

UNITED STATES DISTRICT COURT
SOUTHERN DISTRICT OF NEW YORK

SECURITIES AND EXCHANGE COMMISSION,

Plaintiff,

-against-

FERNANDO J. ESPUELAS, JACK C. CHEN,
STEVEN J. HELLER, PETER R. MORALES,
WALTHER MÖLLER, BETSY D. SCOLNIK,
ADRIANA J. KAMPFNER, and PETER E. BLACKER,

Defendants.

Civil No. 06 Civ 2435(RJH)

AMENDED COMPLAINT
(Securities Fraud)

Plaintiff Securities and Exchange Commission (“Commission”), for its complaint against Fernando J. Espuelas (“Espuelas”), Jack C. Chen (“Chen”), Steven J. Heller (“Heller”), Peter R. Morales (“Morales”), Walther Möller (“Möller”), Betsy D. Scolnik (“Scolnik”), Adriana J. Kampfner (“Kampfner”), and Peter E. Blacker (“Blacker”), alleges as follows:

SUMMARY OF ALLEGATIONS

1. This is a financial fraud case involving improper recognition of Internet services revenue by StarMedia Network, Inc. (“StarMedia”), a former New York City-based Internet portal. During 2000 and the first two quarters of 2001, the defendants utilized three types of transactions to inflate StarMedia’s revenue by over \$18 million, in order to meet the company’s revenue projections and secure additional financing for its operations. As a result of the defendants’ fraudulent acts and accounting practices, StarMedia improperly recognized revenue

from certain barter transactions, certain round trip transactions, and certain sales transactions that had undisclosed contingencies or side agreements. As a result of the defendants' conduct, StarMedia filed false and misleading disclosures and financial statements with the Commission and provided false statements to analysts and shareholders. In addition, the company used inflated revenue amounts to persuade corporate investors to purchase \$35 million in convertible preferred shares.

2. Defendants were senior StarMedia executives who planned the fraud or played important roles in its implementation. The defendants include StarMedia's Chief Executive Officer and Chairman at the time, Fernando J. Espuelas; the company's President at the time, Jack C. Chen; the company's Chief Financial Officer, Steven J. Heller; its Senior Vice President for Strategic Development, Betsy D. Scolnik; and its Senior Vice President of Global Sales and the President of StarMedia de Mexico, Adriana J. Kampfner. The remaining defendants are Walther Möller, the President of the company's AdNet S.A. de C.V. ("AdNet") subsidiary, and two other senior StarMedia managers, Peter R. Morales and Peter E. Blacker.

3. In November 2001, the company announced that it would restate its financial statements and examine its revenue recognition practices. Initially, the announced restatement involved transactions at two subsidiaries, AdNet and StarMedia de Mexico, that had generated over \$14 million in improperly recognized revenues. First, during 2000 and 2001, AdNet engaged in a number of so-called "base book" transactions with its former owners, Harry Möller Publicidad, S.A. de C.V. ("HMP") and Grupo MVS, S.A. de C.V. ("MVS"). In these transactions, AdNet immediately recognized as revenue the entire stated value of Internet advertising purchased from it by clients of HMP and MVS, but deferred the recognition of an equal amount of expenses related to

production services that AdNet was contractually obligated to purchase, in exchange, from HMP and MVS. After investigating these base book transactions, StarMedia restated them as barter transactions, in conformity with U.S. generally accepted accounting principles (“GAAP”). In restating the accounting treatment for those transactions, StarMedia considered the transactions as advertising for advertising barter, and it determined the appropriate revenue recognition pursuant to the authoritative guidance set forth in Emerging Issues Task Force Issue No. 99-17 (“EITF 99-17”). As a result, StarMedia wrote off approximately ninety percent of the amount it had previously recorded as revenue.

4. StarMedia also engaged in so-called “incremental revenue” transactions. These were round trip transactions whereby StarMedia improperly recognized revenue from purchases by MVS and HMP of ad space at StarMedia de Mexico and AdNet, purportedly through or on behalf of MVS’s or HMP’s clients. MVS and HMP purchased the ad space in exchange for StarMedia’s promise to provide them with funds in an amount equal to the advertising purchases. After investigating these incremental revenue transactions, StarMedia determined the transactions did not have economic substance and wrote off the entire amounts previously reported as revenue.

5. Subsequently, after StarMedia had conducted an internal investigation, the company determined that it had also improperly recognized revenue based on sales that were contingent, having been altered by oral or written side agreements. After investigating these sales, the company wrote off almost the entire amount of the revenue from these transactions in its restatement of its financial statements.

6. While they were taking part in a fraud designed to artificially inflate StarMedia’s reported revenue, and thereby prop up its stock price, Espuelas, Chen, Heller, and Kampfner each

used for his or her personal financial gain StarMedia common stock that had been inflated as a result of the fraud. Each of them pledged StarMedia shares as collateral for loans in margin accounts at his or her respective broker. When the price of StarMedia stock declined, they each negotiated and received lines of credit from the company in order to provide additional collateral to the brokerages. Each of them used inflated StarMedia stock as collateral for the lines of credit.

7. As part of the defendants' fraudulent acts and practices, StarMedia filed an annual Report on Form 10-K for its fiscal year 2000 and quarterly Reports on Form 10-Q for its quarters ended March 31 and June 30, 2001. These filings contained false disclosures and financial statements that materially overstated the amount and quality of the company's revenue. In addition, the company issued false and misleading press releases and other statements to the public from the second quarter of 2000 through the time of the company's announcement of its restatements in November 2001.

8. Defendant Chen sold 715,000 shares of StarMedia common stock after the company issued false financial statements and other statements and prior to its November 2001 announcement that it would restate its financial statements. At the time that he sold his StarMedia stock, Chen knew that StarMedia's filings with the Commission and statements to the public contained materially misleading information. He obtained this material, nonpublic information as an officer and director of the company. As a result of his use of the nonpublic information, Chen avoided losses of at least \$150,438, through sales of his fraudulently inflated StarMedia stock.

9. By virtue of the foregoing conduct, each of the defendants, directly or indirectly, individually or in concert, has engaged in acts, practices, and courses of business that constitute

violations, or give rise to liability for violations, of the federal securities laws and the rules and regulations thereunder.

10. Unless the defendants are permanently restrained and enjoined, they will again engage in the acts, practices, transactions, and courses of business set forth in this complaint and in acts, practices, transactions, and courses of business of similar type and object.

JURISDICTION AND VENUE

11. The Commission brings this action pursuant to Section 20(b) and (d) of the Securities Act of 1933 ("Securities Act") [15 U.S.C. § 77t(b) and (d)] and Section 21(d) of the Securities Exchange Act of 1934 ("Exchange Act") [15 U.S.C. § 78u(d)].

12. This Court has jurisdiction over this action pursuant to Section 22(a) of the Securities Act [15 U.S.C. § 77v(a)] and pursuant to Sections 21(e) and 27 of the Exchange Act [15 U.S.C. §§ 78u(e) and 78aa].

13. The defendants have made use of the means or instrumentalities of interstate commerce, or of the mails, or the facilities of a national securities exchange in connection with the transactions, acts, practices, and courses of business alleged in this complaint.

14. Certain of the acts, practices, and courses of conduct constituting the violations of law alleged in this complaint occurred within this judicial district, and, therefore, venue is proper pursuant to Section 22 of the Securities Act [15 U.S.C. § 77u] and Section 27 of the Exchange Act [15 U.S.C. § 78aa].

15. The defendants, directly and indirectly, engaged in, and unless restrained and enjoined by this Court will continue to engage in, transactions, acts, practices, and courses of business that violate one or more of: Section 17(a) of the Securities Act [15 U.S.C. § 77q(a)];

Section 10(b) of the Exchange Act [15 U.S.C. § 78j(b)]; and Rules 10b-5, 13b2-1, and 13b2-2 thereunder [17 C.F.R. §§ 240.10b-5, 240.13b2-1, and 240.13b2-2]; and aid and abet violations of one or more of: 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 12b-20, 13a-1, and 13a-13 thereunder [17 C.F.R. §§ 240.12b-20, 240.13a-1, and 240.13a-13].

DEFENDANTS

16. Fernando J. Espuelas, age 42, is a resident of North Salem, New York. Espuelas founded StarMedia in 1996 and was the company's Chief Executive Officer from March 1996 through August 2001 and its Chairman from March 1996 through November 2001. As Chief Executive Officer, Espuelas managed all corporate functions of StarMedia, including its accounting practices. Espuelas was StarMedia's principal spokesperson on matters concerning the company's financial performance. As a member of StarMedia's Board of Directors, he approved StarMedia's filings with the Commission. As Chief Executive Officer of StarMedia, Espuelas signed StarMedia's annual Reports on Form 10-K.

17. Jack C. Chen, age 42, is a resident of Hanover, New Hampshire. Chen co-founded StarMedia with Espuelas in 1996. He was StarMedia's President from April 1996 through May 2001, served on its Board of Directors from April 1996 to August 2001, and was the Vice Chairman of the Board from June through August 2001. As President, Chen managed the day-to-day affairs of the company. As a member of StarMedia's Board of Directors, he signed or approved StarMedia's filings with the Commission, including the company's annual Reports on Form 10-K. Chen received an undergraduate degree and an MBA from Harvard University.

18. Steven J. Heller, age 43, is domiciled in Natick, Massachusetts. Heller was a Senior Vice President and the Chief Financial Officer of StarMedia from May 1999 through November 2001.

19. Betsy D. Scolnik, age 43, is a resident of Washington, D.C. Scolnik was employed by StarMedia from February 1998 through November 2001. From February 1999 through November 2001, Scolnik was first StarMedia's Senior Vice President for Strategic Development and later an Executive Vice President. In these positions, she first reported to Espuelas, later to Chen, and ultimately to a successor Chief Executive Officer of StarMedia.

20. Adriana J. Kampfner, age 36, is a resident of Brooklyn, New York. Kampfner was employed by StarMedia from August 1997 through December 2001. During the years 2000 and 2001, Kampfner was StarMedia's Senior Vice President, Global Sales and the President of StarMedia de Mexico. As Senior Vice President, Global Sales, Kampfner reported to Chen and Espuelas. Kampfner received an undergraduate business degree in finance from the University of Michigan.

21. Walther Möller, age 48, is a Mexican citizen residing in Mexico. StarMedia employed Möller as the President of AdNet pursuant to an employment agreement entered into at the time StarMedia acquired AdNet. Prior to the acquisition, Möller was a senior executive at his family's advertising firm, HMP.

22. Peter R. Morales, age 52, is a resident of Franklin Lakes, New Jersey. Morales was employed by StarMedia from June 1998 through November 2001 as the Controller and Vice President, Finance.

23. Peter E. Blacker, age 38, is a resident of Miami, Florida. Blacker was employed

by StarMedia from December 1997 through May 2001 as the company's Senior Vice President, Global Sales Strategy & Partnerships.

RELEVANT ENTITIES

24. StarMedia Network, Inc. was incorporated in Delaware in March 1996 and maintained its headquarters in New York, New York. The company was an Internet portal that targeted Spanish- and Portuguese-speaking markets. During the years 2000-2001, its fiscal year ended on December 31. StarMedia's common stock was registered with the Commission pursuant to Section 12(g) of the Exchange Act [15 U.S.C. § 78l(g)] and traded on the National Market System of the NASDAQ Stock Market, Inc. In November 2001, StarMedia had approximately 70.4 million shares of common stock outstanding. On February 1, 2002, the NASDAQ National Market System delisted the common stock of StarMedia. On December 23, 2003, the company formerly known as StarMedia filed a voluntary petition for reorganization under Chapter 11 of the U.S. Bankruptcy Code. Pursuant to Chapter 11, the company's assets were liquidated and the proceeding closed.

25. AdNet, S.A. de C.V. was acquired by StarMedia in April 2000. At the time, AdNet was a leading Mexican Internet search portal and Web directory. StarMedia acquired AdNet from its shareholders, MVS and HMP, for \$5 million in cash and StarMedia common stock valued at approximately \$15 million, with an earnout provision requiring payment of additional StarMedia common stock if AdNet met certain revenue targets. There was no cap on the number of StarMedia shares that could be earned by MVS and HMP pursuant to the earnout agreement.

26. AMG International, Inc., ("AMG"), was an "Internet incubator" that provided seed capital for Latin American and Asian Internet start-up companies in exchange for a percentage of

ownership. AMG sought to develop the companies through its contacts with larger U.S.-based Internet portals. Among the companies that AMG invested in were Media4.com, Gemelo, and Official Kiosk Group.

BACKGROUND

27. With others, Espuelas and Chen founded StarMedia in 1996. The company's May 1999 initial public offering raised \$105 million. A secondary public offering in October 1999 raised \$204 million. The price of StarMedia's common stock rose from the initial public offering price of \$15 per share to a high of \$70 per share in the third quarter of 1999. After its initial and secondary offerings, StarMedia used acquisitions as one method of expanding its network in the Latin American market.

28. StarMedia communicated the results of its operations through its filings with the Commission and its public statements to shareholders and analysts. In these communications, StarMedia disclosed not only its revenue results and trends but also the quality of its revenue, that is, whether the reported revenue was derived from cash sales or barter transactions. StarMedia first communicated the percentage of its revenue to barter transactions in its registration statement filed with the Commission for its initial public offering and continued to do so in subsequent filings. For example, StarMedia disclosed that revenue derived from barter transactions represented substantially all of the company's revenue in 1997, forty-one percent of its revenue in 1998, and twenty-seven percent of its revenue in 1999.

29. StarMedia's filings also cautioned shareholders and the public about the market risks associated with revenue recorded from barter transactions, because the company received no cash in such arrangements.

The AdNet Acquisition

30. In the fall of 1999, investment bankers acting on behalf of AdNet's owners approached StarMedia to ascertain its interest in acquiring AdNet from MVS and HMP. MVS was a leading Mexican media operator, with radio and television properties. StarMedia ultimately agreed to acquire AdNet because of its interest in AdNet's ongoing business relationships with MVS and HMP.

31. During StarMedia's consideration of an AdNet acquisition, Espuelas, Chen, and Kampfner learned that AdNet maintained business arrangements with MVS, HMP, and their customers. Pursuant to those arrangements, MVS and HMP purchased Internet advertising from AdNet for their clients, and in return AdNet purchased an equal dollar amount of radio or television advertising from MVS or of advertising services from HMP. The transactions resulting from these arrangements provided as much as sixty percent of AdNet's pre-acquisition revenue, and StarMedia sought to continue these "base book" transactions.

32. HMP was owned by Möller's family, and Möller was an executive at the firm. Accordingly, in order to keep the business relationships among AdNet, HMP, and MVS intact, StarMedia employed Möller post-acquisition as President of AdNet and entered into service and advertising agreements with HMP and MVS.

33. The service and advertising agreements executed as part of the acquisition did not disclose that in order to preserve the pre-existing relationship, StarMedia had agreed, post-acquisition, that AdNet would be required to purchase a dollar amount of advertising or advertising services from MVS and HMP equal to the dollar amount of Internet advertising that MVS and HMP would direct their clients to purchase from AdNet.

34. As part of the acquisition, the parties entered into a five-year earnout agreement that set certain revenue targets for each year and provided for additional payments of StarMedia common stock to the former owners of AdNet if the targets were met. The earnout agreement was drafted in dollar terms and did not set a cap on the number of StarMedia shares the former owners of AdNet would be paid if the revenue targets were met.

35. StarMedia acquired AdNet from MVS and HMP on April 6, 2000. Accordingly, from that date forward, AdNet's financial condition and results of operations were consolidated into StarMedia's financial statements.

36. The acquisition documents, StarMedia's filings with the Commission, and its public statements in 2000 and 2001, failed to disclose the reciprocal nature of the continuing business and advertising arrangements among MVS, HMP, and AdNet.

StarMedia's Revenue Crisis

37. During 2000, StarMedia's stock price steadily declined, in part because of a general decline in Internet advertising revenues. The company also experienced a decline in its cash reserves during this period. Nevertheless, throughout 2000, the company issued optimistic predictions of continued revenue growth. In addition, a consortium led by BellSouth Corporation ("BellSouth") emerged as a potential source of additional financing. To secure that financing, however, the company needed to demonstrate that it had met its revenue targets.

StarMedia's Accounting Manipulations by Defendants

Fiscal Year 2000

38. In the second quarter of 2000, Espuelas, Chen, Heller, Scolnik, and Kampfner learned from internal reports that StarMedia's actual sales and revenues were falling significantly

short of budget projections. Each responded by using fraudulent means to inflate StarMedia's revenue.

39. Espuelas and Chen knew, or were reckless in not knowing, that the linked nature of the base book transactions would not be apparent to the finance department. By failing to memorialize the transactions, as required by the company's internal controls, Espuelas and Chen prevented that department and StarMedia's independent auditors from perceiving and analyzing the reciprocal nature of the transactions. The finance department was deceived because it received AdNet insertion orders at one point in time and MVS and HMP invoices for services at a different time, without any indication they were all part of a linked agreement. As a result, the two aspects of the arrangement were viewed by the finance department as separate and unrelated, and therefore, StarMedia recognized as advertising revenue the full amount AdNet invoiced customers of MVS and HMP for advertising.

40. To present financial statements in conformity with GAAP, StarMedia could not have recognized and recorded as revenue the full amount of the transactions with customers of MVS and HMP. Had StarMedia's finance department analyzed the "base book" transactions as advertising-for-advertising barter transactions with MVS and HMP, as required by GAAP, StarMedia would have recognized little or no revenue from the transactions.

41. Nonmonetary exchanges such as barter transactions are accounted for under Accounting Principles Board Opinion No. 29, *Accounting for Nonmonetary Exchanges* ("APB 29"), which was issued in 1973. Under APB 29, transactions such as the exchange of Internet advertising for goods or services are accounted for based on the fair value of the Internet

advertising provided or the fair value of the goods or services received, whichever is more clearly evident.

42. In 1999 accounting rule-makers became increasingly concerned that (a) revenue growth, regardless of profitability, had become the key metric in determining the market capitalization of Internet companies whose major revenue source was advertising, and (b) that Internet advertising revenues were being inflated by assigning dollar values to barter transactions involving Internet advertising swaps which could not be supported by evidence of actual cash sales of the same Internet advertising at the same value. Consequently in early 2000, the Emerging Issues Task Force issued the abstract for EITF 99-17, *Accounting for Advertising Barter Transactions*, which provided additional guidance for revenue recognition for exchanges of Internet advertising. EITF 99-17 essentially required that the fair value of Internet barter advertising would be determined based on similar cash sales within six months before the barter transaction and that if there were no comparable cash sales for similar advertising the fair value of the barter advertising “likely will be zero.”

43. StarMedia subsequently restated the base book transactions in its restatement of its financial statements. After analyzing the transactions, StarMedia treated them like barter transactions, under the relevant GAAP provisions, and the company wrote off over ninety percent of the revenue previously reported from the transactions.

44. At the time that StarMedia utilized the base book transactions, Espuelas and Chen were familiar with barter transactions as a result of their executive positions, their knowledge of the company’s business, and StarMedia’s disclosures in its filings with the Commission and in its statements to shareholders and the public. Each had signed StarMedia’s registration statement

for its initial public offering that was filed with the Commission in March 1999. That registration statement described barter co-marketing arrangements with media companies, disclosed the company's accounting for barter transactions, indicated that the company derived substantially all of its revenues from barter transactions in its fiscal year 1997, and stated that StarMedia derived approximately \$2.4 million in revenue from barter in its fiscal year 1998. In an amendment to that registration statement and in its prospectus filed in May 1999, StarMedia cautioned investors that it had derived a portion of its revenues from reciprocal advertising agreements, which did not generate cash revenue. Espuelas signed the amendments to the registration statement.

45. Similar types of disclosure concerning barter were included in filings between the initial public offering in May 1999 and the company's secondary public offering in October 1999. Filings with the Commission, including StarMedia's quarterly Reports on Form 10-Q, during its fiscal year 1999, and the company's annual Report on Form 10-K for its fiscal year 1999, disclosed the risk inherent in the fact that barter did not generate cash revenue and provided period-over-period comparisons of the percentage or amount of revenue derived from barter. Espuelas and Chen signed the annual report, and as members of StarMedia's Board of Directors, they authorized and delegated Heller to sign the quarterly reports.

46. At times in 2000, analysts questioned whether the company was increasing revenue by using barter. In April and October 2000, Espuelas assured analysts that the company had "surging revenue" and that barter would probably fall "below 10 percent by the end of the year." Espuelas and Chen knew that StarMedia's filings disclosed the amount or percentage of the company's revenue that was derived from barter. Both were aware that analysts used the

percentage of barter to revenue as a metric to gauge StarMedia's business. Both, as members of the executive team, had received StarMedia's written policies, and revisions thereto, with respect to revenue recognition, including barter transactions. Espuelas and Chen each knew, or was reckless in not knowing, that his conduct in failing to document or communicate the reciprocal base book transactions among MVS, HMP, and AdNet hid the fact that those transactions were barter transactions and therefore caused StarMedia's filings and public statements to be materially false and misleading.

47. In addition, during the second quarter of 2000, StarMedia improperly booked revenue from a contingent sales transaction. The Internet incubator AMG orally agreed to purchase \$500,000 of Internet advertising from StarMedia on behalf of Gemelo, a company in AMG's portfolio, contingent on AMG's approval of the advertising services. If AMG did not approve of the advertising services, its liability was limited to a payment of \$10,000. Scolnik, Kampfner, and Blacker agreed that StarMedia would provide the services on this contingent basis. At Blacker's direction, a \$500,000 insertion order was submitted to StarMedia's finance group. In order to cause the company to recognize the entire \$500,000 from the transaction as revenue, Scolnik, Kampfner, and Blacker did not inform StarMedia's finance department of the contingent terms of the transaction.

48. As a direct result of Scolnik's, Kampfner's, and Blacker's failure to communicate the contingent terms of the oral agreement with AMG to StarMedia's finance department, StarMedia recognized as revenue and recorded in its books and records \$500,000, the full amount listed on the StarMedia insertion order.

49. The oral agreement, including the approval contingency, was subsequently memorialized in December 2000. Although Scolnik, Kampfner, and Blacker were aware of the memorialization, none of them disclosed or submitted the now-written side agreement to StarMedia's finance department. The advertising services ultimately proved unacceptable to AMG, and it did not pay the balance of \$490,000.

50. In the third quarter of 2000, Blacker, in consultation with Kampfner and under pressure from Scolnik, negotiated a bogus transaction with Groupe Danone ("Danone"). Blacker and Kampfner sought to induce Danone to use StarMedia on a large project involving a range of Internet services in Latin America. Blacker, with Kampfner's knowledge and consent, offered Danone's media buyer \$500,000 of Internet services at no charge, as an incentive for Danone to select StarMedia for the project. Blacker, with Kampfner's knowledge and consent, told Danone's media buyer that StarMedia required a signed insertion order to reserve space on StarMedia's delivery schedule even though the deal was a contingent one.

51. At Blacker's direction, a \$500,000 insertion order was submitted to StarMedia's finance department. The insertion order did not reflect that the advertising was being provided to Danone free of charge. Blacker, Kampfner, and Scolnik knew that the services were to be provided free of charge, but they withheld that information from StarMedia's finance department.

52. In addition, during the third quarter of 2000, Espuelas and Chen again failed to memorialize the linked nature of the base book transactions, and each deceived the company's finance department and StarMedia's independent auditors as to the reciprocal nature of the relationship among MVS, HMP, and Adnet. Thus, each caused StarMedia to book the full amount of AdNet's base book transactions, \$774,000, as revenue rather than providing sufficient

information about the linked transactions for the finance department to properly analyze the transactions under GAAP. During this time, both Espuelas and Chen were familiar with barter transactions at StarMedia and with the company's statements about them. Each had signed StarMedia filings that disclosed the percentage of the company's revenue derived from barter. Both had received the company's written policies regarding revenue recognition from barter transactions. As a result, Espuelas and Chen each knew or were reckless in not knowing that these amounts were improperly recorded as revenue and that the disclosures in the company's public statements concerning the dollar amount and percentage of revenue derived from barter transactions were false and misleading.

53. Thus, by utilizing the contingent transaction with Danone and improperly recognizing revenue in the full amount of the base book transactions, StarMedia fraudulently inflated its revenue by \$1.274 million in the third quarter of 2000.

54. Scolnik, Kampfner, and Blacker each knew that StarMedia had implemented a process that required the finance department to receive an accurate insertion order or contract for each transaction so that StarMedia could determine the appropriate amount of revenue to record in its books and records for that transaction. Each also knew from StarMedia's sales and business practices materials that amounts recorded as revenue by the finance department were used by the company in its reporting and filings with the Commission.

55. Blacker knew that, as a result of his conduct, StarMedia could not have properly recognized revenue from the transactions with Danone and with AMG's portfolio company, because the insertion orders did not reflect all the terms of the transactions.

56. Scolnik and Kampfner each received revenue reports generated from StarMedia's books and records, both during the calendar period and in the several-week period after the quarter-end when the company finalized its books and records for financial statement and periodic reporting purposes. In the period between the quarter-end and when StarMedia closed its books and records, Kampfner assisted the finance department in resolving issues concerning sales documentation and the resulting revenue recognition. Thus, Kampfner had specific knowledge of the revenue the company was calculating during the closing process, including revenue recognized from the contingent transactions with Danone and with AMG's portfolio company, and StarMedia's final revenue for the period once the books were closed. As a result, Scolnik and Kampfner each knew that StarMedia had improperly recognized and recorded revenue from the contingent transactions with Danone and with AMG's portfolio company. Each also knew that as a result of her conduct, StarMedia's periodic filings with the Commission and statements to shareholders and the public were false and misleading.

57. In the fourth quarter of 2000, StarMedia's management again learned from internal reports that projected revenue would fall significantly short of budget and analyst expectations. Espuelas, Chen, Heller, Kampfner, and Scolnik again set about finding additional sources of revenue to close the gap. This time, together with Möller, they devised a set of round trip transactions to help StarMedia inflate its revenues.

58. In November 2000, Möller approached StarMedia seeking a loan for HMP. StarMedia at first attempted to locate a banker that would lend HMP funds using the shares of StarMedia that HMP owned as collateral for the loan. However, because the price of StarMedia

common stock had fallen substantially, no bank would loan HMP funds on that basis. When the efforts failed, StarMedia ultimately loaned \$100,000 to HMP.

59. Espuelas, Chen, Heller, Scolnik, and Kampfner discussed using Möller's connections with MVS and HMP to inflate StarMedia's revenue. Scolnik and Kampfner had initial discussions with Möller regarding transactions that could effectuate such a plan. At Chen's direction, Heller became involved in those discussions and ultimately, acted as a conduit between Chen and Möller.

60. On November 29, 2000, Möller sent Heller an e-mail outlining what became known as the "incremental revenue" transactions. Möller attached a diagram to this e-mail illustrating how the proposed scheme could be structured. The diagram showed that the transactions were round trip transactions that allowed StarMedia to fund its own revenue. Heller spoke to Chen about the transactions, and Chen gave his approval to Heller to go ahead.

61. On November 30, 2000, Heller, in New York City, spoke by telephone with Espuelas and Kampfner, in Mexico City, about a meeting Espuelas and Kampfner were to have later that day with Möller. During the call, they discussed possible terms for the incremental revenue transactions. After the call, Espuelas and Kampfner met with Möller, and they communicated to him that StarMedia agreed to the structure of the transactions as he had proposed them.

62. As part of the transactions, StarMedia agreed to provide AdNet with funds, characterized as "capital contributions." Pursuant to the agreement, AdNet, using the purported capital contributions and some of its own funds, would purchase \$3.2 million of services from HMP and MVS. In return, HMP and MVS agreed to direct the purchase of \$3.2 million of

advertising to StarMedia. Ultimately, \$2.6 million of advertising was placed at StarMedia de Mexico, and \$623,000 of advertising was placed at AdNet, purportedly on behalf of the clients of HMP and MVS.

63. On December 4, 2000, StarMedia wired \$345,000 to an HMP bank account. On December 5, 2000, the third business day after the agreement, Möller sent an e-mail to Kampfner naming fifteen clients and the dollar amount of advertising for each client. The amount of the proposed advertising was \$1.9 million. The e-mail asked Kampfner to recommend the “inventory” to be run for each client, so that the information could be placed on insertion orders. Subsequently, Möller sent Kampfner the names of additional clients, bringing the aggregate amount of advertising to \$3.2 million.

64. On December 7, 2000, Möller sent an e-mail to Heller confirming the transactions, their timing, and the responsibilities of the parties pursuant to the agreement reached in Mexico on November 30, 2000.

65. In some instances, the HMP and MVS clients purportedly involved in these transactions had no knowledge of “their” advertising purchases. Other clients apparently knew of the purchases but were indifferent toward them because, from their perspective, HMP and MVS were paying, directly or indirectly, for the advertising.

66. As a result of the agreement, StarMedia, through AdNet, essentially agreed to pay HMP and MVS, through Möller, \$3.2 million, which in turn would be paid back to StarMedia, either directly or through AdNet, for advertising sales in the fourth quarter.

67. StarMedia did not document the oral agreement underlying the incremental revenue transactions, and, accordingly, no written document was executed by StarMedia, AdNet,

HMP, and MVS. The absence of a written document showing all the terms of the agreement contravened StarMedia's internal controls requiring all terms of a sales contract to be in writing and deceived StarMedia's finance department when it received the insertion orders prepared to process the Internet services StarMedia delivered. The absence of a document that set forth all elements of the agreement prevented the finance department and StarMedia's independent auditors from knowing, and analyzing under GAAP, all the aspects of the transactions. That result was intended by Chen, Espuelas, and Heller, who had entered into the round trip transactions to artificially inflate StarMedia's reported revenue. Consequently, in the fourth quarter of 2000, StarMedia improperly recognized and recorded from the incremental revenue transactions \$2.6 million in revenue through StarMedia de Mexico and \$623,000 through AdNet.

68. Although the \$3.2 million of revenue from the incremental revenue transactions represented approximately sixteen percent of StarMedia's fourth quarter revenue, the company did not make any public announcement or disclosure concerning the transactions.

69. In the fourth quarter of 2000, StarMedia paid only \$345,000 of the \$3.2 million it had promised to HMP and MVS. Subsequently, in the first quarter of 2001, the company made additional payments totaling \$1.08 million, after complaints from Möller that the company was not abiding by their agreement.

70. Morales had not been involved in the negotiations of the incremental revenue transactions. He learned about the scheme from Heller early in December 2000. When Heller first told Morales about the incremental revenue transactions, he also told him the planned accounting treatment for them. Heller told Morales that StarMedia would recognize all revenue from the transactions in the fourth quarter but defer recognition of the expenses related to the

offsetting, purchased services until the quarter in which the services were utilized. Morales initially did not agree with this treatment. Moreover, he told Heller the transactions appeared to be barter transactions and should be classified and recorded as such. Morales relented only after Heller assured him that he would deal with the company's auditors if they raised any questions.

71. In December 2000, Heller asked Morales to prepare and authorize a payment to HMP. Morales followed through and approved the wire transfer of \$345,000 from StarMedia directly to HMP. That payment provided the initial funds used to capitalize the incremental revenue transactions.

72. During the fourth quarter of 2000, Espuelas and Chen each again failed to memorialize the agreement among MVS, HMP, and AdNet in the base book transactions and prevented the finance department and StarMedia's independent auditors from perceiving and analyzing the transactions as barter. As a result, StarMedia again improperly recognized advertising revenue from the base book transactions, thereby further inflating StarMedia's revenue by \$599,000.

73. During that same quarter, StarMedia improperly recognized \$1 million of revenue from insertion orders from Danone. Those insertion orders, once again, had been described to Danone's media buyer as simply a means of reserving network space for services that StarMedia would deliver free of charge to Danone as a sales incentive. Blacker submitted the orders to StarMedia's finance department without disclosing that the customer had no obligation to pay. Scolnik and Kampfner knew that Danone was not required to pay for the services, yet neither of them informed the finance group. Subsequently, Scolnik and Kampfner both received revenue reports that listed the Danone transaction as revenue, as Scolnik and Kampfner intended, and

neither communicated to the finance department that, based on a side agreement, the revenue should not be recognized because Danone had no obligation to pay the amount purported to be due.

74. That same quarter, StarMedia improperly recognized \$750,000 on an advertising transaction with International Kiosk Group, a portfolio company of AMG, that was contingent on customer approval. Scolnik and Blacker were involved in negotiating the terms of that transaction with AMG's President and its in-house counsel. Kampfner subsequently approved the terms of the transaction. Scolnik, Kampfner, and Blacker did not disclose the contingency to StarMedia's finance group, and, as a result, StarMedia recognized as revenue the full amount of the transaction from the face of the insertion order, as Scolnik and Kampfner intended.

(Ultimately, AMG was not satisfied with the services and therefore did not pay StarMedia.)

75. As part of its restatement of its financial statements, StarMedia wrote off \$600,000 of revenue from this contingent transaction.

76. In all, for its fiscal year 2000, StarMedia improperly recognized at least \$8.4 million in revenue, overstating its revenue by sixteen percent. As noted, that improper revenue recognition came from base book transactions, incremental revenue transactions, and contingent sales transactions. StarMedia's fraudulent revenue recognition in 2000 allowed the company to meet analysts' revenue projections and significantly off-set the company's actual decline in revenue from business operations.

77. During the implementation of the fraudulent schemes, Espuelas, Chen, Heller, and Kampfner each had pledged StarMedia shares as collateral for loans in margin accounts at their respective brokers. When the price of StarMedia stock declined during 2000, they each

requested and received lines of credit from the company to satisfy the need for additional collateral to provide to the brokerage firms. They each used their artificially inflated StarMedia stock as collateral for the lines of credit. At December 31, 2000, the principal balance owed to the company on the lines of credit was \$649,000 for Espuelas; \$1,991,165 for Heller; and \$1,057,788 for Kampfner.

78. Espuelas, Chen, Heller, Scolnik, Kampfner, and Blacker each knew that StarMedia had implemented a process that required an accurate insertion order or contract to be forwarded to the finance department for each transaction so that StarMedia could determine the appropriate amount of revenue to record in its books and records for that transaction.

79. Espuelas, Chen, Heller, Scolnik, and Kampfner each knew that from time to time StarMedia entered into reciprocal agreements with other entities in which it exchanged Internet advertising for other advertising or services. Each of them had also received StarMedia's written revenue recognition policies as part of their executive, sales, or accounting functions at the company. In 2000, Kampfner also had reviewed changes to the company's policy related to revenue recognition from barter transactions with Heller and the executive responsible for revenue recognition at StarMedia. (As noted above, the changes in the policy resulted from new accounting guidelines concerning barter that the company's independent auditors had communicated to StarMedia.) On March 30, 2001, Espuelas and Chen both signed StarMedia's annual Report on Form 10-K for the company's fiscal year 2000 that disclosed that barter revenues and expenses were recognized in accordance with EITF 99-17.

80. Espuelas and Chen knew that the reciprocal nature of the base book transactions had not been memorialized, disclosed to the public, or communicated to the finance department.

Espuelas, Chen, Heller, Morales, Möller, Scolnik, and Kampfner knew that not all material aspects of the incremental revenue transactions had been memorialized, disclosed to the public, or communicated to the finance department. Moreover, each knew that the failure to memorialize a transaction meant that the transaction would be less likely to be reviewed by the company's auditors during its procedures at quarter-end or year-end.

81. Espuelas, Chen, Heller, Morales, Scolnik, and Kampfner each received revenue reports generated by the finance department, near the end of 2000 and again in the period between December 31, 2000 and the time when StarMedia closed its books and records for its fiscal year 2000. During that post-calendar-close period, Kampfner assisted the finance department in resolving issues concerning sales documentation and the resulting revenue recognition. As a result, Kampfner had specific knowledge of the revenue the company was calculating during the closing process, including revenue recognized from the incremental revenue transactions and the contingent transactions with Danone and AMG's portfolio company, and StarMedia's final revenue figures. Espuelas, Chen, Heller, Morales, Scolnik, and Kampfner each knew that, as a result of his or her conduct, StarMedia had improperly recognized revenue from the incremental revenue transactions. Espuelas and Chen also knew that StarMedia had improperly recognized revenue from the base book transactions.

82. Scolnik, Kampfner, and Blacker each knew that, as a result of his or her conduct, StarMedia had improperly recognized revenue from the contingent transaction with Danone and the transaction with the portfolio company of AMG. Thus, each knew that StarMedia's filings with the Commission and statements to shareholders and others were false and misleading.

83. Morales and Möller also each knew that StarMedia had implemented a process

that required the finance department to receive an accurate insertion order or contract for each transaction so that it could determine the appropriate amount of revenue from that transaction. Morales and Möller each knew that, as a result of his conduct, the finance department did not receive accurate information with respect to the incremental revenue transactions and, consequently, StarMedia had improperly recognized revenue from those transactions for the company's fiscal year 2000.

First Quarter 2001

84. StarMedia's fraudulent revenue recognition continued in 2001. In the first quarter of 2001, StarMedia improperly recorded \$5.9 million in revenue, overstating actual revenue by sixty-seven percent.

85. In January and February 2001, Espuelas told analysts and investors, in interviews and conference calls, that StarMedia's revenue continued to grow and that its outlook for 2001 remained positive. However, during the first quarter, Espuelas, Chen, Heller, Kampfner, and Scolnik learned from internal revenue reports that StarMedia's expected revenue for the quarter was again below budget. Each set about to close the gap by once again resorting to fraudulent methods.

86. In the first quarter of 2001, Espuelas and Chen each caused StarMedia to recognize and improperly record as revenue \$1.8 million from the AdNet base book transactions. Both knew or were reckless in not knowing that, at best, these transactions were in fact an exchange of advertising for advertising and should be accounted for as barter transactions. Both knew that the base book transactions had not been memorialized, as required by StarMedia's internal controls, and as a result they had deceived the company's finance department and

independent auditors.

87. In addition, in the first quarter of 2001, Espuelas, Chen, Heller, Scolnik, Kampfner, Morales, and Möller caused StarMedia to recognize \$2.6 million in revenue through StarMedia de Mexico, by utilizing the incremental revenue transactions.

88. On March 10, 2001, Kampfner communicated to Espuelas, Chen, and Heller that she had discussed with Möller the company's 2001 revenue shortfall and the possibility of again using incremental revenue transactions to close that shortfall. Kampfner communicated to them that Möller had first said he could provide \$2 million in base book revenue for Adnet and that Kampfner had told him "to do it." Additionally, she told Espuelas, Chen, and Heller that Möller would also confer with a top executive at MVS concerning the possibility of more "one-for-one" transactions with the goal of reaching StarMedia's quarterly target through an additional \$3 million in revenue from incremental revenue transactions.

89. On March 14, 2001, Kampfner told Espuelas, Chen, and Heller that Möller had indicated that the incremental revenue target could be met, but that a few issues needed to be resolved. Specifically, she recounted, Möller was demanding that StarMedia issue certain StarMedia shares earned by HMP and MVS under the earnout provision of the AdNet acquisition agreement and pay \$1 million due in the fourth quarter of 2000 pursuant to the incremental revenue agreement.

90. On March 24, 2001, Kampfner updated Espuelas, Chen, Heller, and Scolnik concerning StarMedia's first quarter revenue situation, including progress on the base book revenues and the incremental revenues.

91. On March 27, 2001, Kampfner communicated to Chen that Möller was close to

having placed enough client advertising to meet the incremental revenue target for that quarter.

92. Scolnik subsequently suggested to Chen that Möller be rewarded for his efforts on the base book and incremental revenue transactions. Chen relayed the suggestion to Espuelas. Espuelas invited Möller and his wife to dinner, and he directed StarMedia to provide Möller and his wife with a European vacation as a reward.

93. After the close of the first quarter of 2001, StarMedia, through AdNet, paid \$950,000 to HMP, for advertising purchased pursuant to the incremental revenue transactions in that quarter. Chen approved the disbursement, and Heller directed Morales to effect the transfer of funds from StarMedia to Adnet. Chen's approval of the payment, in response to Möller's demands for compliance with the incremental revenue agreement, demonstrated Chen's understanding that the incremental revenue transactions were an agreement by StarMedia to purchase its own revenue. Heller confirmed to Chen that funds had been sent to AdNet earmarked for payment to HMP.

94. In the first quarter of 2001, StarMedia also improperly recognized \$1.5 million of contingent revenue from two transactions with portfolio companies of AMG. Scolnik, Kampfner, and Blacker took part in these transactions by negotiating or approving the terms, including side agreements that made the transactions contingent. None of them communicated the side agreements to StarMedia's finance group.

95. Espuelas, Chen, Heller, Morales, Scolnik, Kampfner, Möller, and Blacker each knew that StarMedia had implemented a process that required the finance department to receive an accurate insertion order or contract for each transaction so that StarMedia could determine the appropriate amount of revenue to record in its books and records for that transaction.

96. Espuelas, Chen, Heller, Morales, Scolnik, and Kampfner each knew that from time to time that StarMedia had entered into barter transactions, that is, reciprocal agreements with other entities in which it exchanged Internet advertising for other advertising or services. Each of them had also received StarMedia's written revenue recognition policies as part of their executive, sales, or accounting functions at the company. During 2000, Kampfner had also reviewed changes to the company's policy related to barter revenue recognition with the executive responsible for revenue recognition at StarMedia. (The changes in the policy resulted from new accounting guidelines that the company's auditor had communicated to StarMedia.) On March 30, 2001, Espuelas and Chen both signed StarMedia's annual Report on Form 10-K for the company's fiscal year 2000 that disclosed that barter revenues and expenses were recognized in accordance with EITF 99-17.

97. Espuelas and Chen each knew that the linked nature of the base book transactions had not been memorialized, disclosed publicly, or communicated to the finance department. Espuelas, Chen, Heller, Morales Scolnik, Kampfner, and Möller each knew that the true nature of the incremental revenue transactions had not been memorialized, disclosed publicly, or communicated to the finance department. Moreover, Espuelas, Chen, Heller, Morales, Scolnick, and Kampfner each knew that the failure to memorialize a transaction meant that the transaction would be unlikely to be reviewed by the company's independent auditors during its procedures at quarter-end or year-end.

98. Espuelas, Chen, Heller, Morales, Scolnik, and Kampfner each received revenue reports generated by the finance department, near the end of the first quarter of 2001 and again in the period between March 31, 2001 and the time when StarMedia closed its books and records

for its first quarter of 2001. During that post-quarter-close period, Kampfner assisted the finance department in resolving issues concerning sales documentation and the resulting revenue recognition. As a result, Kampfner had specific knowledge of the revenue the company was calculating during the closing process, including the revenue improperly recognized pursuant to the transactions with AMG and incremental revenue transactions, and StarMedia's final revenue figures.

99. Espuelas and Chen each also knew that as a result of his conduct, the finance department did not receive accurate and complete information with respect to the base book transactions and, consequently, StarMedia had improperly recognized revenue from the base book transactions in the first quarter of 2001, as they had intended. Espuelas, Chen, Heller, Morales, Scolnik, Kampfner, and Möller each knew that as a result of his or her conduct, the finance department did not receive accurate information with respect to the incremental revenue transactions and, consequently, StarMedia improperly recognized revenue from the incremental revenue transactions in its first quarter of 2001, as each of them had intended.

100. Scolnik, Kampfner, and Blacker each knew that as a result of his or her conduct, StarMedia improperly recognized revenue from transactions with AMG's portfolio companies, as each of them had intended.

101. During the first quarter of 2001, Espuelas and Chen drew additional funds from their lines of credit with StarMedia. They continued to use artificially inflated StarMedia stock as collateral for their lines of credit. By March 31, 2001, the outstanding principal balance for Espuelas was \$1,550,000 and for Chen, \$1,500,000. On or about April 2, 2001, Chen's outstanding principal balance increased to \$4 million. On or about May 1, 2001, Espuelas's

outstanding principal balance increased to \$2,675,000. At the time they increased their StarMedia-stock-backed balances, Espuelas and Chen each knew that StarMedia's reported revenue had been artificially inflated, although the company's investors did not.

Second Quarter of 2001

102. In the second quarter of 2001, Espuelas, Heller, Kampfner, and Scolnik learned from internal revenue reports that StarMedia's expected revenue once again was below budget. They again resorted to fraudulent methods to increase StarMedia's reported revenue. As a result, in the second quarter of 2001, StarMedia improperly recorded \$3.725 million of revenues, overstating actual revenues by fifty-nine percent.

103. This overstatement included \$1.05 million in AdNet base book revenues that Espuelas caused to be recorded in StarMedia's books and records. (Chen was no longer President of StarMedia by the second quarter of 2001.) Espuelas knew that the linked nature of the transactions had not been memorialized, as required by the company's internal controls, thus preventing the finance department and StarMedia's independent auditors from perceiving and analyzing the reciprocal nature of the transactions. Espuelas knew or was reckless in not knowing that these transactions should have been accounted for as barter transactions.

104. In addition, StarMedia recognized \$2.675 million of incremental revenues through StarMedia de Mexico. Espuelas, Heller, Kampfner, Scolnik, Möller, and Morales each knowingly or recklessly directed or implemented those transactions in the second quarter of 2001.

105. After the close of the second quarter of 2001, StarMedia, through AdNet, paid \$517,500 to HMP, for advertising purchased pursuant to the incremental revenue agreement in

the first and second quarter of 2001. Heller, Morales, and Kampfner directed the transfer of funds from StarMedia to AdNet and knew that the funds were to be paid to HMP as part of the incremental revenue agreement. By directing the payment of these funds, pursuant to the agreement, they each demonstrated their understanding that the incremental revenue agreement was an agreement by which StarMedia funded its own revenue.

106. Espuelas, Heller, Morales, Scolnik, Kampfner, and Möller each knew that StarMedia had implemented a process that required the finance department to receive an accurate insertion order or contract for each transaction so that StarMedia could determine the appropriate amount of revenue to record in its books and records for that transaction.

107. Espuelas, Heller, Morales, Scolnik, and Kampfner each received revenue reports generated by the finance department, near the end of the second quarter of 2001 and again in the period between June 30, 2001 and the time when StarMedia closed its books and records for its second quarter of 2001.

108. During the post-quarter-close period, Kampfner assisted the finance department in resolving issues concerning sales documentation and the resulting revenue recognition. As a result, Kampfner had specific knowledge of the revenue the company was calculating during the closing process, including the improper recognition of revenue from the incremental revenue transactions, and StarMedia's final revenue figures.

109. Espuelas, Heller, Morales, Scolnik, and Kampfner each knew that from time to time StarMedia entered into barter transactions, that is, reciprocal agreements with other entities in which it exchanged Internet advertising for other advertising or services. Each of them had also received StarMedia's written revenue recognition policies as part of their executive, sales, or

accounting functions at the company.

110. Espuelas knew that the linked nature of the base book transactions had not been memorialized or disclosed in a document provided to the finance department. Espuelas, Heller, Morales, Scolnik, Kampfner, and Möller each knew that the true nature of the incremental revenue transactions had not been memorialized, communicated to the finance department, or disclosed to the public. Moreover, Espuelas, Heller, Morales, Scolnick, and Kampfner each knew that the failure to memorialize a transaction meant that the transaction would be unlikely to be reviewed by the company's independent auditor during its procedures at quarter-end or year-end.

111. Espuelas knew that, as a result of his conduct, StarMedia improperly recognized revenue from the base book transactions in its second quarter of 2001, as he intended. Espuelas, Heller, Morales, Scolnik, Kampfner and Möller each knew that as a result of each of his or her conduct, StarMedia improperly recognized revenue from the incremental revenue transactions in its second quarter of 2001.

Misleading Disclosures and Financial Statements in Filings and Public Statements

112. As a result of its improper revenue recognition from the base book transactions, incremental revenue transactions, and contingent sales transactions, StarMedia filed with the Commission periodic reports that contained materially false and misleading statements and financial information for the year ended December 31, 2000, and for the quarters ended March 31 and June 30, 2001.

113. At the time Espuelas and Chen signed StarMedia's annual Report on Form 10-K for its fiscal year ended December 31, 2000, both knew or were reckless in not knowing that the

filing contained false disclosures and financial statements that contained materially false and misleading statements and financial information with respect to the quality and quantity of revenues recognized in the base book and incremental revenue transactions. Moreover, Espuelas and Chen knew that the base book transactions and incremental revenue transactions were conducted pursuant to oral agreements that had not been memorialized.

114. At the time that Heller signed StarMedia's quarterly Reports on Form 10-Q for the quarters ended March 31, 2001, and June 30, 2001, and the company's annual Report on Form 10-K for its fiscal year ended December 31, 2000, he knew or was reckless in not knowing that the filings contained materially false and misleading statements and financial information with respect to the incremental revenue transactions. Heller also knew that the incremental revenue transactions were conducted pursuant to oral agreements that had not been memorialized.

False Statements to the Company's Independent Auditors

115. StarMedia did not disclose to its independent auditors, Ernst & Young LLP, the true economic realities of the base book transactions, the incremental revenue transactions, or the contingent Danone and AMG sales transactions.

116. Chen, Heller, and Morales signed management representation letters as part of Ernst & Young LLP's audit of StarMedia's financial statements for the company's fiscal year 2000 and that firm's review of the company's financial statements for the first and second quarters of 2001. Chen, Heller, and Morales signed the management representation letter, dated March 28, 2001, with respect to the audit of StarMedia's financial statements for the company's fiscal year 2000, that expressly represented: "We have made available to you all significant contracts and agreements"; "[r]eceivables represent valid claims . . . and do not include amounts

for . . . other types of arrangements not constituting sales”; “[w]e have disclosed to you all sales terms, including all rights of return or price adjustments”; “[w]e have provided you with all sales agreements . . . [and] [t]hese represent the entire arrangements and are not supplemented by other agreements either written or oral”; “[t]here has been no fraud involving management or employees who have significant roles in internal control”; and “[t]here has been no fraud involving other employees that could have a material effect on the financial statements.” Chen, Heller, and Morales also signed the management representation letter related to the review of StarMedia’s financial statements for the first quarter 2001, that stated the representations made to the auditors with respect to the audit of StarMedia’s financial statements for its fiscal year 2000 “remain current.” Heller and Morales subsequently signed the management representation letter for the review of StarMedia’s financial statements for the second quarter 2001 that stated the representations made to the auditors with respect to the audit of StarMedia’s financial statements for its fiscal year 2000 “remain current.” The representations in the letters were all false as Chen, Heller, and Morales each had structured, directed, or implemented transactions for which all terms and agreements had not been disclosed to the auditors, including, for Chen, the base book transactions, and for Chen, Heller, and Morales, the incremental revenue transactions.

Espuelas, Chen, Heller, and Scolnik Present False Information to Potential Investors

117. In mid-2000, Chen directed Scolnik to begin working to secure financing for StarMedia from a consortium of investors led by BellSouth. Chen explained that StarMedia needed to meet its revenue goals in order to close the financing.

118. The BellSouth consortium did provide additional financing to StarMedia in the form of the purchase of \$35 million worth of convertible preferred shares, by means of a

transaction that closed on May 30, 2001. Prior to that closing, Scolnik acted as a conduit between those making requests at BellSouth for additional financial information and those at StarMedia providing the responsive information. When Scolnik needed financial information to present to BellSouth, she would request it from Heller, someone that reported to Heller, or the executive responsible for revenue recognition at StarMedia. When she received the information, she would forward it to BellSouth.

119. Chen and Heller presented financial information to BellSouth while it was considering whether to provide financing to StarMedia, including information relating to StarMedia's revenue in 2000 and the first quarter of 2001.

120. In providing the financing, BellSouth entered into a Securities Purchase Agreement with StarMedia. Espuelas executed the agreement on behalf of StarMedia, and both he and Chen approved the agreement as members of StarMedia's Board of Directors. As part of the Securities Purchase Agreement, StarMedia made certain representations to BellSouth with respect to StarMedia's filings with the Commission and its financial information. StarMedia represented that, as of their respective filing dates, none of the Commission filings contained any materially false or misleading statements and that its financial statements complied with GAAP and fairly presented in all material respects the financial position of the company as of the dates of the statements and the results of its operations and cash flows for the periods then ended.

121. As a result, Espuelas, Chen, Heller, and Scolnik each played an important role in the presentation of financial information to, and discussions and negotiations with, BellSouth. Espuelas, Chen, Heller, and Scolnik each knew or was reckless in not knowing that the financial information provided to Bell South contained materially false and misleading information with

respect to the revenue of StarMedia in 2000 and the first quarter of 2001, based on their involvement in the base book transactions, incremental revenue transactions, or transactions with contingencies. Moreover, Espuelas and Chen knew or were reckless in not knowing that representations made in the agreement with BellSouth were materially false and misleading.

Chen Avoids Losses on His Sales of StarMedia Common Stock

122. Chen sold 715,000 shares of StarMedia common stock in the period from August 13 to November 1, 2001, prior to the November 19, 2001 StarMedia announcement that it would restate its financial statements. At the time of his sales, Chen knew that StarMedia's filings with the Commission and other public statements contained materially false and misleading disclosures and financial information, including the fraudulent overstatement of StarMedia's amount and quality of revenue. Chen learned the information as a result of his employment at StarMedia, while authorizing and implementing the fraud. By selling StarMedia stock while aware of the fraud, but while investors were not, Chen avoided losses of at least \$150,438.88.

123. Chen knew or was reckless in not knowing that he sold his StarMedia stock while in possession of material nonpublic information about the company's inflated financial condition and that trading on the basis of the information was improper and in breach of a duty of trust or confidence he owed to StarMedia and its shareholders.

FIRST CLAIM

**FRAUD IN THE OFFER OR SALE OF SECURITIES
Violations of Section 17(a) of the Securities Act
(Against Espuelas, Chen, Heller, and Scolnik)**

124. The Commission realleges and incorporates by reference ¶¶ 1 through 121 above.

125. Each of defendants Espuelas, Chen, Heller, and Scolnik, by engaging in the conduct described above, in connection with the offer or sale of StarMedia securities to BellSouth and others, directly or indirectly, in the offer or sale of securities by the use of means or instruments of transportation or communication in interstate commerce or by use of the mails:

- a. with scienter, employed devices, schemes, or artifices to defraud;
- b. obtained money or property by means of untrue statements of a material fact or by omitting to state a material fact necessary in order to make the statements made, in light of the circumstances under which they were made, not misleading; or
- c. engaged in transactions, practices, or courses of business which operated or would operate as a fraud or deceit upon the purchaser.

126. By engaging in the conduct described above, each of defendants Espuelas, Chen, Heller, and Scolnik violated, and unless restrained and enjoined will continue to violate, Section 17(a) of the Securities Act [15 U.S.C. § 77q(a)].

SECOND CLAIM

**FRAUD IN CONNECTION WITH THE PURCHASE
OR SALE OF SECURITIES**

**Violations of Section 10(b) of the Exchange Act
and Rule 10b-5 thereunder
(Against Espuelas, Chen, Heller, Scolnik, Kampfner, and Möller)**

127. The Commission realleges and incorporates by reference ¶¶ 1 through 121 above.

128. Each of defendants Espuelas, Chen, Heller, and Scolnik, by engaging in the conduct described above, directly or indirectly, in connection with the purchase or sale of a security, by the use of means or instrumentalities of interstate commerce, of the mails, or of the facilities of a national securities exchange, with scienter:

- a. employed devices, schemes, or artifices to defraud;
- b. made untrue statements of a material fact or omitted to state a material fact 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 other persons.

129. By engaging in the conduct described above, each of defendants Espuelas, Chen, Heller, and Scolnik violated, and unless restrained and enjoined will continue to violate, Section 10(b) of the Exchange Act [15 U.S.C. § 78j(b)] and Rule 10b-5 thereunder [17 C.F.R. § 240.10b-5].

130. Each of Defendants Kampfner and Möller knowingly or recklessly provided substantial assistance to StarMedia's violations of Section 10(b) of the Exchange Act [15 U.S.C. § 78j(b)] and Rule 10b-5 thereunder [17 C.F.R. § 240.10b-5].

131. By engaging in the conduct described above and pursuant to Section 20(e) of the Exchange Act [15 U.S.C. § 78t(e)], defendants Kampfner and Möller each aided and abetted StarMedia's violations, and unless restrained and enjoined will continue to aid and

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

THIRD CLAIM

FRAUDULENT STOCK SALES

**Violations of Section 17(a) of the Securities Act,
Section 10(b) of the Exchange Act and Exchange Act Rule 10b-5
(Against Chen)**

132. The Commission realleges and incorporates by reference ¶¶ 1 through 123 above.

133. After concealing material information, resulting in false and misleading disclosures and financial statements in StarMedia's filings with the Commission, and after providing false statements to analysts and shareholders, Chen knowingly or recklessly sold StarMedia common stock, in breach of a duty that he owed to StarMedia and its shareholders.

134. By reason of the foregoing, Chen directly or indirectly, violated Section 17(a) of the Securities Act [15 U.S.C. § 77q(a)], Section 10(b) of the Exchange Act [15 U.S.C. § 78j(b)], and Exchange Act Rule 10b-5 [17 C.F.R. § 240.10b-5].

FOURTH CLAIM

REPORTING VIOLATIONS

**Aiding and Abetting Violations of Section 13(a) of the Exchange Act
and Rules 12b-20, 13a-1, and 13a-13 thereunder
(Against Espuelas, Chen, Heller, Scolnik, Kampfner, Morales, Möller, and Blacker)**

135. The Commission realleges and incorporates by reference ¶¶ 1 through 121 above.

136. StarMedia violated Section 13(a) of the Exchange Act [15 U.S.C. § 78m(a)] and Exchange Act Rules 12b-20, 13a-1, and 13a-13 [17 C.F.R. §§ 240.12b-20, 240.13a-1, and

240.13a-13], by filing with the Commission a materially false and misleading annual Report on Form 10-K for its fiscal year 2000 and materially false and misleading quarterly Reports on Form 10-Q for the first two quarters of 2001.

137. Defendants Espuelas, Chen, Heller, Scolnik, Kampfner, Morales, Möller, and Blacker, and each of them, acted with knowledge or recklessly, and thereby knowingly provided substantial assistance to one or more of StarMedia's violations of Section 13(a) of the Exchange Act [15 U.S.C. § 78m(a)] and Exchange Act Rules 12b-20, 13a-1, and 13a-13 [17 C.F.R. §§ 240.12b-20, 240.13a-1, and 240.13a-13].

138. By engaging in the conduct described above and pursuant to Section 20(e) of the Exchange Act [15 U.S.C. § 78t(e)], each of defendants Espuelas, Chen, Heller, Scolnik, Kampfner, Morales, Möller, and Blacker aided and abetted one or more of StarMedia's violations, and unless restrained and enjoined will continue to aid and abet violations, of Section 13(a) of the Exchange Act [15 U.S.C. § 78m(a)] and Exchange Act Rules 12b-20, 13a-1, and 13a-13 [17 C.F.R. §§ 240.12b-20, 240.13a-1, and 240.13a-13].

FIFTH CLAIM

RECORD-KEEPING VIOLATIONS

**Aiding and Abetting Violations of Section 13(b)(2)(A)
of the Exchange Act
(Against Espuelas, Chen, Heller, Scolnik, Kampfner, Morales, Möller, and Blacker)
and Violations of Rule 13b2-1 thereunder
(Against Espuelas, Chen, Scolnik, Kampfner, Morales, Möller, and Blacker)**

139. The Commission realleges and incorporates by reference ¶¶ 1 through 121 above.

140. StarMedia violated Section 13(b)(2)(A) of the Exchange Act

[15 U.S.C. § 78m(b)(2)(A)] by failing to make or keep books, records, and accounts that in reasonable detail accurately and fairly reflected its transactions and disposition of its assets.

141. Each of defendants Espuelas, Chen, Heller, Scolnik, Kampfner, Morales, Möller, and Blacker acted with knowledge or recklessly, and thereby knowingly provided substantial assistance to StarMedia's violations of Section 13(b)(2)(A) of the Exchange Act [15 U.S.C. § 78m(b)(2)(A)] .

142. By engaging in the conduct described above, each of defendants Espuelas, Chen, Heller, Scolnik, Kampfner, Morales, Möller, and Blacker aided and abetted StarMedia's violations, and unless restrained and enjoined will continue to aid and abet violations, of Section 13(b)(2)(A) of the Exchange Act [15 U.S.C. § 78m(b)(2)(A)].

143. By engaging in the conduct described above, each of defendants Espuelas, Chen, Scolnik, Kampfner, Morales, Möller, and Blacker violated Exchange Act Rule 13b2-1 [17 C.F.R. § 240.13b2-1] by, directly or indirectly, falsifying or causing to be falsified StarMedia's books, records, and accounts subject to Section 13(b)(2)(A) of the Exchange Act [15 U.S.C. § 78m(b)(2)(A)]. Unless restrained and enjoined, defendants will continue to violate Exchange Act Rule 13b2-1 [17 C.F.R. § 240.13b2-1].

SIXTH CLAIM

FALSE STATEMENTS TO AUDITORS

Violation of Exchange Act Rule 13b2-2 (Against Chen, Heller, and Morales)

144. The Commission realleges and incorporates by reference ¶¶ 1 through 121 above.

145. By engaging in the conduct described above, each of defendants Chen, Heller, and Morales violated Rule 13b2-2 of the Exchange Act [17 C.F.R. § 240.13b2-2] by directly or indirectly making or causing to be made materially false or misleading statements or omitting to state, or causing another person to omit to state, material facts necessary in order to make the statements made, in light of the circumstances under which such statements were made, not misleading to an accountant in connection with an audit, review, or examination of an issuer's financial statements required to be made by the Exchange Act, or the preparation or filing of a document or report required to be filed with the Commission. Unless restrained and enjoined, defendants Chen, Heller, and Morales will continue to violate Exchange Act Rule 13b2-2 [17 C.F.R. § 240.13b2-2].

PRAYER FOR RELIEF

WHEREFORE, the Commission respectfully requests that this Court enter Orders:

A. Permanently restraining and enjoining Espuelas from violating Section 17(a) of the Securities Act [15 U.S.C. § 77q(a)] and Section 10(b) of the Exchange Act [15 U.S.C. § 78j(b)] and Exchange Act Rules 10b-5 and 13b2-1 [17 C.F.R. §§ 240.10b-5, 240.13b2-1]; and aiding and abetting violations of Sections 13(a) and 13(b)(2)(A) of the Exchange Act [15 U.S.C. §§ 78m(a), 78m(b)(2)(A)] and Exchange Act Rules 12b-20, 13a-1, and 13a-13 [17 C.F.R. §§ 240.12b-20, 240.13a-1, and 240.13a-13];

B. Permanently restraining and enjoining Chen from violating Section 17(a) of the Securities Act [15 U.S.C. § 77q(a)] and Section 10(b) of the Exchange Act [15 U.S.C. § 78j(b)] and Exchange Act Rules 10b-5, 13b2-1, and 13b2-2 [17 C.F.R. §§ 240.10b-5, 240.13b2-1, 240.13b2-2]; and aiding and abetting violations of Sections 13(a) and 13(b)(2)(A) of the

Exchange Act [15 U.S.C. §§ 78m(a), 78m(b)(2)(A)] and Exchange Act Rules 12b-20, 13a-1, and 13a-13 [17 C.F.R. §§ 240.12b-20, 240.13a-1, and 240.13a-13];

C. Permanently restraining and enjoining Heller from violating Section 17(a) of the Securities Act [15 U.S.C. § 77q(a)] and Section 10(b) of the Exchange Act [15 U.S.C. § 78j(b)] and Exchange Act Rules 10b-5 and Rule 13b2-2 [17 C.F.R. §§ 240.10b-5, 240.13b2-2]; and aiding and abetting violations of Sections 13(a) and 13(b)(2)(A) of the Exchange Act [15 U.S.C. §§ 78m(a), 78m(b)(2)(A)] and Exchange Act Rules 12b-20, 13a-1, and 13a-13 [17 C.F.R. §§ 240.12b-20, 240.13a-1, and 240.13a-13];

D. Permanently restraining and enjoining Morales from violating Exchange Act Rule 13b2-1 [17 C.F.R. § 240.13b2-1]; and aiding and abetting violations of Sections 13(a) and 13(b)(2)(A) of the Exchange Act [15 U.S.C. §§ 78m(a), 78m(b)(2)(A)] and Exchange Act Rules 12b-20, 13a-1, and 13a-13 [17 C.F.R. §§ 240.12b-20, 240.13a-1, and 240.13a-13];

E. Permanently restraining and enjoining Möller from violating Exchange Act Rule 13b2-1 [17 C.F.R. § 240.13b2-1]; and aiding and abetting violations of Sections 10(b), 13(a), and 13(b)(2)(A) of the Exchange Act [15 U.S.C. §§ 78j(b), 78m(a), 78m(b)(2)(A)] and Exchange Act Rules 10b-5, 12b-20, 13a-1, and 13a-13 [17 C.F.R. §§ 240.10b-5, 240.12b-20, 240.13a-1, and 240.13a-13];

F. Permanently restraining and enjoining Scolnick from violating Section 17(a) of the Securities Act [15 U.S.C. § 77q(a)] and Section 10(b) of the Exchange Act [15 U.S.C. § 78j(b)] and Exchange Act Rules 10b-5 and 13b2-1 [17 C.F.R. §§ 240.10b-5, 240.13b2-1]; and aiding and abetting violations of Sections 13(a) and 13(b)(2)(A) of the Exchange Act [15 U.S.C. §§ 78m(a), 78m(b)(2)(A)] and Exchange Act Rules 12b-20, 13a-1, and 13a-13

[17 C.F.R. §§ 240.12b-20, 240.13a-1, and 240.13a-13];

G. Permanently restraining and enjoining Kampfner from violating Exchange Act Rule 13b2-1 [17 C.F.R. § 240.13b2-1]; and aiding and abetting violations of Sections 10(b), 13(a), and 13(b)(2)(A) of the Exchange Act [15 U.S.C. §§ 78j(b), 78m(a), 78m(b)(2)(A)] and Exchange Act Rules 10b-5, 12b-20, 13a-1, and 13a-13 [17 C.F.R. §§ 240.10b-5, 240.12b-20, 240.13a-1, and 240.13a-13];

H. Permanently restraining and enjoining Blacker from violating Exchange Act Rule 13b2-1 [17 C.F.R. § 240.13b2-1]; and aiding and abetting violations of Sections 13(a) and 13(b)(2)(A) of the Exchange Act [15 U.S.C. §§ 78m(a), 78m(b)(2)(A)] and Exchange Act Rules 12b-20, 13a-1, and 13a-13 [17 C.F.R. §§ 240.12b-20, 240.13a-1, and 240.13a-13];

I. Imposing civil monetary penalties on each of Espuelas, Chen, Heller, and Scolnik pursuant to Section 20(d) of the Securities Act [15 U.S.C. § 77t(e)];

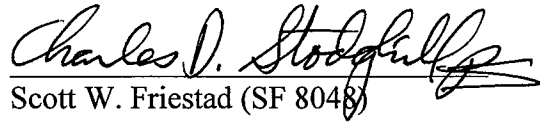
J. Imposing civil monetary penalties on each of Espuelas, Chen, Heller, Scolnik, Kampfner, Morales, and Blacker pursuant to Section 21(d) of the Exchange Act [15 U.S.C. § 78u(d)];

K. Prohibiting, pursuant to Section 20(e) of the Securities Act [15 U.S.C. § 77t(e)] and Section 21(d) of the Exchange Act [15 U.S.C. § 78u(d)], each of Espuelas, Chen, Heller, and Scolnik, and pursuant to Section 21(d) of the Exchange Act [15 U.S.C. § 78u(d)], Kampfner, from acting as an officer or a 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)];

L. Ordering Chen to disgorge all ill-gotten gains, with prejudgment interest, from the illicit sales of his StarMedia common stock; and

M. Granting such other and additional relief as this Court may deem just and proper.

Dated: December 9, 2008



Scott W. Friestad (SF 8048)

David Frohlich

Paul W. Sharratt

Charles D. Stodghill (Lead Trial Attorney)

100 F Street, N.E .

Washington, D.C. 20549-4010A

(202) 551-4413 (Stodghill)

(202) 772-9246 (Stodghill fax)

Attorneys for Plaintiff

Securities and Exchange Commission