

UNITED STATES DISTRICT COURT
FOR THE
DISTRICT OF COLUMBIA

FILED

OCT 27 1999

NANCY MAYER WHITTINGTON, CLERK
U.S. DISTRICT COURT

SECURITIES AND EXCHANGE COMMISSION
450 Fifth Street, N.W.
Washington, DC 20549

Plaintiff,

v.

KENNETH SILVERMAN
160 Jeremy Hill Road
Pelham, NH 03076

Defendant.

CASE NUMBER 1:99CV02844

JUDGE: Gladys Kessler

Civil

DECK TYPE: Civil General

DATE STAMP: 10/27/1999

United States District Court
For the District of Columbia
A TRUE COPY
NANCY MAYER WHITTINGTON, Clerk
By Cahin P. Orange
6/10/03 Deputy Clerk

COMPLAINT

Plaintiff Securities and Exchange Commission ("Commission" or "SEC") alleges:

INTRODUCTION

1. The SEC brings this action to enjoin Defendant Kenneth Silverman ("Silverman") from further violations of the registration provisions of the federal securities laws, to recover Silverman's ill-gotten gains, and to impose a civil monetary penalty for his conduct.

2. In three separate transactions between August 1995 and March 1996, Silverman acquired a total of 2,716,897 shares of newly-issued Systems of Excellence, Inc. ("SOE") stock at a total cost of \$600,000. In each instance, Silverman soon sold all or most of those shares for profits totaling \$2,457,718. Because the shares sold were neither registered nor exempt from registration, Silverman violated the registration provisions of the federal securities laws.

3. Silverman, directly or indirectly, has engaged in transactions, acts, practices, and courses of business which constitute violations of Sections 5(a) and 5(c) of the Securities Act of

1933 (“Securities Act”) [15 U.S.C. §§ 77e(a) and 77e(c)], and, unless enjoined, is likely to do so in the future.

JURISDICTION AND VENUE

4. This Court has jurisdiction over this action pursuant to Section 22(a) of the Securities Act [15 U.S.C. § 77v(a)].

5. The Commission brings this action pursuant to authority conferred upon it by Sections 20(b) and 20(d) of the Securities Act [15 U.S.C. §§ 77t(b) and 77t(d)].

6. Defendant, directly and indirectly, used the means and instrumentalities of interstate commerce, of the mails, or of the facilities of a national securities exchange, in connection with the acts, practices, and courses of business alleged herein.

DEFENDANT

7. Kenneth Silverman (“Silverman”), age 51, is a self-employed professional securities trader. In account opening documents at various brokerage firms, Silverman indicated that he possessed a “high” degree of experience in the areas of stock, option, and bond trading.

OTHER INDIVIDUALS AND ENTITIES

8. Systems of Excellence, Inc. (“SOE” or the “Company”), was a Florida corporation that, at the relevant time, was purportedly engaged in the manufacture and distribution of dental software and then video teleconferencing equipment, and its stock was quoted on the National Association of Securities Dealers’ OTC Bulletin Board. SOE is currently in bankruptcy liquidation proceedings.

9. Charles O. Huttoe (“Huttoe”) was formerly the Chairman and Chief Executive

Officer of SOE. In a prior action filed with this Court on November 7, 1996 (styled SEC v. Huttoe, et al., Civ. Act. No. 96-2543 (GK)(D.D.C.)), plaintiff accused Huttoe of violating the antifraud provisions of the federal securities laws for his role in a massive market manipulation of SOE securities during the period from March 1995 through October 7, 1996. Huttoe consented to the entry of a civil injunction and, in a related criminal case, pleaded guilty to securities fraud and money laundering.

10. Sheldon Kraft (“Kraft”) is a former stockbroker who acted as a promoter for SOE. In a prior action filed with this Court on January 14, 1998 (styled SEC v. Kraft, Civ. Act. No. 98-0095 (GK) (D.D.C.)), plaintiff accused Kraft of violating the antifraud provisions of the federal securities laws for his conduct relating to SOE. Kraft consented to the entry of a civil injunction and, in a related criminal case, pleaded guilty to conspiracy to commit securities fraud, money laundering, and failure to file tax returns.

CLAIM

SILVERMAN’S SALE OF UNREGISTERED SOE SECURITIES VIOLATED SECTIONS 5(a) AND 5(c) OF THE SECURITIES ACT

11. Sections 5(a) and 5(c) of the Securities Act prohibit persons, directly or indirectly, from using any means or instruments of transportation or communication in interstate commerce or of the mails to sell, offer to sell, or offer to buy any security unless: (i) a registration statement has been filed with the Commission and is in effect, or (ii) an exemption from the registration provisions applies.

July and August 1995
Silverman is Introduced to Huttoe and Purchases 810,000 SOE Shares

12. In July 1995, Kraft introduced Silverman to Huttoe, who was seeking investors in SOE, at that time a dental software company which Huttoe and Kraft were promoting.

13. On August 14, 1995, Silverman purchased 810,000 SOE shares directly from the Company at \$.185 per share for a total purchase price of \$150,000.

14. Although these 810,000 privately placed shares were not registered, they were issued without a restrictive legend after SOE, acting through Huttoe, presented its transfer agent with an S-8 Registration Statement that falsely described Silverman as "PR Professional" retained to promote the business of SOE. Attached to the S-8 was a cover letter falsely reflecting that the S-8 Registration Statement had been filed with the Commission on or about August 8, 1995.

15. In fact, no S-8 Registration Statement for these shares had been filed with the SEC when the shares were issued to Silverman nor had Silverman ever acted as a "PR Professional" or promoter for SOE.

16. From August 11 to August 17, 1995, Silverman sold all 810,000 shares into the market for \$241,500, realizing profits of \$91,500.

17. The false S-8 Registration Statement purporting to register the 810,000 shares issued to Silverman on August 14, 1995 was not filed with the Commission until December 1, 1995 -- after the shares were issued to Silverman, and after he had sold them into the market.

December 1995 and January 1996
Silverman Loans SOE Cash in Exchange for more SOE Shares

18. In December 1995, Kraft and Huttoe solicited Silverman to make another investment in SOE, which needed capital for its acquisition of a private company engaged in the video teleconferencing industry.

19. On January 4, 1996, Silverman loaned \$200,000 to SOE, to be repaid with interest in one month. As additional consideration for making this loan, the Company also gave Silverman 700,000 SOE shares on January 25, 1996.

20. SOE's transfer agent issued these 700,000 shares without restriction based, once again, on correspondence from SOE indicating that the shares had been properly registered on an S-8 Registration Statement.

21. In fact, the 700,000 shares issued to Silverman on January 25, 1996 were not registered with the Commission and were not otherwise exempt from registration.

22. On or about February 5, 1996, SOE repaid Silverman the entire \$200,000 principal amount of the loan he made a month earlier.

23. In a series of transactions between January 24 and May 3, 1996, Silverman sold all of these newly-acquired 700,000 shares into the market, realizing profits of \$390,913.

January to March 1996
Silverman Purchases 1,206,897 Shares in SOE's "Private Placement"

24. In January 1996, as an additional means of raising capital for the Company, Huttoe arranged for SOE to make a \$1 million offering through a private placement of SOE stock. These SOE shares were offered and sold to investors pursuant to a Confidential Private Placement

Memorandum (“CPPM”).

25. Pursuant to the CPPM, investors were offered Units, which consisted of a one-year note in the amount of their investment plus 10% interest payable semi-annually, and an opportunity to acquire SOE shares at no additional cost to the investor.

26. Purchasers of Units were supposed to complete a Subscription Agreement and Questionnaire, in which purchasers represented, among other things, that they had read and understood the CPPM, that they understood that the Units had not been registered under the Securities Act, and that the Units were not being acquired with a view to distribution. In addition, the CPPM stated the following:

ALL INVESTORS WILL BE REQUIRED TO UNDERTAKE THAT THEY WILL NOT RESELL THE UNITS EXCEPT IN A TRANSACTION WHICH IS PURSUANT TO REGISTRATION UNDER THE 1933 ACT OR WHICH DOES NOT REQUIRE REGISTRATION UNDER THE 1933 ACT.

27. As Huttoe and others began marketing the private placement, Kraft approached Silverman about investing in the private placement. Initially there was little interest by investors, including Silverman, in the private placement. As the manipulation of the market for SOE gained momentum, the shares to be issued to private placement investors gained a market value in excess of the loan amount, and demand for the offering increased.

28. Thereafter, Silverman and Huttoe discussed the prospect of Silverman investing in the private placement. Huttoe agreed to allow Silverman to invest \$250,000 pursuant to the CPPM, which carried with it 1,206,897 shares of SOE. Those shares had a market value of nearly \$1 million at the time they were issued to Silverman.

29. In March 1996, Silverman obtained a copy of the CPPM and learned that the

shares he was to receive in the private placement would be restricted from resale for one year. Silverman contacted Kraft and Huttoe to voice his dissatisfaction with the trading restriction.

30. Silverman obtained Huttoe's agreement that Silverman would receive free trading stock, which Huttoe intended to accomplish by preparing an S-8 Registration Statement in which Silverman would be described as a "consultant" for SOE. Because Silverman was infusing capital into the company and was not rendering any services to SOE, his shares were not eligible for registration on Form S-8.

31. The 1,206,897 shares Silverman received for his investment in the private placement were purportedly registered with the Commission on an S-8 Registration Statement dated September 26, 1996. But, as with all other SOE shares issued to Silverman, this false S-8 Registration Statement was not filed with the Commission until well after the transfer agent issued the shares to Silverman.

32. Silverman began to sell the shares that he purchased in the private placement on May 6, 1996. By October 7, 1996, when the Commission suspended trading in the securities of SOE, Silverman had sold 945,500 of the 1,206,897 shares for proceeds of \$2,225,305, realizing a profit of \$1,975,305.

33. Since at least August 1995 and continuing through October 1, 1996, Defendant Silverman, directly or indirectly:

(a) made use of the means or instruments of transportation or communication in interstate commerce or of the mails to sell securities as described herein, through the use or medium of a prospectus or otherwise;

(b) carried securities or caused such securities, as described herein, to be carried through the mails or in interstate commerce, by any means or instruments of transportation, for the purpose of sale or delivery after sale; and/or

(c) made use of the means or instruments of transportation or communication in interstate commerce or of the mails to offer to sell or offer to buy through the use or medium of any prospectus or otherwise, as described herein,

without a registration statement having been filed or being in effect with the Commission as to such securities.

34. By reason of the foregoing, Defendant Silverman violated Sections 5(a) and 5(c) of the Securities Act [15 U.S.C. §§ 77e(a) and 77e(c)].

RELIEF REQUESTED

WHEREFORE, the SEC respectfully requests that the Court issue an Order:

A. permanently enjoining and restraining Defendant Silverman, his officers, agents, servants, employees, attorneys, and all persons in active concert or participation with them, and each of them, from violating Sections 5(a) and 5(c) of the Securities Act [15 U.S.C. §§ 77e(a) and 77e(c)];

B. requiring Silverman to disgorge \$2,457,718, representing all profits or proceeds that he received as a result of the acts and/or courses of conduct complained of herein, together with prejudgment interest of \$462,494;

C. directing Defendant Silverman to pay civil penalties pursuant to Section 20(d) of the Securities Act, 15 U.S.C. § 77t(d) in the amount of \$50,000; and

D. granting such other and further relief as may be necessary and appropriate.

Respectfully submitted,



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Dated: October 27, 1999
Washington, D.C.