

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

**RECEIVED**

AUG - 9 2007

MICHAEL W. DOBBINS  
CLERK, U.S. DISTRICT COURT

UNITED STATES SECURITIES  
AND EXCHANGE COMMISSION,

Plaintiff,

Case No.

**07C 4483**

v.

Judge

**JUDGE ZAGEL**

THOMAS FISHER,  
KATHLEEN HALLORAN,  
AND GEORGE BEHRENS

Defendants.

Magistrate Judge

**MAGISTRATE JUDGE VALDEZ**

JURY TRIAL REQUESTED

COMPLAINT

Plaintiff, the United States Securities and Exchange Commission (the "Commission"), alleges the following:

INTRODUCTION

1. From 1999 through 2002, defendants Thomas Fisher ("Fisher"), Kathleen Halloran ("Halloran"), and George Behrens ("Behrens") engaged in, or approved of, improper transactions, made material misrepresentations in financial statements and documents filed with the Commission, and failed to disclose material information regarding Nicor, Inc.'s ("Nicor") rigged reductions in gas inventory levels that enabled it to improperly manipulate its earnings and to increase Nicor's revenues under a performance-based rate plan ("PBR" or "PBR Plan") administered by the Illinois Commerce Commission ("ICC"). Fisher, Halloran, and Behrens also materially understated Nicor's expenses during the first and second quarters of 2001 by improperly bundling a weather-insurance contract with an agreement to supply gas to its

insurance provider at below-market prices. Fisher, Halloran, and Behrens caused the losses on the supply agreement with its insurance provider to be charged to Nicor's customers, which they knew was prohibited by the ICC. As a result, Nicor's expenses were understated. These transactions allowed Nicor to manipulate its earnings to achieve its earnings targets for the PBR. By entering into these manipulative transactions, Nicor materially overstated its reported income for the years ending 2000 and 2001, and for each of the quarters within those years ("Reports") and the financial statements filed with those Reports. By their conduct, the defendants violated the antifraud provisions of the federal securities laws and aided and abetted Nicor's violations of the reporting provisions of the same laws.

2. In addition to engaging in materially improper transactions, Fisher, Halloran, and Behrens failed to make disclosures required by Generally Accepted Accounting Principles ("GAAP") about the effects of LIFO inventory liquidations on Nicor's reported income. Nicor, through Fisher, Halloran, and Behrens, failed to disclose in either its Management's Discussion & Analysis ("MD&A") section of its 2000 and 2001 annual and quarterly reports, or in its financial statements filed with those reports, that it had recorded material increases to income resulting from the liquidation of its LIFO inventory, and that the continued liquidation of Nicor's low-cost inventory was not sustainable. The income realized in the PBR program from LIFO inventory liquidations amounted to as much as 23% of pre-tax income in a quarterly reporting period. By their conduct, the defendants violated the antifraud provisions of the federal securities laws and aided and abetted Nicor's violations of the reporting provisions of the same laws.

3. During the relevant period, Nicor filed the following periodic reports with the Commission pursuant to Section 13(a) of the Securities Exchange Act of 1934 ("Exchange Act")

and the rules and regulations promulgated thereunder, each of which contained the consolidated financial statements of Nicor:

Period	Date Filed	Form
Quarter ended March 31, 2000	5/12/00	10-Q
Quarter ended June 30, 2000	8/8/00	10-Q
Quarter ended Sept. 30, 2000	11/7/00	10-Q
Year ended Dec. 31, 2000	3/12/01	10-K
Quarter ended March 31, 2001	5/9/01	10-Q
Quarter ended June 30, 2001	8/1/01	10-Q
Quarter ended Sept. 30, 2001	10/31/01	10-Q
Year ended Dec. 31, 2001	3/8/02	10-K
Quarter ended March 31, 2002	4/25/02	10-Q
Quarter ended June 30, 2002	8/14/02	10-Q

During the relevant period, Fisher signed Nicor’s annual reports and reviewed and approved its quarterly reports, Halloran signed Nicor’s quarterly and annual reports, and Behrens reviewed and approved its quarterly and annual reports.

4. After the fraud was discovered, on March 10, 2003, Nicor restated its financial statements for the fiscal years ended December 1999, 2000, and 2001. It also restated its financial statements for each of the first three quarters in 2000, 2001 and 2002.

5. Fisher, Halloran, and Behrens, directly or indirectly, have engaged in, and, unless restrained and enjoined by this Court, will continue to engage in, transactions, acts, practices, and

courses of business, which violate Sections 17(a)(1), 17(a)(2) and 17(a)(3) of the Securities Act of 1933 (“Securities Act”) [15 U.S.C. §§77q(a)(1), 77q(a)(2), and 77q(a)(3)].

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

7. Fisher, Halloran, and Behrens by aiding and abetting Nicor’s false filings with the Commission, have engaged in, and, unless restrained and enjoined by this Court, will continue to engage in, transactions, acts, practices, and courses of business, which violate Section 13(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] thereunder.

8. The Commission brings this action pursuant to Sections 20(b) and 20(d) of the Securities Act [15 U.S.C. §77t(b) and 77t(d)] and Sections 21(d) and (e) of the Exchange Act [15 U.S.C. §78u(d) and (e)] for an order permanently restraining and enjoining the defendants, requiring disgorgement and prejudgment interest from the defendants, imposing civil penalties on the defendants, prohibiting the defendants from acting as officers or directors of any issuer whose securities are registered pursuant to Section 12 of the Exchange Act [15 U.S.C. §78l], and required to file reports under Section 15(d) of the Exchange Act [15 U.S.C. §78o(d)] and granting other equitable relief.

## JURISDICTION

9. This Court has jurisdiction over this action pursuant to Section 22(a) of the Securities Act [15 U.S.C. §77v(a)] and Sections 21(e) and 27 of the Exchange Act [15 U.S.C. §§78u(e) and 78aa] and 28 U.S.C. §1331.

10. In connection with the acts, practices, and courses of business alleged in this complaint, the defendants, Fisher, Halloran, and Behrens, directly or indirectly, have made use of the means or instrumentalities of interstate commerce and/or of the mails.

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

## DEFENDANTS

12. At all relevant times, defendant Fisher served as Chairman, Chief Executive Officer and President of Nicor and of Nicor's principal subsidiary, Nicor Gas. Fisher began his career with the company in 1967 and has held various positions at Nicor Gas and Nicor. He served as Chief Financial Officer of both companies as well as Nicor's Vice President of operations. Fisher retired from his position at Nicor in April 2005. Fisher is about 61 years old and a resident of Aurora, Illinois.

13. From May 1999 to November 2003, defendant Halloran was the Executive Vice President and Chief Financial Officer of Nicor and Nicor Gas. Prior to 1999, Halloran held many financial-related positions at Nicor, including Treasurer and Controller. In November 2003, Halloran became Nicor's Executive Vice President and Chief Risk Officer. Halloran resigned from her positions with Nicor in August 2004. She is an unlicensed certified public accountant. Halloran is about 54 years old and a resident of St. Charles, Illinois.

14. At all relevant times, defendant Behrens was Vice President Administration and Treasurer of Nicor. Prior to that position, he was Vice President and Controller. Behrens received a bachelor's degree in accounting in 1976 and a master's degree in finance in 1982. Behrens resigned from his position with Nicor in June 2006. Behrens is an unlicensed certified public accountant. Behrens is about 51 years old and a resident of Aurora, Illinois.

#### RELATED ENTITY

15. Nicor Inc. is a gas utility holding company headquartered in Naperville, Illinois. Its principal business is gas distribution. Its common stock is registered pursuant to Section 12(b) of the Exchange Act and trades on the New York Stock Exchange. On July 15, 2002, an anonymous whistleblower faxed to the Citizen's Utility Board, a public utility advocacy group, a detailed memorandum claiming that Nicor's officers and managers were manipulating Nicor's PBR plan. Around July 15, 2002, Nicor's board of directors appointed a special committee to conduct an inquiry into the allegations raised by the whistleblower. On October 28, 2002, the consultant that had been retained by Nicor's special committee to investigate the whistleblower's allegations issued a report to the special committee of Nicor's board detailing his findings and conclusions. On October 29, 2002, Nicor issued a press release explicitly accepting the findings and conclusions of the report. On March 29, 2007, the Commission filed an action (*United States Securities and Exchange Commission v. Nicor Inc. et al.*, Civil Action No. 07C 1739) against Nicor and a former controller alleging that they violated the antifraud provisions of the federal securities laws, that Nicor violated the reporting provisions of the federal securities laws, and that a former controller aided and abetted Nicor's violations of the same laws. On the same day, without admitting or denying the allegations in the Commission's complaint, Nicor and its former controller co-defendant consented to the entries of Final Judgments and both paid

substantial financial penalties. The Final Judgments against Nicor and the former controller were entered on April 30, 2007.

## STATEMENT OF FACTS

### I. Background

#### A. Nicor's LIFO Inventory and the Inventory Value Team

16. Fisher's, Halloran's and Behren's improper conduct stems from Nicor's implementation of the PBR Plan on January 1, 2000. During the relevant period, Nicor valued its natural gas inventory using the LIFO cost method. Under this method, the inventory consisted of gas "layers" priced at historical prices from 1954 to 1996. In late 1999, Nicor's inventory totaled approximately 105 billion cubic feet ("bcf") of gas. The most recent layers of Nicor's LIFO inventory consisted of about 30 bcf of gas and were carried at costs that approximated current market prices as of 1999. The remaining layers consisted of about 75 bcf of gas and were carried at very low unit costs, reflecting prices that prevailed during the 1950s and the 1960s. At the end of 1999, the difference between the market value and the LIFO cost of Nicor's gas inventory was approximately \$170 million. During calendar year 2000, the unit cost of gas skyrocketed from \$2 to \$10 per million btu. Those increasing gas prices caused the difference between the market value and the LIFO cost basis of Nicor's gas to balloon to about \$500 million.

17. Under its traditional regulatory plan, Nicor had no incentive to tap into lower cost layers of gas as it was required to pass its cost of gas directly to customers without a mark up (i.e., if the lower cost layers of gas were liquidated, customers would be billed at those lower costs). In March 1998, Nicor's senior management assembled a group of Nicor employees into

the Inventory Value Team, and charged them with determining how Nicor could capture the value of Nicor's LIFO inventory. In mid-1998, the Inventory Value Team prepared a report – The Inventory Value Team Report – that analyzed various ways to “capture” the value of the LIFO inventory. After discussing the pros and cons of each approach, the Inventory Value Team, in its report, concluded that implementing a performance based rate plan was “the recommended method for the Company to capture the value from the LIFO layers.”

18. Generally, a performance based rate plan is a plan whereby a utility compares its actual cost of gas distribution against a market-sensitive benchmark. To the extent that the actual costs are lower than the benchmark, the savings are shared between the utility and its customers. To the extent that actual costs are higher than the benchmark, the resulting losses likewise are shared between the utility and its customers. The percentage of savings/losses attributed to each are often the subject of negotiation between the utility, the public advocate for consumers, and the regulator.

19. The Inventory Value Team presented its report and findings to Fisher, Halloran, Behrens, and other senior Nicor executives at a meeting in late 1998 or early 1999. During the meeting, the Inventory Value Team discussed the reasons why it had concluded that the PBR plan was the recommended method to capture the value of the LIFO layers. Among the important benefits of a PBR plan that was discussed was the fact that the benefit Nicor was expecting to reap from the LIFO inventory liquidations was “not explicit.” Indeed, during or shortly after that meeting, Nicor officers issued a directive that Nicor employees be careful not to highlight the LIFO benefit in Nicor's filings with the ICC. In an August 2000 memorandum to the file, Nicor's then controller wrote that on an interim basis, Nicor “will need to be careful to

not highlight the LIFO benefit. In the actual year-end PBR computation, the LIFO benefit will be very difficult to recognize. It may be more transparent on an interim basis.” This memorandum was shared with, at least, Behrens and Halloran.

20. In mid-1999, Fisher, Halloran, and Behrens authorized their subordinates to prepare and file with the ICC an application for approval of a performance based rate plan. As Fisher, Halloran, and Behrens knew, Nicor’s stated reasons for the PBR plan were false and misleading. The primary purpose of the PBR Plan was to give Nicor the ability to capture the market value of its low-cost LIFO gas inventory, a feat that could not be accomplished under the traditional ICC regulatory framework.

#### B. The Performance Based Rate Plan

21. The purported purpose of the PBR Plan was to give Nicor an incentive to lower ratepayers’ gas costs. Under the PBR plan, Nicor’s savings and losses relative to the market-sensitive benchmark were to be shared equally between the company and customers. Nicor’s PBR Plan was subject to further review after two years by the ICC.

22. During the proceeding, at which the ICC approved the PBR, Nicor indicated that “the primary reason for entering into an alternative regulatory plan for its gas costs was to enable it to respond to changes in the gas supply markets, which offered both challenges and opportunities to aggressively pursue cost minimization through innovative, non-traditional means.” Nicor also indicated the PBR was based on three objectives: “(1) an alignment of shareholder and ratepayer interests by providing economic incentives for Nicor to improve its performance in providing ratepayers with the best gas prices available, while recognizing the need for continued reliability and security of supply; (2) encouraging the appropriate use of

competitive market opportunities and risk management mechanisms for the procurement of gas supply, transportation and storage services by establishing a reasonable balance between risk and reward; and (3) a reduction of regulatory costs by establishing an objective, market-based standard for evaluating gas supply purchasing, planning, and management, while also eliminating after-the-fact prudence reviews.” In reality, Nicor was using the PBR to financially benefit from the liquidation of low-cost LIFO gas. Nicor hid the real purpose of the PBR from its investors and the ICC.

## II. Fisher, Halloran, and Behrens Knowingly or Recklessly Permitted Nicor to Engage in Sham Transactions In Order to Access Nicor’s Low-Cost LIFO Inventory Layers

23. Nicor used sham transactions to manipulate the reductions in its reported inventory levels and to manipulate its PBR earnings while it actually maintained control over much higher inventory levels in connection with its duty under the Illinois Public Utility Act to ensure the availability of gas to its ratepayers.

24. In order to access Nicor’s low-cost LIFO gas, Fisher and Behrens knowingly or recklessly permitted the DSS transaction described below, and Fisher, Halloran, and Behrens knowingly or recklessly permitted the prefill transactions described below. These transactions had the effect of overstating the PBR Plan profits and, therefore, Nicor’s reported income.

25. Moreover, Fisher, Halloran, and Behrens failed to disclose in Nicor’s annual and quarterly reports, and in the financial statements filed with those reports, that Nicor had recorded material increases to income resulting from the liquidation of its low-cost LIFO inventory. By so doing, Fisher, Halloran and Behrens misrepresented and failed to disclose material information about the PBR plan.

## A. 1999 Sale of DSS Gas to Third Party

### i. DSS Transaction

26. DSS is a delivered storage service provided by Natural Gas Pipeline Company of America. The gas supplied under this arrangement was accounted for as inventory by Nicor. On December 10, 1999, less than a month before Nicor implemented the PBR, Nicor entered into a transaction with a third party designed to artificially shift Nicor's last remaining high-cost layer off of its books. This maneuver set the stage for Nicor to begin liquidating its low-cost gas inventory once the PBR program took effect. Under the agreement, Nicor sold 18.8 bcf of gas to a third party and recorded \$41.4 million in proceeds from that sale and an 18.8 bcf reduction in its gas storage inventory. As a part of the agreement, Nicor was obligated to repurchase the inventory from the third party; in fact, Nicor needed the DSS gas inventory in order to meet peak customer demand during the winter season. The pricing for the sale and repurchase was established at the time of the sale: the third party was to buy the gas at \$2.20 per unit, and then resell to Nicor 2.8 bcf of gas in December at the purchase price and the remainder of the 18.8 bcf of gas in early 2000 at the then prevailing market prices.

27. Based on a side agreement with Nicor, the third party purchased gas futures contracts in December 1999 for Nicor's account, and for its benefit, effectively hedging Nicor's market risk to rising prices during the repurchase period. With the hedges in place, Nicor effectively sold the gas to the third party at \$2.20 in December and bought it back at the same price in the period from January through March. The transfer of gas to the third party did not result in a sale under GAAP and should not have reduced Nicor's high cost LIFO layers of gas

inventory. By its restatement of its financial statements, Nicor has conceded that the transfer of gas to the third party was not a sale.

28. On December 8, 1999, a meeting was held at Nicor to discuss the impact of Nicor's sale of DSS gas to the third party. A number of Nicor officers, including Behrens, attended the meeting. The major topic of discussion was whether the proposed transaction would hurt ratepayers since Nicor would be selling gas to the third party at current market prices which were below Nicor's cost of the DSS gas that was to be sold. This loss would be borne entirely by the ratepayers, rather than shared with Nicor, as would have been the case if the sham sale had not taken place and the related gas was then distributed to Nicor's customers during the early winter months of the PBR program.

29. Nicor officers were concerned that if the purported sale occurred after January 1, 2000, under the PBR, it would have an adverse impact on Nicor's PBR results. An argument for completing the DSS transaction prior to January 2000, which was discussed at the meeting on December 8, 1999, was to allow the third party to lock in financial hedges on behalf of Nicor for the month of January. According to the head of Nicor's gas supply accounting department, the real motive behind this transaction was to "eat into the more expensive LIFO layers in preparation for the new Performance Based Rate [Plan]."

#### B. Storage Prefill Transactions

30. The Inventory Value Team Report discussed a potential method to access Nicor's lower cost LIFO inventory—what later came to be known as storage "prefills." Through prefills, Nicor could continue to liquidate the low-cost LIFO layers by filling its storage system with gas for which the "title holder" would be an unaffiliated third party and with gas that Nicor was

