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U.S. DISTRICT COURT

SEP 29 2000

LITIGATION  
J.P.  
Clerk of Court

IN THE UNITED STATES DISTRICT COURT  
FOR THE NORTHERN DISTRICT OF GEORGIA  
ATLANTA DIVISION

SECURITIES AND EXCHANGE COMMISSION, :

Plaintiff, :

ETS PAYPHONES, INC. and  
CHARLES E. EDWARDS, :

Defendants. :

Civil Action File No.

1:00-CV-2532

COMPLAINT FOR INJUNCTIVE AND OTHER RELIEF

It appears to Plaintiff, Securities and Exchange Commission ("Commission" or "SEC"), and it alleges that:

OVERVIEW OF DEFENDANTS' SCHEME

1. This matter involves a fraudulent and unregistered offering of securities by ETS Payphones, Inc. ("ETS") and its chief executive officer, Charles E. Edwards ("Edwards") in violation of the registration and antifraud provisions of the federal securities laws. The scheme is based upon purported investments in customer-owned coin-operated telephones, and has raised approximately \$300 million from more than 10,000 investors. ETS offers and sells pay telephones with leaseback contracts. Investments are offered and sold in units involving a telephone, site lease, lease/back agreement and buy/back agreement. The investments constitute investment contracts and therefore are securities. The investment program has operated as a Ponzi scheme, i.e. a scheme whereby returns are paid to investors from monies contributed by later investors.

2. No registration statement has ever been filed in connection with the securities.

3. Selling materials issued to investors state that pay phones are a profitable business. Edwards has represented to investors that ETS is profitable. In fact, ETS is operating in the manner of a Ponzi scheme and is incurring significant net losses from payphone operations.

4. ETS is dependent on the sale of new payphone investments in order to meet its current financial obligations, such as investor lease payments and refunds.

5. An ETS disclosure document given to investors grants the investor the right to sell their payphone back to ETS for the original purchase price. However, ETS does not have the financial resources to purchase the phones if a significant number of investors request refunds.

6. Based on the foregoing, the Commission is seeking an order prohibiting the destruction of documents, preliminary and permanent injunctions, accountings, disgorgement together with prejudgment interest, and civil penalties against ETS and Edwards and an asset freeze as to Edwards, based on violations of Sections 5(a), 5(c) and 17(a) of the Securities Act of 1933 ("Securities Act"), [15 U.S.C. 77e(a), 77e(c) and 77q(a)] and Section 10(b) of the Securities Exchange Act of 1934 ("Exchange Act") [15 U.S.C. 78j(b)] and Rule 10b-5 [17 C.F.R. 240.10b-5] thereunder.

#### JURISDICTION AND VENUE

7. 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 21(e) of the Exchange Act [15 U.S.C. 78u(d) and 78u(e)] to enjoin the defendants from engaging in transactions, acts, practices and courses of business alleged in this complaint, and transactions, acts, practices, and courses of business of similar purport and object, for disgorgement of illegally obtained funds and other equitable relief, and for civil money penalties.

8. The Court has jurisdiction of this action pursuant to Sections 20(b), 20(d) and 22(a) of the Securities Act [15 U.S.C. 77t(b), 77t(d) and 77v(a)] and Sections 21(d), 21(e) and Section 27 of the Exchange Act [15 U.S.C. 78u(d), 78u(e) and 78aa].

9. The defendants, directly and indirectly, made use of the mails, and the means and instrumentalities of transportation and communication in interstate commerce, in connection with the transactions, acts, practices and courses of business alleged in the complaint.

10. Certain of the transactions, acts, practices and courses of business constituting violations of the Securities Act and the Exchange Act have occurred in the Northern District of Georgia, including the solicitation of investors who reside within the Northern District of Georgia. Furthermore, defendant ETS is situated in and defendant Edwards resides within the Northern District of Georgia.

11. The defendants, unless restrained and enjoined by this Court, will continue to engage in the transactions, acts, practices and courses of business of similar purport and object.

#### THE DEFENDANTS

12. ETS Payphones, Inc. is a Georgia corporation formed in October 1994. Edwards owns ninety-nine percent of the ETS shares outstanding. ETS claims that it currently owns or operates 47,000 private payphones in 32 states. ETS's offices are located in Lithia Springs, Georgia, an Atlanta suburb. ETS filed a voluntary petition under Chapter 11 of the bankruptcy code on or about September 11, 2000.

13. Charles E. Edwards, age 61 and a resident of Duluth, Georgia, is the founder and chairman of ETS. ETS sales documents state that Edwards has over thirty years of experience

building successful sales organizations and that he has spent the last nine years in the telecommunications industry.

### FACTS

#### A. The ETS Investment Program

14. Beginning in or about October 1994 until on or about September 11, 2000, ETS under the direction of Edwards, offered "pay telephone" investments to the general public. Investments were offered in units, which include a pay telephone, a site location, a lease/back agreement, and a buy/back agreement.

15. Each unit was sold for \$6,750. ETS received \$5,250. The marketing company received the difference.

16. The investments have been sold through various means, including sales agreements with marketing companies. The marketing companies have made arrangements with licensed insurance agents to market and sell the ETS payphones.

17. The marketing companies or their agents have made the sale and ETS and its subsidiary PSA, Inc. has purportedly assigned a payphone to the investor.

18. There has been as much as a three-month lag between the time an investor purchased his payphone until the time he actually was assigned the payphone.

19. ETS manages the operations of the payphones, and currently has approximately 47,000 payphones under management.

20. ETS and the marketing companies have used the mails and other jurisdictional means to market the investments.

21. ETS operates a website which contains statements such as “there are millions to be made from owning pay phones” and describe payphone ownership as “virtually recession-proof” and offering a “steady, immediate cash flow.”

22. Many of the investors are elderly. Substantially all have no experience managing payphones and are dependent upon the experience and resources of ETS to obtain the promised return.

23. ETS and the marketing companies have offered three basic programs for payphone purchasers. However, the program recommended by the selling agents and the program that substantially all investors have subscribed to is called the Payphone Equipment Lease Program (“lease program”).

24. Under this agreement, the investor purchased a payphone and entered into an agreement to lease the payphone back to ETS for a period of sixty months (the investor becomes the lessor and ETS becomes the lessee of the payphone). ETS agreed to pay the investor a lease payment of \$82 per month per unit over the sixty-month period. These lease payments represent a 15% annual return to the investor, and are to be paid regardless of the revenue obtained from the specific payphone owned by the investor.

25. At the end of the sixty-month period, the investor had the option of renewing the lease or selling the payphone back to ETS for a full refund of the investment amount.

26. ETS also offered a full refund within 180 days of the investor’s request during the initial sixty-month period.

27. During the term of the lease, the investors can cancel their leases upon 90 days notice and take possession of their phones.

28. Investors under the lease program have no involvement in the operation of the pay telephone site.

29. ETS manages and maintains the payphones, including interior and exterior maintenance as well as coin retrieval. Title to the phone and all tax advantages purportedly remain with the investor.

30. Under the lease program, ETS has the right to move the phone from one location to another.

31. The second alternative program, which was purportedly available but hardly ever sold, was called the Internal Maintenance Program ("internal program"). Under the internal program, investors would be responsible for external maintenance, including general appearance of the telephone and of the site, as well as collection of the coins. Under this program, ETS would manage internal telephone monitoring and determine the service needs of the telephone. ETS would be responsible for sending service technicians to make necessary repairs, and for reporting repairs and non-coin revenues (such as from credit cards or telephone cards) to the owners on a monthly basis. ETS would perform these services for a fixed monthly fee. Under this alternative the return to the investor would, at least hypothetically, vary depending on the revenues received by the assigned telephone.

32. As a third option, ETS also purported to offer to sell telephone equipment with no associated agreements. However, this option, like the internal program, was hardly ever sold.

33. The lease program units are securities. ETS has never filed a registration statement with the Commission in connection with the offer and sale of these securities. No exemption from registration is applicable.

34. At least some ETS sales package included a selling brochure and a “Basic Disclosure Document Presented by ETS Payphones, Inc.” (the “disclosure document”), which was presented to investors and potential investors at Edwards’s direction.

35. The selling brochure includes general information about the payphone industry and includes discussions about the “profitability” of payphones.

36. The disclosure document contains brief descriptions of the company, brief biographies of management, and descriptions of the payphone management options available to investors. It also includes copies of the “telephone equipment lease agreement” and “the option to sell agreement” to be signed by ETS and the investor.

37. ETS also has a website on the Internet which includes three brief sections describing the business of ETS, the payphone industry generally and the “profitable opportunities” of payphones.

38. The ETS selling brochure contains statements in bold print such as “watch the profits add up” and “why are pay phones so profitable.” The selling brochure also contains a table entitled “Incremental Economics of a Medium-Volume Pay Phone” which shows a positive gross margin of \$164 per month.

39. On July 1, 2000, Edwards sent a document to investors which represented, among other things, that ETS was profitable. Edwards also verbally represented to investors that ETS was profitable.

40. Unaudited financial statements of ETS as of December 31, 1998, March 31, 1999 and June 30, 2000 reveal that ETS has consistently been in a precarious financial situation and

that payphone operations were not profitable. At all times during the course of the scheme, Edwards was aware of the true financial condition of ETS.

41. For example, ETS financial statements prepared in accordance with generally accepted accounting principles revealed that ETS had a stockholders' deficit of \$24,493,531 at March 31, 1999 and that ETS had a net loss from operations of \$32,033,347 for the fifteen-month period ending March 31, 1999.

42. ETS has continued to lose money on its telephone operations, and specifically lost more than \$33 million from its telephone operations during the first six months of 2000.

43. In fact, ETS has consistently been dependent on the sale of new payphones in order to meet its lease and refund obligations.

44. The financial condition of ETS and its dependency on new investors has not been disclosed to investors.

45. In its lease agreements, ETS contracted to "buy back" the investor's payphone at any time during the first sixty months of the lease term (the "put option").

46. Pursuant to the lease agreements, the investor must notify ETS of his intention to exercise the put option and is promised a full refund of the investment within 180 days of notification.

47. Additionally, an investor can either renew the lease or receive a full refund at the end of the five-year lease term. ETS is obligated to pay the refunds.

48. If a significant number of investors were to exercise their put options or request refunds at or near the same time period, Edwards knew that ETS did not have the cash to make such payments. Edwards knew that fact but it was not disclosed to investors.



49. During the course of the scheme, Edwards has taken at least \$14 million out of ETS through loans and fees paid to companies controlled by him.

CLAIMS FOR RELIEF

COUNT I

Violations of § 17(a) of the Securities Act [15 U.S.C. § 77q(a)]

50. Paragraphs 1-49 are hereby realleged and are incorporated herein by reference.

51. From in or about October 1994 through at least September 10, 2000, defendants ETS and Edwards, in the offer and sale of securities, specifically the above-described securities, by use of the means and instruments of transportation and communication in interstate commerce or by use of the mails,

(a) directly and indirectly employed devices, schemes and artifices to defraud purchasers of such securities;

(b) directly and indirectly 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, not misleading; and

(c) engaged in transactions, practices and a course of business which would have operated as a fraud or deceit upon the purchasers of such securities, all as more particularly described in paragraphs 1-49 above.

52. Defendants ETS and Edwards knowingly, intentionally, and/or recklessly engaged in the aforementioned devices, schemes and artifices to defraud.

53. By reason of the foregoing, defendants ETS and Edwards have violated and, unless restrained and enjoined, will continue to violate §17(a) of the Securities Act [15 U.S.C. § 77q(a)].

## COUNT II

### Violations of § 10(b) of the Exchange Act [§ 15 U.S.C. 78j(b) and Rule 10b-5 Thereunder [17 C.F.R. § 240.10b-5]

54. Paragraphs 1-49 are hereby realleged and are incorporated herein by reference.

55. From in or about October 1994 through at least September 10, 2000, defendants ETS and Edwards, by their conduct as set forth above, singly and in concert, by the use of means and instrumentalities of interstate commerce and by the use of the mails, directly and indirectly:

(a) employed devices, schemes, and artifices to defraud;

(b) made untrue statements of material facts and omitted to state material facts necessary in order to make the statements made, in light of the circumstances under which they were made, not misleading; and

(c) engaged in acts, practices and courses of business which operated as a fraud and deceit upon persons, all more particularly described in paragraphs 1-49 above.

56. Said defendants knowingly, intentionally and/or recklessly engaged in the above-described conduct.

57. The statements and representations alleged herein were known to defendants or recklessly disregarded by them to be materially false and misleading. In making the material

misrepresentations of fact and material omissions described herein, defendants acted with scienter, that is, with an intent to deceive, manipulate or defraud with reckless disregard for the truth.

58. By reason of the foregoing, defendants ETS and Edwards have violated and, unless restrained and enjoined will continue to violate § 10(b) of the Exchange Act [15 U.S.C. § 78j(b)] and Rule 10b-5 thereunder [17 C.F.R. § 240.10b-5].

### COUNT III

#### Violations of § 5(a) and 5(c) of the Securities Act [15 U.S.C. § 77e(a) and 77e(c)]

59. Paragraphs 1-49 are hereby realleged and are incorporated herein by reference.

60. From in or about October 1994 through at least September 10, 2000, defendants ETS and Edwards, directly and indirectly, singly and in concert have, and unless enjoined will continue to:

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

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

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

without a registration statement having been filed or being in effect with the Commission; including but not limited to, the activities described in paragraphs 1-49 above.

PRAAYER FOR RELIEF

WHEREFORE, the Plaintiff Commission, respectfully prays that the Court:

I.

Make findings that each and every defendant committed violations alleged herein.

II.

§ 17(a) of the Securities Act

Issue preliminary and permanent injunctions restraining and enjoining defendants ETS and Edwards, as well as their agents, servants, employees, attorneys and all persons in active concert or participation with them, who receive actual notice of the order of injunction, by personal service or otherwise, and each of them in the offer or sale of any securities by the use of any means or instruments of transportation or communication in interstate commerce or by the use of the mails, from directly or indirectly:

(a) employing any device, scheme, or artifice to defraud;

(b) obtaining 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 the light of the circumstances under which they were made, not misleading; or

(c) engaging in any transaction, practice, or course of business which operates or would operate as a fraud or deceit upon the purchaser of such securities.

III.

§ 10(b) of the Exchange Act and Rule 10b-5 Thereunder

Issue preliminary and permanent injunctions restraining and enjoining defendants ETS and Edwards as well as their agents, servants, employees, attorneys, and all persons in active concert or participation with them, who receive actual notice of the order of injunction, by personal service or otherwise, and each of them in connection with the purchase or sale of securities, by the use of any means or instruments of transportation or communication in interstate commerce or by use of the mails, from directly or indirectly:

(a) employing any device, scheme or artifice to defraud;

(b) making any untrue statement of a material fact or omitting 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) engaging in any act, practice, or course of business which operates or would operate as a fraud or deceit on any person.

#### IV.

#### § 5(a) and 5(c) of the Securities Act

Issue preliminary and permanent injunctions restraining and enjoining defendants ETS and Edwards, as well as their agents, servants, attorneys, and all persons in active concert or participation with them, who receive actual notice of the order of injunction, by personal service, facsimile or otherwise, and each of them, by use of the mails or any means or instrumentality of interstate commerce, from directly or indirectly:

(a) making use of any means or instruments of transportation or communication in interstate commerce or of the mails to sell securities, in the form of common stock or any other

security, through the use or medium of any prospectus or otherwise, unless and until a registration statement is in effect with the Commission as to such securities;

(b) carrying securities, or causing them to be carried through the mails or in interstate commerce, by any means or instruments of transportation, for the purpose of sale or delivery after sale, unless and until a registration statement is in effect with the Commission as to such securities;

(c) making use of any means or instruments of transportation or communication in interstate commerce or of the mails to offer to sell or offer to buy, through the use or medium of any prospectus or otherwise, any interest in securities, in the form of common stock or any other security;

unless a registration statement is in effect with the Commission as to such securities, or while a statement filed with the Commission as to such security is the subject of a refusal order or stop order or (prior to the effective date of the registration statement) any public proceeding or examination under section 8 of the Securities Act. [15 U.S.C. 77h];  
in violation of section 5 of the Securities Act. [15 U.S.C. 77e].

#### V.

#### Order Prohibiting Destruction of Documents

Orders prohibiting defendants ETS and Edwards, their agents, servants, employees, and those persons in active concert or participation with them who receive actual notice of the orders by personal service, facsimile or otherwise, and each of them, from directly or indirectly, tampering with, mutilating, altering, erasing, concealing, removing, destroying or otherwise disposing of any and all books, records, documents, files, correspondence, computer tapes,

computer disks, computer diskettes or any other data recordings or any type, however created, produced or stored, relating to, pertaining to or referring to the defendants, their officers, directors, employees and agents, or any financial transactions by either of the defendants or to which either of the defendants was a party.

VI.

Order Requiring Accounting, Freeze Of Assets And Disgorgement Of Ill-Gotten Gains

Issue Orders requiring an accounting from the defendants of all funds received from the sale of securities described in this Complaint, an order freezing the assets of defendant Edwards and an order for defendants ETS (to be enforced in ETS's bankruptcy proceeding for so long as it is pending or to be enforced in this proceeding in the absence of a pending bankruptcy), and Edwards to disgorge all ill-gotten gains or unjust enrichment with prejudgment interest, to effect the remedial purposes of the federal securities laws.

VII.

Civil Money Penalties

Issue an Order setting the amount of civil penalties against defendants ETS (to be enforced in ETS's bankruptcy proceeding for so long as it is pending or to be enforced in this proceeding in the absence of a pending bankruptcy) and Edwards pursuant to § 20(d) of the Securities Act [15 U.S.C. § 77t(d)] and § 21(d)(3) of the Exchange Act.

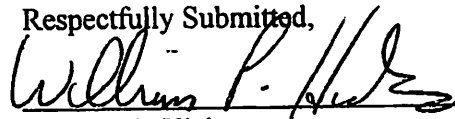
VIII.

Other Relief

Issue findings of fact and conclusions of law in accordance with Rule 52 of the Federal Rules of Civil Procedure, along with such other and further relief as may be just, equitable and appropriate in connection with the enforcement of the federal securities laws and for the

protection of investors. Further, the Securities and Exchange Commission respectfully prays that the Court retain jurisdiction over this action in order to implement and carry out the terms of all orders and decrees that are entered or to entertain any suitable application or motion by the Commission for additional relief within the jurisdiction of this Court.

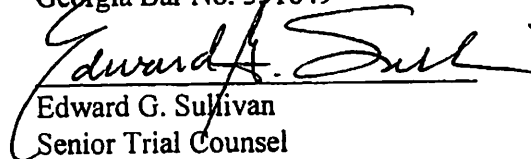
Respectfully Submitted,



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