UNITED STATES DISTRICT COURT
DISTRICT OF COLUMBIA

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

Plaintiff,

v.

WILLIAM B. LUM and MICHAEL SALTZSTEIN,

Defendants.

COMPLAINT

CASE NUMBER 1:99CV00170

JUDGE: Henry H. Kennedy

DECK TYPE: Civil General

DATE STAMP: 01/21/99

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

SUMMARY

1. This insider trading case concerns the defendants' purchases of Regency Health Services, Inc. common stock prior to the July 27, 1997 announcement that Sun Healthcare Group, Inc. would commence a tender offer for Regency's common stock. Defendant William B. Lum, a Hawaiian Airlines Inc. director, was present during a July 13, 1997 dinner meeting of Hawaiian Airlines' directors and senior management when Regency's chief executive officer (also a Hawaiian Airlines director) Richard Matros discussed the nonpublic tender offer negotiations. At a Hawaiian Airlines board meeting the next day, Hawaiian Airlines' chairman John Adams (also Regency's chairman) warned the attendees, including Lum, that they should not trade in Regency securities based on anything they had heard at the prior evening's dinner. Lum, who had been a long time Regency

shareholder, had liquidated part of his position in Regency in late May and early June 1997, selling 16,000 shares as well as 100 call options. Immediately after the board meeting Lum began buying shares of Regency common stock, in breach of his duty to Hawaiian Airlines. Between July 15 and July 22, 1997, Lum purchased 30,000 Regency shares. After the tender offer was announced, Lum sold some of his illegally obtained shares in the open market, and later tendered the remaining shares, realizing profits of $214,043.75.

2. On July 14, 1997, defendant Michael Saltzstein, by virtue of his employment with Regency, was entrusted with material nonpublic information concerning Sun's planned tender offer. In breach of his duty to Regency and its shareholders, on July 22 Saltzstein purchased 400 shares of Regency common stock. After the tender offer was announced, Saltzstein tendered his illegally obtained shares, realizing profits of $2,850.

3. By their insider trading, defendants violated Sections 10(b) and 14(e) of the Securities Exchange Act of 1934 ("Exchange Act") [15 U.S.C. §§ 78j(b) and 78n(e)], and Rules 10b-5 and 14e-3 [17 C.F.R. §§ 240.10b-5 and 240.14e-3] thereunder. The Commission requests that this Court permanently enjoin the defendants from violating the above statutory provisions and rules, order disgorgement of all illegal trading profits with prejudgment interest thereon, and impose civil penalties.

JURISDICTION AND VENUE

4. The Commission brings this action pursuant to authority conferred upon it by Sections 21(d), 21(e), and 21A(a) of the Exchange Act [15 U.S.C. §§ 78u(d), 78u(e), and 78u-1(a)] to permanently restrain and enjoin the defendants from engaging in the acts, practices and courses of business alleged herein, and for other relief.

5. This Court has jurisdiction over this action pursuant to Sections 21(e), 21A(d)(4), and 27 of the Exchange Act [15 U.S.C. §§ 78u(e), 78u-1(d)(4), and 78aa].

6. Defendants, directly or indirectly, have made use of the means and instrumentalities of interstate commerce or of the mails in connection with the acts, practices and courses of business alleged herein.

THE DEFENDANTS

7. William B. Lum, age 60, resides in Short Hills, New Jersey. At all relevant times, Lum was a director of Hawaiian Airlines.

8. Michael Saltzstein, age 36, resides in Spring Valley, California. At all relevant times, Saltzstein was employed by Regency as a risk manager.

RELEVANT ISSUERS

9. Regency, based in Tustin, California, was a provider of inpatient services at 166 facilities in six states. Those services included rehabilitation, skilled nursing, neurological care, and assisted living. Its common stock was registered with the Commission pursuant to Section 12(b) of the Exchange Act [15 U.S.C. § 78l (b)] and traded on the New York Stock Exchange. Regency's options traded on the Chicago Board Options Exchange.

10. Sun, based in Albuquerque, New Mexico, operates long-term care facilities and pharmacies in the United States and United Kingdom. Sun subsidiaries also provide therapy services in the United States, fulfill the medical supply needs of nursing homes, and offer ancillary services for the healthcare industry. Its common stock is registered with the Commission pursuant to Section 12(b) of

the Exchange Act [15 U.S.C. § 78l (b)] and trades on the New York Stock Exchange. Sun's options trade on the Chicago Board Options Exchange.

11. Hawaiian Airlines, based in Honolulu, Hawaii, operates a passenger airline with service to the Hawaiian and other South Pacific islands and selected West Coast cities. Its common stock is registered with the Commission pursuant to Section 12(b) of the Exchange Act [15 U.S.C. § 78l (b)] and trades on the American Stock Exchange.

THE TENDER OFFER NEGOTIATIONS

12. In or about late May 1997, Matros telephoned Sun's chief executive officer Andrew Turner to inquire whether Sun would consider acquiring Regency. Turner expressed interest and, on or about June 3, 1997, Sun and Regency executed a written agreement whereby Regency would negotiate exclusively with Sun for a specified period on a confidential basis. Early that month, Sun also engaged lawyers to advise it with respect to an acquisition of Regency.

13. On June 20, 1997, Regency's board of directors held a special meeting to discuss, among other matters, the possibility of selling Regency to Sun. At the meeting, the board authorized management to "look into the possible sale of the Corporation or other viable alternatives" and, in doing so, to engage investment bankers. On or about July 2, 1997, Regency engaged Smith Barney as its investment banker. On July 3, Sun retained an investment banker to advise it in the negotiations.

14. On July 7 Regency management began working with Smith Barney representatives to determine the expected economic benefits of a transaction with Sun. The next day Sun and Regency executed a second agreement whereby Regency agreed that it would negotiate exclusively with Sun, on a confidential basis, until July 18.

15. On July 9, representatives of Regency and Smith Barney presented an overview of Regency's business to representatives of Sun and Sun's investment banker. That same day, Sun began its due diligence of Regency and, in a letter dated July 12, 1997, communicated to Regency a written indication of interest in acquiring all of Regency's outstanding common stock for $21 per share in cash.

LUM LEARNS OF THE TENDER OFFER NEGOTIATIONS

16. On the evening of July 13, Adams, the chairman of both Hawaiian Airlines and Regency, hosted a dinner for the Hawaiian Airlines board and senior management at the Newport Beach Four Seasons Hotel. The dinner preceded a Hawaiian Airlines board meeting that was to be held, for convenience of the attendees, in Regency's boardroom on July 14. Lum attended both the July 13 dinner and the July 14 board meeting.

17. During the July 13 dinner, Matros, who had just learned of Sun's indication of interest in acquiring Regency for $21 per share, described Regency's negotiations with Sun in an animated way to Robert Coo, an outside director to both Regency and Hawaiian Airlines. Lum and others were present during that dinner and Lum knew, or was reckless in not knowing, that the information Matros disclosed was material and nonpublic and that he had a duty to treat it confidentially.

18. Adams was concerned about Matros' disclosure of material nonpublic information at the dinner and, at the start of the Hawaiian Airlines board meeting on July 14, admonished the attendees that they should not trade in Regency's securities based on anything they had heard the prior evening concerning Regency, and that they should consider themselves insiders of Regency. Lum was present when that instruction was given and did not express any objection to assuming such an obligation.

Further, Lum had a long history of maintaining the confidentiality of information that Adams and Matros confided in him as part of his service on the Hawaiian Airlines board.

19. Hawaiian Airlines prohibited directors from trading in securities while in possession of material nonpublic information obtained as directors. Hawaiian Airlines' "Policy on Avoidance of Insider Trading" included an instruction to Hawaiian Airlines' directors "not to purchase or sell securities of the Company <u>or of any other issuer of a security</u> at a time when the director, officer or employee is aware of any material nonpublic information about the issuer, regardless of how that information was obtained." (Emphasis added.) Prior to this date, Lum had acknowledged in writing that he had reviewed and understood the "Policy on Avoidance of Insider Trading." Adams' warning not to trade was consistent with this policy.

<u>CONCLUSION OF THE NEGOTIATIONS AND INSIDER TRADING</u>

20. On July 14, Regency responded to Sun's indication of interest by requesting a higher price. That same day, Sun increased its offer to $22 per share. At a meeting the next day, Regency's board authorized management to consummate the transaction at that price, subject to board approval at the completion of the negotiations, and receipt of a fairness opinion.

21. In spite of Adams' warning not to trade in Regency stock and Lum's long-standing confidential relationship with Adams and Matros as members of the Hawaiian board, on July 15 Lum purchased 25,000 shares of Regency common stock at prices ranging from $14.6875 to $14.8125 per share.

22. During the next ten days, Sun continued its due diligence and concluded the arrangement for financing the tender offer. On Monday, July 14, Regency's chief financial officer informed

Saltzstein of the negotiations and directed him to assist with Sun's due diligence examination. During the rest of that week Saltzstein worked closely with Sun's risk manager, providing her with nonpublic information about Regency, and the two discussed the contemplated acquisition of Regency by Sun. Saltzstein knew, or was reckless in not knowing, that the information he had received about the planned tender offer was material and nonpublic and that he had a duty to treat the information confidentially.

23. On July 22 Saltzstein purchased 400 shares of Regency stock for $14.875 per share. That same day defendant Lum purchased an additional 5,000 shares of Regency stock, also for $14.875 per share.

24. At the conclusion of Sun's due diligence, the parties negotiated definitive merger and stockholder agreements, which were approved by the boards of Sun and Regency on July 25 and 26, respectively.

25. On July 27, 1997, Sun and Regency jointly announced the tender offer, causing Regency's stock price to increase. Lum sold 5,000 Regency shares on August 11 for $21.3125 per share, and tendered the remaining 25,000 shares he had purchased for $22 per share on October 9, 1997. Saltzstein tendered the shares he had purchased for $22 per share in November 1997.

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FIRST CLAIM

Lum and Saltzstein Violated 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

26. Paragraphs 1 through 25 are realleged and incorporated herein by reference.

27. Lum purchased Regency stock while in possession of material nonpublic information that he misappropriated in breach of his duty to Hawaiian Airlines.

28. Saltzstein purchased Regency stock while in possession of material nonpublic information in breach of his duty to Regency and its shareholders.

29. By reason of the foregoing, Lum and Saltzstein violated 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.

SECOND CLAIM

Lum and Saltzstein Violated Section 14(e) of the Exchange Act [15 U.S.C. § 78n(e)] and Rule 14e-3 [17 C.F.R. § 240.14e-3] Thereunder

30. Paragraphs 1 through 29 are realleged and incorporated herein by reference.

31. On or before July 12, 1997, Sun had taken substantial steps to commence a tender offer for the common stock of Regency.

32. Lum and Saltzstein purchased securities of Regency while in possession of material information concerning Sun's planned tender offer for Regency that they knew or had reason to know was nonpublic and that they acquired from Regency officers.

33. By reason of the foregoing, defendants Lum and Saltzstein violated Section 14(e) of the Exchange Act [15 U.S.C. § 78n(e)] and Rule 14e-3 [17 C.F.R. § 240.14e-3] thereunder.

PRAYER FOR RELIEF

WHEREFORE, the Commission respectfully requests that this Court:

I.

Grant a Final Judgment permanently restraining and enjoining Lum and Saltzstein, and their officers, agents, servants, employees, and attorneys, and all persons in active concert or participation with them, and each of them, from violating Sections 10(b) and 14(e) of the Exchange Act [15 U.S.C. §§ 78j(b) and 78n(e)] and Rules 10b-5 and 14e-3 [17 C.F.R. §§ 240.10b-5 and 240.14e-3] thereunder.

II.

Order Lum and Saltzstein to disgorge their illegal trading profits, plus prejudgment interest, and to pay civil penalties pursuant to Section 21A of the Exchange Act [15 U.S.C. § 78u-1].

III.

Grant such other relief as the Court may deem just and appropriate.

Dated: January ___, 1999

Respectfully submitted,

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