

UNITED STATES DISTRICT COURT  
DISTRICT OF MASSACHUSETTS

SECURITIES AND EXCHANGE COMMISSION,

Plaintiff,

v.

BRUCE HILL,  
GRAHAM MARSHALL, and  
STEVEN PAXHIA,

Defendants.

CIVIL ACTION  
NO. 02 CV 11244 (EFH)

AMENDED COMPLAINT

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

Summary

1. This enforcement action involves material overstatements of revenue during 1998 by Inso Corporation ("Inso"), a publicly-traded company then headquartered in Boston, Massachusetts. Between approximately September 1998 and April 1999, Defendants Bruce Hill ("Hill"), then general counsel of Inso, and Graham Marshall ("Marshall"), then vice president and general manager of Inso's electronic publishing division, engaged in a fraudulent revenue recognition scheme designed to falsely boost the amount of Inso's third quarter and annual revenues for 1998.

2. By on or about September 30, 1998, the last day of Inso's 1998 fiscal third quarter, Inso's sales team had failed to conclude a sale of \$3 million of software licenses to US Airways Group, Inc. ("US Airways") that Inso had been negotiating since at least early 1998. Although no distributor had been involved in this deal prior to the end of the third quarter of

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1998, on or about September 30, 1998, Marshall and others at Inso attempted to locate a distributor who would place an immediate order for the \$3 million of software licenses in order to allow Inso to record revenue from the transaction in the third quarter.

3. On or about September 30, 1998, Marshall contacted a potential distributor for the US Airways deal -- a software company located in Malaysia ("the Malaysian distributor"). Hill and Marshall then entered into a phony \$3 million sales transaction with the Malaysian distributor. The sales transaction was a sham because of an undisclosed oral side agreement between Hill and Marshall and the Malaysian distributor which provided that Inso would sell the software to US Airways directly and that the Malaysian distributor would not have to pay for its supposed \$3 million purchase.

4. Hill and Marshall took further actions after the third quarter of 1998 to cover up the sham nature of the third quarter transaction with the Malaysian distributor. Among other things, Hill orchestrated the providing of \$4 million in letters of credit to the Malaysian distributor to finance the payment of the third quarter receivable, caused a false board resolution to be provided to Inso's bank purporting to authorize the letters of credit, and gave false information to Inso's chief financial officer ("CFO") and outside auditors about the purpose of the letters of credit. Marshall provided false information and documents to Inso's CFO to conceal the purpose of a payment to the Malaysian distributor.

5. During the same time period, Defendant Steven Paxhia ("Paxhia"), then Inso's president and chief executive officer, did not take steps to learn about or prevent the side agreement with the Malaysian distributor and the fraudulent revenue recognition scheme carried out by Hill and Marshall. Among other things, after learning on or about September 30, 1998,

that Inso's sales team had failed to conclude the \$3 million US Airways deal, Paxhia authorized others under his control at Inso to find a distributor for the deal before the end of the quarter. Because of his position as CEO of Inso, Paxhia should have known that finding a distributor in so short a period risked having Inso enter a transaction that was not consistent with its revenue recognition policies or with generally accepted accounting principles ("GAAP"). Further, Paxhia did not inquire into certain factors concerning the transaction that Hill and Marshall entered into with the distributor, namely that the distributor was located in Malaysia, that the distributor had not previously been involved in the sale to US Airways, and that, with little notice, the distributor purportedly accepted responsibility for a \$3 million transaction on the last night of the quarter.

6. In March 1999, after conducting an internal investigation, Inso restated its financial results for the first three quarters of 1998, reversing approximately \$3 million in revenue from the fraudulent transaction entered into by Hill and Marshall in the third quarter of 1998.

7. As a result of the acts and omissions of Hill, Marshall, and Paxhia, Inso's financial statements included in Form 10-Q filed with the Commission for the third quarter of 1998, and referenced in a Form S-3 filed in connection with an offering of stock in December 1998, and summarized in a press release issued in October 1998, materially overstated Inso's third quarter revenue by approximately \$3 million. Inso's internal books and records also materially misrepresented the company's true financial condition.

8. By engaging in the acts and practices alleged in this Complaint, Defendants Hill and Marshall, directly or indirectly, violated the antifraud, periodic reporting, books and records, and internal accounting controls provisions of the federal securities laws. Hill and Marshall,

directly or indirectly, engaged in acts, practices, and courses of business that constitute violations of Section 17(a) of the Securities Act of 1933 ("Securities Act")[15 U.S.C. § 77q(a)] and Sections 10(b) and 13(b)(5) of the Securities Exchange Act of 1934 ("Exchange Act")[15 U.S.C. §§ 78j(b) and 78m(b)(5)] and Rules 10b-5, 13b2-1, and 13b2-2 thereunder [17 C.F.R. §§ 240.10b-5, 240.13b2-1, and 240.13b2-2]. In addition, Hill and Marshall aided and abetted Inso's violations 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 13a-13 and 12b-20 [17 C.F.R. §§ 240.13a-13 and 240.12b-20].

9. By engaging in the acts and practices alleged in this Complaint, Defendant Paxhia, as a controlling person of Inso under Section 20(a) of the Exchange Act [15 U.S.C. § 78t(a)], is liable for Inso's uncharged violations of Sections 10(b), 13(a) and 13(b)(2)(A) of the Exchange Act [15 U.S.C. §§ 78j(b), 15 U.S.C. §§ 78m(a) and 78m(b)(2)(A)] and Rules 10b-5, 13a-13 and 12b-20 thereunder [17 C.F.R. §§ 240.10b-5, 240.13a-13, and 240.12b-20].

10. Unless restrained and enjoined, Defendants Hill and Marshall will continue to engage in acts, practices, and courses of business as set forth in this Complaint or in acts, practices, and courses of business of similar object and purpose.

11. Unless restrained and enjoined, Defendant Paxhia will continue to engage in acts, practices, and courses of business as set forth in this Complaint or in acts, practices, and courses of business of similar object and purpose.

### **Jurisdiction**

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

13. Defendants, directly or indirectly, 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 herein.

14. The Commission brings this action pursuant to the enforcement authority conferred upon it by Section 20 of the Securities Act [15 U.S.C. § 77t] and Section 21 of the Exchange Act [15 U.S.C. § 78u] to: (i) enjoin the Defendants permanently; (ii) prohibit Defendants Hill and Marshall from acting as officers or directors 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)]; (iii) require Defendants Hill and Marshall to pay civil monetary penalties; (iv) require Defendants Hill, Marshall, and Paxhia to disgorge losses avoided, plus prejudgment interest thereon; and (v) obtain other equitable relief.

#### **Defendants**

15. Bruce Hill was vice president, secretary, and general counsel of Inso from March 1994 through March 1999, when he was demoted to vice president of business development following Inso's restatement of 1998 revenues. Hill left Inso in 2000.

16. Graham Marshall was vice president and general manager of Inso's electronic publishing solutions division from January 1997 through April 1999, when he resigned following Inso's restatement of 1998 revenues.

17. Steven Paxhia was chief executive officer, president, and chairman of the board of directors of Inso from March 1994 until March 1999, when he resigned following Inso's restatement of 1998 revenues.

**Related Party**

18. During the relevant period, Inso was a Delaware corporation with its headquarters in Boston, Massachusetts, and with offices and/or sales representatives worldwide. Inso changed its name to eBT International, Inc. on August 28, 2000, and moved its headquarters to Providence, Rhode Island. At all relevant times, Inso was a supplier of software for sharing and publishing electronic information. Inso's 1998 fiscal year ended on December 31, 1998. Since March 1994, when Inso became a publicly traded company, Inso's common stock has been traded on the NASDAQ National Market System and registered with the Commission pursuant to Section 12(g) of the Exchange Act. On May 23, 2001, the company, operating under the name eBT International, Inc., announced plans to cease operations and liquidate its remaining assets.

**Background Facts**

19. During 1998, Inso derived revenue primarily from the sale of software licenses, software maintenance fees, and royalties from license arrangements with resellers. After its March 1999 restatement, Inso's revenue for 1998 was \$60 million, compared to \$81.8 million for 1997.

20. During the relevant period, Inso's senior management had substantial financial incentives to meet revenue goals set by Inso's board of directors. Managers received salaries plus significant annual bonuses based, in large part, on meeting revenue targets. By meeting targets, Paxhia could earn a bonus amounting to approximately 40% or more of his salary; Hill and Marshall could earn bonuses of approximately 30% of their salaries if the company met revenue targets. If the company did not meet its revenue targets, they did not receive a bonus.

21. Hill, Marshall, and others at Inso experienced firsthand significant repercussions at Inso when the company failed to meet its revenue targets in the second quarter of 1997. Following the announcement of disappointing second quarter results in 1997, Inso's stock price dropped, and Inso terminated the employment of its vice president of worldwide sales. Inso also underwent a restructuring and job cuts, and Inso's top managers received no bonuses for 1997.

22. In early 1998, Inso adopted as its revenue recognition policy Statement of Position 97-2 ("SOP 97-2"), entitled "Software Revenue Recognition," as amended, issued by the American Institute of Certified Public Accountants. SOP 97-2 required the following in order to recognize revenue: (a) persuasive evidence of an arrangement exists; (b) delivery has occurred; (c) the vendor's fee is fixed or determinable; and (d) collectibility is probable. SOP 97-2 also required consideration of "informal communications, or other factors [that] indicate that payment is substantially contingent on [a] reseller's success in distributing...the product."

**The Fraudulent \$3 Million Sale  
To a Malaysian Software Company on September 30, 1998**

23. Throughout 1998, Inso had been trying to close a \$3 million sale of software licenses to US Airways. Paxhia received regular updates regarding the proposed sale throughout 1998, because the sale was expected to be one of Inso's largest and a strategically important one for the company. In or about September 1998, Inso's head of worldwide sales reported at Paxhia's weekly senior staff meeting that he expected Inso to conclude the sale that quarter.

24. By approximately the last day of the third quarter, September 30, 1998, Inso's sales team still had not concluded the sale to US Airways. Paxhia attempted to contact the president of US Airways. However, at 6:30 p.m. when he could not reach the president, Paxhia

realized Inso was not going to get a signed contract from US Airways in time to record the \$3 million of revenue in the third quarter. Although no distributor had been involved in the US Airways deal prior to the end of the third quarter of 1998, on or about the evening of the last day of that quarter, Paxhia authorized Inso's head of worldwide sales to find a distributor to purchase the \$3 million of software before the end of that day in order to allow Inso to recognize revenue for the transaction in the third quarter of 1998.

25. Under GAAP, sales of product to distributors may be recognized as revenue in the quarter in which they occur if all conditions for revenue recognition are met, including, among other things, that the distributor takes financial responsibility for the product purchased.

26. On or about September 30, 1998, Inso's head of worldwide sales discussed finding a potential distributor with Marshall. Marshall then contacted a general manager at a large firm (the "Systems Integration Firm") that anticipated providing software systems integration services to US Airways following completion of Inso's sale to US Airways. Marshall proposed that the Systems Integration Firm purchase approximately \$3 million of software and hold it until Inso sold the software to US Airways. Marshall wanted the order from the Systems Integration Firm that same day - before the end of the third quarter. Marshall told the Systems Integration Firm that Inso was certain to obtain the order from US Airways within a short time, and that the transaction would present no risk to the Systems Integration Firm. Marshall promised a sales commission for the order, and assured the Systems Integration Firm that it was not expected to do any selling. The Systems Integration Firm immediately rejected Marshall's proposal.



27. Inso's head of worldwide sales informed Paxhia of the Systems Integration Firm's decision that evening, and Paxhia authorized the head of worldwide sales to continue trying to find a distributor. The head of worldwide sales then spoke to Marshall again to see whether Marshall knew of any other company that would place an order on the spot for the \$3 million US Airways transaction. Marshall offered to contact his acquaintance, Chan Hong Saik ("Chan"), the owner of Hong Hong Printing, a Malaysian company, with whom Marshall had previously done business.

28. On or about September 30, 1998, Marshall telephoned Chan and asked if he would act as a distributor for Inso's sale to US Airways. Marshall told Chan that Inso would complete the sale to US Airways early in the fourth quarter and that US Airways, not Chan, would be the actual purchaser and would be responsible for paying Inso for the purchase. Marshall said that he needed an order from Chan that day so that Inso could book the order within the third quarter. Marshall informed Chan that Inso would pay a \$160,000 commission for placing the order immediately, and that Chan would be taking no financial risk because Inso's sale of the software to US Airways was imminent. Following his conversation with Chan, Marshall informed the head of worldwide sales that Chan would place the order.

29. Also on or about September 30, 1998, Paxhia informed Hill that a distributor was placing an order for the US Airways deal, and instructed Hill to prepare the purchase order. Hill drafted a "non-cancelable, non-refundable" purchase order that stated payment was due upon resale of the software licenses or on December 31, 1998, whichever occurred first. Hill knew, or was reckless in not knowing, the terms of the oral side agreement with Chan. However, Hill did not include the terms of the oral side agreement between Marshall and Chan in the purchase

order, which Hill signed. The oral side agreement contradicted the terms of the purchase order because payment was not expected unless and until Inso, rather than Chan, completed the sale to US Airways. In addition, the term in the purchase order making payment from Chan due in full on December 31, 1998 was negated by Marshall's promise to Chan that he was taking no financial risk because of the impending sale by Inso to US Airways.

30. Later, on or about the evening of September 30, 1998, Marshall placed another call to Chan in Malaysia to determine whether Chan had received the purchase order from Inso, and whether he was going to place the order. When Chan asked Marshall about the terms that stated the order was "non-cancelable" and "non-refundable," Marshall gave Chan his word that Chan would not have to pay, and that he simply needed to pass the US Airways order through Chan in order to record the revenue in the third quarter. Following Marshall's second call to Chan, at approximately 9:30 p.m. on September 30, 1998, Inso received a fax of the purchase order signed by Chan.

31. To ensure that Inso would recognize the \$3 million of revenue in the third quarter, Marshall failed to inform Inso's CFO about the oral side agreement with Chan. Based on the actions of Hill and Marshall, including the false purchase order drafted and signed by Hill, Inso recorded approximately \$3 million in revenue from the sale in the third quarter of 1998.

32. Paxhia did not take steps to learn about or prevent others at Inso from entering the side agreement with the distributor. Because of his position as CEO of Inso, Paxhia should have known that finding a distributor in so short a period of time risked having Inso enter into a transaction that was not consistent with its revenue recognition policies or with GAAP. Further, Paxhia did not inquire into certain factors concerning the deal with Chan, namely that Chan was

located in Malaysia, that he had not previously been involved in the sale to US Airways, and that, with little notice, Chan purportedly accepted responsibility for a \$3 million deal on or about the evening of September 30, 1998.

33. As a result of the acts and omissions described above, nearly \$3 million was improperly entered as revenue in Inso's books and records for the quarter ended September 30, 1998, and reported in the financial statements submitted with Inso's Form 10-Q filed with the Commission for that quarter.

34. The third quarter 1998 transaction with Chan failed to conform with Inso's revenue recognition policies and GAAP. GAAP requires consideration of "informal communications, or other factors [that] indicate that payment is substantially contingent on [a] reseller's success in distributing...the product." The oral side agreement with Chan that he would take no financial risk, and that Inso, rather than Chan, would resell the product, is an "informal communication" indicating that payment is contingent, in this case *on Inso's success* selling the software. The transaction also failed to meet the GAAP requirements that there must be a valid exchange of product for cash or a valid claim to cash. Inso did not have a valid claim to cash from Chan because, under the terms of the side agreement, Inso remained responsible for selling the software, and Chan assumed no financial risk. In addition, in order to recognize revenue from a sale, the seller must substantially accomplish what it must do to be entitled to the benefits represented by the revenue. Inso was not entitled to the benefits of the revenue because it had not substantially accomplished its obligation to complete the sale of the software to US Airways.

35. Hill and Marshall each knew, or were reckless in not knowing, that the revenue from the sale to Chan in the third quarter of 1998 did not conform with Inso's revenue recognition policies or with GAAP.

**Inso Publicly Reported False Third Quarter 1998 Financial Results**

36. On or about October 15, 1998, Inso issued a press release falsely announcing that revenue for the quarter ended September 30, 1998 was \$18,707,000. This false statement of revenue allowed Inso to meet its third quarter revenue targets, and was reported in financial statements submitted with Inso's Form 10-Q filed with the Commission on or about November 16, 1998. In addition, on or about December 18, 1998, Inso filed a Form S-3 for an offering of \$29 million of common stock in connection with its acquisition of Sherpa Corp. The Form S-3 incorporated by reference the false and misleading Form 10-Q filed for the first three quarters of 1998. Defendants Hill and Marshall each knew, or were reckless in not knowing, that the press release, Form 10-Q, and Form S-3 materially overstated Inso's revenue for the third quarter of 1998.

**Hill and Marshall Took Steps After the Third Quarter of 1998 to Cover Up the Improper Revenue Reported in the Third Quarter**

37. Hill and Marshall engaged in a series of fraudulent arrangements after the third quarter of 1998 relating to Chan in order to cover up the sham nature of the transaction recorded on September 30, 1998.

38. During the fourth quarter of 1998, Inso's sales team continued to negotiate the sale to US Airways. On or about November 16, 1998, Paxhia, Hill, and Marshall learned at a senior managers meeting that Inso had encountered a serious setback in its negotiations with US

Airways, and that the sale to US Airways was no longer expected to close by the end of 1998. Hill and Marshall knew that Chan's account would become due at year-end for the phony \$3 million transaction. Hill and Marshall also knew that Chan was not planning to make the \$3 million payment because of the oral side agreement he had reached with Marshall. Detection of the fraudulent revenue was likely if Chan's payment was not received by the end of the year, because Inso's outside auditors would begin the year-end audit early in January 1999. The auditors would seek to confirm with the customer a \$3 million transaction that appeared on Inso's list of receivables at year-end.

39. On approximately December 24, 1998, Paxhia telephoned Hill and requested that Hill meet with Chan in Malaysia before the end of the year. Paxhia identified three goals for Hill's trip to Malaysia. Paxhia told Hill to obtain payment from Chan for the \$3 million third quarter sale, and to conclude with Chan two new deals -- a \$2.6 million original equipment manufacturer ("OEM") deal, and a separate distribution agreement granting Chan rights to distribute Inso's software in southeast Asia.

40. During the fourth quarter, Inso's CFO informed Hill, Marshall, and Paxhia that revenue could not be recorded from the separate \$2.6 million OEM transaction with Chan unless Chan paid for the \$3 million sale from the third quarter. However, revenue from the OEM transaction was needed to meet Inso's annual and fourth quarter revenue targets. Accordingly, Hill and Marshall entered into certain sham transactions in the fourth quarter of 1998 to continue concealment of the fraudulent nature of the \$3 million third quarter sale to Chan and to ensure recognition of revenue from the \$2.6 million OEM transaction in Inso's 1998 revenue.

41. As described below, Paxhia approved certain unusual arrangements with Chan during the fourth quarter, and did not take steps to learn about or prevent the false and misleading acts of Hill and Marshall during the fourth quarter. These arrangements with Chan during the fourth quarter should have alerted Paxhia to the fact that Hill's and Marshall's fraudulent conduct was continuing.

**Marshall Misled Inso's CFO to Justify a Payment to Chan**

42. As part of the effort to obtain payment from Chan for the \$3 million order, at or near the end of December 1998, Marshall, with Hill's knowledge, provided false information to Inso's CFO to support paying Chan the \$160,000 commission promised to Chan on September 30, 1998.

43. At or about the end of December 1998, Marshall informed Hill that his negotiations with Chan in Malaysia would go more smoothly if Chan received the \$160,000 commission. Chan repeatedly had contacted Marshall during the fourth quarter of 1998 seeking the \$160,000 commission. As a result, in or about the last week of December 1998, Marshall developed a plan to pay Chan the \$160,000 by claiming that Chan had performed software development work for Inso when, in fact, Chan had not.

44. On or about December 30, 1998, in order to obtain authorization for the \$160,000 payment to Chan, Marshall provided to Inso's CFO a purported contract document, signed only by Marshall, that described software development work performed by Chan. The CFO asked for further documentation to show that the work had been performed, and Marshall provided the CFO a letter signed by Marshall and Chan stating that Chan had performed the software development work. Marshall falsely informed the CFO that Chan had performed the work to his

satisfaction, and that an engineer in Marshall's group also was satisfied with Chan's work. However, the engineer never reviewed any software development work performed by Chan. Further, Chan could not have performed the work because Inso had not provided Chan technical specifications necessary to perform the work described in the purported contract.

45. Paxhia knew about Marshall's request for the \$160,000 payment to Chan at the end of December 1998. Before sending the payment to Chan, Inso's CFO complained to Paxhia that Marshall should have previously informed the CFO of software development work for which the CFO would need to budget payment. Despite knowing that Chan purportedly still owed Inso \$3 million for the third quarter transaction, and that Inso was negotiating other transactions with Chan, Paxhia did not take steps to confirm the legitimacy of the \$160,000 payment or the software development work purportedly performed by Chan. Rather, Paxhia excused Marshall by saying he probably did not mention it to the CFO because the amount was within Marshall's budget for his division. Following the CFO's discussion with Paxhia, the CFO wired \$160,000 to Chan.

46. In or about the last week of December 1998, Marshall informed Hill of his plan to satisfy Chan's repeated requests for the \$160,000 commission for the third quarter transactions by requesting that the CFO pay Chan \$160,000 for purported software development work. During the last few days of December 1998, Hill learned that Inso paid \$160,000 to Chan. Despite knowing Marshall's plan, Hill never informed Inso's CFO that the payment was actually fulfilling the terms of the side agreement promising Chan a \$160,000 commission on the third quarter sale.

**Hill Arranged for Inso to Finance Chan's  
Payment for the Third Quarter Transaction**

47. Hill met with Chan in Malaysia in the last few days of December 1998. While in Malaysia, Hill told Chan that the US Airways transaction had not closed, but that it was nonetheless very important that Chan wire \$3 million to Inso in payment for the third quarter receivable. Chan refused, and told Hill he did not have the funds to pay \$3 million for the third quarter transaction. Hill attempted to persuade Chan to pay by offering to make Chan a distributor for Inso's Far East territory, and by guaranteeing that Chan would earn \$4 million in revenue over two years under the distribution agreement. However, because Hill wanted the \$3 million payment by the next day, Chan insisted that he needed \$4 million in letters of credit from Inso to secure a bank loan in order to pay the third quarter 1998 receivable.

48. Hill drafted the letters of credit so that they were immediately available to Chan without reference to Inso's performance under the distribution agreement.

49. Hill then falsely informed Inso's CFO by telephone that Inso needed to provide the revenue guarantees and letters of credit as an incentive to Chan to sign the distribution agreement. Hill also falsely told the CFO that Chan could not obtain funds based on the letters of credit unless Inso failed to perform under the revenue guarantees in the distribution agreement when, in fact, Hill knew that Chan was going to immediately draw on the letters of credit to pay the third quarter receivable.

50. Inso's CFO telephoned Paxhia at his home and informed him that Hill wanted to grant Chan \$4 million in letters of credit. Paxhia approved providing Chan the letters of credit, and assured the CFO that Chan would achieve the \$4 million in revenues Inso had guaranteed



him.

**Hill Caused a False Board Resolution  
to Be Provided to Inso's Bank**

51. In order to obtain the letters of credit from Inso's bank, at or near the end of December 1998, Hill caused others at Inso to provide to Inso's bank a false board resolution purporting to authorize the letters of credit to Chan. During a telephone call from Malaysia on December 30, 1998, Hill instructed an attorney in Inso's legal department who reported to Hill to prepare documents required by Inso's bank for the letters of credit. Hill told the Inso attorney that the documents would contain a representation that the board had passed a resolution approving the letters of credit. Hill told the Inso attorney that the board had not actually voted, but that it was not expedient or practical for the board to meet before the end of the year. Hill assured the Inso attorney that it had been his practice to have the board subsequently ratify votes.

52. The Inso attorney prepared the board resolution documents. While Hill was still in Malaysia, the Inso attorney read to Hill over the telephone a "certificate of secretary" that contained a resolution purportedly adopted by Inso's board of directors on December 28, 1998, authorizing \$4 million in letters of credit to Chan. Hill told the Inso attorney to affix Hill's signature stamp to the certificate of secretary and provide the documents to Inso's bank, which the Inso attorney did.

53. Inso's bank required the signature of Inso's CFO on the certificate of secretary as Inso's corporate treasurer. In or about the last few days of December 1998, before signing the document, the CFO contacted Paxhia and told him that: (a) Hill had instructed her to provide to Inso's bank a certificate of secretary stating that the board approved the letters of credit by vote

on December 28, 1998, and; (b) because the board had not voted to approve the letters of credit, that the board would need to be convened later to ratify the letters of credit. Paxhia agreed that the board would later convene to ratify the letters of credit, and he authorized the CFO to complete the document, even though the board had not approved this action, and provide it to Inso's bank to obtain the letters of credit, which the CFO did.

54. Following the issuance of the letters of credit, neither Hill nor Paxhia sought ratification by Inso's board of directors of the purported December 28, 1998 board resolution approving the letters of credit to Chan.

**Hill Used a Questionable Check From Chan as Evidence  
of Chan's Payment for the Third Quarter Receivable**

55. Hill knew that Inso's CFO would not approve recognition of the separate \$2.6 million in revenue from the fourth quarter OEM transaction with Chan unless Chan first paid the third quarter receivable. Accordingly, on December 31, 1998, Hill accepted from Chan and faxed to Inso a check in Malaysian currency, purportedly in satisfaction of the third quarter receivable. However, Chan had not yet been able to obtain funds to pay for the \$3 million third quarter 1998 receivable pursuant to the letters of credit, and he told Hill that this check might not clear. Hill did not inform Inso's CFO of any problem with Chan's check.

56. As a result of receiving Chan's check, Inso's finance department considered Chan's third quarter receivable paid. Accordingly, Inso recorded the separate \$2.6 million in revenue from the OEM transaction with Chan in the fourth quarter. Shortly thereafter, Chan canceled payment on the check he had given to Hill. In January 1999, after Chan's bank accepted Inso's letters of credit, Chan drew on the letters of credit and wired \$3 million to Inso to

satisfy the third quarter 1998 receivable. Chan never undertook to act as Inso's distributor, pursuant to the terms of the purported distribution agreement.

**Hill Provided False Information to Inso's  
Auditors Regarding the Chan Transactions**

57. In approximately January 1999, Hill concealed from Inso's outside auditors Inso's funding of Chan's payment for the \$3 million third quarter 1998 receivable. During a meeting on or about January 20, 1999, Hill falsely told the outside audit manager and partner that Inso had granted the letters of credit to Chan to support the revenue guarantees in the distribution agreement. Hill also falsely stated that Chan's payment for the third quarter transaction demonstrated that Chan could pay for the separate \$2.6 million fourth quarter OEM transaction, when Hill knew Inso had financed Chan's payment of the third quarter 1998 receivable. Hill further falsely stated that the \$4 million in revenue guarantees in the distribution agreement were unimportant, rather than informing the auditors that the revenue guarantees were merely the purported justification for providing Chan \$4 million in letters of credit. Hill failed to inform the auditors that Inso actually provided Chan \$4 million in letters of credit to finance his payment of the third quarter receivable.

**Hill, Marshall, and Paxhia Avoided Losses by Selling  
Their Inso Stock Before the Fraud Became Public**

58. Hill, Marshall, and Paxhia each sold shares of Inso stock in late November 1998, at a time when Inso's stock price was artificially inflated by the inclusion of the false sale to Chan in Inso's reported financial results.

59. On or about November 23, 1998, Hill sold 3,604 shares of Inso stock at \$27.50 per share, for total proceeds of \$99,110. On or about February 1, 1999, after the reversal of the

revenue from the Chan transaction became public along with the reversal of other unrelated transactions involving other Inso employees, Inso's stock price dropped to as low as \$9.00 per share. Accordingly, Hill avoided a loss of \$66,674.

60. On or about November 25, 1998, Marshall sold 597 shares of Inso stock at \$28.87 per share, for total proceeds of \$17,238. On November 30, 1998, Marshall sold 12,000 additional shares at \$27.87 per share, for total proceeds of \$334,500. On or about February 1, 1999, after the reversal of the revenue from the Chan transaction became public along with the reversal of other unrelated transactions involving other Inso employees, Inso's stock price dropped to as low as \$9.00 per share. Accordingly, Marshall avoided a loss of \$11,865 through his sale of Inso stock on about November 25, 1998, and avoided a loss of \$226,500 through his sale of Inso stock on or about November 30, 1998, for a total loss avoided from both sales of \$238,365.

61. On or about November 24, 1998, Paxhia sold 4,000 shares of Inso stock at \$28.25 per share, for total proceeds of \$113,000. On or about February 1, 1999, after the reversal of the revenue from the Chan transaction became public along with the reversal of other unrelated transactions involving other Inso employees, Inso's stock price dropped to as low as \$9.00 per share. Accordingly, Paxhia avoided a loss of \$77,000.

**Hill and Marshall Caused Inso to Falsify its Books and Records  
and Circumvented Internal Accounting Controls**

62. Between approximately September 1998 and April 1999, Hill and Marshall each caused the falsification of Inso's books and records and each knowingly circumvented Inso's system of required internal accounting controls by providing materially false information

regarding revenue to employees of Inso's finance department who were responsible for maintaining Inso's books and records. Hill and Marshall each caused the entry into Inso's books and records of revenue that they knew, or were reckless in not knowing, failed to conform with GAAP.

63. Hill prepared and signed the false purchase order with Chan in the third quarter of 1998, knowing that Inso's finance department relied on the purchase order to support recognition of nearly \$3 million in revenue for that quarter.

64. Hill failed to inform members of Inso's finance department that Chan did not have funds to support the check provided in December 1998 in payment of the third quarter receivable.

65. Hill falsely informed members of Inso's finance department that funds from the \$4 million in letters of credit were not immediately available to Chan, which was information that supported the improper recording of revenue from the separate \$2.6 million fourth quarter 1998 OEM transaction with Chan.

66. In the fourth quarter of 1998, Hill authorized providing a false board resolution to Inso's bank in order to ensure recording of revenue from the \$2.6 million fourth quarter OEM transaction with Chan.

67. Marshall failed to inform members of Inso's finance department at the end of the third quarter of 1998 that he had entered into a side agreement with Chan providing that Inso, not Chan, would sell the \$3 million of software to US Airways, and that Chan would make a \$160,000 commission while taking no financial risk.

68. In or about December 1998, Marshall also provided false information and documents to Inso's CFO to obtain payment of the commission Marshall had promised to Chan in September 1998.

**In March 1999, Inso Restated its Financial Results  
Reported on Forms 10-Q for the First Three Quarters of 1998**

69. In March 1999, Inso corrected improperly reported financial results contained in its Form 10-Q filings for the first three quarters of 1998. In its restatement of financial results, Inso reduced nine-month revenue for the first three quarters of 1998 by approximately \$7.1 million, from \$52.5 million to \$45.4 million; and reduced net income (profit) by approximately \$3.2 million, from \$5.6 million to \$2.4 million. Approximately \$3 million of the reduction in revenue was attributable to the fraudulent third quarter 1998 sale to the Malaysian distributor.

**FIRST CAUSE OF ACTION**

**Hill and Marshall Violated Section 17(a) of the Securities Act**

70. Paragraphs 1 through 69 are hereby realleged and incorporated herein by reference.

71. Between approximately September 1998 and April 1999, Defendants Hill and Marshall provided false and misleading revenue information and/or failed to provide material revenue information to Inso's finance department regarding the third quarter sales transaction with Chan. As a result of Hill's and Marshall's conduct, Inso's Form S-3 filed on or about December 18, 1998 (that incorporated Inso's third quarter financial statements by reference) reported materially false and misleading financial results that included revenue that did not conform with GAAP or with the company's own revenue recognition policy. Accordingly, this

public offering document contained untrue statements of material fact and omitted to state material facts necessary to make the statements made, in light of the circumstances under which they were made, not misleading.

72. Defendants Hill and Marshall knew, or were reckless in not knowing, that Inso's Form S-3 was materially false and misleading.

73. Defendants Hill and Marshall, in the offer or sale of a security by use of the means or instruments of transportation or communication in interstate commerce or by use of the mails, directly or indirectly: (a) employed a device, scheme, or artifice to defraud; or (b) obtained money or property by means of any untrue statement of a material fact or any omission 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 any transaction, practice or course of business which operates or would operate as a fraud or deceit upon the purchaser in violation of Section 17(a) of the Securities Act [15 U.S.C. § 77q(a)].

74. By reason of the foregoing, Defendants Hill and Marshall each violated Section 17(a) of the Securities Act.

### **SECOND CAUSE OF ACTION**

#### **Hill and Marshall Violated Section 10(b) of the Exchange Act and Rule 10b-5 Thereunder**

75. Paragraphs 1 through 74 are hereby realleged and incorporated herein by reference.

76. Inso's Form 10-Q for the quarter ended September 30, 1998 contained false and misleading statements of material fact. The Form 10-Q filed with the Commission and made

available to the public contained financial statements that were not in conformity with GAAP or with the company's own revenue recognition policy, and which falsely inflated Inso's revenue and income. This public filing contained untrue statements of material fact and omitted to state material facts necessary to make the statements made, in light of the circumstances under which they were made, not misleading.

77. Between approximately September 1998 and April 1999, Defendants Hill and Marshall provided false and misleading revenue information and/or failed to provide material revenue information to Inso's finance department regarding the third quarter sales transactions with Chan. As a result of Hill's and Marshall's conduct, Inso's Form 10-Q for the third quarter of fiscal 1998 and a press release reported materially false and misleading financial results that included revenue that did not conform with GAAP or with the company's own revenue recognition policy. These public statements contained untrue statements of material fact and omitted to state material facts necessary to make the statements made, in light of the circumstances under which they were made, not misleading.

78. Defendants Hill and Marshall knew, or were reckless in not knowing, that Inso's Form 10-Q for the third quarter of fiscal 1998 and the press release issued in connection with third quarter financial results were false and misleading.

79. Defendants Hill and Marshall, in connection with the purchase or sale of securities, by the use of means or instrumentalities of interstate commerce or of the mails, directly or indirectly: (a) employed devices, schemes or artifices to defraud; (b) made untrue statements of material facts or omitted to state material facts necessary in order to make the statements made, in the light of the circumstances under which they were made, not misleading;



or (c) engaged in acts, practices or courses of business which operated or would operate as a fraud or deceit upon other persons, including purchasers and sellers of such securities, in violation of Section 10(b) of the Exchange Act [15 U.S.C. §78j(b)] and Rule 10b-5 [17 C.F.R. § 240.10b-5] thereunder.

80. By reason of the foregoing, Defendants Hill and Marshall violated Section 10(b) of the Exchange Act and Rule 10b-5 thereunder.

### **THIRD CAUSE OF ACTION**

#### **Hill Aided and Abetted Inso's Uncharged Violations of Section 10(b) of the Exchange Act and Rule 10b-5 Thereunder**

81. Paragraphs 1 through 80 are hereby realleged and incorporated herein by reference.

82. Inso's Form 10-Q for the quarter ended September 30, 1998 contained false and misleading statements of material fact. The Form 10-Q filed with the Commission and made available to the public contained financial statements that were not in conformity with GAAP or with the company's own revenue recognition policy, and which falsely inflated Inso's revenue and income. This public filing contained untrue statements of material fact and omitted to state material facts necessary to make the statements made, in light of the circumstances under which they were made, not misleading. As a result, Inso violated Section 10(b) of the Exchange Act [15 U.S.C. §78m(a)] and Rule 10b-5 thereunder [17 C.F.R. §240.10b-5].

83. Between approximately September 1998 and April 1999, Defendant Hill provided false and misleading revenue information and/or failed to provide material revenue information to Inso's finance department regarding the third quarter sales transactions with Chan. As a result

of Hill's conduct, Inso's Form 10-Q for the third quarter of fiscal 1998 and a press release reported materially false and misleading financial results that included revenue that did not conform with GAAP or with the company's own revenue recognition policy. These public statements contained untrue statements of material fact and omitted to state material facts necessary to make the statements made, in light of the circumstances under which they were made, not misleading.

84. Defendant Hill knew, or was reckless in not knowing, that Inso's Form 10-Q for the third quarter of fiscal 1998 and the press release issued in connection with third quarter financial results were false and misleading.

85. By reason of the foregoing, Hill provided knowing and substantial assistance to Inso's materially false and misleading public statements concerning its third quarter 1998 financial results.

86. As a result, Hill aided and abetted Inso's violations of Section 10(b) of the Exchange Act [15 U.S.C. §78m(a)] and Rule 10b-5 thereunder [17 C.F.R. §240.10b-5].

#### **FOURTH CAUSE OF ACTION**

##### **Hill and Marshall Aided and Abetted Inso's Uncharged Violations of Section 13(a) of the Exchange Act and Rules 13a-13 and 12b-20 Thereunder**

87. Paragraphs 1 through 86 are hereby realleged and incorporated herein by reference.

88. Section 13(a) of the Exchange Act requires all issuers subject to the reporting requirements of the Exchange Act to file periodic and other reports containing such information as the Commission's rules prescribe. Rule 13a-13, promulgated pursuant to Section 13(a),

requires issuers to file with the Commission accurate quarterly reports, including accurate disclosures of their revenues and net income. Rule 12b-20 requires issuers of securities registered under Section 12 of the Exchange Act to add to any required information in a statement or report any such further material information as may be necessary to make the required statements, in light of the circumstances under which they were made, not misleading.

89. Inso violated Section 13(a) of the Exchange Act [15 U.S.C. § 78m(a)] and Rules 13a-13 and 12b-20 [17 C.F.R. §§ 240.13a-13 and 240.12b-20] (the "Reporting Provisions") by including in its Form 10-Q for the third quarter of fiscal 1998 financial statements that included revenue from the sham sale of software licenses to Chan, and that therefore inaccurately reported Inso's revenue and failed to conform with GAAP (as required by Regulation S-X [17 C.F.R. § 210.1-01, et seq.]). In addition, the description of Inso's financial condition in those periodic reports violated the Reporting Provisions by making untrue statements of material fact and omitting to state material facts necessary to make the statements made, in light of the circumstances under which they were made, not misleading.

90. By knowingly rendering substantial assistance to Inso's violations, Defendants Hill and Marshall each aided and abetted Inso's violations of Section 13(a) of the Exchange Act, and Rules 13a-13 and 12b-20 thereunder.

#### **FIFTH CAUSE OF ACTION**

#### **Hill and Marshall Aided and Abetted Inso's Uncharged Violation of Section 13(b)(2)(A) of the Exchange Act**

91. Paragraphs 1 through 90 are hereby realleged and incorporated herein by reference.

92. Inso violated Section 13(b)(2)(A) of the Exchange Act [15 U.S.C. § 78m(b)(2)(A)] by maintaining false and misleading books and records, which, among other things, materially overstated the Company's revenue for the third quarter of 1998.

93. By knowingly rendering substantial assistance to Inso's violations, Defendants Hill and Marshall each aided and abetted Inso's violations of Section 13(b)(2)(A) of the Exchange Act.

### **SIXTH CAUSE OF ACTION**

#### **Hill and Marshall Violated Section 13(b)(5) of the Exchange Act and Rule 13b2-1 Thereunder**

94. Paragraphs 1 through 93 are hereby realleged and incorporated herein by reference.

95. Defendants Hill and Marshall contributed to Inso's accounting failures by knowingly failing to provide to those responsible for maintaining Inso's books and records material information that should have been reflected in Inso's financial records, and by providing materially false documents and information to those responsible for maintaining Inso's books and records. Accordingly, each of them violated Section 13(b)(5) of the Exchange Act [15 U.S.C. § 78m(b)(5)] by knowingly circumventing or failing to implement a system of internal accounting controls and/or knowingly falsifying the books, records and accounts of Inso.

96. Defendants Hill and Marshall caused Inso's internal books and records to be falsified in violation of Rule 13b2-1 of the Exchange Act [17 C.F.R. § 240.13b2-1], which provides, in part, that "[n]o person shall directly or indirectly, falsify or cause to be falsified, any book, record, or account."

**SEVENTH CAUSE OF ACTION**

**Hill and Marshall Violated Rule 13b2-2  
Promulgated Under Section 13(b) of the Exchange Act**

97. Paragraphs 1 through 96 are hereby realleged and incorporated herein by reference.

98. Between approximately September 1998 and April 1999, Defendants Hill and Marshall, officers of Inso, directly or indirectly, made or caused to be made materially false or misleading statements or omissions to accountants in connection with an audit or examination of Inso's financial statements, Inso's public filings, and Inso's preparation or filing of documents or reports required to be filed with the Commission.

99. By reason of the foregoing, Defendants Hill and Marshall violated Rule 13b2-2 promulgated under Section 13(b) of the Exchange Act. [17 C.F.R. § 240.13b2-2].

**EIGHTH CAUSE OF ACTION**

**Paxhia is Liable as a Control Person for Inso's Uncharged Violations  
of Sections 10(b), 13(a), and 13(b)(2)(A) of the Exchange Act,  
and Rules 10b-5, 12b-20, and 13a-13 thereunder**

100. Paragraphs 1 through 99 are hereby realleged and incorporated herein by reference.

101. Between approximately September 1998 and March 1999, Defendant Paxhia was, directly or indirectly, a controlling person of Inso for purposes of Section 20(a) of the Exchange Act [15 U.S.C. §78t(a)].

102. Between approximately September 1998 and March 1999, Inso violated Sections 10(b), 13(a), and 13(b)(2)(A) of the Exchange Act [15 U.S.C. §§ 78j(b), 78m(a), and

78m(b)(2)(A)] and Rules 10b-5, 12b-20, and 13a-13 thereunder [17 C.F.R. §§ 240.10b-5, 240.13a-13, and 240.12b-20], through the actions of Defendants Hill and Marshall, as alleged above.

103. As a controlling person of Inso between approximately September 1998 and March 1999, Defendant Paxhia is jointly and severally liable with and to the same extent as Inso for Inso's violations of Sections 10(b), 13(a), and 13(b)(2)(A) of the Exchange Act [15 U.S.C. §§ 78j(b), 78m(a), and 78m(b)(2)(A)] and Rules 10b-5, 12b-20, and 13a-13 thereunder [7 C.F.R. §§ 240.10b-5, 240.13a-13, and 240.12b-20] during this time period alleged above.

**PRAYER FOR RELIEF**

104. Accordingly, the Commission respectfully requests that this Court issue a Final Judgment of Permanent Injunction and Other Relief:

A. Permanently restraining and enjoining Defendants Hill and Marshall, their agents, servants, employees, and attorneys, and those persons in active concert or participation with them, and each of them from violating, directly or indirectly, Sections 10(b), 13(a), 13(b)(2)(A), and 13(b)(5) of the Exchange Act and Rules 10b-5, 12b-20, 13a-13, 13b2-1, and 13b2-2 thereunder;

B. Permanently restraining and enjoining Defendant Paxhia, his agents, servants, employees, and attorneys, and those persons in active concert or participation with him, and each of them from violating, directly or indirectly, Sections 10(b), 13(a), and 13(b)(2)(A) of the Exchange Act and Rules 10b-5, 12b-20, and 13a-13 thereunder;

C. Ordering Defendants Hill and Marshall to pay civil penalties pursuant to Section 20(d) of the Securities Act and Section 21(d) of the Exchange Act;

D. Ordering Defendants Hill and Marshall to disgorge losses avoided, plus pre-judgment interest from their sale of Inso stock as described above;

E. Ordering Defendant Paxhia to disgorge losses avoided, plus pre-judgment interest from his sale of Inso stock as described above;

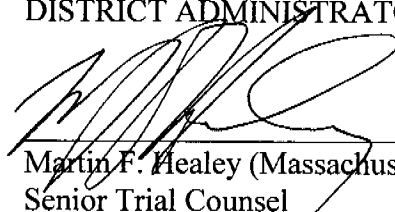
F. Pursuant to Section 20(e) of the Securities Act [15 U.S.C. § 77t(e)] and Section 21(d)(2) of the Exchange Act [15 U.S.C. § 78u(d)(2)], prohibiting Defendants Hill and Marshall from acting as officers or directors of any issuer that has a class of securities registered pursuant to Section 12 of the 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)]; and

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

Respectfully submitted,

JUAN MARCEL MARCELINO  
DISTRICT ADMINISTRATOR

By:

  
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November 18, 2002

**CERTIFICATE OF SERVICE**

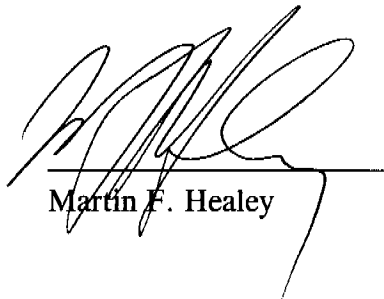
This certifies that on November 18, 2002, I caused copies of Plaintiff Securities & Exchange Commission's Opposition to Defendant Hill's Motion to Dismiss and copies of the Amended Complaint in this matter to be served on counsel for defendants and/or the defendants at the below addresses:

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