

UNITED STATES DISTRICT COURT  
EASTERN DISTRICT OF WASHINGTON

In Re:

NO: 2:12-CV-6-RMP

BRUCE P. KRIEGMAN, solely in his capacity as court-appointed Chapter 11 Trustee for LLS America, LLC,

Adv. Proc. No. 11-80130-FPC11

Plaintiff

V.

## THEODORE SCHULTZ.

## Defendants.

## AMENDED FINDINGS OF FACT AND CONCLUSIONS OF LAW

This consolidated action was tried before the Court on September 2, 2014.

18 Plaintiff, Bruce P. Kriegman, the court-appointed Chapter 11 Trustee for LLS  
19 America, LLC (“Trustee”), was represented by Richard L. Mount and Samuel C.  
20 Thilo of Witherspoon Kelley. The Court hereby amends its prior Findings of Fact

1 and Conclusions of Law, ECF No. 118, to reflect the Court's finding that all  
2 transfers to and from Defendants were in Canadian currency.

3 Dillon Jackson and Adam Coady of Foster Pepper appeared telephonically  
4 on behalf of Defendants Geoff Toews, Rory and Cathy Bjarnason, and CLB  
5 Holdings (collectively, "Defendants"). Foster Pepper previously moved to  
6 withdraw as counsel for all Defendants because Defendant Toews had terminated  
7 them as his counsel and because Defendants Bjarnason and CLB Holdings had  
8 ceased all communication with Foster Pepper. ECF Nos. 56, 100. The Court  
9 denied Foster Pepper's motions. ECF Nos. 80, 112. At trial, Foster Pepper  
10 explained that it attended trial in order to comply with the Court's orders but that  
11 it lacked authority to represent Defendants. Defense counsel stated that it knew of  
12 no contact from Defendants. Defendants themselves were not present at trial.

13  
14 Having heard witness testimony, having reviewed the admitted exhibits,  
15 and being fully informed, the Court makes the following findings of fact and  
16 conclusions of law:

#### 17 PREVIOUS RULINGS

##### 18 1. Ponzi Scheme and Insolvency

19 On July 1, 2013, the Bankruptcy Court issued its Report and  
20 Recommendation Re Plaintiff's Motion for Partial Summary Judgment on

1 Common Issues (“Report and Recommendation”) recommending that the District  
2 Court grant the Trustee’s Amended Motion for Partial Summary Judgment on two  
3 “Common Issues”: (1) Debtor operated a Ponzi scheme; and (2) Debtor was  
4 insolvent at the time of its transfers to Defendants. On August 19, 2013, this  
5 Court adopted the Bankruptcy Court’s Report and Recommendation and entered  
6 an order granting the Trustee’s Amended Motion for Partial Summary Judgment  
7 on the Common Issues (“Order Adopting Report and Recommendation”). *See*  
8 2:11-cv-00357-RMP, ECF No. 92. Therefore, this Court has determined that  
9 Debtor operated a Ponzi scheme and was insolvent at the time of each of the  
10 transfers to Defendants.

11 All of the findings and conclusions set forth in the Report and  
12 Recommendation and the Order Adopting Report and Recommendation are  
13 incorporated by this reference and are the law of this case.

14 **2. Omnibus Hearing for the Testimony of Charles B. Hall**

15 On January 31, 2014, this Court entered its Order Granting Plaintiff’s  
16 Motion for Omnibus Hearing. ECF No. 55. Pursuant to that Order, the court-  
17 appointed examiner, Mr. Charles B. Hall, testified at an Omnibus Hearing in open  
18 court commencing on February 25, 2014. His testimony consists of written direct  
19 examination testimony that was filed on or about February 17, 2014, and the oral  
20 testimony that he gave at the Omnibus Hearing. Mr. Hall was cross examined by

1 several defense attorneys, including those from Foster Pepper, and by some pro se  
2 defendants. Mr. Hall's testimony at the Omnibus Hearing is part of the record in  
3 this adversary action.

4 **FINDINGS OF FACT**

5 1. Debtor is the Little Loan Shoppe group of companies, which was  
6 formed originally in 1997. PO-1 at 11.

7 2. Debtor operated a Ponzi scheme, whereby investors' loans were  
8 sometimes used to pay other investors' promised returns on investments. PO-1 at  
9 16.

10 3. Over the course of its existence, Debtor acquired approximately  
11 \$135.4 million in funds invested by individual lenders, documented by promissory  
12 notes promising interest in the range of 40% to 60% per annum. PO-1 at 7 n.2, 15.

13 4. Defendants are lenders who received payments from Debtor.

14 5. Debtor accumulated payday loan bad debts of approximately \$29  
15 million, which were written off in 2009. PO-1 at 41.

16 6. Debtor was never profitable at any time during its existence and, thus,  
17 at no time did it generate sufficient profits to pay the amounts due the lenders. PO-  
18 1 at 16, 53.

19 7. Defendants Rory and Cathy Bjarnason and Geoff Toews made loans  
20 to Debtor. P-23; P-63.

1       8. All Defendants received multiple payments from Debtor. P-23; P-33;  
2 P-63.

3       9. Dozens of the payments that Defendants received were written on  
4 checks showing Debtor's Spokane address. P-24 at 13-98; P-34 at 1-20; P-64 at  
5 143-389.

6       10. Debtor voided approximately 29,000 of the post-dated checks that it  
7 had issued to lenders, including Defendants. PO-1 at 26; P-25; P-35; P-65.

8       11. Defendant Toews received promissory notes that were "rolled into"  
9 or renewed into other promissory notes. P-66 at 256-57, 259.

10       12. Defendants Bjarnason made a number of loans without receiving any  
11 promissory note or other written documentation in return. P-26 at 12; *see also* P-  
12 20 at 2.

13       13. All of the transfers that the Trustee seeks to avoid were made within  
14 the period of September 1997 to July 21, 2009. P-23; P-33; P-63.

15       14. Indicia and characteristics of the Ponzi scheme present in this case  
16 include:

17           a. Proceeds received from new investors masked as profits from  
18 running a payday loan business; PO-1 at 16, 22;

19           b. Promise of a high rate of return, usually between 40% to as  
20 much as 60%, on the invested funds; PO-1 at 19;

1                   c.     Debtor paid commissions to third parties who solicited new  
2     lenders, typically 10% annually of the amount received from the new  
3     lender; PO-1 at 20-21;

4                   d.     Debtor solicited funds as loans evidenced by promissory notes  
5     but demonstrated a pattern of “rolling over” the promissory notes when due  
6     onto new notes instead of paying off the obligation; PO-1 at 26;

7                   e.     Debtor, throughout its history, made false and misleading  
8     statements to current and potential lenders; PO-1 at 53-54;

9                   f.     Debtor was insolvent from its inception to the filing of its  
10     bankruptcy; PO-1 at 67.

11                15.    The court-appointed examiner, Charles B. Hall, by way of education,  
12     experience, and vocation, is qualified to analyze and review the legitimacy of an  
13     enterprise’s operation and to detect a fraud based on Ponzi scheme operations.

14                16.    Mr. Hall’s expert opinion is credible.

15                17.    Mr. Curtis Frye’s testimony, which pertained to Debtor’s record  
16     keeping and the accounting of investment, payments, and consulting  
17     fees/commissions to Defendants, is credible.

18                18.    Defendants received interest and principal payments from Debtor.

19                19.    Defendants are “net winners.”

1       20. Defendants were promised high rates of return from Debtor and were  
2 issued promissory notes with a promised rate of return between 40% and 60% per  
3 annum. P-26 at 12, 33, 34; P-36 at 10; P-66 at 20.

4       21. There is no evidence that the Bjarnason Defendants or Defendant  
5 CLB Holdings ever received any account statements or financial statements from  
6 Debtor. *See* P-26 at 9-11, 13; P-36 at 8-9, 10-11. Defendant Toews's response to  
7 an interrogatory indicates that he was permitted to view a limited number of  
8 financial statements, but that Debtor did not allow Defendant Toews to remove  
9 the statements from her custody or to make copies of them. P-66 at 21.

10       22. Defendants received post-dated checks from Debtor. P-26 at 16-17;  
11 P-36 at 13; P-66 at 29.

12       23. Defendant Toews loaned funds to Debtor after Debtor had "rolled"  
13 earlier loans into new promissory notes when payment became due. *See* P-60 at  
14 3; P-62 at 1.

15       24. Cathy Bjarnason was the owner of CLB Holdings. P-36 at 8, 17.

16       25. Plaintiff requests the Court to pierce the corporate veil and hold  
17 Defendant Cathy Bjarnason liable for any judgment that the Court imposes on the  
18 Defendant CLB Holdings. Washington courts have established two factors  
19 necessary to show that the corporate form should be disregarded. "First, the  
20 corporate form must be intentionally used to violate or evade a duty; second,

1 disregard must be ‘necessary and required to prevent unjustified loss to the injured  
2 party.’” *Meisel v. M & N Modern Hydraulic Press Co.*, 97 Wn. 2d 403, 410  
3 (1982) (quoting *Morgan v. Burks*, 93 Wn.2d 580, 587 (1980)).

4 26. A court may pierce the corporate veil under the alter ego theory  
5 “when ‘the corporate entity has been disregarded by the principals themselves so  
6 that there is such a unity of ownership and interest that the separateness of the  
7 corporation has ceased to exist.’” *Grayson v. Nordic Constr. Co.*, 92 Wn.2d 548,  
8 553 (1979) (quoting *Burns v. Norwesco Marine, Inc.*, 13 Wn. App. 414, 418  
9 (1975)). *See also J. I. Case Credit Corp. v. Stark*, 64 Wn. 2d 470, 475 (1964)  
10 (“[T]here must be such a commingling of property rights or interests as to render  
11 it apparent that they are intended to function as one, and, further, to regard them as  
12 separate would aid the consummation of a fraud or wrong upon others.”).

13 27. Undercapitalization of a corporate entity, by itself, does not constitute  
14 abuse of the corporate form, *Norhawk Investments, Inc. v. Subway Sandwich*  
15 *Shops, Inc.*, 61 Wn. App. 395, 399-400 (1991), although “there may be situations  
16 in which a corporation is so thinly capitalized that it manifests a fraudulent  
17 intent,” *Truckweld Equip. Co., Inc. v. Olson*, 26 Wn. App. 638, 645 (1980).

18 28. The Court finds that Defendant Cathy Bjarnason used Defendant  
19 CLB Holdings as an alter ego. Defendant CLB Holdings’ banking records  
20 indicate that Defendant Cathy Bjarnason used the entity’s coffers as an extension

1 of her personal account. For example, the records show multiple months during  
2 which funds were transferred from an account in Defendant Cathy Bjarnason's  
3 name into CLB Holdings' account, but the exact same amount was withdrawn  
4 again shortly thereafter. *See, e.g.*, P-36 at 32, 33, 38, 40, 49. Similarly, transfers  
5 from Debtor frequently were transferred or withdrawn from Defendant CLB  
6 Holdings shortly after checks from Debtor had been deposited. *See, e.g.*, P-36 at  
7 54-55, 69-70, 83, 90, 96. These practices often left only a small amount of funds  
8 in the entity's account, which at times contained less than \$50.00. *See, e.g.*, P-36  
9 at 70, 71.

10 29. Defendant Cathy Bjarnason presented no proof to contradict this  
11 evidence that she disregarded the separate corporate form of CLB Holdings and  
12 instead treated the company's assets as her personal funds. Moreover, the Court  
13 finds that Defendant Cathy Bjarnason must be held liable for any judgment that  
14 the Court imposes on Defendant CLB Holdings in order to minimize injury to  
15 other creditors. Accordingly, the Court pierces the corporate veil.

16 30. Defendants Rory and Cathy Bjarnason are net winners. The  
17 following summarizes the evidence of investments made by them and the  
18 payments that they received:

19 Total Payments: \$228,900.00 CAD  
20 Total Investments: \$103,000.00 CAD  
MIMO: \$125,900.00 CAD

1       31. Defendant CLB Holdings is net winner. The following summarizes  
2 the evidence of investments made by it and the payments that it received:

3           Total Payments:           \$99,250.00 CAD  
4           Total Investments:       \$0.00  
5           MIMO:                   \$99,250.00 CAD

6       32. Defendant Geoff Toews is a net winner. The following summarizes  
7 the evidence of investments made by him and the payments that he received:

8           Total Payments:           \$388,219.39 CAD  
9           Total Investments:       \$175,000.00 CAD  
10          MIMO:                   \$213,219.39 CAD

11       33. Total transfers to Defendants are as follows:

12           • Rory and Cathy Bjarnason for \$228,900.00 CAD;  
13           • CLB Holdings for \$99,250.00 CAD;  
14           • Geoff Toews for \$388,219.39 CAD.

15       34. All transfers to Defendants were made with actual fraudulent intent  
16 and in furtherance of a Ponzi scheme.

## 17                                   **CONCLUSIONS OF LAW**

18       1. This Court has jurisdiction of this proceeding pursuant to 28 U.S.C. §  
19           1334 and 28 U.S.C. § 157(d).

20       2. This Court has jurisdiction over Defendants.

21       3. This action was timely commenced.

1       4. At least one unsecured creditor existed who triggered the strong arm  
2 power of 11 U.S.C. § 544(b)(1) because the creditor did not and should not  
3 reasonably have discovered the fraudulent nature of Debtor's Ponzi scheme  
4 transfers within one year before the bankruptcy petition was filed. *See* 2:11-cv-  
5 00362-RMP, ECF No. 197.

6       5. Washington State law governing fraudulent transfers applies.

7       6. Under the statutes relating to fraudulent transfers, 11 U.S.C. § 548  
8 and RCW 19.40, *et seq.*, payments received from Debtor are recoverable from  
9 each Defendant by the Trustee, subject to the defense of good faith pursuant to 11  
10 U.S.C. § 548(c) and RCW 19.40.081(a).

11       7. Transfers made in furtherance of a Ponzi scheme constitute actual  
12 fraud under the Bankruptcy Code and Washington's version of the Uniform  
13 Fraudulent Transfer Act (UFTA). *See* Bankr. Adv. Proc. No. 11-80299-FPC, ECF  
14 No. 378 at 21-25. "Where causes of action are brought under UFTA against Ponzi  
15 scheme investors, the general rule is that to the extent innocent investors have  
16 received payments in excess of the amounts of principal that they originally  
17 invested, those payments are avoidable as fraudulent transfers . . . ." *Donell v.*  
18 *Kowell*, 533 F.3d 762, 770 (9th Cir. 2008).

19       8. A transferee of a fraudulent transfer may keep funds that it took for  
20 reasonably equivalent value and in good faith. *See* 11 U.S.C. § 548(c); RCW

1 19.40.081(a). As recipients of transfers that constitute actual fraud, the burden of  
2 proof in establishing the affirmative defense of good faith is on Defendants. *In re*  
3 *Agric. Research and Tech. Grp., Inc.*, 916 F.2d 528, 535 (9th Cir. 1990); 5  
4 COLLIER ON BANKRUPTCY ¶ 548.09[2][c] at 548-98.2 (16th ed. 2011).

5 9. Although “good faith” is not defined precisely in case law, at least  
6 one court has noted that the absence of good faith is shown by a transferee who  
7 knows that a debtor is operating a Ponzi scheme. *See In re Agric. Research*, 916  
8 F.2d at 535 (citing *In re Indep. Clearing House*, 77 B.R. 843, 861 (D. Utah  
9 1987)). The Ninth Circuit has quoted favorably an explanation in an early case  
10 that a transferee’s “knowledge or actual notice of circumstances sufficient to put  
11 him, as a prudent man, upon inquiry as to whether his brother intended to delay or  
12 defraud his creditors . . . should be deemed to have notice . . . as would invalidate  
13 the sale as to him.” *Id.* at 535 (quoting *Shauer v. Alterton*, 151 U.S. 607, 621  
14 (1894)).

15 10. Thus, courts measure good faith by an objective standard, looking to  
16 what a transferee “‘knew or should have known’ in questions of good faith, rather  
17 than examining what the transferee actually knew from a subjective standpoint.”  
18 *Id.* at 536.

19 11. Under the Bankruptcy Code, Washington’s UFTA, as well as  
20 relevant case law, the Court does not contemplate a recipient’s intent when

1 deciding whether to avoid fraudulent transfers. 5 COLLIER ON BANKRUPTCY ¶  
2 548.04[2] at 548-63; *Thompson v. Hanson*, 168 Wn.2d 738, 749 (2010).  
3 Accordingly, a transfer that constitutes actual fraud is avoided in its entirety  
4 unless the transferee establishes that a reasonable person in the transferee's  
5 position would not and should not have known of the fraud, not simply whether he  
6 or she *actually* acted in good faith.

7 12. Transfers made by Debtor in furtherance of its Ponzi scheme are  
8 transfers made with actual intent to hinder, delay and/or defraud creditors under  
9 both state law, RCW Ch. 19.40, and federal law, 11 U.S.C. § 548(a)(1).

10 13. As discussed above, Defendants terminated or stopped  
11 communicating with their counsel and did not personally attend trial, participate at  
12 trial, or offer any evidence. Thus, Defendants have not met their burden of  
13 establishing that they acted in good faith.

14 14. Under RCW 19.40.041(a)(1), RCW 19.40.091(a) and the "strong arm  
15 powers" that 11 U.S.C. § 544(b)(1) grants to bankruptcy trustees, all of Debtor's  
16 transfers to Defendants, regardless of the date of transfer, are hereby set aside and  
17 avoided.

18 15. The Trustee is entitled to claw back and recover all transfers to  
19 Defendants.

1       16. The Trustee is entitled to repayment of all commissions without any  
2 right of off set.

3       17. Defendant CLB Holdings, operating through Cathy Bjarnason, was  
4 the initial transferee of payments received from Debtor, and the Trustee is entitled  
5 to recover all transfers to Defendants.

6       18. The Trustee is entitled to pre-judgment interest at the applicable  
7 federal rate from July 21, 2009, when the bankruptcy case commenced.

8       19. Pursuant to 11 U.S.C. § 548(a), 544, 550 and 551 and RCW  
9 19.40.041(1) and 19.40.071, the Trustee is entitled to and is granted a judgment  
10 for the benefit of the Liquidating Trust of Debtor against **Rory and Cathy**  
11 **Bjarnason** in the amount of **\$228,900.00 CAD**, plus pre-judgment interest from  
12 July 21, 2009, at the applicable federal judgment rate and post-judgment interest  
13 at the federal judgment rate from the date of judgment to the date the judgment is  
14 paid in full, *see* 28 U.S.C. § 1961.

15       20. Pursuant to 11 U.S.C. § 548(a), 544, 550 and 551 and RCW  
16 19.40.041(1) and 19.40.071, the Trustee is entitled to and is granted a judgment  
17 for the benefit of the Liquidating Trust of Debtor against **CLB Holdings and**  
18 **Cathy Bjarnason** in the amount of **\$99,250.00 CAD**, plus pre-judgment interest  
19 from July 21, 2009, at the applicable federal judgment rate and post-judgment

interest at the federal judgment rate from the date of judgment to the date the judgment is paid in full, *see* 28 U.S.C. § 1961.

21. Pursuant to 11 U.S.C. § 548(a), 544, 550 and 551 and RCW  
19.40.041(1) and 19.40.071, the Trustee is entitled to and is granted a judgment  
for the benefit of the Liquidating Trust of Debtor against **Geoff Toews** in the  
amount of **\$388,219.39 CAD**, plus pre-judgment interest from July 21, 2009, at  
the applicable federal judgment rate and post-judgment interest at the federal  
judgment rate from the date of judgment to the date the judgment is paid in full,  
*see* 28 U.S.C. § 1961.

22. The Trustee is entitled to reimbursement of its costs for pursuing this action.

23. Trustee is awarded all applicable interest, costs and disbursements of this action against each Defendant.

IT IS SO ORDERED.

The District Court Clerk is hereby directed to enter this Order and to provide copies to counsel.

**DATED** this 13th day of January 2015.

s/ Rosanna Malouf Peterson  
ROSANNA MALOUF PETERSON  
Chief United States District Court Judge