

FILED

February 18, 2021

UNITED STATES BANKRUPTCY COURT
EASTERN DISTRICT OF CALIFORNIA

NOT FOR PUBLICATION

UNITED STATES BANKRUPTCY COURT
EASTERN DISTRICT OF CALIFORNIA

In re:

INTERNATIONAL MANUFACTURING GROUP,
INC.,

Debtor.

Case No. 14-25820-A-11

BEVERLY N. MCFARLAND,

Plaintiff,

V.

LARRY A. CARTER et al.,

Defendants.

Adv. No. 15-2122-A

IWC-11

MEMORANDUM

Argued and submitted on February 17, 2021

at Sacramento, California

Honorable Fredrick E. Clement, Bankruptcy Judge Presiding

Appearances: Christopher D. Sullivan, Karen Diep, Lynn
Hollenbeck, Diamond McCarthy LLP for
plaintiff Beverly N. McFarland; Ian W.
Craig, Law Offices of Ian W. Craig and
Glenn W. Peterson, Peterson Watts Law
Group, LLP for defendants Larry A. Carter,
Jack T. Sweigart, Victoria J. Sweigart,
JTS Communities, Inc., C.I.M.G. JV, LLC,
Bristol Insurance Company, and SCB
Investments

1 May a plaintiff seek to impose liability arising from the same
2 transaction or occurrence against different defendants under different
3 positions? Yes, provided the plaintiff's positions in the different
4 actions are not mutually exclusive.

5 **I. FACTS**

6 **A. International Manufacturing Group**

7 International Manufacturing Group, Inc. ("IMG") imported latex,
8 nitrile and other medical gloves manufactured in Asia for sale in the
9 United States. It purported to have two sides of its business: a
10 retail division and a wholesale division. Sometimes the retail
11 division broke even; sometimes it lost money.

12 In reality, the wholesale division was a \$150 million dollar
13 Ponzi scheme. The central player in the IMG's Ponzi scheme was Deepal
14 Wannakuwatte ("Wannakuwatte"). Starting in 2004, Wannakuwatte
15 "solicited investors to invest in 'bids' related to purported
16 shipments of gloves from Asian manufacturers—primarily Malaysia—to
17 IMG's purposed customers, in particular the U.S. Department of
18 Veterans Affairs." Compl. 4:5-7, June 8, 2015, ECF No. 1. "IMG's
19 investors were told that their investments were directly related to
20 such shipments, and they were essentially financing IMG's supposedly
21 highly profitable inventory purchases." *Id.* at 4:7-9. In exchange,
22 investors received short-term promissory notes paying between 12% and
23 20%. Rather than being used to purchase and import gloves, the
24 investor's monies were used to fuel the Ponzi scheme and were diverted
25 to Wannakuwatte and others.

26 Wannakuwatte used account number 4841 at California Bank & Trust
27 to carry out his financial machination. That account functioned as a
28 "common pot" into which monies from new investors were deposited and

1 payments to existing creditors were made. *Id.* at 4:15-20. "Virtually
2 all payments made to IMG's investors were made with funds obtained
3 from new investors and/or other lenders." *Id.* at 4:20-21.

4 Among Wannakuwatte's investors were Larry A. Carter, Jack T.
5 Sweigart and related entities (collectively "Carter and Sweigart").
6 Carter and Sweigart invested \$83.2 million in IMG. They also provided
7 standby letters of credit to IMG, which Wannakuwatte used as
8 collateral for loans from California Bank & Trust. The California
9 Bank & Trust loans provided Wannakuwatte large amounts of cash that
10 Wannakuwatte used to prop up his Ponzi scheme. Carter and Sweigart
11 sustained a net loss of \$26.7 million in the Ponzi scheme (investing
12 \$83.2 million and receiving \$56.5 million back). Gabrielson Dep.
13 202:24-203:3 and McFarland Dep. 127:14-128:4, Separate Statement
14 Undisputed Facts Exh. 14 & 15, October 13, 2020, ECF No. 545.

15 In 2014, IMG sought Chapter 11 protection. Beverly McFarland
16 ("McFarland") was appointed the Chapter 11 trustee. A liquidating
17 plan was confirmed, which continued McFarland's service as trustee.

18 Wannakuwatte was charged with, and pled guilty to, fraud. First
19 Am. Compl. 5:5-10, ECF No. 1. For this role, he was sentenced to 20
20 years in prison. *Id.*

21 **B. The Carter/Sweigart Action**

22 In 2015, McFarland filed the instant adversary proceeding against
23 Carter and Sweigart to recover fraudulent conveyances. Compl., ECF
24 No. 1; 11 U.S.C. §§ 548(a)(1)(A), 544; Cal. Civ. Code § 3439.04
25 ("Carter/Sweigart action"). Carter and Sweigart filed an answer, ECF
26 No. 13.

27 **C. The California Bank & Trust Action**

28 In 2016, McFarland filed an adversary proceeding against

1 California Bank & Trust. *McFarland v. California Bank & Trust*, No.
2 16-02090 (Bankr. E.D. Cal. May 6, 2016) ("California Bank & Trust
3 action"). That complaint alleged causes of action for fraud. 11
4 U.S.C. § 544; Cal. Civ. Code § 3439 et seq.; First Am. Compl., August
5 24, 2016, ECF No. 54. McFarland's contentions are well-summarized in
6 her statements that California Bank & Trust "played a pivotal role in
7 facilitating Wannakuwatte's scheme," advanced funds to Wannakuwatte on
8 his "instruction," and without "any supporting documentation," and
9 "turn[ed] a blind eye to many glaring red flags of potential fraud on
10 the part of IMG." First Am. Compl. 3:8-19.

11 Eventually, McFarland and California Bank & Trust settled the
12 action for a sizable (though confidential) sum.

13 **II. PROCEDURE**

14 Carter and Sweigart now move for summary judgment. Fed. R. Civ.
15 P. 56, incorporated by Fed. R. Bankr. P. 7056. They contend that
16 McFarland is judicially estopped by her statements in the California
17 Bank & Trust action from asserting that they are "active participants"
18 in the Ponzi scheme rather than "victims." Mem. P.&A. 1:27-28,
19 October 13, 2020, ECF No. 543. McFarland opposes the motion.¹

20 **III. JURISDICTION**

21 This court has jurisdiction. 28 U.S.C. §§ 1334(a)-(b), 157(b);
22 see also General Order No. 182 of the Eastern District of California.
23 This is a statutorily core, but a constitutionally non-core,
24 proceeding. 28 U.S.C. § 157(b)(2)(H). The parties have consented to

25 ¹ Carter and Sweigart have objected to portions of Christopher Sullivan's
26 declaration. Objection, November 17, 2020, ECF No. 563. Defendants'
27 objections are sustained and overruled as follows: (1) Objection No. 1:
28 entire Decl. of Sullivan, overruled, LBR 7056-1(f) (lack of particularity and
identification of impacted separate statement of facts); (2) Objection No. 2:
sustained, Fed. R. Evid. FRE 602, 701; and (3) Objection No. 3: sustained
insofar as it addresses plaintiff McFarland's intentions, Fed. R. Evid. 602.

1 final orders and judgments by this court by failing to object in a
2 timely manner. Scheduling Order 2:12, 6:3-7, September 1, 2016, ECF
3 No. 30 (setting deemed consent deadline 45 days prior to October 19,
4 2017); 28 U.S.C. § 157(c)(1). *Executive Benefits Ins. Agency v.*
5 *Arkison*, 573 U.S. 25, 38 (2014) (fraudulent conveyances); *Wellness*
6 *Int'l Network, Ltd. v. Sharif*, 135 S.Ct. 1932, 1939 (2015) (implied
7 consent).

8 **IV. LAW**

9 **A. Summary Judgment**

10 Federal Rule of Civil Procedure 56 requires the court to grant
11 summary judgment on a claim or defense "if the movant shows that there
12 is no genuine dispute as to any material fact and the movant is
13 entitled to judgment as a matter of law." Fed. R. Civ. P. 56(a),
14 *incorporated by* Fed. R. Bankr. Proc. 7056. "[T]he mere existence of
15 some alleged factual dispute between the parties will not defeat an
16 otherwise properly supported motion for summary judgment; the
17 requirement is that there be no genuine issue of material fact."
18 *California v. Campbell*, 138 F.3d 772, 780 (9th Cir. 1998) (citing
19 *Anderson v. Liberty Lobby, Inc.*, 477 U.S. 242, 247-48 (1986)). "A
20 fact is 'material' when, under the governing substantive law, it could
21 affect the outcome of the case." *Thrifty Oil Co. v. Bank of Am. Nat'l*
22 *Trust & Sav. Ass'n*, 322 F.3d 1039, 1046 (9th Cir. 2003) (citing
23 *Anderson v. Liberty Lobby, Inc.*, 477 U.S. 242, 248 (1986)).

24 "The court must view the evidence in the light most favorable to
25 the non-movant and draw all reasonable inferences in the non-movant's
26 favor." *Swoger v. Rare Coin Wholesalers*, 803 F.3d 1045, 1047 (9th
27 Cir. 2015) (citing *Clicks Billiards Inc. v. Sixshooters Inc.*, 251 F.3d
28 1252, 1257 (9th Cir. 2001)).

1 A shifting burden of proof applies to motions for summary
2 judgment. *In re Oracle Corp. Sec. Litig.*, 627 F.3d 376, 387 (9th Cir.
3 2010). "The moving party initially bears the burden of proving the
4 absence of a genuine issue of material fact." *Id.*

5 "Where the non-moving party [e.g., a plaintiff] bears the burden
6 of proof at trial, the moving party need only prove that there is an
7 absence of evidence to support the non-moving party's case. Where the
8 moving party meets that burden, the burden then shifts to the non-
9 moving party to designate specific facts demonstrating the existence
10 of genuine issues for trial." *Id.* (citation omitted). The Ninth
11 Circuit has explained that the non-moving party's "burden is not a
12 light one. The non-moving party must show more than the mere
13 existence of a scintilla of evidence." *Id.* "In fact, the non-moving
14 party must come forth with evidence from which [the factfinder] could
15 reasonably render a verdict in the non-moving party's favor." *Id.*

16 When the moving party has the burden of persuasion at trial
17 (e.g., a plaintiff on claim for relief or a defendant as to an
18 affirmative defense), the moving party's burden at summary judgment is
19 to "establish beyond controversy every essential element of its . . .
20 claim." *S. California Gas Co. v. City of Santa Ana*, 336 F.3d 885, 888
21 (9th Cir. 2003) (internal quotation marks omitted). In such a case,
22 there is no need to disprove the opponent's case "[i]f the evidence
23 offered in support of the motion establishes every essential element
24 of the moving party's claim or [affirmative] defense." Hon. Virginia
25 A. Phillips & Hon. Karen L. Stevenson, *Federal Civil Procedure Before*
26 *Trials, Calif. & 9th Cir. Edit.*, Summary Judgment, Burden of Proof ¶
27 14:126.1 (Rutter Group 2019).

28 A party may support or oppose a motion for summary judgment with

1 affidavits or declarations that are "made on personal knowledge" and
2 that "set out facts that would be admissible in evidence." Fed. R.
3 Civ. P. 56(c)(4). The assertion "that a fact cannot be or is
4 genuinely disputed" may be also supported by citing to other materials
5 in the record or by "showing that the materials cited do not establish
6 the absence or presence of a genuine dispute, or that an adverse party
7 cannot produce admissible evidence to support the fact." Fed. R. Civ.
8 P. 56(c)(1).

9 "A motion for summary judgment cannot be defeated by mere
10 conclusory allegations unsupported by factual data." *Angel v.*
11 *Seattle-First Nat'l Bank*, 653 F.2d 1293, 1299 (9th Cir. 1981) (citing
12 *Marks v. U.S. Dep't of Justice*, 578 F.2d 261, 263 (9th Cir. 1978)).
13 "Furthermore, a party cannot manufacture a genuine issue of material
14 fact merely by making assertions in its legal memoranda." S.A.
15 *Empresa de Viacao Aerea Rio Grandense v. Walter Kidde & Co.*, 690 F.2d
16 1235, 1238 (9th Cir. 1982).

17 **B. Judicial Estoppel**

18 "[W]here a party assumes a certain position in a legal
19 proceeding, and succeeds in maintaining that position, he may not
20 thereafter, simply because his interests have changed, assume a
21 contrary position, especially if it be to the prejudice of the party
22 who has acquiesced in the position formerly taken by him." *Davis v.*
23 *Wakelee*, 156 U.S. 680, 689 (1895); *New Hampshire v. Maine*, 532 U.S.
24 742, 749 (2001). Known as judicial estoppel, where applicable, the
25 rule prevents parties from changing positions. *Pegram v. Herdrich*,
26 530 U.S. 211, 227, n. 8 (2000). The rule applies to inconsistent
27 positions taken in "the same litigation" and "in two different cases."
28 *Rissetto v. Plumbers and Steamfitters Local 343*, 94 F.3d 597, 605 (9th

1 Cir. 1996) (citations omitted).

2 Judicial estoppel protects the integrity of the judicial process
3 and falls within the trial court's discretion. *New Hampshire*, 532
4 U.S. at 750; *Soames Lane Trust v. Gonzalez (In re Soames Lane Trust)*,
5 2016 WL 4198426 *5 (9th Cir. August 8, 2016). To determine whether to
6 invoke judicial estoppel, the court considers the following:

7 (1) Is the party's later position clearly inconsistent with
8 its earlier position? (2) Did the party succeed in
9 persuading a court to accept its earlier position, creating
10 a perception that the first or second court was misled? and
(3) Will the party seeking to assert an inconsistent
position "derive an unfair advantage or impose an unfair
detriment on the opposing party?"

11 *Baughman v. Walt Disney World Co.*, 685 F.3d 1131, 1133 (9th Cir.
12 2012), quoting *New Hampshire*, 532 U.S. at 750-751 (quotation marks
13 omitted).

14 For the first element, the inconsistencies apparent in the latter
15 case must be material to the issues in dispute in the prior case.
16 *Baughman*, 685 F.3d at 1133 (holding that the Americans With
17 Disabilities Act plaintiff's statement about her inability to use a
18 wheelchair was not "peripheral" or "immaterial[,] " but "central" to
19 her earlier claim that she couldn't access the defendant's facilities
20 by using a wheelchair). Moreover, "clearly inconsistent positions"
21 exactly oppose one another, and do not just undermine one another.
22 *King v. Herbert J. Thomas Mem'l Hosp.*, 159 F.3d 192, 196 (4th Cir.
23 1998) (holding that judicial estoppel requires "mutually inconsistent
24 positions"); See e.g., *Baughman*, 685 F.3d 1133. "Doubts about
25 inconsistency" should be resolved against the party asserting judicial
26 estoppel. *Contech Const. Prod., Inc. v. Heierli*, 764 F.Supp.2d 96,
27 116 (D.D.C. 2011); *Shea v. Clinton*, 880 F.Supp.2d 113, 117 (D.D.C.
28 2012).

1 The party asserting judicial estoppel bears the burden of proof
2 as to its applicability. *Abara v. Altec Indus., Inc.*, 838 F.Supp.2d
3 995, 1006 (E.D. Cal. 2011).

4 **V. DISCUSSION**

5 A trustee's right to avoid payments to Ponzi scheme investors is
6 largely determined by three things: (1) the amount of monies received
7 by the investors (net positive or negative to the initial investment);
8 (2) the investors' good faith, or lack thereof; and (3) what payments
9 they received within the statute of limitations:

10 ...[F]ederal courts have generally followed a two-step
11 process. First, to determine whether the investor is
12 liable, courts use the so-called "netting rule." Amounts
13 transferred by the Ponzi scheme perpetrator to the investor
14 are netted against the initial amounts invested by that
15 individual. If the net is positive, the receiver has
16 established liability, and the court then determines the
17 actual amount of liability, which may or may not be equal
18 to the net gain, depending on factors such as whether
19 transfers were made within the limitations period or
20 whether the investor lacked good faith. If the net is
21 negative, the good faith investor is not liable because
22 payments received in amounts less than the initial
23 investment, being payments against the good faith losing
24 investor's as-yet unsatisfied restitution claim against the
25 Ponzi scheme perpetrator, are not avoidable within the
26 meaning of UFTA....

27 Second, to determine the actual amount of liability, the
28 court permits good faith investors to retain payments up to
the amount invested, and requires disgorgement of only the
"profits" paid to them by the Ponzi scheme.... Payments up
to the amount of the initial investment are considered to
be exchanged for "reasonably equivalent value," and thus
not fraudulent, because they proportionally reduce the
investors' rights to restitution. If investors receive
more than they invested, "[p]ayments in excess of amounts
invested are considered fictitious profits because they do
not represent a return on legitimate investment activity."
Donell v. Kowell, 533 F.3d 762, 771-72 (9th Cir. 2008).

29 In deciding whether the trustee's Carter/Sweigart action is
30 barred by judicial estoppel, this court needs not look further than

1 the "clearly inconsistent positions" element.² *New Hampshire*, 532
2 U.S. at 750-51; *Baughman*, 685 F.3d at 1133.

3 **A. Different Standards**

4 Carter and Sweigart argue that McFarland's characterization of
5 them as "victims" or "investors" in the California Bank & Trust action
6 is inconsistent with her characterization of them as "co-
7 perpetrators." Their argument fails since Carter and Sweigart may
8 easily be both given the circumstances and the two positions are not
9 mutually inconsistent. *Herbert J. Thomas Mem'l Hosp.*, 159 F.3d at
10 196.

11 Having sustained a net loss of \$26.7 million the defendants are
12 unquestionably victims. But whether they will be allowed to retain
13 funds received from IMG/Wannakuwatte up to the amount of their initial
14 investment is determined by their good faith, or lack thereof.
15 *Donell*, 533 F.3d at 771 n. 3. Good faith is an objective standard and
16 may be defeated if "circumstances would place a reasonable person on
17 inquiry and a lack of due diligence." *In re Agric. Research & Tech.*
18 *Group*, 916 F.2d 528, 535-36 (9th Cir. 1990). Since the standard
19 requiring the defendants' disgorgement of monies received is
20 relatively low, i.e., inquiry notice and a lack of due diligence,
21 these differing positions, even if supported by the evidentiary

22 ² This court believes that Carter and Sweigart have waived this affirmative
23 defense by failing to plead it, ECF No. 13. *Go Global, Inc. v. Sig Rogich*
24 (*In re Go Global, Inc.*), 2016 WL 6901265 *10 (9th Cir. BAP November 22, 2016)
25 (judicial estoppel is an affirmative defense that must be pled); First Am.
26 Answer, July 6, 2017, ECF No. 43 (fourth and sixth affirmative defenses
27 pleading equitable estoppel and estoppel by full performance). Though
28 judicial estoppel may be raised sua sponte, *Allen v. C & H Distribs., LLC*,
813 F.3d 566, 571 n.4 (5th Cir. 2015), the court will not do so in this case.
Lest the defendants perceive the court's ruling as based on a procedural
deficiency that might be corrected by seeking leave to file an amended
answer, Fed. R. Civ. P. 15(a)(2), incorporated by Fed. R. Bankr. P. 7015, the
court will address the merits of the defense.

1 record, are not mutually inconsistent.

2 **B. Clear Inconsistency**

3 Carter and Sweigart failed to show that McFarland took "clearly
4 inconsistent positions" with respect to their actions.³ In the present
5 action, McFarland contends that Carter and Sweigart are not "Innocent
6 Investors" in the IMG Ponzi scheme. Responses to Request for
7 Admission, Set One, Request No. 97 (Carter) and Request No. 100
8 (Carter), Response to Separate Statement of Undisputed Material Facts
9 Exhs. 2 & 3, November 3, 2020, ECF No. 557.⁴

10 Carter and Sweigart contend that McFarland's assertion is
11 directly contrary to her position towards them in the California Bank
12 & Trust action. This court disagrees. In the California Bank & Trust
13 action, McFarland's complaint specifically names those investors whom
14 she believed to have acted without knowledge or notice of the fraud:

15 [International Manufacturing Group] had a number of
16 creditors whom could have avoided the [California Bank &
17 Trust] Purported Principal Transfers...These creditors
18 include, but are not limited to, the following (along with
other innocent creditors, the "Innocent Creditors"): Ron
Ashely, Ryan Ashley, Ashely Backman, Arless Botta, Inger

19 ³ The parties' discussion about what California Bank & Trust knew, or should
20 have known, and when they knew, or should have known it, with respect to
21 Wannakuwatte's activities is not germane to determine whether McFarland is
22 judicially estopped with respect to Carter and Sweigart. The key issue is
whether McFarland has taken mutually inconsistent positions with respect to
California Bank & Trust. Any argument that McFarland's position in the
California Bank & Trust action was that California Bank & Trust was
Wannakuwatte's sole abettor is not supported by the record.

23 ⁴ Clear and unambiguous responses to requests for admission bind; ambiguous
24 responses may be construed by the court to determine their scope and effect.
25 *Johnson v. DeSoto County Bd. of Commrs*, 204 F.3d 1335, 1340 (11th Cir. 2000).
The court has considered the plaintiff's responses to the numerous requests
for admission cited and believes that both individually and collectively
those admissions fall well short of admitting Carter and Sweigart's good
faith in this matter and/or their status as innocent investors. Moreover, in
26 response to the key Request for Admissions, Nos. 97, 100, which stated,
27 "Admit that YOUR definition of Innocent Investors" in Paragraph 327 of the
CBT COMPLAINT [includes Carter and Sweigart]," the plaintiff responded,
28 "Denied."

1 Brenner, Dennis & Kathryn DeLucio, David & Alaina Divine,
2 Richard Gere, David & Janice Hill, Michael & Janine Jones,
Ellen Karlstad, Thomas Kim, July Leuvrey.

3 The Innocent Creditors could not have reasonably discovered
4 the existence of the Ponzi scheme, the existence of
[California Bank & Trust] Purported Principal Transfers, or
5 the fraudulent nature of the [California Bank & Trust]
Purported Principal Transfer prior to May 31, 2013...

6 First Am. Compl. ¶¶ 327-328, *McFarland v. California Bank & Trust*, No.
7 16-2090 (Bankr. E.D. Cal. 2016), ECF No. 54.

8 Later, in the California Bank & Trust action McFarland answered
9 an interrogatory stating:

10 The Innocent Investors, as defined in the [First Amended
11 Complaint] who were actual unsecured creditors of
[International Manufacturing Group] and did not know or
12 suspect the existence of the [International Manufacturing
Group] Ponzi scheme until on or after May 31, 2013. The
13 Innocent Investors are believed to include but not be
limited to the Innocent Investors identified in the [First
14 Amended Complaint] by name in paragraph 327 of the [First
Amended Complaint]. Additional Innocent Investors may
15 include but not be limited to Steven and Deanna Green
(Claim No. 3), and David Wellenbrock (Claim No. 14). The
16 Innocent Investors could not have discovered the
[International Manufacturing Group] Ponzi scheme prior to
May 31, 2013....

17 Plaintiff's Response to California Bank & Trust Interrogatories, Set
18 One, Interrogatory No. 4, *McFarland v. California Bank & Trust*, No.
19 16-2090 (Bankr. E.D. Cal. 2016).

20 Carter and Sweigart are absent from each list of "Innocent
21 Creditors." This is not the "clearly inconsistent" stance
22 contemplated by *Pegram, New Hampshire*, or their children. As a
23 result, the motion will be denied.

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1 **VI. CONCLUSION**

2 For each of these reasons, defendants' motion for summary
3 judgment is denied. The court will issue an order from chambers.

4 Dated: February 18, 2021

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7 _____/s/_____
Fredrick E. Clement
8 United States Bankruptcy Judge
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Instructions to Clerk of Court

Service List - Not Part of Order/Judgment

The Clerk of Court is instructed to send the Order/Judgment or other court generated document transmitted herewith *to the parties below*. The Clerk of Court will send the document via the BNC or, if checked ☐, via the U.S. mail.

Attorneys for the Plaintiff(s)	Attorneys for the Defendant(s) (if any)
Bankruptcy Trustee (if appointed in the case)	Office of the U.S. Trustee Robert T. Matsui United States Courthouse 501 I Street, Room 7-500 Sacramento, CA 95814
Anthony Napolitano 1000 Wilshire Blvd #1500 Los Angeles, CA 90017	Marc A. Caraska 2100 Northrop Avenue, Ste 900 Sacramento, CA 95825
Joel Samuels 1000 Wilshire Blvd #1500 Los Angeles, CA 90017	