UNITED STATES DISTRICT COURT
FOR THE NORTHERN DISTRICT OF ILLINOIS
EASTERN DIVISION

SECURITIES AND EXCHANGE COMMISSION Plaintiff, v. STEPHEN L. HOLDEN, SCOTT P. SKOOGLUND, KULDARSHAN S. PADDA, and STEPHAN C. BEAL, Defendants.	Case No. 01C 7463 JUDGE NORDBERG MAGISTRATE JUDGE DENLOW DOCKETED SEP 27 2001

COMPLAINT

Plaintiff Securities and Exchange Commission ("Plaintiff" or "Commission") alleges the following:

SUMMARY

1. From 1998 through 1999, Defendants Stephan C. Beal ("Beal"), Stephen L. Holden ("Holden"), Kuldarshan S. Padda ("Padda"), and Scott P. Skooglund ("Skooglund") violated and/or aided and abetted violations of antifraud, reporting, internal controls and record keeping provisions of the Securities Exchange Act of 1934 ("Exchange Act"). In 1998 and 1999, Defendants were executives of Sabratek Corporation ("Sabratek" or "the Company"), an Illinois medical products manufacturer of infusion pumps and flush syringes. During those years, Defendants engaged in a scheme to defraud and made material misstatements and omitted to state material facts regarding, among other things, Sabratek's financial condition and results of operations in its Form 10-K for

the year 1998 and Forms 10-Q for the first three quarters of 1998 and the first quarter of 1999. Defendants used fictitious sales, inventory parking arrangements, improper revenue recognition and fictitious billings for services to overstate Sabratek's net sales by a total of $30.7 million (62%) and operating income by approximately $18.3 million (229%) over the five quarters. As a result of Defendants' efforts, Sabratek reported operating income totaling $10.3 million instead of operating losses totaling approximately $8.0 million over those five periods. In the second half of 1999, when news of Sabratek's inflated operating results began to emerge, the Company's market capitalization declined by $202.5 million, or 98%.

2. Defendants, directly or indirectly, have engaged in, and unless restrained and enjoined by this Court will continue to engage in, transactions, acts, practices, and courses of business, which violate Section 10(b) of the Securities Exchange Act of 1934 ("Exchange Act") [15 U.S.C. §78j(b)] and Rule 10b-5 thereunder [17 C.F.R. §240.10b-5].

3. Defendants, directly or indirectly, or by aiding and abetting, have engaged in, and unless restrained and enjoined by this Court will continue to engage in, transactions, acts, practices, and courses of business, which violate Sections 13(a) and 13(b)(2)(A) of the Exchange Act [15 U.S.C. §§78m(a) and 78m(b)(2)(A)] and Rules 13a-1, 13a-13, 13b2-1 and 12b-20 thereunder [17 C.F.R. §§240.13a-1, 240.13a-13, 240.13b2-1, and 240.12b-20].

4. Defendants Holden, Skooglund, and Padda directly or indirectly, or by aiding and abetting, have engaged in, and unless restrained and enjoined by this Court will continue to engage in, transactions, acts, practices, and courses of business, which violate Section 13(b)(2)(B) of the Exchange Act [15 U.S.C. §78m(b)(2)(B)] and Rule 13b2-2 thereunder [17 C.F.R. §240.13b2-2].

5. Defendants Holden, Padda, and Beal, directly or indirectly, have engaged in, and unless restrained and enjoined by this Court will continue to engage in, transactions, acts, practices, and courses of business, which violate Section 13(b)(5) of the Exchange Act [15 U.S.C. §78m(b)(5)].

6. Defendant Holden, as a control person under Section 20(a) of the Exchange Act [15 U.S.C. §78t(a)], has engaged in, and unless restrained and enjoined by this Court will continue to engage in, transactions, acts, practices, and courses of business that violate Sections 10(b), 13(a), 13(b)(2)(A), 13(b)(2)(B), and 13(b)(5) of the Exchange Act [15 U.S.C. §§78j(b), 78m(a), 78m(b)(2)A), 78m(b)(2)(B), and 78m(b)(5)] and Rules 10b-5, 13a-1, 13a-13, 13b2-1, 13b2-2, and 12b-20 [17 C.F.R. §§240.10b-5, 240.13a-1, 240.13a-13, 240.13b2-1, 240.13b2-2, and 240.12b-20].

7. The Commission brings this action pursuant to the authority conferred upon it by Sections 21(d) and (e) of the Exchange Act [15 U.S.C. §78u(d) and (e)] for an order permanently restraining and enjoining Defendants, imposing civil penalties on the Defendants, prohibiting Holden from acting as an officer or director of any issuer whose securities are registered pursuant to Section 12 of the Exchange Act [15 U.S.C. §78*l*], and granting other equitable relief.

JURISDICTION AND VENUE

8. This Court has jurisdiction over this action pursuant to Sections 21(e) and 27 of the Exchange Act [15 U.S.C. §§78u(e) and 78aa]. Venue lies in this Court pursuant to Section 27 of the Exchange Act [15 U.S.C. §78aa].

9. In connection with the acts, practices, and courses of business alleged in this Complaint, each of the Defendants, directly or indirectly, has made use of the means or instrumentalities of interstate commerce and/or of the mails.

10. Certain of the acts, practices and courses of business constituting the violations alleged herein occurred within this judicial district.

ENTITY INVOLVED

11. At all times relevant herein, Sabratek was a Delaware corporation based in Skokie, Illinois. Sabratek was a developer and seller of remote healthcare equipment, including infusion pumps and flush syringes, and related equipment and software used in both hospital and home healthcare situations. Sabratek sold both to the end-users, such as hospitals, pharmacies, and nursing homes, as well as to distributors, which resold Sabratek products to other distributors or the end-users. Sabratek's securities were registered with the Commission pursuant to Section 12(g) of the Exchange Act [15 U.S.C. §78*l*(g)] and were traded on Nasdaq. On December 17, 1999, Sabratek filed a petition to reorganize under Chapter 11 of the Bankruptcy Code.

DEFENDANTS

12. At all times relevant herein, Defendant Kuldarshan S. Padda, a resident of Chicago, Illinois, served as Sabratek's Chief Executive Officer ("CEO") and Chairman of the Board. Padda's duties included: communicating with stock analysts about Sabratek's financial outlook; determining the short and long term strategy for Sabratek's business ventures; approving non-standard sales terms; negotiating sales agreements with customers; reviewing Sabratek's financial statements; preparing or reviewing information in public filings, including the management, discussion & analysis section ("MD&A") in annual and quarterly reports; and preparing or reviewing Sabratek's press releases.

13. Defendant Stephen L. Holden, a resident of Deerfield, Illinois, served as Sabratek's Chief Financial Officer ("CFO"), Controller and Treasurer from August 1996 to July 1998. From July 1998 to January 2000, Holden served as President and Treasurer of Sabratek. As CFO and Controller, Holden's duties included preparing or reviewing Sabratek's financial statements, preparing or reviewing Sabratek's press releases, serving as a liaison with Sabratek's auditors,

and providing information about Sabratek's internal controls, books, records and accounts to Sabratek auditors. As President, Holden's duties included: operating Sabratek on a day-to-day basis; communicating with stock analysts about Sabratek's financial outlook; negotiating sales agreements with customers; reviewing and approving drafts of Sabratek's financial statements; serving as a liaison with Sabratek's auditors; providing information about Sabratek's internal controls, books, records and accounts to Sabratek auditors; preparing or reviewing information in public filings, including the MD&A section in annual and quarterly reports; and preparing or reviewing press releases. Holden exercised control over Sabratek generally and over the accounting and sales departments, having the power to approve sales transactions involving large quantities or containing non-standard terms.

14. At all times relevant herein, Defendant Stephan C. Beal, a resident of Norwell, Massachusetts, served as Sabratek's Vice President of Sales. Beal's duties included negotiating sales agreements with Sabratek customers, managing Sabratek's sales force, and supervising Sabratek's sales order entry function.

15. At all times relevant herein, Defendant Scott S. Skooglund, a resident of Woodridge, Illinois, served as Sabratek's Vice President of Finance and Chief Accounting Officer. Skooglund's duties included preparing Sabratek's financial statements, overseeing Sabratek's budgeting process, and providing information about Sabratek's internal controls, books, records and accounts to Sabratek auditors.

DEFENDANTS' FRAUDULENT SCHEME

The Improper Recognition of Pump Revenue

16. During their employment at Sabratek, Defendants were familiar with accounting rules concerning the recognition of revenue for sales transactions, including that revenue from sales

with right-of-return or consignment terms could not be recognized by Sabratek until its customer had resold the products.

17. During their employment at Sabratek, Defendants knew that Sabratek had a general practice of automatically recognizing sales when products were shipped.

18. Defendants also knew that Sabratek's customer service department, which was part of the sales department rather than the accounting department, initiated the recognition of sales by entering new orders into the sales order entry system ("system"). In many cases, written purchase orders were forwarded to the customer service department for it to input the information contained therein into the system. Sabratek customer service staff routinely entered orders based on oral instructions communicated by Sabratek sales personnel or Sabratek management, or directly from the customer. Customer service representatives knew that all orders greater than 20 pumps required a written purchase order. These large orders also had to be approved by Beal before they could be entered into the system. Beal also had to approve any purchase order containing non-standard terms before customer service could process it.

19. Once an order was approved, the customer service staff entered the quantity ordered, the price, shipping information and customer name into the system. Typically, the only other terms entered were the number of days the customer had to make payment. Standard payment terms were for payment in 30 days. Sabratek's system had the ability to store other detailed terms. Regardless of how complicated or non-standard the terms of a particular transaction were, customer service did not enter those additional terms in the system. After the order was entered into the system, the information was transmitted to the shipping department, which shipped the products that were purportedly ordered to the destination indicated by the customer service

department. Once products were shipped, the system automatically recognized the order as a sale and generated an invoice to the customer.

20. At the end of each quarter and year, Skooglund's staff prepared drafts of financial statements based on information contained in Sabratek's system. Skooglund reviewed the draft financial statements and forwarded them to Padda and Holden for additional review. Skooglund then incorporated any changes suggested by Padda and Holden based on their review of the draft financial statements. Holden, Skooglund, and Padda reviewed the financial statements before they were presented to Sabratek's directors and auditors and before they were included in Commission filings or in press releases. When Holden, Skooglund, and Padda reviewed drafts of financial statements, they did not review purchase orders or sales agreements even though they knew that Sabratek had entered into significant end-of-the-quarter sales to its customers. Holden, Skooglund, and Padda did not review journal entries made into the system and did not take any steps to verify the existence of any non-standard terms or side agreements before approving the financial statements' publication and filing.

21. Although the customer service department did not review purchase orders with the accounting department before they were entered, written purchase order and sales agreements were accessible to accounting department personnel. Holden and Skooglund knew that the customer service department maintained copies of the sales agreements and purchase orders.

22. During the relevant time period, Sabratek's pump and flush syringe businesses were the Company's two primary sources of sales. Prior to 1998, Sabratek capitalized on strong demand for pumps from large institutional customers to increase its sales. In 1998, however, Sabratek faced slowing demand for pumps from these same institutional customers. To maintain continued growth, Sabratek shifted its marketing focus to small distributors. These distributors,

however, did not have the financial ability, warehousing space, or customer bases necessary to purchase large quantities of pumps. Furthermore, in late 1998 Food and Drug Administration ("FDA") safety concerns forced Sabratek to cease distribution of its flush syringes, which made up nearly 25% of its sales. Despite these setbacks, however, Padda and Holden told analysts that Sabratek's sales would continue to grow in 1988. Based on Padda and Holden's representations, analysts projected that Sabratek's net sales would grow significantly in 1998. From 1994 to 1997, Sabratek's sales had increased from $3.3 million to $43.1 million, and many analysts expected Sabratek's sales to increase to approximately $66 million in 1998.

23. To meet the analysts' sales expectations they had created, Holden, Padda, and Beal, and other Sabratek management set 1998 sales quotas higher than those for 1997 and 1999 quotas that were even higher. In setting these quotas, Defendants Holden, Padda, and Beal disregarded warnings from Sabratek sales staff that demand for Sabratek pumps had declined significantly. At the end of each quarter in 1998 and the first quarter of 1999, Padda reiterated to Beal that sales quotas must be met. In response, Beal pressured his staff to get more orders before the end of the quarter. Beal told his staff that "failure was not an option" and could result in termination. As a result of these last-minute efforts, a large amount of Sabratek's sales were improperly recorded at the end of the quarters.

24. During the relevant period, Defendants Holden, Padda and Beal brought about many of the purported end-of-the-quarter sales. In some instances, they created fictitious sales of pumps that had not been ordered by customers, but instead were parked at third-party warehouses. In other instances, they entered into sales agreements containing consignment or right-of-return provisions. In still other instances, they agreed to significant seller's obligations, including promises that Sabratek's sales force would assist Sabratek's customers in the resale of

these pumps to end-users. Generally Accepted Accounting Principles ("GAAP") did not permit the recognition of such transactions as sales.

First Quarter 1998 – The Defendants Used Right-of-return And Consignment Terms To Inflate Sales

25. In the first quarter of 1998, the Defendants were able to conceal the increasing weakness in demand for Sabratek's pumps by improperly booking sales with consignment or right-of-return provisions. On March 13, 1998, Padda and the President of a customer named Omnicare, Inc. ("Omnicare"), with Holden and Beal present, orally agreed that Omnicare would purchase up to 1,500 pumps from Sabratek for $2,542,500. Under this agreement, Omnicare only had to pay for the pumps that were ordered by and shipped to Omnicare branch pharmacies within 180 days. Padda also agreed to credit Omnicare for any pumps not shipped after 180 days. Before the end of March 1998, Omnicare confirmed these terms in writing a letter to Sabratek's sales agent, who reported to Beal. Under Beal's direction, the 1,500 pumps were shipped to a third-party warehouse, Jett Services ("Jett"), in Lake Forest, Illinois. Omnicare never authorized that 1,500 pumps be shipped to Jett. Sabratek's invoices designated this warehouse the "Omnicare Dist. Center," though it was not associated with Omnicare. Defendants Holden and Skooglund deliberately or recklessly allowed the full $2,542,500 from the Omnicare transaction to be improperly reported as sales in the Company's Form 10-Q for the first quarter of 1998. This transaction represented 17% of Sabratek's sales for the quarter.

26. Holden and Skooglund also allowed the full $2,542,500 from the Omnicare transaction to be improperly reported as part of year-to-date sales in the Company's Forms 10-Q for the second and third quarters of 1998 and its Form 10-K for the year 1998. In June 1998, Skooglund learned that the Omnicare agreement contained non-standard terms, providing 180

days for payment instead of the standard 30 days. Despite this warning sign, however, Skooglund did nothing to determine whether these terms precluded Sabratek from including the full $2,542,500 from Omnicare transaction in the year-to-date sales in the Form 10-Q for the second quarter of 1998. By September 1998, only 233 pumps had been ordered by and shipped to Omnicare branches. In September 1998, Omnicare notified Skooglund in a letter that Sabratek should only expect payment for the pumps that had already been ordered by its branches and sent him a $394,935 check as payment in full for those pumps, demanding a credit for the balance owed. Nevertheless, Skooglund did not credit Omnicare, record an allowance for the return of the pumps, or determine whether the prior recognition of the relevant $2,542,500 in sales should be reversed. Instead, Skooglund deliberately or recklessly allowed the full $2,542,500 to be improperly reported as part of the year-to-date sales in the Company's Form 10-Q for the third quarter of 1998.

27. Throughout 1998, Holden, Skooglund, and Beal received an internal report detailing the monthly shipments to Omnicare branches. They thus knew by September 1998 that Omnicare had in fact ordered and received only 233 pumps, not the full 1,500. By the end of 1998, Sabratek was still warehousing approximately 1,000 pumps from the March 1998 order, supposedly for Omnicare's benefit. Moreover, by December 1998, Sabratek's accounting staff was openly questioning Holden and Skooglund about why Omnicare had not paid for all the 1,500 pumps and whether there were special terms involved. However, Holden and Skooglund did not act to write off the improperly reported sales.

28. In 1998 and 1999, Defendants Holden and Skooglund received periodic internal reports captioned "Top 40 Receivables," which listed the 40 customers who had the largest unpaid bills. These reports also showed the aging of the receivables by the number of days that

payment was overdue. In the March 1999 "Top 40 Receivables" report, issued prior to the filing of the Company's 1998 Form 10-K, Omnicare was listed as the largest unpaid receivable with an amount due of $2,370,124, constituting 13.92% of all the Company's outstanding receivables. Of this amount, $1,728,900 was from the March 1998 pump transaction. Defendants Holden and Skooglund did not act to write off the $1,728,900 in improper Omnicare sales and instead allowed those sales to be improperly reported in the Company's 1998 Form 10-K.

29. In the middle of March 1998, Beal also told his sales staff to contact Wren Medical Systems, Inc. ("Wren") for a 200-pump order.

30. Padda had a pre-existing personal relationship with Wren, having secured financial support for Wren to start its business. In January 1998, Padda served as sole guarantor of a bank loan to Wren for $150,000 and used 8,000 shares of his own Sabratek stock as collateral for the loan. In July 1998, Padda provided the collateral necessary for the bank loan to be increased to $250,000.

31. After receiving Padda's instructions, Beal intimated to his sales staff that Padda had a special relationship with Wren that guaranteed a sale. In fact, Padda had directed Beal to get an order from Wren and before the end of the first quarter of 1998 Sabratek sales staff met with Wren's president and arranged for Wren to order 200 pumps for $383,000 with non-standard payment terms. Those non-standard terms gave Wren six months to pay for any pumps it sold within the six-month period. Afterward, Wren could pay Sabratek as Wren sold the pumps. Wren did not have to pay Sabratek for any pumps until they were resold. Holden and Skooglund deliberately or recklessly allowed the $383,000 Wren transaction to be improperly reported as sales in the Company's Form 10-Q for the first quarter of 1998.

32. By the end of 1998, Wren had only paid $33,600 for the pumps that it had resold. Wren was listed as the sixteenth largest receivable on the March 1999 "Top 40 Receivables" report, which Skooglund and Holden received before the 1998 Form 10-K was filed. Despite knowing these facts, however, Holden and Skooglund allowed the full $349,400 from the Wren transaction to be improperly reported as part of the year-to-date sales in the Company's Forms 10-Q for the second and third quarters of 1998 and its Form 10-K for the year 1998.

33. In addition to the Omnicare and Wren transactions, in late March 1998, Sabratek shipped 500 infusion pumps priced at $987,500 to Tacy Medical ("Tacy") without a firm agreement between Tacy and Sabratek as to terms. By March 31, 1998, Tacy agreed in a written purchase order that it would pay Sabratek only for any pumps it sold by August 31, 1998 and would have the option to return any unsold pumps to Sabratek. The Tacy transaction was a large, end-of-the quarter sale for Sabratek with a new customer. Despite these "red flags," however, Holden and Skooglund deliberately or recklessly allowed $987,500 from the Tacy transaction to be improperly reported as sales in the Company's Form 10-Q for the first quarter of 1998.

34. After the first quarter of 1998, Sabratek's accounting department treated the Tacy transaction as a consignment sale in collection efforts monitored by Skooglund, demanding payment from Tacy only for those pumps that it resold or leased. On or about September 2, 1998, all the Defendants received copies of a letter sent by Sabratek's Eastern Divisional Sales Manager to Tacy indicating that Sabratek had received payment of $250,000 from Tacy for the pumps sold by Tacy and no longer in Tacy's inventory. The letter requested monthly tracking information on the pumps that Tacy sold in the future. As of September 23, 1998, Tacy had placed 132 pumps with its customers and had only paid Sabratek $250,000 for those pumps. On

the March 1999 "Top 40 Receivables" report Holden and Skooglund received prior to the filing of the Company's 1998 Form 10-K, Tacy was ranked as the seventh largest receivable, with $671,528 still remaining to be paid from the March 1998 transaction. Despite these warning signs, Defendants Holden and Skooglund deliberately or recklessly allowed the full $987,500 from this Tacy transaction to be improperly reported as part of the year-to-date sales in the Company's Forms 10-Q for the second and third quarters of 1998 and its Form 10-K for the year 1998.

35. Padda and Beal knew or were reckless in not knowing that the Omnicare, Wren and Tacy transactions described in paragraphs 25 through 34 above were improperly reported as sales in the Company's Form 10-Q for the first quarter of 1998, and improperly included as part of the year-to-date sales in the Company's Forms 10-Q for the second and third quarters of 1998 and its Form 10-K for the year 1998.

Second Quarter Of 1998 - Sabratek Entered Into Parking Arrangements To Maintain Sales Growth

36. In the second quarter of 1998, Padda told Beal to find a wholesaler who could distribute Sabratek pumps and help Sabratek meet its sales quota for the quarter. Beal understood that the purpose of using a wholesaler in the second quarter of 1998 was to "achieve the sales now versus having to wait later." Following Padda's instructions, Beal arranged for the Burrows Company ("Burrows") to serve as a wholesaler for Sabratek. Holden subsequently directed Beal to obtain a 2,000-pump order from Burrows for approximately $4.2 million before the end of June 1998. Beal then approached Burrows through Sabratek's sales agent and told its representatives that Sabratek needed someone to distribute a large quantity of pumps to Tenet HealthSystem Medical, Inc. ("Tenet"), a national hospital and pharmacy system with which

Sabratek was then negotiating a sales agreement. Beal induced Burrows to send Sabratek a written purchase order by the end of the second quarter of 1998. This purchase order provided that Burrows would order 2,000 pumps for approximately $4.2 million, but had no obligation to pay for the pumps until the pumps were resold to Tenet. Beal agreed that if Burrows was unable to sell the pumps to Tenet within 90 days, Sabratek would credit Burrows for the entire amount of the invoice. Beal also arranged for Sabratek to warehouse the pumps at Sabratek's expense. Holden and Skooglund knew before the end of the second quarter of the Burrows transaction. They knew that the Burrows transaction was large and occurred at the end of the quarter with a customer, which had done no prior business with Sabratek. Holden and Skooglund deliberately or recklessly allowed this $4.2 million, approximately 25% of Sabratek's sales for the quarter, to be improperly reported as sales in the Company's Form 10-Q for the second quarter of 1998.

37. Sabratek did not sell the 2,000 pumps to Tenet within 90 days of the Burrows order; and, when Burrows requested a credit in September 1998, Holden and Beal arranged for Sabratek to credit Burrows in full. Skooglund's accounting department recorded this credit in Sabratek's books. The pumps originally meant for Burrows were designated at the end of the third quarter for an order from another customer, Q-Care Medical, Inc. ("Q-Care"). In October 1998, prior to the filing of the Company's Form 10-Q for the third quarter of 1998, Skooglund learned that the Burrows pumps were being used to fill the Q-Care order. Despite this knowledge, Holden and Skooglund never questioned the validity of the sale to Burrows and made no effort to restate the second quarter sales decreasing it by the amount recognized for the Burrows transaction.

38. In late June 1998, Beal directed his sales staff to obtain a 500-pump order from CoMedical, Inc. ("CoMedical"), a medical products distributor. CoMedical agreed to order pumps as long as it did not have to pay for the pumps until they were sold, and as long as

Sabratek agreed to fill orders that it received from its own customers with pumps from CoMedical's pump inventory. Beal agreed to these terms. On June 25, 1998, after receiving a written purchase order containing these terms, Sabratek shipped 500 pumps worth $927,500 to CoMedical. Despite this being a large transaction occurring at the end of the quarter, Holden and Skooglund deliberately or recklessly allowed this $927,500 transaction to be improperly reported as sales in the Company's Form 10-Q for the second quarter of 1998.

39. Although Sabratek recognized the CoMedical transaction as a sale in June 1998, CoMedical still had not paid for any of the pumps by the end of December 1998. In the second half of 1998, Skooglund learned from his staff that CoMedical understood that it was not required to pay for any pumps until they were resold. Skooglund asked Beal about CoMedical's statements regarding not having to pay for pumps until it resold them. Beal denied that Sabratek had agreed to any such terms. Despite this conflict between Beal and the accounting department staff, Skooglund did not even read the CoMedical purchase order to determine whether his staff's concerns were correct.

40. In March 1999, prior to the filing of the Company's 1998 Form 10-K, Holden and Skooglund received a "Top 40 Receivables" report, which ranked CoMedical as the sixth largest account. Holden and Skooglund deliberately or recklessly allowed $927,500 from the June 1998 CoMedical transaction to be improperly reported as part of the year-to-date sales in the Company's Form 10-Q for the third quarter of 1998 and its Form 10-K for the year 1998.

41. Padda and Beal knew or were reckless in not knowing that the Burrows and CoMedical transactions described in paragraphs 36 through 40 above were improperly reported as sales in the Company's Form 10-Q for the second quarter of 1998 and improperly included as

part of the year-to-date sales in the Company's Forms 10-Q for the third quarter of 1998 and its Form 10-K for the year 1998.

Third Quarter Of 1998 – Padda and Holden Masked Burrows Credit

42. The unraveling of the Burrows transaction in the third quarter put the Defendants under tremendous pressure to make up for the shortfall resulting from the $4.2 million credit given to Burrows and still meet projected sales growth. At the time, Padda and Holden were negotiating a large pump sale with Adventist Health System ("Adventist"), an end-user of pumps.

43. On September 30, 1998, the last day of the third quarter, Padda pressured Adventist to sign a term sheet which provided, among other things, that Q-Care, a wholly owned subsidiary of Adventist, commit to purchase $15 million in pumps and related supplies ("sets") from Sabratek. This term sheet contained significant seller's obligations. Q-Care had the option to exchange any of its $15 million in pumps and sets for any other Sabratek products at the same price. Sabratek also committed to buy back from Q-Care any unsold products at the end of 18 months. At Padda's suggestion, on October 2, 1998, Q-Care's President faxed a copy of a check for $10 million to Holden while additional details of the transaction were still being worked out.

44. Based on this faxed copy of a check, Skooglund recorded a $10 million cash receipt in the third quarter and reduced receivables by $10 million. The distortion created by reducing receivables at quarter-end impacted Sabratek's Consolidated Statement of Cash Flows for the third quarter of 1998. It indicated that Sabratek had used $2.8 million of cash for operations when Sabratek had, in fact, used $12.8 million. Sabratek's improper accounting for the $10 million facsimile check in the third quarter of 1998 enabled it to mask a material change – a material decrease - in its cash flows from operations. Furthermore, recording the fax copy as if it

were a real check allowed Sabratek to falsely tout its "strong cash collections" in summarizing third quarter results it its November 5, 1998 press release.

45. On October 23, 1998, after further negotiations with Adventist, Padda and Holden agreed to an addendum to the term sheet. This addendum provided that in the event that Q-Care had any unsold Sabratek product in its inventory after April 1, 2001, Sabratek was required to fill at least 10% of Sabratek's own orders with pumps from Q-Care's inventory and had to provide Q-Care with a 7% profit for these assigned sales.

46. Sabratek shipped approximately $8.17 million in pumps and sets to Q-Care in the third quarter of 1998 and approximately an additional $1.25 million in pumps and sets in the fourth quarter of 1998.

47. Prior to November 16, 1998, when Sabratek filed its third quarter Form 10-Q, Holden and Skooglund knew that: Sabratek had entered into an end-of-the-quarter transaction with Q-Care, a new customer; that the Q-Care transaction was the largest pump sale in Sabratek's history; and that Q-Care had faxed Holden a copy of a check for $10 million on October 2, 1998. Since Holden negotiated both the term sheet and the addendum, he knew the terms of the Q-Care sale. At no time, however, did Holden or Skooglund make any allowance for the future return of pumps by Q-Care or Sabratek's obligation to assign future sales to Q-Care. Instead, Holden, Skooglund deliberately or recklessly allowed approximately $8.2 million from the Q-Care transaction to be improperly reported as sales in Sabratek's 1998 third quarter Form 10-Q and approximately $9.4 million from that transaction to be improperly reported as sales in its 1998 Form 10-K.

48. In September 1998, while Holden and Padda were negotiating with Adventist and Q-Care, Beal entered into a written pricing agreement for future orders by a national pharmacy

distributor named PharMerica, Inc. ("PharMerica"). This pricing agreement allowed PharMerica to order up to 1,400 pumps at a specific price by December 15, 1998. The pricing agreement was not an order for any pumps. Nevertheless, Holden and Skooglund treated this agreement as if it were an actual order for 1,400 pumps. Sabratek shipped 1,400 pumps to AllPro, a third-party warehouse, which was falsely designated as "PCA Remote Warehouse" on the invoice. PharMerica did not authorize this shipment of pumps to AllPro and was not under any obligation to pay for them.

49. By early October 1998, before the third quarter Form 10-Q was filed, Skooglund learned about this "significant" transaction for pumps between Sabratek and PharMerica with "special" terms. Skooglund saw an initial draft of the pricing agreement with PharMerica, but never followed up to see the final terms of the agreement. Skooglund also knew that the pumps were being shipped to a warehouse instead of directly to PharMerica. Holden and Skooglund knew that there had been revenue recognition issues concerning a previous PharMerica transaction in December 1997. Nevertheless, Holden and Skooglund deliberately or recklessly allowed $2,513,000 from the purported PharMerica order to be improperly reported as sales in the Company's Form 10-Q for the third quarter of 1998.

50. In March 1999, prior to the filing of the 1998 Form 10-K, Holden, and Skooglund received a "Top 40 Receivables" report, which ranked PharMe-Distrib. Center as the fourth largest receivable. Holden and Skooglund deliberately or recklessly allowed $2,513,000 for this PharMerica transaction to be improperly reported as sales in the Company's 1998 Form 10-K.

51. Since at least 1997, Health Care Technology ("HCT"), a distributor of Sabratek pumps, had paid for pumps as it resold them to customers, as if they were consignment sales. At the end of September 1998, Beal arranged for HCT to order 250 pumps from Sabratek under

these same terms. There was no written agreement or purchase order. Based on past practice with Sabratek, HCT understood the terms to be that HCT did not have to pay for this order until HCT resold these pumps. HCT did not pay for any of these pumps in 1998. At the end of 1998, without Beal's knowledge, some of the Sabratek accounting staff under Skooglund's management tried to collect payment from HCT for this transaction. HCT told the accounting staff that HCT did not have to pay and that they should contact Beal. The accounting staff immediately reported this conversation with HCT to Skooglund, who in turn said he would talk to Beal. Soon afterward, Holden and Beal directed the Sabratek accounting staff not to collect from HCT.

52. Although the accounting staff also put HCT on credit-hold several times in late 1998, Padda and Holden quickly instructed the accounting staff to take HCT off this credit-hold without any explanation.

53. In March 1999, prior to the filing of the 1998 Form 10-K, Holden and Skooglund received a "Top 40 Receivables" report, which ranked HCT as the ninth largest receivable. Skooglund and Holden deliberately or recklessly allowed $403,750 for this HCT transaction to be improperly reported as sales in its 1998 third quarter Form 10-Q and 1998 Form 10-K.

54. Padda and Beal knew or were reckless in not knowing that the Q-Care, PharMerica and HCT transactions described in paragraphs 42 through 53 above were improperly reported as sales in the Company's Form 10-Q for the third quarter of 1998 and improperly included as part of the sales in the Company's Form 10-K for the year 1998.

Fourth Quarter Of 1998 – Defendants Tried To Make Up For Lost Flush Syringe Sales

55. In November 1998, the FDA forced Sabratek to cease distribution of its flush syringes, which accounted for 25% of Sabratek's sales. With the suspension of its flush syringe business, Sabratek was under still more pressure to record additional sales in order to meet its sales goals.

56. At the end of the fourth quarter, at Padda's direction, Beal arranged for Medical Sales Professionals ("MSP"), a medical products distributor located in Virginia with which Sabratek had never had any business dealings, to serve as a distributor of Sabratek pumps purportedly for an upcoming sale to a new customer named Aurora Health Systems ("Aurora"). At the end of December 1998, Beal entered into an agreement with MSP for 950 pumps worth $2,080,250. Under the agreement, MSP was not obligated to pay for pumps until they were resold and was not responsible for warehousing. MSP never paid for any of these pumps and never received any of them. Moreover, the sale to Aurora never materialized. At the end of 1998, Beal helped arrange shipment of 950 pumps to AllPro, a third-party warehouse that had no connection with either MSP or Aurora. AllPro was designated in Sabratek's sales system as "Aurora/Advocate." The pumps were parked at AllPro throughout 1999 and into 2000 with MSP labels on their containers. In March 1999, before Sabratek's 1998 Form 10-K was filed, Holden and Skooglund received a "Top 40 Receivables" report ranking MSP as the second largest receivable, with $2,080,250 still unpaid and representing 12.22% of all of Sabratek's receivables. Holden and Skooglund deliberately or recklessly allowed $2,080,250 from this large, year-end transaction with a new distributor to be improperly reported as sales in the Company's Form 10-K for 1998.

57. Padda and Beal knew or were reckless in not knowing that the MSP transaction described in paragraph 56 above was improperly reported as a sale in the Company's Form 10-K for the year 1998.

First Quarter Of 1999 – The Defendants Stuffed Distribution Channels And Recorded Fictitious Sales

58. By March 16, 1999, Sabratek was still approximately $10 million short of the sales projections Padda and Holden had made to analysts for the first quarter of 1999. This shortfall intensified the Defendants' efforts to secure additional sales. Through offering special terms and creating fictitious sales, on the last three days of the first quarter of 1999, Sabratek was able to ship $9.1 million in pumps. These end-of-quarter transactions represented 95% of all pumps shipped in the entire first quarter of 1999.

59. More than half of the end-of-the-quarter sales in March 1999 came from transactions with HCT for $2,841,500 and with Wren for $2,467,750. At the time, HCT had paid only $14,950 of the $403,750 owed on the September 1998 order alleged in paragraph 51 through 53 above. In soliciting the March 1999 order for 1,700 pumps worth $2,841,500, Padda told HCT that Sabratek had large national orders pending, and implied that Sabratek would fill those orders with pumps from HCT's inventory over the next several months. When HCT representatives said that their company did not have room for that many pumps, Padda offered to compensate HCT with free goods and to pay HCT's warehousing costs. At this time, HCT already had enough pumps in its inventory to meet its expected future sales for more than a year. As a further inducement, Beal told HCT representatives that HCT could exchange the newly ordered pumps for any other Sabratek products.

60. After HCT agreed to order the 1,700 pumps, they were shipped to a third-party warehouse in Quincy, Massachusetts, on March 31, 1999. HCT paid storage and insurance costs and deducted the amount of these costs when paying Sabratek's invoices for prior orders.

61. In late March 1999, at Padda's direction, Beal contacted Wren and said that Sabratek wanted an order of 1,470 pumps worth $2,467,750. In exchange, Beal offered Wren other products and accessories worth approximately $50,000, and discounts of 25% on pump supplies ("sets"). Beal also stated that there "was no real time frame on payment [on the pumps]." Beal offered Wren the ability, at any time, to exchange the pumps for flush syringes of equal value. At the time, Wren still owed Sabratek more than $300,000 from the March 1998 transaction alleged in paragraphs 29 through 32 above. Wren agreed to order the pumps and Sabratek shipped 1,470 pumps to Wren on March 29 and 30, 1999.

62. On or about March 25, 1999, at Padda's direction, Beal wrote letters to HCT and Wren confirming to each the quantity of pumps shipped and the offer to exchange pumps for flush syringes. At Padda's request, Beal sent Holden copies of these letters. In April 1999, prior to the filing of the first quarter Form 10-Q, Beal told Skooglund that Sabratek had taken orders with extended payment terms from Wren and HCT, and that the accounting department staff should not contact these distributors about their orders for six months. Skooglund did not ask Beal for any details about these transactions even though he knew that HCT and Wren still owed Sabratek for past invoices and had been put on credit hold by accounting. Prior to the filing of the first quarter Form 10-Q, Skooglund also knew that the HCT and Wren transactions were large and occurred in the last days of the quarter. Soon after talking to Beal, Skooglund provided Holden with sales information about Wren and HCT, including the timing and size of the transactions. Wren and HCT were ranked sixteenth and ninth, respectively, on the March 1999

"Top 40 Receivables" report distributed to Skooglund and Holden before the first quarter Form 10-Q was filed. Despite these "red flags," Holden and Skooglund deliberately or recklessly allowed $2,841,500 for the HCT transaction and $2,467,750 for the Wren transaction to be improperly reported as sales in the Company's Form 10-Q for the first quarter of 1999.

63. The arrangements with HCT and Wren met only half the $10 million in sales Sabratek needed to meet Padda and Holden's predictions for the first quarter of 1999. Sabratek's prospects for the remaining half were dashed when a large order from another potential customer fell through. The Defendants once again turned to MSP to make up the shortfall. MSP, however, refused to place any more orders with Sabratek. Nevertheless, on March 31, 1999, Sabratek shipped 1,290 pumps, valued at $2.8 million, to AllPro, a third-party warehouse, and invoiced MSP for the order. MSP did not know that the pumps had been shipped to AllPro and did not authorize the shipment. In April 1999, prior to the filing of the first quarter Form 10-Q, Beal told Skooglund that Sabratek had taken an order with extended payment terms from MSP, and that the accounting department should not contact MSP about the order for six months. Skooglund did not ask Beal for any details about this transaction even though he knew that MSP still owed the full amount on its December 1998 invoice of $2,080,250. Soon after talking to Beal, Skooglund provided Holden with sales information about MSP, including the timing and size of the transaction.

64. By early April 1999, Holden and Skooglund both knew the new MSP order was a large, end-of-quarter sale to a customer, which had never done business with Sabratek prior to December 1998, and which still owed over $2 million on a purported December 1998 pump order. Moreover, MSP was ranked second on the March 1999 "Top 40 Receivables" report distributed to Skooglund and Holden before the first quarter 1999 Form 10-Q was filed. Despite

this knowledge, however, Holden and Skooglund deliberately or recklessly allowed $2,841,500 from the March 1999 MSP transaction to be improperly reported as sales in the Company's Form 10-Q for the first quarter of 1999.

65. Also, at the end of the first quarter of 1999, Sabratek entered into a 300-pump transaction worth $628,500 with CoMedical to help meet the shortfall in sales. CoMedical agreed to make this order under the condition that it receive terms similar to its June 30, 1998 pump order. Beal agreed to the non-standard terms that CoMedical did not have to pay Sabratek for any pumps until it resold them and that Sabratek would help CoMedical sell the pumps to Sabratek customers. The 300 pumps were shipped to CoMedical on March 30, 1999. In April 1999, before the first quarter Form 10-Q was filed, Beal told Skooglund that Sabratek had taken an order with extended payment terms from CoMedical, and that the accounting department should not contact CoMedical about this order for six months. Skooglund did not ask Beal for any details about this transaction even though he knew, as alleged in paragraph 39 above, that CoMedical had rebuffed Sabratek's collection efforts in 1998, stating that it would pay for pumps as it resold them. At the time the 300 pumps were shipped to CoMedical, Skooglund also knew that CoMedical still owed approximately $927,500, the entire amount due on the June 30, 1998 pump order. Soon after talking to Beal, Skooglund communicated details of CoMedical's new order to Holden, including the timing and size of the transaction. CoMedical was ranked sixth on the March 1999 "Top 40 Receivables" report distributed to Skooglund and Holden before the first quarter Form 10-Q was filed. Despite these "red flags," Holden and Skooglund deliberately or recklessly allowed $628,500 from the new CoMedical transaction to be improperly reported as sales in the Company's Form 10-Q for the first quarter of 1999.

66. In late March 1999, Beal arranged for a sale of 150 pumps for $318,647 to Medical Marketing, Inc. ("Medical Marketing"), a medical products distributor, with extended payment terms of 90 days for pumps resold within 90 days of delivery and the promise that Sabratek's sales force would help sell the pumps if Medical Marketing was not able to sell a significant number of pumps within six months. Under these favorable terms, on March 31, 1999, Medical Marketing agreed to order pumps. Holden and Skooglund deliberately or recklessly allowed $318,647 from this Medical Marketing transaction to be improperly reported as sales in the Company's Form 10-Q for the first quarter of 1999.

67. Padda and Beal knew or were reckless in not knowing that the HCT, Wren, MSP and CoMedical transactions described in paragraphs 58 through 66 above were improperly reported as sales in the Company's Form 10-Q for the first quarter of 1999.

The Creation of Fraudulent Billings for Consulting Services

68. Throughout 1998 and the first quarter of 1999, the Defendants also inflated Sabratek's sales by billing Unitron Medical Communications, Inc. d/b/a Moon Communications ("Unitron") a total of $4.5 million for "consulting" services that Sabratek executives in fact largely never provided.

69. In or about early 1998, Holden entered into discussions with Unitron about furthering business opportunities between Sabratek and Unitron. These discussions resulted in Sabratek and Unitron entering into two agreements in March 1998: an exclusive marketing agreement under which Unitron agreed to market Sabratek products in exchange for a $2.7 million fee; and an agreement through which Sabratek would provide Unitron with consulting services. When Holden approached Unitron with these agreements, Unitron was in desperate need of money and Sabratek still owed Unitron $3 million from a prior commitment to fund Unitron's research and

development efforts. Sabratek was Unitron's sole source of working capital for the two-year period prior to Sabratek's acquisition of Unitron in July 1999. Since its inception, Unitron had insignificant revenue apart from Sabratek. Unitron officials believed that under the marketing and consulting agreements, Sabratek would fund Unitron's research and development.

70. Beginning in March 1998, at the end of each quarter, Padda and Holden set the amount that Sabratek would bill Unitron for consulting services ostensibly provided by Sabratek's executives. Holden then told Skooglund the amount to bill, and Skooglund invoiced Unitron for that amount. At Holden's direction, Skooglund simultaneously wired funds to Unitron, supposedly under the marketing agreement, for Unitron to use to pay Sabratek's invoice for the purported consulting services. Skooglund then contacted Unitron's accountant and told him that he was faxing an invoice for consulting services and wiring funds due Unitron under the marketing agreement. Skooglund then asked Unitron's accountant to wire the funds back to Sabratek, purportedly as payment for the consulting services. Sabratek billed Unitron, and wired the funds with which Unitron paid Sabratek's billings in the amounts of $650,000, $1,200,000, and $250,000 for the first, second, and third quarters of 1998, respectively.

71. For the fourth quarter of 1998, Holden and Padda set the amount billed Unitron for the consulting services at $600,000. Unlike the prior quarters, Skooglund did not wire funds back and forth between Sabratek and Unitron, and did not invoice Unitron for consulting services. Instead, Skooglund merely recorded the $600,000 as sales for the quarter. Because no funds were exchanged or invoices faxed, no one at Unitron even knew that Sabratek had "billed" Unitron $600,000 for the fourth quarter 1998. Unitron did not learn of the fourth quarter 1998 billing until Unitron was audited in mid-1999.

72. In all of 1998, Sabratek billed Unitron $2.7 million for consulting services, the exact amount that Sabratek owed Unitron under the marketing agreement. Holden and Skooglund deliberately or recklessly allowed the entire $2.7 million to be improperly reported as sales in the Company's 1998 Form 10-K. Padda knew or was reckless in not knowing that the $2.7 million was improperly reported as sales in the Company's 1998 Form 10-K.

73. Padda and Holden set the amount to bill Unitron for "consulting services and other expenses" related to Unitron in the first quarter of 1999 at $1.8 million. After Holden communicated this amount to Skooglund, Skooglund prepared a journal entry to improperly record $1 million of the amount billed as sales and $800,000 as an offset to selling, general, and administrative expenses. Without Unitron's authorization, instead of sending out an invoice, Skooglund merely added the $1.8 million to the balance Unitron owed Sabratek under a Standby Senior Credit Facility, which Sabratek and Unitron entered into in October 1998 and under which Sabratek could lend Unitron up to $10 million. Unitron learned of this $1.8 million "billing" for the first time in mid-1999. Holden and Padda knew or were reckless in not knowing that this $1.8 million was improperly recorded in the Company's Form 10-Q for the first quarter of 1998.

74. In mid-1999, in connection with their 1998 audit of Sabratek, Sabratek's auditor, KPMG Peat Marwick ("KPMG"), asked Skooglund for supporting documentation for the Unitron billings. Skooglund told the audit manager that Sabratek did not have any back-up for the billings, and explained that Holden and Unitron orally agreed to the amounts. However, when KPMG contacted Unitron, it denied agreeing to any amounts billed by Sabratek pursuant to the consulting agreement. KPMG then told Skooglund that he needed something in his file to support this invoicing. Skooglund, with Holden's input, then developed an after-the-fact

schedule purporting to list services performed in each of the five quarters from the first quarter of 1998 through the first quarter of 1999. Skooglund arbitrarily filled the schedule with amounts equal to the amounts that had been billed. Skooglund prepared at least two or three drafts of the schedule, which Holden reviewed and edited. Under this schedule, the hourly rates for services were on average $961, and ranged from a low of $852 per hour to more than $1,000 per hour.

75. There is no documentation to support the amounts Sabratek billed Unitron. Eight senior Sabratek executives, who purportedly provided 80% of the hours in Holden and Skooglund's after-the-fact schedules, could not come up with even 25% of the Unitron-related hours reported in the schedule. Further, the time spent by Sabratek's senior executives as Unitron-related was not, in several instances, for consulting services. Besides Holden and Padda, other Sabratek senior executives did not even know that Sabratek had billed Unitron for consulting services supposedly provided by them.

76. As a result of this fictitious billing for consulting services, from March 1998 through March 1999, Sabratek fabricated $4.5 million in non-existent sales.

Sabratek's False Press Releases, Filings, and MD&A Sections

77. During the period from January 1, 1998 through May 14, 1999, Sabratek periodically issued press releases announcing its financial results. Sabratek issued such press releases for the following periods on the following dates:

	Period	Date Issued
a.	Quarter ended 3/31/98	May 5, 1998
b.	Quarter ended 6/30/98	August 6, 1998
c.	Quarter ended 9/30/98	November 5, 1998
d.	Year ended 12/31/98	March 16, 1999
e.	Quarter ended 3/31/99	May 11, 1999

78. During the period from 1998 through May 14, 1999, Sabratek filed required periodic reports with the Commission pursuant to Section 13(a) of the Exchange Act. Sabratek filed these reports for the following periods on the following dates:

	Period	Form	Date Filed
a.	Quarter ended 3/31/98	10-Q	May 15, 1998
b.	Quarter ended 6/30/98	10-Q	August 13, 1998
c.	Quarter ended 9/30/98	10-Q	November 16, 1998
d.	Year ended 12/31/98	10-K	March 26, 1999
e.	Year ended 12/31/98 (Amended)	10-K/A	April 9, 1999
f.	Quarter ended 3/31/99	10-Q	May 14, 1999

79. As a result of the conduct alleged in paragraphs 16 through 76, Sabratek's 1998 and 1999 press releases and filings overstate the Company's sales and operating income as set forth below:

(in millions)	Net Sales Reported	Net Sales Actual	Operating Income (Loss) Reported	Operating Income (Loss) Actual
1st quarter 1998	$15.2	$10.5	$2.8	$0.2
2nd quarter 1998	$16.3	$10.0	$3.4	($0.7)
3rd quarter 1998	$18.8	$12.5	$3.9	$1.1
Year 1998	$66.9	$46.0	$8.6	($3.0)
1st quarter 1999	$13.6	$3.8	$1.7	($5.0)
Five Quarters	$80.5	$49.8	$10.3	($8.0)

80. Sabratek's misleading sales and operating income information was repeated in the Management's Discussion and Analysis ("MD&A") section of Sabratek's 1998 Forms 10-Q and 10-K, and 1999 first quarter Form 10-Q. Padda and Holden prepared, reviewed, or approved the contents of the MD&A section in the 1998 Forms 10-Q and 10-K, and the 1999 first quarter

Form 10-Q. Holden, Skooglund, and Padda all signed at least one of Sabratek's Commission filings: Padda and Skooglund signed all three of the 1998 Forms 10-Q, the 1998 Form 10-K, and the Form 10-Q for the first quarter of 1999, and Holden signed all these filings except for the Form 10-Q for the third quarter of 1998.

81. The overstated sales and operating income figures were also trumpeted in Sabratek's 1998 and 1999 press releases. In each of those press releases, Sabratek compared its sales and operating income to the same period in the prior year. Padda and Holden were primarily responsible for preparing or reviewing press releases before they were distributed to the press. Until he became President in July 1998, Holden drafted the quarterly press releases for 1998 containing Sabratek's financial results, which were reviewed and approved by Padda. After July 1998, even where these press releases were initially prepared by others, Padda and Holden reviewed them and approved their distribution to the public.

82. Market analysts reacted favorably to Sabratek's positive financial news. In May and August 1998 reports, Wheat First Union recommended Sabratek as a "BUY" based on its strong "in-line" financial results in the first and second quarters of 1998. Wheat noted that Sabratek had met or exceeded its expectations every quarter. Sabratek would not have met this analyst's expectations if it had disclosed its actual sales and operating income. In November 1998, Credit Suisse issued a report titled Sabratek Pumps Out Another Positive Surprise; Price Target Raised, in which the firm reiterated its "BUY" recommendation and raised its price target for Sabratek stock from $35 to $40 per share. Credit Suisse made this recommendation after Sabratek reported third quarter 1998 net sales of $18.8 million, a 60% increase over the $11.8 million in the third quarter of 1997. If actual sales of $12.5 million for the third quarter had been compared with 1997 third quarter sales, Sabratek could have shown only a 6% increase.

83. For the first quarter of 1998, neither Sabratek's press release nor the MD&A section of its Form 10-Q disclosed that reported sales were achieved through special inducements and concessions. Sales of $3.9 million, or 45.3% of all pump sales in the quarter, were made with terms that extended the payment period and gave customers the right to return merchandise.

84. Padda stated in a press release related to the second quarter of 1998: "The Company posted another record financial quarter while both expanding the markets we serve and continue (sic) to build upon our existing customer base." Neither the press release nor the MD&A section of the Company's second quarter Form 10-Q disclosed that the record sales touted by Padda were achieved primarily through three transactions: the Burrows and CoMedical pump sales, which represented 59.3% of all pump sales made in the second quarter, and $1.2 million in fraudulent Unitron billings. Without these transactions, the increase in Sabratek's comparable quarter net sales was only 2%, significantly less than the 66% touted by Sabratek. The failure to identify and quantify the purported sales to Burrows and CoMedical, with significant right-of-return provisions, as a significant factor in reported sales growth was a material omission of facts necessary to understand Sabratek's reported net sales and results of operations.

85. In its 1998 second quarter MD&A, Sabratek attributed the increase in sales to a number of factors, including "additional sales of the MediVIEW products, and the sale of licensed products from GDS Technology, Inc." There was no discussion of the Unitron billings, even though the fees Sabratek charged Unitron exceeded sales from its MediVIEW products and sales of GDS Technology, as well as several main line products. The failure to identify and quantify the Unitron billings as a significant factor in explaining the change in sales was a material omission of facts necessary to understand Sabratek's reported net sales and results of operations.

86. In its 1998 third quarter press release, Padda again touted the Company's record financial results. But the earnings trend touted was due largely to the Defendants' fraudulent, undisclosed activities. A significant part of the third quarter results came from three "sales" to Q-Care, PharMerica, and HCT, representing 69.3% of all pumps sales for the quarter, and $250,000 in fraudulent Unitron billings. There was no disclosure in Sabratek's third quarter MD&A or press release that Sabratek was only able to achieve it purported sales growth for the quarter by arranging "sales" with Q-Care and HCT that were contingent on right-of-return provisions or other obligations, by treating a pricing agreement with PharMerica as a sale, and by including the fictitious $250,000 billing to Unitron in sales.

87. Sabratek's year-end press release and MD&A section in the 1998 Form 10-K did not disclose that more than half of all the pump sales reported for 1998 did not meet the recognition requirements of GAAP sales and that the non-GAAP sales and fraudulent Unitron billings materially distorted the Company's reported financial results. Without these transactions, Sabratek's net sales for fiscal year 1998 had increased a modest 6.7%, significantly less than the 55% increase Sabratek reported.

88. For the first quarter of 1999, neither Sabratek's press release nor the MD&A section of its Form 10-Q disclosed the Company's channel stuffing activities, which reached an unprecedented $8.8 million, or 92.6% of all pumps sold in the first quarter 1999. The Defendants generated these sales by creating fictitious sales with MSP, and offering right-of-return provisions and other contingencies to HCT, Wren, and Medical Marketing. Sabratek's undisclosed channel stuffing and $1.8 million in fraudulent Unitron billings materially impacted reported financial results. Without these fraudulent transactions, Sabratek's net sales for the quarter were only $3.8 million, a decline of 72% from first quarter 1998. Sabratek's pre-tax net

loss without the fraudulent transactions was approximately $5 million, a decline of more than 278% from the first quarter of 1998.

89. On August 13, 1999, Sabratek announced that its 1999 second quarter earnings would be significantly below Wall Street estimates and that the release of earnings information would be delayed pending completion of a review by KPMG. On August 23, 1999, Sabratek missed an extended Commission deadline for filing its Form 10-Q for the second quarter of 1999. On October 7, 1999, Sabratek announced that it would further delay the filing of its 1999 second quarter Form 10-Q and on November 3, 1999, due to its inability to file, Sabratek stock was delisted by Nasdaq. As a result of these announcements, Sabratek's market capitalization declined by $202.5 million, or 98%, from July 30, 1999 until it was delisted on November 3, 1999.

Defendants' Misrepresentations To Auditors

90. Padda and Skooglund signed representation letters in connection with the 1998 audit and three 1998 quarterly reviews of Sabratek, which represented to KPMG that there were no side agreements with customers that allowed for the return of merchandise and that material transactions were properly recorded in the accounting records underlying the financial information.

91. When questioned orally by Sabratek's auditors during the 1998 audit of Sabratek, Holden and Skooglund lied by falsely telling Sabratek's auditors that Sabratek had not entered into any side agreements with customers and that the only material sales terms were those contained in Sabratek's standard distributor agreements.

92. Holden and Skooglund did not provide auditors with any of the purchase orders or sales agreements that Sabratek had received in 1998 that contained right-of-return or

consignment provisions or other contingent terms. Holden did not provide the auditors with the provisions contained in the Q-Care term sheet and addendum.

93. Holden and Skooglund did not inform the auditors about the terms of the Burrows transaction and that a credit had been issued to Burrows when the promised sale to Tenet failed to materialize.

94. Holden and Skooglund failed to inform the auditors that the billings to Unitron each quarter were not based on any hours actually performed by Sabratek executives, and that the after-the-fact schedules created by Holden and Skooglund were not based on any actual hours worked.

COUNT I

Violations of Section 10(b) of the Exchange Act [15 U.S.C. §78j(b)] and Rule 10b-5 [17 C.F.R. §240.10b-5] promulgated thereunder

95. Plaintiff repeats and realleges paragraphs 1 through 94 above.

96. Defendants Holden, Skooglund, Padda and Beal, and through them, Sabratek, engaged in the conduct alleged in paragraph 95 with knowledge of or reckless disregard for the truth.

97. As a result of the activities described in paragraphs 95 and 96 above, Defendants Holden, Skooglund, Padda and Beal, and through them, Sabratek, in connection with the purchase or sale of securities, by the use of means or instrumentalities of interstate commerce or of the mails, directly or indirectly: (a) employed devices, schemes or artifices to defraud; (b) made untrue statements of material facts or omitted to state material facts necessary in order to make the statements made, in the light of the circumstances under which they were made, not misleading; or (c) engaged in acts, practices or courses of business which operated or would operate as a fraud or

deceit upon purchasers of securities in violation of Section 10(b) of the Exchange Act [15 U.S.C. §78j(b)] and Rule 10b-5 [17 C.F.R. §240.10b-5] thereunder.

98. As a result of the activities described in paragraphs 95 through 97 above, Defendant Holden, as a control person under Section 20(a) of the Exchange Act [17 U.S.C. §78t(a)], is liable for violations by Sabratek, Skooglund, and Beal, of Section 10(b) of the Exchange Act [15 U.S.C. §78j(b)], and Rule 10b-5 [17 C.F.R. §240.10b-5] promulgated thereunder.

COUNT II

Violations of Section 13(a) of the Exchange Act [15 U.S.C. § 78t(a)] and Rules 12b-20, 13a-1 and 13a-13 [17 C.F.R. §§ 240.12b-20, 240.13a-1, and 240.13a-13] Promulgated Thereunder

99. Plaintiff repeats and realleges paragraphs 1 through 94 and incorporates them by reference as if set forth fully herein.

100. The financial statements Sabratek filed with the Commission in its Forms 10-Q and 10-K for 1998 and its Form 10-Q for the first quarter of 1999 were not prepared in accordance with GAAP.

101. Sabratek, through Defendants Holden, Skooglund, Padda, and Beal, directly and indirectly, filed with the Commission an annual report on Form 10-K for the year ending December 31, 1998 and quarterly reports on Form 10-Q for the first three quarters of 1998 and the first quarter of 1999 that were not in accordance with such rules and regulations that the Commission has prescribed as necessary and appropriate in the public interest and for the protection of investors, and also failed to include in those reports such further material information, as way necessary to make the required statements, in light of the circumstances under which they were made, not misleading.

102. By reason of the activities alleged in paragraphs 99 through 101 above, Defendants Holden, Skooglund, Padda, and Beal aided and abetted violations by Sabratek of Section 13(a) of the Exchange Act [15 U.S.C. § 78m(a)] and Rules 12b-20, 13a-1, and 13a-13 [17 C.F.R. 240.12b-20, 240.13a-1, and 240,13a-13] promulgated thereunder.

103. As a result of the activities described in paragraphs 99 through 102 above, Defendant Holden, as a control person under Section 20(a) of the Exchange Act [15 U.S.C § 78t(a)], is liable for Sabratek's violations of Section 13(a) of the Exchange Act [15 U.S.C. § 78m(a)] and Rules 12b-20, 13a-1, and 13a-13 [17 C.F.R. 240.12b-20, 240.13a-1, and 240,13a-13] promulgated thereunder.

COUNT III

Violations of Section 13(b)(2)(A) and 13(b)(2)(B) of the Exchange Act [15 U.S.C. §§ 78m(b)(2)(A) and 78m(b)(2)(B)]

104. Plaintiff realleges paragraphs 1 through 94 and incorporates them by reference as if set forth fully herein.

105. Beginning in at least 1998 and through at least March 1999, Sabratek, aided and abetted by Defendants Holden, Skooglund, Padda and Beal, directly and indirectly, failed to make and keep books, records, and accounts, which in reasonable detail accurately and fairly reflected the transactions and disposition of the assets of Sabratek.

106. Beginning in at least 1998 and through at least March 1999, Sabratek, aided and abetted by Defendants Holden, Skooglund and Padda, directly and indirectly, failed to devise and maintain a system of internal accounting controls sufficient to provide reasonable assurances that transactions were recorded as necessary to permit preparation of financial statements in

conformity with generally accepted accounting principles or any other criteria applicable to such statements

107. By reasons of the activities alleged in paragraphs 104 through 106 above, Defendants Holden, Skooglund, Padda, and Beal aided and abetted violations by Sabratek of Section 13(b)(2)(A) and Holden, Skooglund and Padda added and abetted violations by Sabratek of Section 13(b)(2)(B) of the Exchange Act [15 U.S.C. §§ 78m(b)(2)(A) and 78m(b)(2)(B)].

108. As a result of the activities described in paragraphs 104 through 107 above, Defendant Holden, as a control person under Section 20(a) of the Exchange Act [15 U.S.C. §78t(a)], is liable for Sabratek's violations of Sections 13(b)(2)(A) and 13(b)(2)(B) of the Exchange Act [15 U.S.C. §§ 78m(b)(2)(A) and 78m(b)(2)(B)].

COUNT IV

Violations of Exchange Act Rule 13b2-1

109. Plaintiff realleges paragraphs 1 through 94 and incorporates them by reference as if set forth fully herein.

110. Beginning in at least 1998 and through at least March 1999, Defendants Holden, Skooglund, Padda, and Beal, directly and indirectly, falsified or caused to be falsified books, records, and accounts subject to Section 13(b)(2)(A) of the Exchange Act [15 U.S.C. §§78m(b)(2)(A)].

111. By reason of the activities alleged in paragraphs 109 and 110 above, Defendants Holden, Skooglund, Padda, and Beal violated Rule 13b2-1 [17 C.F.R. 240.13b-2-1] promulgated under Section 13(b)(2) of the Exchange Act [15 U.S.C. §§ 78m(b)(2)].

112. As a result of the activities described in paragraphs 109 through 111 above, Defendant Holden, as a control person under Section 20(a) of the Exchange Act [15 U.S.C. §78t(a)], is liable for Skooglund and Beal's violations of Rule 13b2-1 [17 C.F.R. 240.13b-2-1] promulgated under Section 13(b)(2) of the Exchange Act [15 U.S.C. §§ 78 m(b)(2)].

COUNT V

Violation of Exchange Act Rule 13b2-2

113. Plaintiff realleges paragraphs 1 through 94 and incorporates them by reference as if set forth fully herein.

114. Beginning in at least 1998 and through at least March 1999, Defendants Holden, Skooglund and Padda, directly and indirectly, made or caused to be made materially false and misleading statements, or omitted to state or caused another person to omit to state, material facts necessary in order to make statements made, in light of the circumstances under which such statements were made, not misleading to an accountant in connection with an audit and examination of the financial statements of Sabratek or the preparation and filing of a document or report required to be filed with the Commission.

115. By reason of the activities alleged in paragraphs 113 and 114 above, Defendants Holden, Skooglund, and Padda violated Rule 13b2-2 [17 C.F.R. 240.13b2-2] promulgated under Section 13(b)(2) of the Exchange Act [15 U.S.C. §78m(b)(2)].

116. As a result of the activities described in paragraphs 113 through 115 above, Defendant Holden, as a control person under Section 20(a) of the Exchange Act [15 U.S.C. §78t(a)], is liable for Skooglund's violations of Rule 13b2-2 [17 C.F.R. 240.13b-2-2] promulgated under Section 13(b)(2) of the Exchange Act [15 U.S.C. §§78m(b)(2)].

COUNT VI

Violations of Section 13(b)(5) of the Exchange Act

117. Plaintiff realleges paragraphs 1 through 94 and incorporates them by reference as if set forth fully herein.

118. Beginning in at least 1998 and through at least March 1999, Defendants Holden, Padda, and Beal knowingly circumvented and knowingly failed to implement a system of internal accounting controls and knowingly falsified books, records, and accounts described in Section 13(b)(2) of the Exchange Act [15 U.S.C. § 78 m(b)(2)]

119. By reason of the activities described in paragraphs 117 and 118 above, Defendants Holden, Padda, and Beal violated Section 13(b)(5) of the Exchange Act [15 U.S.C. § 78 m(b)(5)].

120. As a result of the activities described in paragraphs 117 through 119 above, Defendant Holden, as a control person under Section 20(a) of the Exchange Act [15 U.S.C. §78t(a)], is liable for Beal's violations of Section 13(b)(5) of the Exchange Act [15 U.S.C. §§78m(b)(5)].

PRAYER FOR RELIEF

WHEREFORE, the Commission requests that the Court:

I.

Issue findings of fact and conclusion of law that the Defendants committed the violations charged and alleged herein.

II.

Issue an Order of Permanent Injunction, in a form consistent with Rule 65(d) of the Federal Rules of Civil Procedure, permanently restraining and enjoining Defendant Holden, his officers, 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 acts, practices of course of business alleged above, or in conduct of similar purport and object, in violation of, or that aid and abet violations of, Sections 10(b), 13(a), 13(b)(2)(A), 13(b)(2)(B) and 13(b)(5) of the Exchange Act [15 U.S.C. §§ 78j(b), 78m(a), 78m(b)(2)(A), 78m(b)(2)(B) and 78m(b)(5)], Rules 10b-5, 12b-20, 13a-1, 13a-13, 13b2-1 and 13b2-2 [17 C.F.R. 240.10b-5, 240.12b-20, 240.13a-1, 240.13a-13, 240.13b2-1 and 240.13b2-2] promulgated thereunder.

III.

Issue an Order of Permanent Injunction, in a form consistent with Rule 65(d) of the Federal Rules of Civil Procedure, permanently restraining and enjoining Defendant Skooglund, his officers, 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 acts, practices of course of business alleged above, or in conduct of similar purport and object, in violation of, or that aid and abet violations of, Sections 10(b), 13(a), 13(b)(2)(A) and 13(b)(2)(B) of the Exchange Act [15 U.S.C. §§ 78j(b), 78m(a), 78m(b)(2)(A) and 78m(b)(2)(B)], Rules 10b-5, 12b-20, 13a-1, 13a-13, 13b2-1 and 13b2-2 [17 C.F.R. 240.10b-5, 240.12b-20, 240.13a-1, 240.13a-13, 240.13b2-1 and 240.13b2-2] promulgated thereunder.

IV.

Issue an Order of Permanent Injunction, in a form consistent with Rule 65(d) of the Federal Rules of Civil Procedure, permanently restraining and enjoining Defendant Padda, his officers, 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 acts, practices of course of business alleged above, or in conduct of similar purport and object, in violation of, or that aid and abet violations of, Sections 10(b), 13(a), 13(b)(2)(A), 13(b)(2)(B) and 13(b)(5) of the Exchange Act [15 U.S.C. §§ 78j(b), 78m(a), 78m(b)(2)(A), 78m(b)(2)(B) and 78m(b)(5)], Rules 10b-5, 12b-20, 13a-1, and 13a-13, 13b2-1 and 13b2-2 [17 C.F.R. 240.10b-5, 240.12b-20, 240.13a-1, 240.13a-13, 240.13b2-1 and 240.13b2-2] promulgated thereunder.

V.

Issue an Order of Permanent Injunction, in a form consistent with Rule 65(d) of the Federal Rules of Civil Procedure, permanently restraining and enjoining Defendant Beal, his officers, 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 acts, practices of course of business alleged above, or in conduct of similar purport and object, in violation of, or that aid and abet violations of, Sections 10(b), 13(a), 13(b)(2)(A) and 13(b)(5) of the Exchange Act [15 U.S.C. §§ 78j(b), 78m(a), 78m(b)(2)(A) and 78m(b)(5)], Rules 10b-5, 12b-20, 13a-1, and 13a-13 and 13b2-1 [17 C.F.R. 240.10b-5, 240.12b-20, 240.13a-1, 240.13a-13 and 240.13b2-1] promulgated thereunder.

VI.

Issue an Order pursuant to Section 21(d)(2) of the Exchange Act [15 U.S.C. § 78u(d)(2)] prohibiting Defendant Holden, permanently and unconditionally, from acting as an officer or director of any issuer that has a class of securities registered pursuant to Section 12 of the Exchange Act [15 U.S.C. § 78l] or that is required to file reports pursuant to Section 15(d) of the Exchange Act [15 U.S.C. § 78o(d)]

VII.

Issue an Order requiring Defendants Holden, Skooglund, and Beal to disgorge the ill-gotten gains that they received as a result of their wrongful conduct, plus prejudgment interest thereon.

VIII.

With regard to the Defendants' violative acts, practices and courses of business set forth herein, issue an Order imposing upon them appropriate civil penalties pursuant to Section 21(d)(3) of the Exchange Act [15 U.S.C. § 78u(d)(3)].

IX.

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.

X.

Grant Orders for such further relief as the court may deem appropriate.

Respectfully Submitted,

John E. Birkenheier
James A. Davidson
Pravin B. Rao

SECURITIES AND EXCHANGE COMMISSION
500 W. Madison Street, Suite 1400
Chicago, Illinois 60661
Telephone: (312) 353-7390

Dated: September 27, 2001

UNITED STATES DISTRICT COURT
NORTHERN DISTRICT OF ILLINOIS

Civil Cover Sheet

Cat 3

This automated JS-44 conforms generally to the manual JS-44 approved by the Judicial Conference of the United States in September 1974. The data is required for the use of the Clerk of Court for the purpose of initiating the civil docket sheet. The information contained herein neither replaces nor supplements the filing and service of pleadings or other papers as required by law. This form is authorized for use only in the Northern District of Illinois.

Plaintiff(s): **U.S. Securities and Exchange Commission**

County of Residence: Cook

Plaintiff's Atty: John E. Birkenheier
U.S. Securities and Exchange Commission
500 West Madison Street,
Suite 1400
(312) 353-7390

Defendant(s):**Stephen L. Holden, Scott P. Skooglund, Kuldarshan S. Padda, Stephen C. Beal**

County of Residence: Lake

Defendant's Atty:
See Attachment

01C 7463

JUDGE NORDBERG

MAGISTRATE JUDGE DENLOW

DOCKETED
SEP 27 2001

II. Basis of Jurisdiction: **1. U.S. Gov't Plaintiff**

III. Citizenship of Principle Parties **(Diversity Cases Only)**
Plaintiff:- **N/A**
Defendant:- **N/A**

IV. Origin : **1. Original Proceeding**

V. Nature of Suit: **850 Securities / Commodities / Exchange**

VI.Cause of Action: **Defendants violated and aided and abetted violations of antifraud, reporting, internal controls and recordkeeping provisions of the Securities and Exchange Act of 1934 (15 U.S.C. 78j(b), 78m(a), 78m(b)(2)(A), 78m(b)(2)(B), 78m(b)(5).**

VII. Requested in Complaint
Class Action: **No**
Dollar Demand:
Jury Demand: **No**

VIII. This case **IS NOT** a refiling of a previously dismissed case.

FILED-EDS
01 SEP 27 AM 11: 39
CLERK
U.S. DISTRICT COURT

Signature: John E. Birkenheier

Date: September 27, 2001

If any of this information is incorrect, please go back to the Civil Cover Sheet Input form using the *Back* button in your browser and change it. Once correct, print this form, sign and date it and submit it with your new civil action. **Note: You may need to adjust the font size in your browser display to make the form print properly.** **Revised: 06/28/00**

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UNITED STATES DISTRICT COURT
NORTHERN DISTRICT OF ILLINOIS

Eastern Division

In the Matter of

Securities and Exchange Commission

v.

Stephen L. Holden, et al.

01C 7463

Case Number: JUDGE NORDBERG

MAGISTRATE JUDGE DENLOW

APPEARANCES ARE HEREBY FILED BY THE UNDERSIGNED AS ATTORNEY(S) FOR:

Plaintiff

(A)	(B)
SIGNATURE	SIGNATURE
NAME: John E. Birkenheier	NAME
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IDENTIFICATION NUMBER (SEE ITEM 4 ON REVERSE): IL 6270993	IDENTIFICATION NUMBER (SEE ITEM 4 ON REVERSE)
MEMBER OF TRIAL BAR? YES ☑ NO ☐	MEMBER OF TRIAL BAR? YES ☐ NO ☐
TRIAL ATTORNEY? YES ☑ NO ☐	TRIAL ATTORNEY? YES ☐ NO ☐
	DESIGNATED AS LOCAL COUNSEL? YES ☐ NO ☐

(C)	(D)
SIGNATURE	SIGNATURE
NAME	NAME
FIRM	FIRM
STREET ADDRESS	STREET ADDRESS
CITY/STATE/ZIP	CITY/STATE/ZIP
TELEPHONE NUMBER	TELEPHONE NUMBER
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TRIAL ATTORNEY? YES ☐ NO ☐	TRIAL ATTORNEY? YES ☐ NO ☐
DESIGNATED AS LOCAL COUNSEL? YES ☐ NO ☐	DESIGNATED AS LOCAL COUNSEL? YES ☐ NO ☐

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