

UNITED STATES DISTRICT COURT
DISTRICT OF COLUMBIA

FILED

SEP - 9 2010

Clerk, U.S. District & Bankruptcy
Courts for the District of Columbia

SECURITIES AND EXCHANGE COMMISSION,
100 F Street N.E. Washington D.C. 20549

Plaintiff,

vs.

AFFILIATED COMPUTER SERVICES, INC.,

Defendant.

Civil Action No.

COMPLAINT

ECF CASE

Case: 1:10-cv-01515

Assigned To : Sullivan, Emmet G.

Assign. Date : 9/9/2010

Description: General Civil

Plaintiff Securities and Exchange Commission (the "Commission") alleges as follows:

SUMMARY

1. During the period from 1995 through 2006, Affiliated Computer Services, Inc. ("ACS" or the "company"), through the conduct of two of its former senior officers, one of whom served at various times as Chief Executive Officer, Chief Operating Officer, and Chief Financial Officer (the former "CEO"), while the other served at various times as Chief Financial Officer and Senior Vice President of Finance and Accounting (the former "CFO"), engaged in a fraudulent and deceptive scheme to provide executives and other employees undisclosed compensation.¹ The former CEO and CFO backdated the grant dates of ACS stock options to coincide with the dates of low closing prices for the company's stock, resulting in disguised "in-the-money" option grants.

¹ Both the former CEO and the former CFO referred to herein entered into separation agreements with ACS, which provided that they would resign their positions as officers on or about November 26, 2006 and further provided that their employment with ACS would terminate on or about June 30, 2007.

2. The former CEO and CFO approved the filing of periodic reports with the Commission that they knew, or were reckless in not knowing, failed to include the compensation expenses associated with the “in-the-money” portions of the grants. The reports also falsely stated that ACS complied with stock option accounting rules and, in certain cases, stated that ACS granted options at the fair market value of the company’s stock on the grant date.

3. On January 23, 2007, ACS restated its financial results for the first three quarters of the fiscal year ended June 30, 2006, each of the quarters of the fiscal year ended June 30, 2005 and each of the fiscal years ended June 30, 2005 and June 30, 2004, as well as the selected consolidated financial data for the fiscal years ended June 30, 2003 and 2002. ACS’s restatement recorded \$51 million in compensation expenses for 72 of the 73 option grants it awarded between 1994 and 2005. ACS intentionally backdated many of these grants and failed to record any required compensation expense. The former CEO and CFO backdated the option grants by looking back at historical stock prices to pick a date coinciding with a low point in the company’s stock price and using that date as the purported grant date. After stock options backdating became a public scandal in early 2006, ACS, through the former CEO and CFO, made materially false disclosures, including in two ACS filings with the Commission, denying that intentional backdating had ever occurred at ACS.

4. By virtue of the foregoing, ACS engaged in acts, practices and courses of business that violated Section 17(a) of the Securities Act [15 U.S.C. § 77q(a)], Sections 10(b), 13(a), 13(b)(2)(A), and 13(b)(2)(B) of the Exchange Act [15 U.S.C. §§ 78j(b), 15 U.S.C. §§ 78m(a), 78m(b)(2)(A) and 78m(b)(2)(B)] and Exchange Act Rules 10b-5, 13a-

1, 13a-13, and 12b-20 [17 C.F.R. §§ 240.10b-5, 240.13a-1, 240.13a-13, 240.12b-20].

Unless enjoined, ACS is likely to commit such violations in the future.

JURISDICTION AND VENUE

5. This Court has jurisdiction over this action pursuant to Sections 20(b) and 22(a) of the Securities Act [15 U.S.C. §§ 77t(b) and 77v(a)], and Sections 21(d), 21(e) and 27 of the Exchange Act [15 U.S.C. §§ 78u(d), 78u(e) and 78aa]. The defendant, directly or indirectly, has made use of 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 in this Complaint.

6. This district is an appropriate venue for this action under Section 22 of the Securities Act [15 U.S.C. § 77v] and Section 27 of the Exchange Act [15 U.S.C. § 78aa], because certain of the acts alleged herein constituting violations of the Securities Act and the Exchange Act occurred in this District, including, ACS's filing of materially false and misleading annual and quarterly reports, and other documents with the Commission in the District of Columbia.

DEFENDANT

7. Prior to February 2010, ACS was a Fortune 500 company in the business of providing business process and information technology services to commercial and government clients. ACS was incorporated in Delaware in 1988 and based in Dallas, Texas. At the time of the conduct described in this Complaint, ACS's common stock was registered with the Commission pursuant to Section 12(b) of the Exchange Act and was listed on the New York Stock Exchange. ACS's fiscal year ended on June 30.

8. On or about February 5, 2010, ACS was acquired by Xerox Corporation (“Xerox”). ACS is now a non-trading, wholly-owned subsidiary of Xerox that functions as a legal entity under the name Affiliated Computer Services, Inc., and is not a separate reporting entity.

FACTS

A. ACS Stock Option Plan

9. The company granted stock options to its employees pursuant to shareholder-approved stock option plans. ACS’s 1988 Stock Option Plan (as amended and restated on August 30, 1990) required that for Nonstatutory Stock Options “the per Share exercise price shall be no less than 85% of the Fair Market Value per Share on the date of grant.” ACS’s 1997 Stock Incentive Plan provided that in “the case of a Nonstatutory Stock Option granted to any person the per Share exercise price shall be determined by the Administrator.”

B. Accounting for Employee Stock Options

10. Generally Accepted Accounting Principles (“GAAP”), and in particular Accounting Principles Board Opinion No. 25, *Accounting for Stock Issued to Employees* (“APB 25”), did not require a company to record any compensation expense for employee stock options so long as the option exercise price was not below the stock’s market price on the date of the grant. Under APB 25, employers were required to record as an expense on their financial statements the “intrinsic value” of a fixed stock option on its “measurement date.” The measurement date, as defined by APB 25, is the first date on which the following information is known: (i) the number of options that an individual employee is entitled to receive, and (ii) the exercise price.

11. An employee option granted with an exercise price lower than the quoted market price of the company's stock on the date of grant (an "in-the-money" option) has "intrinsic value," and thus the difference between the exercise price and the quoted market price of the company's stock must be recorded as compensation expense to be recognized over the vesting period of the option. Options that are at-the-money or out-of-the-money on the measurement date need not be expensed.

C. Stock Option Grant Process

12. During the period described herein, the stock option grant process at ACS generally began when ACS's Chairman of the Board ("Chairman") decided that the time was right to grant stock options. For grants to ACS executives, the Chairman obtained oral approval for the grants from ACS's Compensation Committee, then one or more of the former senior executives completed the paperwork necessary to effect the grants. For option grants to non-executive employees, one or more of the former senior executives determined the grant recipients and amounts of options for each grantee and completed the paperwork necessary to effect the grants without the Chairman first seeking approval from ACS's Compensation Committee.

13. The former CEO, CFO or, at times, other individuals participated in preparing a "Recommendation Memo" to ACS's Compensation Committee specifying the grant date, exercise price, and recipients for the option grant. Some Recommendation Memoranda were signed by both the Chairman and the CEO at the time and others were signed by just the Chairman. Once signed, each Recommendation Memo was sent to ACS's Legal Department for transmittal to ACS's Compensation Committee. ACS's Legal Department sent each Compensation Committee member the Recommendation

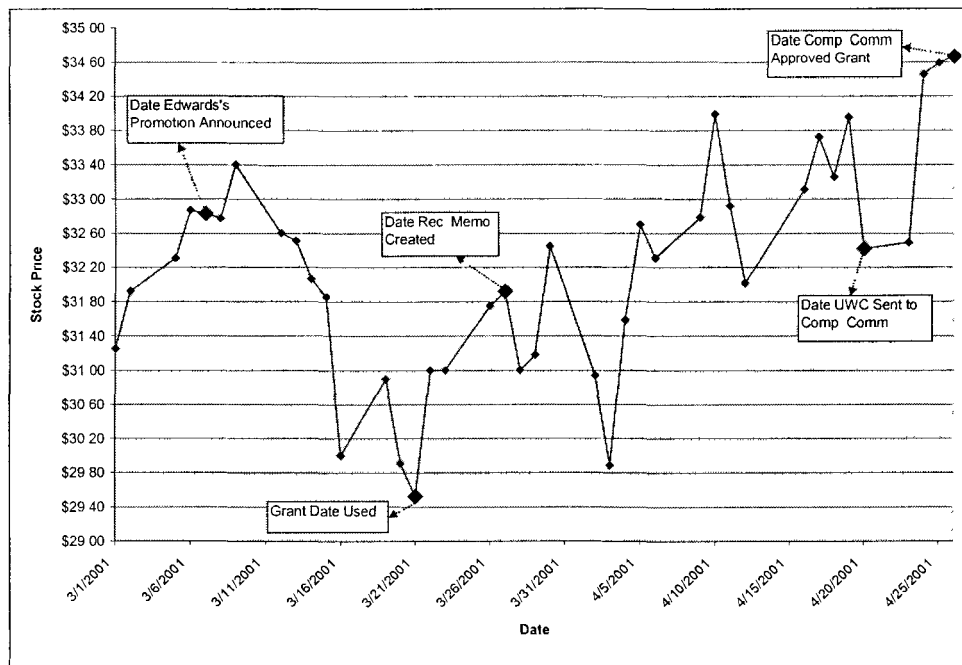
Memo and a Unanimous Written Consent (“UWC”) dated “as of” the grant date specified on the Recommendation Memo. For example, the UWC for the May 18, 2001 grant read: “[T]he undersigned constituting all of the members of the Special Compensation Committee, have executed this Consent to be effective as of May 18, 2001.” The Compensation Committee members approved each option grant by signing the UWC and returning it to ACS’s Legal Department.

14. After the Chairman gave instructions to initiate the option grant process, the former CEO and CFO would wait before taking further action to effect certain grants so that they could look back in time to pick a grant date with an advantageous strike price.

15. At that point, the former CEO, CFO or, at times, another former executive, created, or instructed a lower-level employee (“Employee”) to create, a Recommendation Memo for the Compensation Committee. The former CEO or CFO told the Employee what the grant date should be for each Recommendation Memo. The former CEO instructed the Employee in 2000 to date the Recommendation Memo the day immediately following the recorded grant date, despite the fact that in many cases he was not asked to create the Recommendation Memo until a much later point in time.

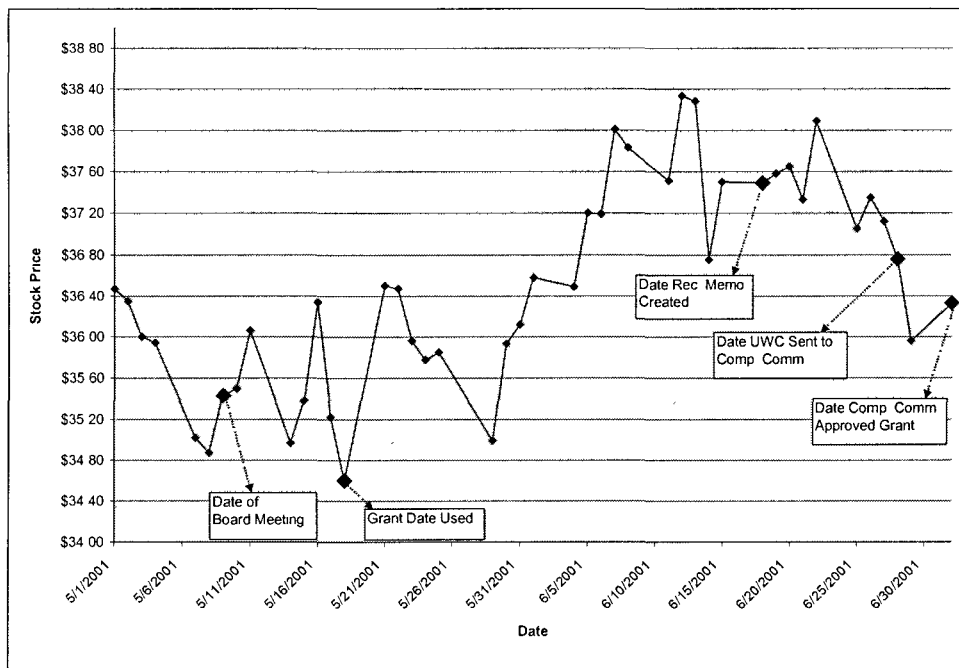
16. Through these actions, ACS intentionally backdated numerous grants and failed to record any required compensation expense. Each of these grants was backdated to a date corresponding to a relative low point in the trading of the company’s stock. The manner by which the backdating scheme was carried out is illustrated by the following three grants:

a. **March 21, 2001 Option Grant**



17. ACS's March 21, 2001 option grant to senior executives was backdated by at least six days. The grant was partly made in connection with the former CFO's promotion. The promotion was publicly announced on March 7, 2001. The Employee created a Recommendation Memo for the grant dated March 22, 2001 and recommending a grant date of March 21, 2001. The Employee did not create the Recommendation Memo until March 27, 2001. In ACS's files, there was a stock price print-out dated March 27, 2001, the same day the Recommendation Memo was created, showing that the March 21, 2001 grant date was at the lowest price between the date of the promotion and the Recommendation Memo create date. The Recommendation Memo was not transmitted to the Compensation Committee until April 2, 2001 and was not approved by the Compensation Committee until April 26, 2001.

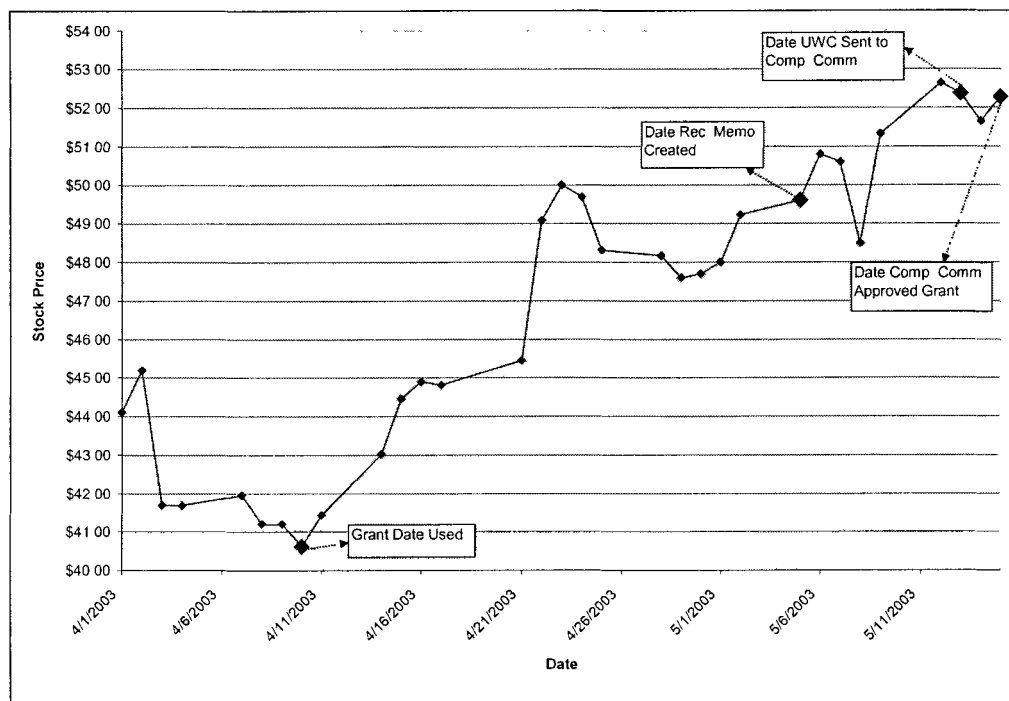
b. May 18, 2001 Option Grant



18. ACS's May 18, 2001 option grant to non-executive employees was backdated by 31 days. On June 20, 2001, the former CFO sent an email to another ACS employee attaching a draft Recommendation Memo for an option grant with a May 18, 2001 grant date. The Recommendation Memo was created on June 18, 2001. The email stated, "here is the draft of the stock option grant memo. The new price is \$69.20 (lowest price subsequent to the BOD meeting)." The former CFO could not have known the "lowest price" subsequent to the Board meeting (which occurred on May 9, 2001) and before June 18, 2001 without looking back in time. Consistent with this fact, the former CFO maintained a list of ACS's daily stock price from May 8, 2001 to June 18, 2001 on which the May 18 stock price was circled for selection as the "grant date." The stock price on May 18 was the lowest price in the six week period from the time of the most recent board meeting to the date on which the Recommendation Memo was created. The stock option grant documentation was not transmitted to the Compensation Committee

until June 28, 2001 and the grant was not approved by all of the members of the Compensation Committee until July 2, 2001.

c. April 10, 2003 Option Grant



19. ACS's April 10, 2003 option grant to non-executive employees was backdated by at least 25 days. The Employee created a Recommendation Memo, with the former CEO in the "from" line, dated April 11, 2003 and recommending a grant date of April 10, 2003. On May 5, 2003, the Employee e-mailed the former CEO saying that the former CFO "asked that I prepare a short option grant list and have you review . . . [d]o you have any changes before I finalize a recommendation memo to send to [the former CFO] by end of day." The former CEO responded that same day "looks okay. I'd finalize it." The Recommendation Memo was not created until the same date as this e-mail, May 5, 2003. The April 10, 2003 date ultimately used for this grant was the lowest price in the quarter. The Recommendation Memo was not transmitted to the

Compensation Committee until May 13, 2003 and was not approved by the Compensation Committee until May 15, 2003.

D. Materially False and Misleading Financial Statements and other Filings

20. As a public company, ACS was required to file with the Commission annual reports that included audited financial statements, certified by the company's outside auditors. ACS's annual reports affirmatively stated that the Company accounted for its stock options granted to employees in accordance with GAAP.

21. ACS's Forms 10-K filed with the Commission on September 30, 1996, September 29, 1997, September 28, 1998, September 28, 1999, September 28, 2000, August 27, 2001, September 18, 2002, September 17, 2003, September 13, 2004, and September 13, 2005, all state that ACS accounted for stock options in accordance with APB 25.

22. ACS's Forms 10-K filed with the Commission on September 29, 1997, September 28, 1998, September 28, 1999, September 28, 2000, August 27, 2001, September 18, 2002, September 17, 2003, September 13, 2004, and September 13, 2005, all state that as a result of accounting for stock options in accordance with APB 25, no compensation cost has been recognized.

23. ACS's Forms 10-K filed with the Commission on September 17, 2003, September 13, 2004 and September 13, 2005, all state that "under APB 25, no compensation expense is recognized for our stock-based compensation plans since the exercise prices of awards under our plans are at current market prices of our stock on the date of the grant."

24. Contrary to the representations in paragraphs 21, 22, and 23, ACS incurred material compensation expenses as a result of granting in-the-money employee stock options. ACS filed its restatement on January 23, 2007, recording \$51 million in compensation expense for a total of 72 grants out of the 73 grants granted from 1994 to 2005. The annual impacts of ACS's unrecorded compensation on net income for the 72 restated option grants are: .2% in 1995, 1.3% in 1996, 2.9% in 1997, 2.8% in 1998, 3.1% in 1999, 4.2% in 2000, 4.6% in 2001, 3.4% in 2002, 2.9% in 2003, 1.6% in 2004, 1.6% in 2005, and .9% in 2006.

25. In addition, ACS filed thirty-five quarterly reports between May 12, 1995 and May 15, 2006, which falsely reflect that ACS incurred no compensation expense for options granted to employees with exercise prices below the company's stock price on the date of grant, with the exception of one grant dated March 9, 1995.

26. ACS filed Forms S-3 on June 10, 1996, April 2, 1998, February 8, 1999 and November 15, 1999, March 30, 2001 and August 30, 2001 and a Form S-4 on November 17, 1997. These registration statements incorporated by reference materially false and misleading financial statements, as well as materially false and misleading disclosures, from ACS's annual reports on Form 10-K and quarterly reports on Form 10-Q.

27. As a result of the backdating misconduct, ACS's books and records falsely and inaccurately reflected, among other things, the dates of option grants, the Company's stock-based compensation expenses, and the Company's financial condition. In addition, ACS's former CEO and former CFO circumvented internal accounting controls and failed to maintain a system of internal accounting controls sufficient to provide

assurances that stock option grants were recorded as necessary to permit the proper preparation of financial statements in conformity with GAAP.

F. False Denials of Intentional Backdating in Public Statements and Filings After ACS Begins its Internal Investigation

28. In an April 27, 2006 ACS earnings call for investors concerning ACS's financial results for the period ended March 31, 2006, ACS's former CEO read a statement denying the "intentional granting of look-back stock options to executive officers and directors in order to achieve lower option exercise prices." The former CEO, who instigated the use of this language, and the former CFO both reviewed the script for the earnings call and were on the call. Though ACS's outside counsel at the time advised the former CFO not to make these representations because an internal investigation of the matter was still ongoing, the former CEO and the former CFO participated in and approved the decision to have the statement in the former CEO's presentation.

29. On May 10, 2006, ACS filed with the Commission a Form 12b-25 (Notification of Late Filing) explaining that it could not file its Form 10-Q for the quarter ended March 31, 2006 on time because of the volume of data to be reviewed in connection with its internal investigation into allegations of stock option backdating. ACS stated in this filing that "ACS does not believe that any director or officer of the Company has engaged in the intentional backdating of stock option grants in order to achieve a more advantageous exercise price." In this filing, ACS estimated that it would have to record a compensation expense of up to \$40 million as a consequence of revising the accounting measurement dates for option grants. Both the former CEO and the former CFO reviewed drafts of the filing and the former CFO signed the filing.

30. On May 15, 2006, ACS filed with the Commission its Form 10-Q for the quarter ended March 31, 2006. Note 3 to the financial statements of this filing repeats the statement approved by the former CEO and CFO that “ACS does not believe that any director or officer of the Company has engaged in the intentional backdating of stock option grants in order to achieve a more advantageous exercise price.” Both the former CEO and the former CFO reviewed the filing and the former CFO signed it.

31. Both the former CEO and the former CFO knew, or were reckless in not knowing, that the aforementioned statements were materially false and misleading.

32. On the morning of August 7, 2006, ACS filed a Form 8-K with the Commission attaching a press release, which stated that it believed that the internal investigation would be substantially complete by September 2006, that the ACS Audit Committee had engaged its own independent outside legal counsel in connection with the stock option investigation, and that the information set forth in Note 3 to its May 15, 2006 Form 10-Q concerning the stock option investigation “can no longer be relied upon” and “will be superseded by the Company’s updated announcement” concerning the investigation.

33. The materiality of ACS’s misrepresentations in its April 27, 2006 earnings call, May 10, 2006 Form 12b-25 and May 15, 2006 Form 10-Q is evidenced by the market’s reaction to the disclosures about ACS’s stock option investigation. As discussed above, on August 7, 2006 at 9:00 a.m., ACS filed its Form 8-K stating that investors could not rely on Note 3 of the May 2006 Form 10-Q, which in part stated that ACS did not believe that any officer or director of the company engaged in the

intentional backdating of stock option grants. That same day the company's stock price dropped 4.54%, while the S&P dropped only .36%.

FIRST CLAIM FOR RELIEF

Violations of Section 17(a) of the Securities Act by ACS

34. The Commission realleges and incorporates by reference Paragraphs 1 through 33, above.

35. As a result of the conduct described above, ACS, directly or indirectly, in the offer or sale of securities, by the use of the 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 omissions 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; and
- (c) engaged in transactions, practices, or courses of business which operated or would operate as a fraud or deceit upon purchasers of securities.

36. By reason of the foregoing, ACS has 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 FOR RELIEF

Violations of Section 10(b) of the Exchange Act and Rule 10b-5 Thereunder by ACS

37. The Commission realleges and incorporates by reference Paragraphs 1 through 33, above.

38. As a result of the conduct described above, ACS, with scienter, directly or indirectly, in connection with the purchase or sale of securities, by the use of means or instrumentalities of interstate commerce or of the mails, or of facilities of a national securities exchange:

(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; and

(c) engaged in acts, practices, or courses of business which operated or would operate as a fraud or deceit upon other persons, including purchasers and sellers of securities.

39. By reason of the foregoing, ACS has 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].

THIRD CLAIM FOR RELIEF

Violations of Section 13(a) of the Exchange Act and Rules 12b-20, 13a-1, and 13a-13 Thereunder by ACS

40. The Commission realleges and incorporates by reference Paragraphs 1 through 33, above.

41. Based on the conduct alleged in paragraphs 20 through 27, and 29 through 30 above, including filing with the Commission annual reports on Forms 10-K on September 28, 1995, September 30, 1996, September 29, 1997, September 28, 1998, September 28, 1999, September 28, 2000, August 27, 2001, September 18, 2002, September 17, 2003, September 13, 2004, and September 13, 2005 and quarterly reports

filed with the Commission between May 12, 1995 and May 15, 2006, ACS, through the misconduct of its former CEO and CFO, 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], which obligate issuers of securities registered pursuant to the Exchange Act to file with the Commission annual and quarterly reports that, among other things, do not contain untrue statements of material fact or omit to state material information necessary in order to make the statements made, in the light of the circumstances under which they were made, not misleading.

42. By reason of the foregoing, ACS has violated, and unless restrained and enjoined will continue to violate Section 13(a) of the Exchange Act, 15 U.S.C. § 78m(a), and Rules 12b-20, 13a-1, and 13a-13, 17 C.F.R. §§ 240.12b-20, 240.13a-1, and 240.13a-13.

FOURTH CLAIM FOR RELIEF

Violations of Section 13(b)(2)(A) of the Exchange Act by ACS

43. The Commission realleges and incorporates by reference Paragraphs 1 through 33, above.

44. Based on the conduct alleged in paragraphs 15, 20 through 27, and 29 through 30 above, including creating and filing with the Commission false annual and quarterly financial statements – annual reports on Form 10-K filed with the Commission on September 28, 1995, September 30, 1996, September 29, 1997, September 28, 1998, September 28, 1999, September 28, 2000, August 27, 2001, September 18, 2002, September 17, 2003, September 13, 2004, and September 13, 2005 and quarterly reports filed with the Commission between May 12, 1995 and May 15, 2006, false registration

statements – filed with the Commission on Aug. 30, 2001, March 30, 2001, Nov. 15, 1999, February 8, 1999, April 2, 1998, June 10, 1996, and November 17, 1997, and false documentation memorializing stock option grants, ACS, through the misconduct of its former CEO and CFO, violated Section 13(b)(2)(A) of the Exchange Act [15 U.S.C. § 78m(b)(2)(A)] which obligates issuers of securities registered pursuant to Section 12 of the Exchange Act [15 U.S.C. § 78l] to make and keep books, records, and accounts, which, in reasonable detail, accurately and fairly reflect the transactions and dispositions of the assets of the issuer.

45. By reason of the foregoing, ACS violated, and unless restrained and enjoined will continue to violate Section 13(b)(2)(A) of the Exchange Act [15 U.S.C. § 78m(b)(2)(A)].

FIFTH CLAIM FOR RELIEF

Violations of Section 13(b)(2)(B) of the Exchange Act by ACS

46. The Commission realleges and incorporates by reference Paragraphs 1 through 33, above.

47. Based on the conduct alleged above, ACS, through the misconduct of its former CEO and CFO, violated Section 13(b)(2)(B) of the Exchange Act [15 U.S.C. § 78m(b)(2)(B)] which obligates issuers of securities registered pursuant to Section 12 of the Exchange Act [15 U.S.C. § 78l] to devise and maintain a sufficient system of internal accounting controls.

48. By reason of the foregoing, ACS has violated, and unless restrained and enjoined will continue to violate Section 13(b)(2)(B) of the Exchange Act [15 U.S.C. § 78m(b)(2)(B)].

PRAYER FOR RELIEF

WHEREFORE, the Commission respectfully requests that this Court:

I.

Issue an order permanently restraining and enjoining ACS and its agents, servants, employees, attorneys, and assigns, and those persons in active concert or participation with them, 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 Rule 10b-5 [17 C.F.R. § 240.10b-5] and issue an order permanently restraining and enjoining ACS and its agents, servants, employees, attorneys, and assigns, and those persons in active concert or participation with them, from violating Sections 13(a), 13(b)(2)(A) and 13(b)(2)(B) of the Exchange Act [15 U.S.C. §§ 78m(a), 78m(b)(2)(A), and 78m(b)(2)(B)], and Exchange Act Rules 12b-20, 13a-1, 13a-13 [17 C.F.R. §§ 240.12b-20, 240.13a-1, and 240.13a-13].

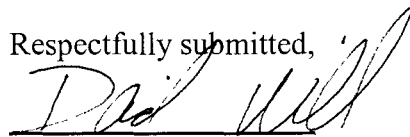
II.

Retain jurisdiction of this action in accordance with the principles of equity and the Federal Rules of Civil Procedure in order to implement and carry out the terms of all orders and decrees that may be entered, or to entertain any suitable application or motion for additional relief within the jurisdiction of this Court.

III.

Grant such other and further relief as this Court may determine to be just and necessary.

Respectfully submitted,



A. David Williams (California Bar No. 183854) ✓

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Dated: September 9, 2010