchandise to the financing investors.

40. These documents were the only evidence of the purported inventory financing transactions that investors ever saw and, as such, they were meant to provide investors with a level of comfort that the transactions were genuine.

41. Numerous individuals and entities invested with Petters Co. in order to obtain the high rates of return Petters promised them on the Notes, together with the safety provided by the security interest in the electronic merchandise underlying each transaction.

42. As of September 2008, the combined balance sheet for Petters Co. and its affiliates reflected total current liabilities, which included outstanding Notes to approximately twenty entities and individuals, of over $3.5 billion.

43. But in reality, Petters's purported purchase order inventory financing business was a complete sham.

44. There were no Retailers, "Big Box" or otherwise.

45. No one ordered any merchandise through Petters Co. Petters and others acting at his discretion fabricated all of the underlying documentation – the purchase orders, bills of sales, and assignments of security interests – that they provided to investors to evidence each transaction.

46. And the two Vendors – Enchanted and Nationwide – were nothing but shell companies with no real operations.

47. The principals of the Vendors were co-conspirators of Petters. They knew there were no Retailers and no real orders to buy merchandise. Each Vendor opened a bank account at Petters's request. The Vendors acted as money conduits for Petters: they accepted monies wired to them by Petters Co. investors; took a percentage of that money as compensation for their role in the scheme; and then funneled the remainder of the cash to Petters. The principals of both Enchanted and Nationwide pleaded guilty in October 2008 to charges of conspiracy to commit money laundering.

48. The truth is that Petters's operation was nothing but a multi-billion-dollar Ponzi scheme. Petters raised money from investors and directed the transfer of that money to the Vendors. Instead of purchasing any merchandise, the Vendors secretly sent most of the investors' money directly to Petters. Between 2002 and September 2008 approximately $12 billion moved from investors, through the bank account of Enchanted, and then to the account of Petters Co. Similarly, over $10 billion was directed to Petters Co. through the bank account of Nationwide. Petters then, directly and through others, diverted much of that money to his own purposes, while using the rest to pay fictional returns to investors.

49. When Petters's scheme collapsed in September 2008, investors were left holding $3.5 billion in worthless Notes.

PEVOST, HARROLD, PB MANAGEMENT, AND PB ADVISER OFFERED AND SOLD INTERESTS IN THE PALM BEACH FUNDS AND THE OFFSHORE FUNDS

50. Between January 2004 and August 2008, Prévost, Harrold, PB Management, and PB Adviser raised over a billion dollars through the sale of interests in the Palm Beach Funds and the Offshore Funds. Prévost, Harrold, PB Management, and PB Adviser invested all these monies in Notes issued by Petters Co.

51. Prévost, Harrold, PB Management, and PB Adviser sold interests in the Palm Beach Funds and the Offshore Funds to dozens of investors, including individuals, foundations, family trusts, and other hedge funds.

52. The monies of persons who invested in each of the Palm Beach Funds and the Offshore Funds were pooled with monies supplied by the other investors in that fund.

53. As represented by Prévost, Harrold, PB Management, and PB Adviser, both orally and in writing, the investors' profits were to come solely from the efforts of Prévost, Harrold, PB Management, and PB Adviser. Investors were not required to do anything more than to contribute money.

PRÉVOST, HARROLD, PB MANAGEMENT, AND PB ADVISER'S CONTROL OF THE PALM BEACH FUNDS AND THE OFFSHORE FUNDS

54. PB Management was the General Partner of the Palm Beach Funds. PB Management had sole responsibility for the management of the Palm Beach Funds' business and investments. PB Management retained PB Adviser to

manage the Palm Beach Funds' investment portfolios on a discretionary basis. PB Adviser also served as the investment manager for the Offshore Funds.

55. Prévost and Harrold exercised absolute control over PB Management and PB Adviser and, through those entities, Prévost and Harrold controlled the day-to-day operations of, and directed the investments of, the Palm Beach Funds.

56. Though the offering materials for the Offshore Funds identified directors other than Prévost and Harrold, those directors had no material input into the day-to-day operation of the Offshore Funds, which were controlled by Prévost and Harrold. Nor did those other directors have any input into how Prévost and Harrold, through PB Adviser, directed the investments of the Offshore Funds.

57. PB Management and PB Adviser, and Prévost and Harrold through those entities, were investment advisers to the Palm Beach Funds and owed those funds a fiduciary duty.

58. PB Adviser, and Prévost and Harrold through PB Adviser, were investment advisers to the Offshore Funds and owed those funds a fiduciary duty.

59. PB Management charged the Palm Beach Funds fees for its services. Those fees comprised a Management Fee and a Performance Allocation. As defined in the confidential information memoranda used to solicit investors in the Palm Beach Funds, the Performance Fee was equal to 12% of the net profits for each calendar quarter and the Management Fee was equal to 0.25% of each Limited Partner's capital account balance on the first business day of each calendar quarter.

60. PB Adviser charged the Offshore Funds similar fees, comprising a Management Fee and an Incentive Fee. As defined in the confidential information memoranda used to solicit investors in the Offshore Funds, the Incentive Fee was equal to 12% of the net profit at the end of each calendar quarter and the Management Fee was equal to 0.25% of the Fund's net assets at the beginning of each calendar quarter.

61. In total, Prévost, Harrold, PB Management, and PB Adviser took more than $58 million in fees from the Palm Beach Funds and the Offshore Funds.

THE INVESTMENT ACTIVITIES OF THE PALM BEACH FUNDS AND THE OFFSHORE FUNDS

62. Prévost, Harrold, PB Management, and PB Adviser used various confidential information memoranda to solicit investments in the Palm Beach Funds. Those memoranda represent that the investment objective of the Palm Beach Funds was to achieve consistent, advantageous rates of return through the purchase of secured notes relating to transaction financing of new, in-the-box, pre-sold, name-brand products.

63. Prévost and Harrold, through PB Management and PB Adviser, used almost all of the money raised through the Palm Beach Funds to invest in Notes issued by Petters Co.

64. Prévost and Harrold also used various confidential information memoranda to solicit investments in the Offshore Funds. Those memoranda represent that the investment objective of the Offshore Funds was to generate

consistent and advantageous rates of return by investing in Investment Notes issued by PBFII.

65. Prévost and Harrold, through PB Adviser, used almost all of the money raised through the Offshore Funds to invest in Investment Notes issued by PBFII. In turn, PBFII used the proceeds from Investment Notes purchased by the Offshore Funds to invest in additional Notes issued by Petters Co.

PRÉVOST AND HARROLD'S SOLICITATION OF INVESTORS

66. From at least as early as 2004 through 2008, Prévost and Harrold solicited investors for the Palm Beach Funds and the Offshore Funds.

67. Prévost and Harrold described the Palm Beach Funds' primary business as investment in secured notes relating to transaction financing of new, in-the-box, pre-sold, name-brand products. They described the Offshore Funds' primary business as investing in unsecured promissory notes issued by PBFII. Among other things, Prévost and Harrold sent confidential information memoranda and other written information about the Funds and the Offshore Funds to prospective investors, met with prospective investors, and conducted due diligence meetings with representatives of investors and prospective investors to discuss the Palm Beach Funds and the Offshore Funds.

68. Prévost and Harrold also provided periodic updates to investors in the Palm Beach Funds and the Offshore Funds regarding the performance of the Funds and the Offshore Funds. Among other things, those updates provided investors with performance charts and monthly return percentages.

THE PALM BEACH FUNDS' PURCHASE OF NOTES

69. Petters utilized an entity named Palm Beach Finance Holdings, Inc. ("Petters Holdings"), to originate the Note transactions between Petters Co. and the Palm Beach Funds. Petters Holdings, which was controlled by Petters, would supposedly enter into contracts with the Vendors that purportedly provided the goods to be sold to the Retailers.

70. On the other side of the Note transactions, Prévost and Harrold used a special purpose vehicle named PBFP Holdings, LLC ("PB Holdings") to originate the transactions with Petters Holdings. After origination, PB Holdings transferred each Note to the individual fund that had provided the purchase money for that Note. The Funds' confidential information memoranda describe this process as essentially contemporaneous with the issuance of the Notes.

71. The Palm Beach Funds' confidential information memoranda stated that the Funds would purchase Notes only if the Note proceeds would be used to pay the cost of specific, identified merchandise that one of the Vendors had "pre-sold" to one of the Retailers, as evidenced by one or more purchase orders for the merchandise.

72. The Funds wired money to the Vendors, which were then supposed to ship the merchandise directly to the Retailers. The Retailers then were supposed to pay the Funds directly for the merchandise they received.

73. Between 2004 and early 2008, the Palm Beach Funds invested in more than 2000 Notes issued by Petters Co.

MISREPRESENTATIONS TO INVESTORS

Cash Flow through the Collateral Account

74. In confidential private placement memoranda and other written materials, Prévost and Harrold, and through them PB Management and PB Adviser, made representations to investors and prospective investors regarding their investments in the Palm Beach Funds (and the Offshore Funds) as well as the Funds' investments in Petters Co. Notes.

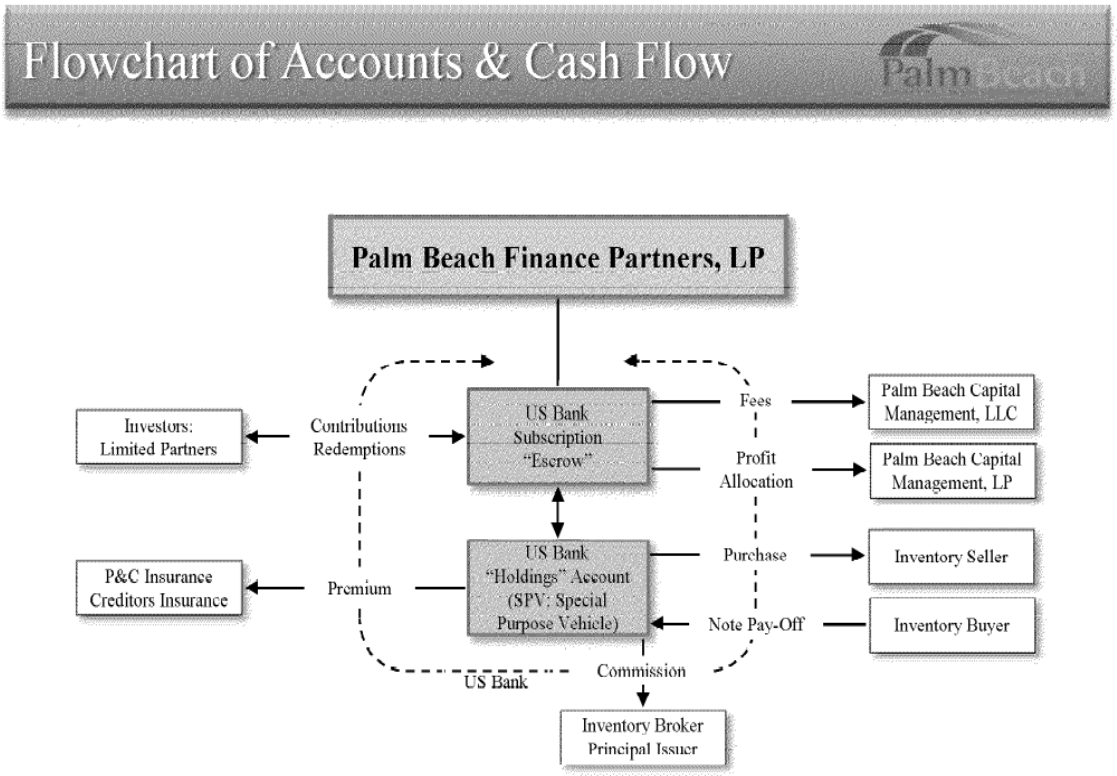
75. Among other things, Prévost and Harrold represented to investors that the Funds and related entities had entered into a Collateral Agreement with US Bank pursuant to which a Collateral Account would be established at US Bank. Prévost and Harrold represented that the purchase price of each Note would be disbursed from the Collateral Account directly to the Vendor that was selling the merchandise corresponding to each Note. Then, when payment became due on each Note, the Retailer that had purchased the merchandise would make payments directly into the Collateral Account.

76. The confidential private placement memoranda distributed to investors by Prévost and Harrold between 2004 and 2008 specifically state that the principal Note issuer (Petters Co.) "has also agreed to direct all inventory purchasers to make their payments directly to the Collateral Account (if payment is made by wire transfer) or to a lockbox account (if payment is made by check)."

77. Certain "Due Diligence Notebooks" that Prévost and Harrold provided to investors and potential investors also state that the "[N]otes are short term,

generally due in 90 days, at which time the buyer sends money directly to the US Bank's Trust Department to pay off the Note."

78. In those same Due Diligence Notebooks, Prévost and Harrold provided investors and potential investors with flow charts, like the following, that purported to depict the cash flow of the Petters transactions:



79. In the flow chart, Prévost and Harrold show the investors' money flowing from the Collateral Account at US Bank directly to the Inventory Seller (Vendor) for the purchase of Notes. The flow chart further depicts "Note Pay-Offs" coming into the Collateral Account directly from the Inventory Buyer (Retailer).

80. The Due Diligence Notebooks identified the Collateral Agreements with US Bank, among other things, as "Portfolio Risk Controls."

81. Prévost and Harrold knew that the Collateral Account and the way that money flowed through it were important elements of the transaction to investors and they touted the Collateral Account as a "risk management aspect" of the Funds.

82. In reality, however, the Collateral Account did not function as Prévost and Harrold, and through them PB Management and PB Adviser, represented it would. In particular, Prévost and Harrold knew from the moment the Funds began operation that the money that was repaid into the Collateral Account never came from any Retailers and instead always came directly from Petters Co. This was a critical problem. Since the payments never came from Retailers, Prévost and Harrold could not independently verify that there were actually any transactions between the Vendors and the Retailers. Instead, Prévost and Harrold simply took Petters at his word that the Retailers were making payments to Petters Co. instead of to the Funds.

83. The fact that the repayments came from Petters Co. and not the Retailers wholly contradicted the representations Prévost and Harrold, and through them PB Management and PB Adviser, made in the confidential private placement memoranda, the Due Diligence Notebooks, and other communications to investors and potential investors.

84. Nevertheless, from 2004 through 2008 Prévost and Harrold concealed the truth about cash flow through the Collateral Account. Throughout that period, Prévost and Harrold continued to represent to investors and prospective investors – in confidential private offering memoranda and other documents – that the repayments that were deposited into the Collateral Account came directly from the Retailers.

The Fraudulent Note Swap Transactions and Fictitious Gains

85. At or about the end of 2007, Petters began to experience difficulties obtaining sufficient cash to sustain his Ponzi scheme. Petters had historically been able to make payments on Notes held by the Funds approximately 90 days after issuance. But by late 2007, Petters was taking significantly longer to repay the Notes.

86. About this time, Petters or his representatives advised Prévost and Harrold that payments from Petters were arriving later than they had in the past because the Retailers were delinquent in paying Petters for their merchandise. Prévost and Harrold could not independently verify that the Retailers were delinquent in making payments because Retailer payments were not flowing directly to the Collateral Account as they should have been. Instead, those payments were purportedly being routed first from the Retailers to Petters Co. and then from Petters Co. to the Collateral Account.

87. By February 2008, Prévost and Harrold had become aware that Petters Co. did not have enough cash to repay Notes held by the Funds that had nearly

reached their full 182-day maturities. Under the terms of the Petters Co. Notes, the failure to pay a Note upon the full 182-day maturity of the Note, constitutes an event of default.

88. At this time, the Petters Co. Notes comprised the entirety of the Palm Beach Funds' investment portfolios. In turn, investment notes issued by PBFII comprised the entirety of the Offshore Funds' investment portfolios.

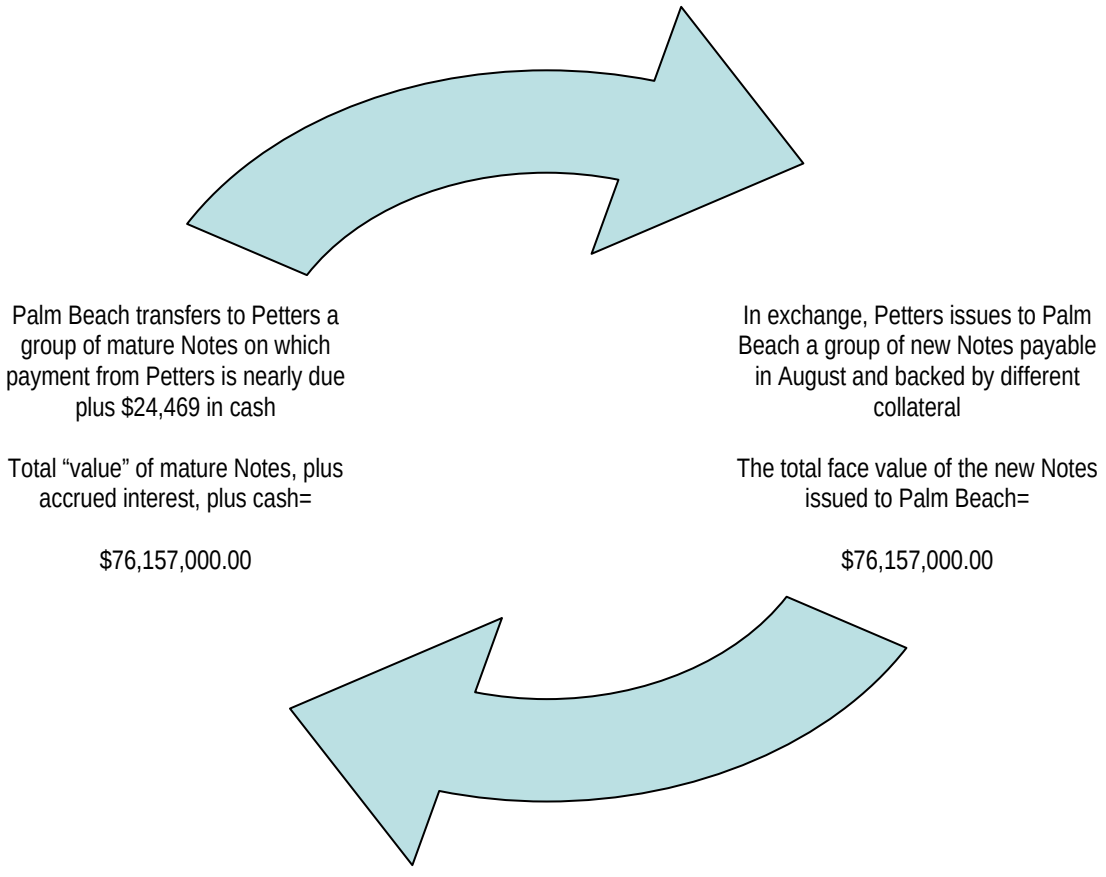
89. Beginning in February, 2008, because Petters did not have the cash to repay Notes held by the Funds' as those Notes became due for payment and in an attempt to avoid holding any defaulted Petters Co. Notes, Prévost and Harrold began entering the Funds into a series of agreements by which the Funds exchanged Notes that had nearly reached their full maturity dates for newly-issued Notes from Petters Co.

90. Prévost and Harrold concealed these Note swap agreements from the investors in the Palm Beach Funds and the Offshore Funds.

91. Each of these bogus transactions used nearly-mature Notes and the interest that had accrued on those Notes as the purchase money for a group of newly-issued Notes backed up by similar, but different, underlying collateral.

92. By way of example, on February 20, 2008, Petters Holdings, PB Holdings, and PBFII entered into an agreement (the "Feb. 20 Swap") under which Petters Holdings sold 19 newly-issued Notes to PB Holdings. The aggregate principal balance of the newly-issued Notes that PB Holdings purchased under the Feb. 20 Swap was $76,157,000.00.

93. Under the Feb. 20 Swap, PB Holdings paid the purchase price for the newly-issued Notes by transferring to Petters Holdings all right, title, and interest in 17 outstanding Notes held by PBFII. The aggregate value of the outstanding Notes exchanged under the Feb. 20 Swap – including both the principal balance and the accrued interest as of the date of the swap – was $76,132,531.00. Because that amount was slightly less than the aggregate value of the newly-issued Notes, PB Holdings made up the balance of the purchase price for the newly-issued Notes with a cash payment of $24,469.00 to Petters Holdings. The Feb. 20 Swap transaction is illustrated below:



94. All of the outstanding Notes that were transferred to Petters Holdings under the Feb. 20 Swap were dated between August 23, 2007 and August 30, 2007. As such, they were all a matter of days away from their full 182-day maturities and of being in default if not paid.

95. The Feb. 20 Swap was to have been an essentially non-cash transaction in which PB Holdings agreed to use a group of outstanding Notes to pay the purchase price for a group of newly-issued Notes. Nevertheless, each of the newly-issued Notes was accompanied by a funding request from Petters Co., directing PB Holdings to wire sums of cash equal to the principal value of each of the newly-issued Notes to one of the Vendors. Further, each of the newly-issued Notes acquired under the Feb. 20 Swap states that "[t]he proceeds of this Note will be used to purchase inventory pursuant to the purchase order attached hereto."

96. An inspection of each newly-issued Note would therefore have indicated business as usual inasmuch as each of the newly-issued Notes purports to memorialize a transaction by which the Funds had advanced cash to one of the Vendors for the purchase of merchandise that was then to be re-sold to one of the Retailers.

97. But Prévost and Harrold knew that, with respect to each of the newly-issued Notes, the Funds would not send any cash to any Vendor for any new merchandise because the newly-issued Notes had simply been exchanged for outstanding Notes. As such, there were no cash "proceeds" derived from the

newly-issued Notes that could have been used to purchase the new merchandise described in the attendant purchase orders.

98. None of the documents associated with the Feb. 20 Swap reveals any other source of cash that might have been transferred to one of the Vendors to purchase the merchandise underlying each of the newly-issued Notes – merchandise that was supposed to have been purchased with the cash proceeds of each of the new Notes.

99. The Feb. 20 Swap was therefore a sham on its face and served no legitimate business purpose. The only reason for entering into the Feb. 20 Swap and other agreements like it was to cover up the fact that Petters could not repay the mature, outstanding Notes swapped under the agreements.

100. Between February and September of 2008, PBFP entered into at least 15 bogus Note swap agreements of the type described above. The total aggregate value of mature Notes swapped (including both principal balance and accrued interest) in those 15 transactions was $209,292,600.83.

101. PBFII entered into at least 22 of the sham note swap agreements. The total aggregate value of mature Notes swapped (including both principal balance and accrued interest) in those 22 transactions was $824,568,519.75. Together, PBFP and PBFII swapped more than $1 billion worth of Notes because Petters Co. was not able to make payment.

102. Each of these additional Note swaps suffered from the same defects as the Feb. 20 Swap. Because no cash was ever advanced to a Vendor to purchase

the inventory underlying each of the newly-issued Notes that the Funds acquired under each of the agreements, each one of them was a sham.

103. Prévost and Harrold never disclosed the Note swap agreements to investors in the Palm Beach Funds or the Offshore Funds.

104. Instead, engaging in the spurious Note swap transactions allowed Prévost and Harrold to conceal from investors the fact that Petters did not have sufficient capital to make payments on mature Notes held by the Funds.

105. Instead of disclosing to investors that Petters did not have sufficient cash to make payments on the Funds' mature Notes, Prévost and Harrold invented a convenient fiction: that exchanging mature Notes and the accrued interest thereon for newly-issued Notes was the same as being repaid in cash and then reinvesting the cash in new Notes, as had been the Funds' practice in the past. Employing that fiction, Prévost and Harrold continued to report to investors, in monthly performance updates, that the Funds were generating the same consistent monthly gains they had been experiencing for years.

106. By way of example, on or about August 18, 2008, Prévost and Harrold or others working at their direction sent a monthly performance update to the Funds' investors. That monthly performance update reported relatively constant monthly gains for the Funds – approximately 0.9-1.0% per month for PBFP and 1.3-1.4% per month for PBFII – from the inception of the Funds through June of 2008.

107. Without disclosures relating to the delinquent payments from Retailers and the swapping, by that time, of the overwhelming majority of the Notes held by each of the Funds, the takeaway for investors from the August 18, 2008 monthly performance update was that things were going well and had been going well, without change or interruption, since the inception of the Funds.

108. But the nature of the reported "gains" had changed fundamentally. In the past, after the Funds received cash repayments plus interest on the Notes, Prévost and Harrold reported realized gains to investors. By August of 2008, the Funds were no longer receiving cash repayments on the Notes. Instead, Prévost and Harrold were generating illusory, unrealized gains by simply exchanging old IOUs for new ones with higher face values. Despite this marked turn for the worse, Prévost and Harrold continued to report the same consistent monthly gains they had always reported as though nothing had changed.

109. The monthly performance numbers that Prévost and Harrold reported to investors after February of 2008 were materially false and misleading because they did not disclose that Petters Co. was not able to make payment on outstanding Notes.

110. The monthly performance numbers that Prévost and Harrold reported to investors after February of 2008 materially overstated the "gains" the Funds had generated by including the fictitious gains generated by swapping mature Notes for newly-issued Notes.

111. Generating fictitious gains on swapped Notes allowed Prévost and Harrold to collect Incentive Allocations and Management Fees on artificially inflated fund values.

112. Prévost and Harrold, and through them PB Management and PB Adviser, deliberately deceived investors by means of the Note swap transactions and subsequent monthly performance updates described above.

113. Prévost and Harrold also continued to solicit and raise funds from investors during this time period without disclosing that Petters was no longer able to repay outstanding Notes held by the Funds.

THE PONZI SCHEME COLLAPSES

114. On September 24, 2008, the FBI and the criminal division of the IRS executed search warrants at the corporate headquarters of Petters Group Worldwide, the offices of Petters Co., and the homes of several top company executives, including Petters, and seized hundreds of thousands of documents.

115. On September 25, 2008, one day after the Petters raid, PB Adviser sent a letter to investors in the Palm Beach Funds and the Offshore Funds advising them of the raid and stating that "we do not know the nature or purpose of the search and what indirect effect it may have on the Funds, if any." The September 25, 2008 letter further advised that redemptions in the Funds and the Offshore Funds would be suspended.

116. On September 26, 2008, two days after the Petters raid, PB Adviser sent another letter to investors stating that "we must share our belief that there has been serious wrongdoing and that the Funds have been affected."

117. On October 3, 2008, Petters was arrested and the U.S. Attorney filed charges against Petters for mail fraud, wire fraud, money laundering and obstruction of justice. On October 6, 2008, the District Court froze the assets of Petters Group, Petters Co. and Petters and appointed a receiver.

118. The Palm Beach Funds filed for bankruptcy protection on November 30, 2009.

COUNT I

Violations of Section 17(a)(1) of the Securities Act (Against All Defendants)

119. Paragraphs 1 through 118 are realleged and incorporated by reference as though fully set forth herein.

120. By engaging in the conduct described above, Prévost, Harrold, PB Management, and PB Adviser, in the offer and sale of securities, by the use of the means and instruments of transportation or communication in interstate commerce or by use of the mails, directly or indirectly, have employed devices, schemes and artifices to defraud.

121. Prévost, Harrold, PB Management, and PB Adviser acted with scienter.

122. By reason of the foregoing, Prévost, Harrold, PB Management, and PB Adviser violated Section 17(a)(1) of the Securities Act [15 U.S.C. § 77q(a)(1)].

COUNT II

Violations of Sections 17(a)(2) and (3) of the Securities Act (Against All Defendants)

123. Paragraphs 1 through 118 are realleged and incorporated by reference as though fully set forth herein.

124. By engaging in the conduct described above, Prévost, Harrold, PB Management, and PB Adviser, in the offer and sale of securities, by the use of the means and instruments of transportation or communication in interstate commerce or by use of the mails, directly or indirectly, have:

a. obtained money or property by means of untrue statements of material fact or by omitting to state material facts necessary in order to make the statements made, in light of the circumstances under which they were made, not misleading; and

b. engaged in transactions, practices, or courses of business that operated or would operate as a fraud or deceit upon the purchasers of such securities.

125. By reason of the foregoing, Prévost, Harrold, PB Management, and PB Adviser have violated Sections 17(a)(2) and (3) of the Securities Act [15 U.S.C. § 77q(a)(2)-(3)].

COUNT III

**Violations of Section 10(b) of the Exchange Act,
and Exchange Act Rule 10b-5
(Against All Defendants)**

126. Paragraphs 1 through 118 are realleged and incorporated by reference as though fully set forth herein.

127. As more fully described in paragraphs 1 through 118 above, Prévost, Harrold, PB Management, and PB Adviser, in connection with the purchase and sale of securities, by the use of the means and instrumentalities of interstate commerce and by the use of the mails, directly and indirectly: used and employed devices, schemes and artifices to defraud; made untrue statements of material fact and omitted to state material facts necessary in order to make the statements made, in light of the circumstances under which they were made, not misleading; and engaged in acts, practices and courses of business which operated or would have operated as a fraud and deceit upon purchasers and sellers and prospective purchasers and sellers of securities.

128. Prévost, Harrold, PB Management, and PB Adviser acted with scienter.

129. By reason of the foregoing, Prévost, Harrold, PB Management, and PB Adviser violated Section 10(b) of the Exchange Act [15 U.S.C. §78j(b)] and Rule 10b-5 thereunder [17 C.F.R. 240.10b-5].

COUNT IV

Violations of Advisers Act Section 206(1)
(Against All Defendants)

130. Paragraphs 1 through 118 are realleged and incorporated by reference as though fully set forth herein.

131. At all times relevant to this Complaint, Prévost, Harrold, PB Management, and PB Adviser acted as investment advisers to the Funds and the Offshore Funds.

132. As more fully described in paragraphs 1 through 118 above, at all times alleged in this Complaint, Prévost, Harrold, PB Management, and PB Adviser, while acting as investment advisers, by use of the mails, and the means and instrumentalities of interstate commerce, directly or indirectly: (i) employed devices, schemes or artifices to defraud their clients or prospective clients; and (ii) engaged in transactions, practices and courses of business which have operated as a fraud or deceit upon their clients or prospective clients.

133. Prévost, Harrold, PB Management, and PB Adviser acted with scienter.

134. By reason of the foregoing, Prévost, Harrold, PB Management, and PB Adviser have violated Section 206(1) of the Advisers Act. [15 U.S.C. § 80b-6(1)].

COUNT V

Violations of Advisers Act Section 206(2)
(Against All Defendants)

135. Paragraphs 1 through 118 are realleged and incorporated by reference as though fully set forth herein.

136. At all times relevant to this Complaint, Prévost, Harrold, PB Management, and PB Adviser acted as investment advisers to the Funds.

137. As more fully described in paragraphs 1 through 118 above, at all times alleged in this Complaint, Prévost, Harrold, PB Management, and PB Adviser, while acting as investment advisers, by use of the mails, and the means and instrumentalities of interstate commerce, directly or indirectly: (i) employed devices, schemes or artifices to defraud their clients or prospective clients; and (ii) engaged in transactions, practices and courses of business which have operated as a fraud or deceit upon their clients or prospective clients.

138. By reason of the foregoing, Prévost, Harrold, PB Management, and PB Adviser have violated Section 206(2) of the Advisers Act. [15 U.S.C. § 80b-6(2)].

COUNT VI

Violation of Advisers Act
Section 206(4) and Rule 206(4)-8 Thereunder
(Against All Defendants)

139. Paragraphs 1 through 118 are realleged and incorporated by reference as though fully set forth herein.

140. At all times relevant to this Complaint, Prévost, Harrold, PB Management, and PB Adviser acted as investment advisers as defined under the Advisers Act. Prévost, Harrold, PB Management, and PB Adviser managed the investments of the Funds and the Offshore Funds in exchange for compensation in the form of performance and management fees.

141. As more fully described in paragraphs 1 through 118 above, at all times alleged in this Complaint, Prévost, Harrold, PB Management, and PB Adviser, while acting as investment advisers, by use of the mails, and the means and instrumentalities of interstate commerce, directly or indirectly: engaged in acts, practices or courses of business which were fraudulent, deceptive, or manipulative. Prévost, Harrold, PB Management, and PB Adviser made untrue statements of a material fact or omitted to state a material fact necessary to make the statements made, in the light of the circumstances under which they were made, not misleading, to any investor or prospective investor in the pooled investment vehicle, and otherwise engaged in acts, practices or courses of business that were fraudulent, deceptive, or manipulative with respect to any investor or prospective investor in the pooled investment vehicle.

142. By reason of the foregoing, Prévost, Harrold, PB Management, and PB Adviser have violated Section 206(4) of the Advisers Act. [15 U.S.C. § 80b-6(4)] and Rule 206(4)-8 [17 C.F.R. 275.206(4)-8] thereunder.

COUNT VII
Aiding and Abetting Violations of the Advisers Act
(Against Prévost and Harrold)

143. Paragraphs 1 through 118 are realleged and incorporated by reference as though fully set forth herein.

144. At all times relevant to this Complaint, PB Management and PB Adviser acted as investment advisers as defined under the Advisers Act.

145. As more fully described in paragraphs 1 through 118 above, at all times alleged in this Complaint, PB Management and PB Adviser, while acting as investment advisers, by use of the mails, and the means and instrumentalities of interstate commerce, directly or indirectly: engaged in transactions, acts, practices or courses of business which are fraudulent, deceptive, or manipulative. PB Management and PB Adviser also employed devices, schemes or artifices to defraud their clients or prospective clients. PB Management and PB Adviser made untrue statements of a material fact or omitted to state a material fact necessary to make the statements made, in the light of the circumstances under which they were made, not misleading, to any investor or prospective investor in the pooled investment vehicle, and otherwise engaged in acts, practices or courses of business that were fraudulent, deceptive, or manipulative with respect to any investor or prospective investor in the pooled investment vehicle. Through their conduct, PB Management and PB Adviser violated Sections 206(1), 206(2) and 206(4) of the Advisers Act [15 U.S.C. §§ 80b-6(1), 80b-6(2) and 80b-6(4)] and Rule 206(4)-8 thereunder [17 C.F.R. § 275.206(4)-8].

146. Prévost and Harrold were the only principals of PB Management and PB Adviser. Prévost and Harrold owned and controlled PB Management and PB Adviser and were generally aware of all of their activities.

147. Prévost and Harrold knowingly provided substantial assistance to PB Management and PB Adviser in connection with the violations described in Paragraphs 1 through 118 above, and summarized in Paragraph 145 above.

148. By reason of the foregoing, Prévost and Harrold aided and abetted PB Management and PB Adviser's violations of Sections 206(1), 206(2) and 206(4) of the Advisers Act [15 U.S.C. §§ 80b-6(1), 80b-6(2) and 80b-6(4)] and Rule 206(4)-8 thereunder [17 C.F.R.§ 275.206(4)-8] as described in Paragraphs 1 to 118 above and as summarized in Paragraph 145 above.

RELIEF REQUESTED

WHEREFORE, the Commission respectfully requests that this Court:

I.

Issue findings of fact and conclusions of law that Defendants Prévost, Harrold, PB Management, and PB Adviser committed the violations charged and alleged herein.

II.

Grant an Order of Permanent Injunction, in a form consistent with Rule 65(d) of the Federal Rules of Civil Procedure, permanently restraining and enjoining Defendants Prévost, Harrold, PB Management, and PB Adviser, and

their agents, servants, employees, attorneys and those persons in active concert or participation with him who receive actual notice of the Order, by personal service or otherwise, and each of them from, directly or indirectly, engaging in the transactions, acts, practices or courses of business described above, or in conduct of similar purport and object, in violation of Section 17(a) of the Securities Act [15 U.S.C. § 77q(a)], Section 10(b) of the Exchange Act [15 U.S.C. § 78j] and Rule 10b-5 [17 CFR § 240.10b-5] thereunder;

III.

Grant a Permanent Injunction, in a form consistent with Rule 65(d) of the Federal Rules of Civil Procedure, restraining and enjoining Defendants Prévost, Harrold, PB Management, and PB Adviser, their officers, agents, servants, employees, attorneys and those persons in active concert or participation with them who receive actual notice of the Order, by personal service or otherwise, and each of them from, directly or indirectly, engaging in the transactions, acts, practices or courses of business described above, or in conduct of similar purport and object, that violate, or aid and abet violations of, Sections 206(1), 206(2) and 206(4) of the Advisers Act [15 U.S.C. §§ 80b-6(1) and 80b-6(2)] and Rule 206(4)-8 thereunder [17 C.F.R.§ 275.206(4)-8].

IV.

Grant a permanent injunction in a form consistent with Rule 65(d) of the Federal Rules of Civil Procedure, restraining and enjoining Defendants Prévost, Harrold, PB Management, and PB Adviser, their officers, agents, servants,

employees, attorneys and those persons in active concert or participation with them who receive actual notice of the Order, by personal service or otherwise, and each of them from, directly or indirectly, aiding and abetting violations of Sections 206(1), 206(2) and 206(4) of the Advisers Act [15 U.S.C. §§ 80b-6(1) and 80b-6(2)] and Rule 206(4)-8 thereunder [17 C.F.R.§ 275.206(4)-8].

V.

Issue an Order requiring the Defendants to disgorge all ill-gotten gains that they received as a result of the violations alleged in this Complaint, including prejudgment interest.

VI.

With regard to Defendants Prévost, Harrold, PB Management, and PB Adviser's violative acts, practices and courses of business set forth herein, issue an Order imposing upon Prévost, Harrold, PB Management, and PB Adviser appropriate civil penalties pursuant to Section 20(d) of the Securities Act [15 U.S.C. § 77t(d)], Section 21(d)(3) of the Exchange Act [15 U.S.C. § 78u(d)(3)], and Section 209(e) of the Advisers Act [15 U.S.C. § 80b-9(e)].

VII.

Retain jurisdiction of this action in accordance with the principles of equity and the Federal Rules of Civil Procedure in order to implement and carry out the

terms of all orders and decrees that may be entered or to entertain any suitable application or motion for additional relief within the jurisdiction of this Court.

VIII.

Grant an Order for any other relief this Court deems appropriate.

Respectfully submitted,

Dated: October 14, 2010

s/ Daniel J. Hayes
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