

Defendant Bruce S. Moody ("Moody"), the trustee of Defendant The 1991 RPM Irrevocable Trust (the "RPM Trust"), helped Moskowitz conceal his beneficial interest in the Ferrofluidics shares held by the RPM Trust, and facilitated Moskowitz's sale of Ferrofluidics stock valued at approximately \$13,000,000 during the time of the fraudulent conduct.

2. As part of the scheme, defendants prepared and disseminated a series of materially false and misleading public statements concerning, among other things, a sham private placement of stock by the company, sales of the company's products, and equity investments made by the company. Defendants also disseminated favorable projections concerning Ferrofluidics' future business prospects and profitability, without having any reasonable basis for such projections. As a result of defendants' activities, potential and actual investors were led to believe that Ferrofluidics was a profitable company with tremendous opportunities for rapid growth and earnings. In fact, Ferrofluidics was then experiencing significant losses and encountering substantial problems developing and manufacturing its products.

3. During the relevant period, Moskowitz sold (through seven family trusts that he controlled), and directed Allen to sell, Ferrofluidics stock worth millions of dollars, in a series of private placements and open market transactions, while in the possession of material, nonpublic information about the company.

4. Defendants (except Moody) violated the antifraud provisions of the federal securities laws. Ferrofluidics, Moskowitz, Kirk and Morin also violated certain reporting, internal controls and record-keeping provisions of the federal securities laws.

5. Allen violated Section 17(b) of the Securities Act of 1933 ("Securities Act") by publishing and circulating The International Investor, a newsletter that ran numerous articles recommending the securities of Ferrofluidics, without disclosing that he had been paid by Moskowitz acting on behalf of the company.

6. Moskowitz and the RPM Trust violated Section 13(d) of the Securities Exchange Act of 1934 ("Exchange Act") and Rule 13d-2 thereunder by failing to make the disclosures and filings required of persons who directly or indirectly acquire a beneficial interest of more than 5% of any class of a registered equity security. By forming voting groups with Moskowitz and failing to make the required disclosures and filings, Kirk and Morin violated Section 13(d) of the Exchange Act and Rule 13d-1 thereunder.

7. Moody aided and abetted Moskowitz's and the RPM Trust's violations of Section 10(b) of the Exchange Act and Rule 10b-5 thereunder by helping Moskowitz conceal his beneficial interest in the Ferrofluidics shares held by the Trust, and by facilitating Moskowitz's sale of Ferrofluidics shares while Moskowitz possessed material nonpublic information about the

company. Moody aided and abetted the RPM Trust's violation of Section 13(d) of the Exchange Act and Rule 13d-2 thereunder by failing to make the required disclosures concerning the Ferrofluidics shares beneficially owned by Moskowitz in the Trust's Schedules 13D.

8. The Commission is seeking injunctive relief, disgorgement of defendants' ill-gotten gains, prejudgment interest, the imposition of civil penalties against Moskowitz, Kirk, Allen, Morin and the RPM Trust, and officer and director bars against Moskowitz, Kirk and Morin.

JURISDICTION

9. The Commission brings this action pursuant to Sections 20(b) and (e) of the Securities Act and Sections 21(d) and (e) of the Exchange Act.

10. This Court has jurisdiction pursuant to Section 22 of the Securities Act and Sections 21 and 27 of the Exchange Act.

11. The defendants, directly or indirectly, used the means and instrumentalities of interstate commerce, the mails, or the facilities of a national securities exchange in connection with the acts, practices and courses of business alleged herein, certain of which occurred within the Southern District of New York.

THE DEFENDANTS

12. Defendant Ferrofluidics, a Massachusetts corporation headquartered in Nashua, New Hampshire, develops, manufactures and markets ferrofluids and related products, including seals and bearings, speaker components and crystal growing systems. Ferrofluids are stable magnetic liquids that can be precisely positioned or controlled when a magnetic force is employed. The fluids are comprised of molecular-sized magnetic particles, and are designed to have a choice of properties such as viscosity, magnetic strength and vapor pressures to perform numerous specific functions such as sealing, sensing, lubricating, damping and heat transfer. During the relevant period, Ferrofluidics' common stock was registered with the Commission pursuant to Section 12(b) of the Exchange Act and was listed for trading on NASDAQ.

13. Defendant Moskowitz, a resident of Hollis, New Hampshire, founded Ferrofluidics in 1968, and during the relevant period was its chief executive officer, chairman of the board of directors and largest shareholder.

14. Defendant Allen, a resident of North Miami Beach, Florida, was a consultant to Ferrofluidics during the relevant period.

15. Defendant Kirk, a resident of Palm Springs, California, was the company's chief financial officer from March 1992 to September 1993.

16. Defendant Morin, a resident of Weare, New Hampshire, was the company's comptroller during the relevant period.

17. Defendant Moody, a resident of Andover, Massachusetts, was a partner with the accounting firm Moody Cavanaugh, Moskowitz's personal accountant, and trustee of the RPM Trust during the relevant period.

18. The RPM Trust is an irrevocable trust ostensibly established by Moskowitz for the benefit of his children. The address of the RPM Trust is 791 Turnpike Street, North Andover, Massachusetts 01845.

FIRST CLAIM

Violations of Section 17(a) of the Securities Act and Section 10(b) of the Exchange Act and Rule 10b-5 thereunder

[Against All Defendants Except Moody]

19. From in or about March 1991 through June 1993, all defendants (except Moody), directly or indirectly, by the use of the means or instrumentalities of interstate commerce, or of the mails, or of the facilities of a national securities exchange, in connection with the offer, purchase or sale of Ferrofluidics securities: (i) employed devices, schemes, or artifices to defraud; (ii) made untrue statements of material fact 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 (iii) engaged in transactions, acts, practices or courses of business which operated as a fraud or

deceit upon persons, including purchasers or sellers of Ferrofluidics securities, as is all more fully set forth below.

Ferrofluidics, Moskowitz and Allen Prepare and Disseminate Materially False and Misleading Statements and Baseless Projections About Ferrofluidics

The Traube Report and Update

20. In January 1992, Moskowitz retained Sheldon Traube ("Traube"), a financial analyst, to prepare a favorable research report on Ferrofluidics. Moskowitz agreed to pay Traube \$3,500 plus expenses to write the report. In order to conceal Ferrofluidics' payment to Traube, Moskowitz arranged to have Traube's fees and expenses paid through one of Ferrofluidics' investor relations consultants.

21. Traube sent the completed report to Dickinson & Co. ("Dickinson"), a registered broker-dealer, which published the report on March 30, 1992. Ferrofluidics received several thousand copies of the report, which it distributed to company shareholders, among others. The report did not disclose that Ferrofluidics had paid Traube to write it, nor did it disclose how much money Traube had received to write the report.

22. In its Third Quarter Report, dated March 31, 1992 and signed by Moskowitz, Ferrofluidics falsely represented that the Traube report was "based on independent research." In fact, Moskowitz extensively reviewed and edited the report, and provided Traube with the report's baseless revenue and earnings projections.

23. During June 1992, Traube agreed to prepare an update to his March 30, 1992 research report in exchange for \$1,500 plus expenses paid by Ferrofluidics. The update was completed by Traube, and published by Dickinson, during July 1992. The update did not disclose either the source or the amount of the compensation that Traube received from Ferrofluidics, and it failed to correct revenue and earnings projections that Moskowitz knew to be false.

The International Investor

24. Allen was ostensibly retained by Moskowitz as a financial consultant to Ferrofluidics in or about March 1991. Allen promoted Ferrofluidics to the investing public by drafting and editing company press releases, and by touting Ferrofluidics' products and financial prospects in The International Investor, a newsletter written and distributed by Allen.

25. From March 1991 through the beginning of 1993, Allen featured Ferrofluidics in at least twenty-one issues of The International Investor. Each of the articles favorably described Ferrofluidics, and many articles contained the same baseless revenue and earnings projections found in the Traube report and update. The International Investor was distributed to Ferrofluidics' shareholders, brokers, mutual fund managers, securities analysts, business writers and editors, and potential investors in the United States and abroad.

26. Moskowitz directed Ferrofluidics to pay Allen approximately \$970,000 from March 1991 through August 1993.

27. Moskowitz also caused Ferrofluidics to grant Allen warrants to purchase Ferrofluidics stock. Between March 1991 and August 1993, Ferrofluidics granted Allen 210,000 warrants, representing the right to purchase an equal number of shares of Ferrofluidics common stock at various prices.

28. Allen exercised all of his warrants and sold 160,000 of the shares that he acquired by doing so, realizing gross proceeds of \$2,818,237 and net profits of \$596,938. Moskowitz controlled Allen's sales of Ferrofluidics stock by (i) directing Allen to sell stock and (ii) requiring that Allen obtain Moskowitz's approval prior to placing any sell orders that were not initiated by Moskowitz.

29. The issues of The International Investor that featured Ferrofluidics did not disclose either the source or the amount of the compensation that Ferrofluidics paid Allen.

The April 1992 Phony Private Placement

30. In early 1992 Moskowitz made plans for a private placement of 720,000 newly-issued, unregistered Ferrofluidics shares.

31. Moskowitz was unable to find legitimate buyers for most of those shares. Instead, Moskowitz and Kirk parked 620,000 shares, approximately 86% of the offering, with sham purchasers, and later sold those shares to the market after Ferrofluidics filed a registration statement for such sales.

32. Kirk recruited three sham purchasers to participate in the scheme. Kirk told the purchasers, in substance, that there

was no risk of loss because the shares would be resold before their payment obligations were due, and that Ferrofluidics would compensate them. Kirk's sham purchasers received a total of \$75,000 from Ferrofluidics for their participation in the scheme. Two of the sham purchasers paid Kirk kickbacks totalling \$23,000.

33. Moskowitz recruited one of Ferrofluidics' investor relations consultants to join the scheme. Moskowitz told the consultant that he would receive any profits from the stock if the stock price moved higher, and would have no risk of loss if the price dropped.

34. None of the sham purchasers ever paid for a single share of Ferrofluidics stock, nor did they have the financial ability to pay for the shares. Moskowitz and Kirk parked a total of 620,000 shares pursuant to the scheme.

35. Ferrofluidics publicly announced, in a press release dated April 23, 1992, that it had "\$12,000,000 of added capital" as a result of the private placement. The condensed balance sheet issued as part of the press release showed an \$11,200,000 increase in working capital and total assets. These statements were false. In fact, the transaction added only \$1,600,000 in equity, from the single legitimate purchaser.

36. Ferrofluidics filed a registration statement with the Commission for the shares that had been purportedly sold in the phony private placement. After the registration statement went effective, Moskowitz began reselling those shares. He resold

305,000 shares to institutional investors at market prices and 315,000 shares to a private Japanese company, at a price that was approximately \$3.25 per share higher than the prevailing market price.

37. On or about May 12, 1992, after 250,000 of the shares that had been parked with the phony purchasers were resold, Moskowitz instructed Morin to set up a sham commissions payable account. That account, which was created by reducing the company's additional paid-in capital account, was used to offset the shortfall between the cash proceeds from the resale of the phony purchasers' shares and the amounts due under their notes. By recording the transactions this way, Moskowitz and Morin enabled Ferrofluidics to book fictitious interest income for the private placement shares as though the phony subscription notes had been paid in full.

38. To conceal the sham commissions payable account and the improperly booked interest income from Ferrofluidics' outside auditors, Moskowitz solicited from a broker who helped resell the private placement shares two backdated letters regarding commissions that Ferrofluidics supposedly owed to him. Morin provided these backdated letters to the company's auditors in connection with the fiscal 1992 audit to support the amount accrued in the sham commissions payable account. At Moskowitz's direction, Morin provided false information to Ferrofluidics' outside auditors when they asked him about the commissions payable account and the broker's commissions.

The Kaiwa Hong Kong Press Release

39. Kaiwa Hong Kong, Ltd. ("Kaiwa") is a Pacific Rim company that, during the relevant time, was in the business of buying and selling scrap crystal pullers, which typically cost no more than \$30,000 apiece.

40. In June 1992, Kaiwa's principals visited Ferrofluidics' facilities. On or about June 23, 1992, Moskowitz, through Kirk, obtained an order from Kaiwa to buy 20 crystal pullers for \$12,000,000. The parties memorialized the deal by signing a one-page purchase order, which did not include, among other things, any product specifications, a delivery schedule or the number of crystal pullers to be purchased. It did, however, contain the following condition: "This order is contingent upon Kaiwa obtaining the necessary funding."

41. Moskowitz and Kirk knew that the Kaiwa purchase order was a sham because Kaiwa did not have the financial ability to pay for such an order, did not understand the technology and did not have any customers for the crystal pullers.

42. Ferrofluidics issued a press release on June 24, 1992, stating that the company had "received an order for 20 silicon crystal systems valued at \$12,000,000 from Kaiwa Hong Kong, Ltd."

The press release omitted material information by not disclosing that the order was contingent on Kaiwa obtaining financing.

43. After the press release was distributed, Ferrofluidics' stock price rose from \$16.00 per share at the close on June 23 to \$18.75 per share at the close on June 24.

44. Moskowitz caused Ferrofluidics to record, and Morin to maintain, the sham Kaiwa purchase order in the company's accounting records and periodic reports, increasing Ferrofluidics' backlog of orders by \$12,000,000. The \$12,000,000 amount attributable to the sham Kaiwa order continued to be reported as backlog in Ferrofluidics' periodic reports until January 1994, when Ferrofluidics restated its 1992 financial statements. Kaiwa never obtained financing for the June 23, 1992 \$12,000,000 purchase order.

The Fiscal 1992 Accounting Fraud

45. In Ferrofluidics' financial statements for the fiscal year ended June 30, 1992, the company's reported net income was overstated by approximately \$2,912,303 or 87%. As set forth more fully below, this overstatement resulted from: (i) improper recognition of \$1,597,303 of income from the sale of crystal pullers, (ii) improper accrual of \$580,000 of interest income from the subscription notes that the company received in connection with the sham private placement, and (iii) improper charging of \$735,000 of expenses against capital.

Crystal Pullers

46. In 1991, Ferrofluidics entered into several contracts for the production of crystal pullers. The most significant of these contracts was with POSCO-HULS Company, Ltd. ("POSCO"),

which ordered twelve crystal pullers, for a total amount of \$7,340,400, on June 10, 1991. The amount of the contract was later increased to \$10,490,658.

47. On September 24, 1991, MEMC Electronic Materials, Inc. ("MEMC") ordered one crystal puller at a price of \$1,195,550. On November 16, 1991, the amount of the purchase order was reduced to \$1,163,550.

48. On April 10, 1992, Toshiba Ceramics Company, Ltd. ("Toshiba") ordered one crystal puller at a price of \$584,700.

49. Under Generally Accepted Accounting Principles ("GAAP"), companies typically recognize revenue from products like crystal pullers when they are shipped. Prior to being shipped, companies may not recognize revenue from the transaction unless it is a "bill and hold" transaction or meets some other exception to the general rule.

50. Accounting and Auditing Enforcement Release No. 108 ("AAER 108") defines a "bill and hold" transaction as "a practice whereby a customer agrees to purchase the goods but the seller retains physical possession until the customer requests shipment to designated locations." In addition, AAER 108 lists the following conditions, among others, which must be met before revenue can be recognized from such transactions: (i) the risks of ownership must have passed to the buyer; (ii) the buyer, not the seller, must request that the transaction be on a bill and hold basis (and the buyer must have a substantial business purpose for ordering the goods on a bill and hold basis); (iii)

the seller must not have retained any specific performance obligations; and (iv) the equipment must be complete and ready for shipment. As set forth below, because these conditions were not met with respect to the POSCO, MEMC and Toshiba crystal puller transactions as of June 30, 1992, Ferrofluidics failed to comply with GAAP when it recognized revenue in fiscal 1992 on the POSCO, MEMC and Toshiba crystal pullers.

51. Only one of the twelve POSCO units was shipped by June 30, 1992, and that unit was accepted by POSCO on a conditional basis. None of the other POSCO units was shipped or accepted by the end of the fiscal year. In addition, as of June 30, 1992, neither the MEMC unit nor the Toshiba unit had been shipped or accepted. As a result, the risks of ownership had not passed to the buyers and there were specific performance obligations remaining to be performed by Ferrofluidics.

52. POSCO, MEMC and Toshiba did not request that their transactions be on a bill and hold basis.

53. The POSCO, MEMC and Toshiba crystal pullers were not complete and ready for shipment on June 30, 1992.

54. As of June 30, 1992, Ferrofluidics was not entitled to payment from POSCO, MEMC or Toshiba under their respective contracts.

55. Moskowitz directed Morin to improperly recognize revenue totalling \$4,683,454 from POSCO (\$3,259,204), MEMC (\$855,250) and Toshiba (\$569,000) for the fiscal year ended June 30, 1992, even though both of them knew that recognizing such

revenue failed to comply with GAAP. The improper revenue recognition materially increased Ferrofluidics' reported net income by \$1,597,303, or 47%, for the 1992 fiscal year.

56. Moskowitz had previously directed Morin to improperly recognize a material amount of crystal puller revenue in Ferrofluidics' Quarterly Report for the third quarter ended March 30, 1992. Moskowitz and Morin knew that recognizing such revenue did not comply with GAAP.

57. Moskowitz and Kirk lied to the company's independent auditors in order to hide the company's improper revenue recognition with respect to the crystal pullers. Moskowitz and Kirk obtained a letter from MEMC falsely stating that the POSCO and MEMC crystal pullers were complete as of the end of fiscal 1992, when in fact they were not. Moskowitz and Kirk provided the letter to the company's auditors.

58. In order to falsely create the appearance that the Toshiba crystal puller was appropriate for revenue recognition during fiscal 1992, Ferrofluidics provided the auditors with an invoice, dated June 26, 1992, for 100% of the purchase price of that unit. In fact, the Toshiba crystal puller was not complete and ready for shipment until fiscal 1993, and Ferrofluidics did not actually send the invoice to Toshiba until August 21, 1992.

Interest on Private Placement Subscription Notes

59. As part of the April 1992 sham private placement, discussed above, the phony purchasers signed subscription notes totalling \$10,230,000 for the Ferrofluidics shares that they

purportedly "purchased." While these notes were "owing," Moskowitz directed Morin to book the interest that accrued on the notes as a receivable, thereby increasing Ferrofluidics' reported net income by approximately \$580,000, or 17%, during fiscal 1992.

The accrued interest was periodically offset against the sham commissions payable account to give the appearance that the interest was being collected from the participants in the phony private placement. Because the phony purchasers never intended to pay interest to Ferrofluidics, the company should not have accrued this interest income.

Write-off of Expenses Against Private Placement Proceeds

60. During the fiscal years ended June 30, 1991 and 1992, Moskowitz directed Morin to record approximately \$735,000 of expenses in a suspense account, treating them as having been incurred in connection with a proposed private placement of shares by Ferrofluidics. In fact, most of these expenses were incurred in connection with Moskowitz's efforts to sell stock owned by his family trusts (including the RPM Trust), Moskowitz's payments to Allen, and Moskowitz's personal travel and expenses.

61. When the sham private placement was completed in April 1992, Moskowitz directed Morin to improperly charge these costs against capital. Because the costs were not incurred in connection with a legitimate private placement of shares by Ferrofluidics, they should have been expensed. As a result of this improper accounting treatment, Ferrofluidics' net income was materially overstated during the relevant period.

62. Moskowitz, Kirk and Morin falsely represented to Ferrofluidics' auditors that the costs were incurred in connection with a private placement of shares by Ferrofluidics.

Molecular BioQuest

63. Molecular BioQuest, Inc. ("Molecular BioQuest") is a small, privately-held company based in Atkinson, New Hampshire. During the relevant time, Molecular BioQuest was engaged in the development and manufacture of biotechnology and pharmaceutical products based on its proprietary technology.

64. Beginning in December 1991, Moskowitz had a series of periodic meetings with senior management of Molecular BioQuest to discuss a possible acquisition of, or investment in, Molecular BioQuest by Ferrofluidics. By late September 1992, Moskowitz and Molecular BioQuest agreed that Ferrofluidics would transfer 100,000 shares of stock to Molecular BioQuest in exchange for a convertible debenture and a development contract.

65. In October 1992, Moskowitz told Molecular BioQuest that the price of the Ferrofluidics stock being transferred would be \$18.00 per share (thus valuing the convertible debenture at \$1,800,000). The price established by Moskowitz was approximately \$1.50 per share higher than the price at which the stock was then trading.

66. During a subsequent October 1992 meeting, Kirk, acting at Moskowitz's direction, offered Molecular BioQuest a \$750,000 line of credit to be used to buy Ferrofluidics stock. The line of credit, by its express terms, could be used only during the

period November 13, 1992 through December 15, 1992 (the date of Ferrofluidics' annual shareholder's meeting). Moskowitz, in a subsequent conversation with Molecular BioQuest, reiterated that the \$750,000 was to be used to purchase Ferrofluidics stock.

67. On October 29, 1992, Ferrofluidics issued a press release that described the agreement with Molecular BioQuest. The press release failed to disclose the existence of the \$750,000 line of credit and that Ferrofluidics would be funding the purchase of Ferrofluidics stock by Molecular BioQuest.

68. The \$750,000 line of credit was intended by Moskowitz to prop up Ferrofluidics' stock price by funding purchases of the company's stock by Molecular BioQuest in the period immediately prior to the annual shareholder's meeting. Molecular BioQuest used \$542,240 of the line of credit to purchase 32,000 shares of Ferrofluidics stock, and timed its purchases and sales to coincide with Moskowitz's timetable. For example, Molecular BioQuest purchased Ferrofluidics shares from November 11, 1992 through the morning of December 15, 1992. Molecular BioQuest began selling its Ferrofluidics shares immediately after the annual shareholder's meeting had ended. By the end of December 1992, all of the Ferrofluidics shares purchased by Molecular BioQuest with the line of credit had been sold.

Fiscal 1993 Accounting Fraud

69. In Ferrofluidics' financial statements for the first three quarters of the fiscal year ended June 30, 1993, the company's reported net income was overstated by a total of

approximately \$2,612,000, or 82%. The overstatement of net income resulted from (i) the improper accrual of \$212,000 of interest income from the subscription notes that the company received in connection with the sham private placement during the first quarter, (ii) the improper recognition of about \$900,000 of income from consignment sales during the first, second and third quarters, and (iii) the improper recognition of \$1,500,000 of license revenue from Fuji Seiki, a private Japanese company, during the third quarter. In addition, Ferrofluidics improperly recognized approximately \$1,900,000 of revenue and \$900,000 of income from consignment sales during the fourth quarter, and its assets and capital accounts were overstated by approximately \$9,250,000, because of the company's overvaluation of its investments in Molecular BioQuest and Fuji Seiki.

Interest on Private Placement Subscription Notes

70. In Ferrofluidics' quarterly report for the first quarter ended September 30, 1992, Morin improperly booked some of the interest that accrued on the phony private placement subscription notes as a receivable, thereby increasing Ferrofluidics' reported net income by approximately \$212,000, or 22%. At Moskowitz's direction, Morin stopped accruing interest on the phony subscription notes part way through the first quarter, when the sham commissions payable account was depleted.

Improper Booking of Consignment Sales

71. During fiscal 1993, Ferrofluidics had licensing and distribution agreements with three companies. Although the terms

of their arrangements with Ferrofluidics differed slightly, each of these distributors received components from Ferrofluidics during fiscal 1993 on a consignment basis or with a right of return.

72. Under GAAP, companies are required to book revenue from goods sold on a consignment basis when the goods are sold by their distributors to end users, not when the companies ship the goods to the distributors.

73. Ferrofluidics failed to comply with GAAP by recognizing revenue (approximately \$4,000,000) for its distributors' orders when the products were shipped. As a result, Ferrofluidics overstated its net income by approximately \$1,800,000.

Improper Revenue Recognition from Fuji Seiki

74. On March 31, 1993, Fuji Seiki agreed to pay Ferrofluidics \$2,500,000 as a non-refundable licensing fee. Ferrofluidics improperly recorded \$1,500,000 of this fee as license revenue in the third quarter ended March 31, 1993. In fact, this payment was simply a return of Ferrofluidics' investment in Fuji Seiki and not revenue.

Overvaluation of Investments

75. As set forth above, during November 1992, Ferrofluidics transferred 100,000 shares of stock to Molecular BioQuest in exchange for a convertible debenture and a development contract.

At Moskowitz's direction, the Ferrofluidics stock transferred to Molecular BioQuest was deemed to be worth \$18.00 per share even though the market price at the time was approximately \$1.50 per

share less than that. As a result, Moskowitz caused Ferrofluidics to book as an asset worth \$1,800,000 the convertible debenture received from Molecular BioQuest, when the actual value of that investment was materially less.

76. Moskowitz also overvalued the company's investment in Fuji Seiki. On September 19, 1992, as part of his efforts to resell the shares that had been "purchased" in connection with the sham private placement, Moskowitz arranged for Fuji Seiki to acquire 315,000 shares at \$16.50 per share, approximately \$3.25 per share higher than the market price on that date. At the same time, Moskowitz committed Ferrofluidics to buy 900,000 shares of Fuji Seiki (approximately 20% of the company) for \$7,450,000. When the transaction was completed, the Fuji Seiki stock was recorded as an asset on Ferrofluidics' books at a materially inflated value.

Insider Trading in Ferrofluidics Stock by
Moskowitz and Allen

77. Moskowitz profited from his fraud by selling millions of dollars worth of Ferrofluidics stock through seven family trusts. His first main trust, The Ronald and Phyllis Moskowitz Irrevocable Trust B ("Trust B"), was created during the 1980's. During 1991, all of the assets of Trust B, with the exception of certain real estate interests, were shifted to the RPM Trust. When the RPM Trust was created, Moody, Moskowitz's personal accountant, became its trustee. By 1991, Moskowitz also had created trusts for each of his five grandchildren.

78. During fiscal 1992 and 1993, the seven trusts together exercised warrants for the purchase of approximately 1,300,000 shares of Ferrofluidics stock. The majority of these warrants (950,000) were exercised by the RPM Trust. The remaining 350,000 warrants were exercised by the grandchildren's trusts. The price of each of the warrants exercised was \$5.00 per share. At the time of exercise, which typically was also the time of sale, the shares had a fair market value of approximately \$19,596,000. Thus, the trusts profited by approximately \$13,000,000 during fiscal 1992 and 1993.

79. The trusts' sales of Ferrofluidics stock were directed by Moskowitz and done for his benefit. Although Moskowitz denied beneficial ownership of the trusts' Ferrofluidics shares and failed to report the trusts' warrant and securities transactions on the forms that he and Ferrofluidics filed with the Commission, Moskowitz received virtually all of the proceeds from all of the trust sales of stock through a series of loans from the RPM Trust.

80. The loans from the RPM Trust to Moskowitz were funded almost exclusively by the sales of Ferrofluidics stock. Moskowitz generally determined when the RPM Trust's shares would be sold by making demands on an \$11,000,000 line of credit from the RPM Trust. Because the RPM Trust's primary asset was Ferrofluidics stock, Moskowitz's demands on the line of credit automatically triggered a sale of stock.

81. Moskowitz was also personally involved with many of the sales of Ferrofluidics stock made by the trusts. On occasion, Moskowitz telephoned Moody's accounting firm and told him or his assistant when (and sometimes at what price) to sell. At other times, Moskowitz personally placed orders to sell shares held by the trusts. The Schedules 13D that Moody filed with the Commission stated falsely that Moody had sole dispositive power with respect to all of the Ferrofluidics shares held by the RPM Trust.

82. Moskowitz also exercised control over the trusts by personally authorizing many of the payments from the trusts. For example, Moskowitz instructed his personal bookkeeper or Moody's assistant regarding when to make gifts from the trusts to the beneficiaries. Moskowitz also instructed them to make other payments from the trusts' bank accounts, transfers from one of the trust's accounts to his personal bank account, and to make payments on a home that he was building in Florida.

83. In addition to controlling stock sales, distributions and payments by the trusts, Moskowitz kept day to day control over trust administration and expenditures. His bookkeeper kept the books for the two main trusts (Trust B and the RPM Trust) from the middle of 1991 until Moskowitz's resignation in August 1993. She also reviewed all securities and bank statements relating to Trust B and the RPM Trust and prepared the majority of the checks drawn on Trust B's and the RPM Trust's bank accounts for Moody's signature.

84. Similarly, the grandchildren's trusts were nothing more than vehicles for Moskowitz, through Moody, to control blocks of Ferrofluidics stock. The trustees of the five grandchildren's trusts were trustees in name only, exercising no control over trust matters.

85. Moskowitz deliberately tried to hide his stock sales and avoid the regulatory reporting requirements on such sales through his control of the grandchildren's trusts. During September 1992, Moskowitz transferred warrants to purchase 200,000 shares of Ferrofluidics stock from the RPM Trust to the grandchildren's trusts (each of which held less than five percent of Ferrofluidics' outstanding shares) so that he could avoid reporting subsequent sales by the trusts.

86. Moskowitz controlled Allen's exercise of warrants and sales of Ferrofluidics stock by (i) directing Allen to sell stock and (ii) requiring that Allen obtain Moskowitz's approval prior to placing any orders to sell Ferrofluidics stock that were not initiated by Moskowitz. During the relevant period, Allen sold 160,000 shares of Ferrofluidics stock, realizing gross proceeds of \$2,818,237 and net profits of \$596,938.

87. Throughout the period of the stock sales controlled by Moskowitz or effected for his benefit, Moskowitz was in possession of adverse material nonpublic information about Ferrofluidics, and owed a duty to the company's shareholders not to use that information for his personal benefit.

88. At the time of Allen's stock sales, Allen knew that Moskowitz was in possession of adverse material nonpublic information about Ferrofluidics, and owed a duty to the company's shareholders not to use that information for his personal benefit.

89. By reason of the foregoing, defendants (except Moody) violated Section 17(a) of the Securities Act and Section 10(b) of the Exchange Act and Rule 10b-5 thereunder.

SECOND CLAIM

Violation of Section 17(b) of
the Securities Act

[Against Defendant Allen]

90. Paragraphs 1 through 89 are realleged and incorporated herein by reference.

91. Allen, directly or indirectly, by the use of the means or instruments of transportation or communication in interstate commerce or the mails, published, gave publicity to and/or circulated, notices, circulars, advertisements, newspapers, articles, letters, investment services, and/or communications about Ferrofluidics, though not purporting to offer such securities for sale, described it for a consideration received or to be received, directly or indirectly, from an issuer, underwriter, or dealer, without fully disclosing the receipt, whether past or prospective, of such consideration and the amount thereof.

92. As set forth above, Allen failed to disclose to the readers and subscribers of The International Investor the source and amount of compensation that he received from Ferrofluidics for recommending the securities of Ferrofluidics.

93. By reason of the foregoing, Allen violated Section 17(b) of the Securities Act.

THIRD CLAIM

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

[Against Defendant Ferrofluidics]

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

95. Section 13(a) of the Exchange Act requires issuers to file such annual and quarterly reports as the Commission may prescribe and in conformity with such rules as the Commission may promulgate. Rules 13a-1 and 13a-13 require the filing of accurate annual and quarterly reports that comply with the Commission's Regulation S-X, which requires that financial statements be presented according to GAAP. Rule 12b-20 requires an issuer to include material information as may be necessary to make the required statements, in the light of the circumstances under which they were made, not misleading.

96. The following financial statements that Ferrofluidics filed with the Commission were not prepared in accordance with GAAP:

- a. Form 10-Q for the period ended September 30, 1991;

- b. Form 10-Q for the period ended December 31, 1991;
- c. Form 10-Q for the period ended March 31, 1992;
- d. Form 10-K for the period ended June 30, 1992;
- e. Form 10-Q for the period ended September 30, 1992;
- f. Form 10-Q for the period ended December 31, 1992;
- and
- g. Form 10-Q for the period ended March 31, 1993;

97. By reason of the foregoing, Ferrofluidics violated Sections 13(a) of the Exchange Act and Rules 13a-1, 13a-13 and 12b-20 thereunder.

FOURTH CLAIM

Violation of Section 13(b)(2)(A) of the Exchange Act

[Against Defendant Ferrofluidics]

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

99. Section 13(b)(2)(A) of the Exchange Act requires issuers to make and keep books, records and accounts which, in reasonable detail, accurately and fairly reflect transactions and disposition of assets.

100. Throughout fiscal 1992 and the first three quarters of fiscal 1993, Ferrofluidics' books, records and accounts did not accurately and fairly reflect transactions and disposition of assets.

101. By reason of the foregoing, Ferrofluidics violated Section 13(b)(2)(A) of the Exchange Act.

FIFTH CLAIM

Violation of Section 13(b)(2)(B) of the Exchange Act

[Against Defendant Ferrofluidics]

102. Paragraphs 1 through 101 are realleged and incorporated herein by reference.

103. Section 13(b)(2)(B) of the Exchange Act requires issuers to devise and maintain a system of internal accounting controls sufficient to provide reasonable assurances that, among other things, transactions are recorded as necessary to permit preparation of financial statements in conformity with GAAP.

104. Throughout fiscal 1992 and the first three quarters of fiscal 1993, Ferrofluidics did not maintain internal accounting controls sufficient to permit the preparation of financial statements in conformity with GAAP.

105. By reason of the foregoing, Ferrofluidics violated Section 13(b)(2)(B) of the Exchange Act.

SIXTH CLAIM

Violations of Section 13(b)(5) of the Exchange Act and Rule 13b2-1 thereunder

[Against Defendants Moskowitz, Kirk and Morin]

106. Paragraphs 1 through 105 are realleged and incorporated herein by reference.

107. Section 13(b)(5) of the Exchange Act makes it unlawful for any person to knowingly circumvent, or fail to implement, a system of internal accounting controls or to knowingly falsify

any book, record or account. Rule 13b2-1 makes it unlawful for any person to, directly or indirectly, falsify or cause to be falsified any book, record or account described in Section 13(b)(2)(A) of the Exchange Act.

108. Defendants Moskowitz, Kirk and Morin knowingly falsified and caused others to falsify the company's books, records and accounts.

109. Defendant Morin knowingly circumvented and failed to implement internal accounting controls.

110. By reason of the foregoing, defendants Moskowitz, Kirk and Morin violated Rule 13b2-1 under the Exchange Act, and defendant Morin violated Section 13(b)(5) of the Exchange Act.

SEVENTH CLAIM

Violations of Rule 13b2-2 under the Exchange Act

[Against Defendants Moskowitz, Kirk and Morin]

111. Paragraphs 1 through 110 are realleged and incorporated herein by reference.

112. Rule 13b2-2 under the Exchange Act provides, in part, that no director or officer of an issuer shall make or cause others to make a materially false or misleading statement or omission to the issuer's auditor in connection with an audit of the financial statements of the issuer.

113. Defendants Moskowitz, Kirk and Morin made and caused others to make materially false and misleading statements and omissions to Ferrofluidics' auditors in connection with the audits for the fiscal years ended June 30, 1992 and 1993.

114. By reason of the foregoing, defendants Moskowitz, Kirk and Morin violated Rule 13b2-2 under the Exchange Act.

EIGHTH CLAIM

Violations of Section 13(d) of the
Exchange Act and Rules 13d-1 and 13d-2 thereunder

[Against Defendants Moskowitz, Kirk, Morin and the RPM Trust]

115. Paragraphs 1 through 114 are realleged and incorporated herein by reference.

116. Section 13(d) of the Exchange Act and Rule 13d-1 thereunder require, among other things, that a person who acquires beneficial ownership of more than five percent of a class of equity securities which is registered with the Commission pursuant to Section 12 of the Exchange Act file a Statement on Schedule 13D disclosing such ownership and certain other information, as prescribed by the Rule and Schedule, within 10 days of the acquisition.

117. During fiscal 1992, a Ferrofluidics shareholder advised the company that he intended to present a proposal at Ferrofluidics' December 15, 1992 annual meeting requesting that the Board of Directors adopt certain limits on executive compensation.

118. Moskowitz embarked on a campaign in the fall of 1992 to defeat the shareholder's proposal by increasing the number of shares outstanding and by soliciting votes against the proposal.

119. To increase the number of Ferrofluidics shares held by officers, employees and other supporters who he knew would vote

against the shareholder's proposal, Moskowitz ensured that these individuals could and would exercise the warrants and non-qualified options that they previously had been granted by: (i) asking several individuals to exercise their warrants and options and to hold the stock; (ii) accelerating the exercise date of warrants and options that had not yet vested so that they could be immediately exercisable; (iii) allowing individuals to exercise their warrants and options with below-market loans provided by Ferrofluidics (the loans were interest-free for an initial period and had a 5% interest rate thereafter); and (iv) changing the record date for the annual meeting from its initial date in mid-October to October 26, 1992, the date on which all of the individuals and entities involved exercised their warrants and options.

120. Moskowitz solicited Kirk, Morin and the RPM Trust, among others, to exercise warrants and agree to vote with Moskowitz against the shareholder's proposal.

121. Moskowitz caused warrants and options for 474,374 shares of Ferrofluidics stock (representing approximately ten percent of the number of shares then outstanding) to be exercised on October 26, 1992. In addition, 195,000 shares were exercised by the RPM Trust pursuant to Moskowitz's direction on October 22 and 23, 1992.

122. As set forth above, Ferrofluidics and Molecular BioQuest entered into a transaction whereby Molecular BioQuest was issued 100,000 shares of Ferrofluidics stock as of the record

date for the annual meeting. Molecular BioQuest agreed with Moskowitz to vote the shares against the shareholder's proposal.

123. Defendants Moskowitz, Kirk, Morin and RPM Trust failed to file timely Schedules 13D or amendments with the Commission disclosing the agreements with respect to voting against the shareholder's proposal, which involved more than five percent of the outstanding common stock.

124. As set forth above, Moskowitz controlled the disposition of and received the benefit from the Ferrofluidics shares owned by the RPM Trust. The Schedules 13D and amendments filed by the RPM Trust with the Commission failed to make such disclosure.

125. By reason of the foregoing, defendants Kirk and Morin violated Section 13(d) of the Exchange Act and Rule 13d-1 thereunder by failing to file a timely Schedule 13D with the Commission disclosing their ownership, along with Moskowitz, of more than five percent of the common stock of Ferrofluidics.

126. By reason of the foregoing, defendants Moskowitz and the RPM Trust violated Section 13(d) of the Exchange Act and Rule 13d-2 thereunder by failing to file a timely Amended Schedule 13D with the Commission disclosing that they had acquired additional shares of Ferrofluidics.

NINTH CLAIM

Violation of Section 14(a) of the
Exchange Act and Rule 14a-9 thereunder

[Against Defendant Ferrofluidics]

127. Paragraphs 1 through 126 are realleged and incorporated herein by reference.

128. Section 14(a) of the Exchange Act and Rule 14a-9 thereunder prohibit proxy statements from containing materially false or misleading statements and omissions.

129. In its proxy statement for the 1992 annual meeting, Ferrofluidics failed to disclose the shares held by the RPM Trust and the shares subject to the voting agreements with Moskowitz in anticipation of the 1992 shareholder's proposal.

130. By reason of the foregoing, Ferrofluidics violated Section 14(a) of the Exchange Act and Rule 14a-9 thereunder.

TENTH CLAIM

Violation of Section 16(a) of the Exchange
Act and Rules 16a-2 and 16a-3 thereunder

[Against Defendant Moskowitz]

131. Paragraphs 1 through 130 are realleged and incorporated herein by reference.

132. Section 16(a) of the Exchange Act and Rules 16a-2 and 16a-3 thereunder require officers and directors of companies whose equity securities are registered with the Commission pursuant to Section 12 of the Exchange Act to file a Form 4 within ten days after the close of each calendar month if there

has been a change in ownership of the issuer's securities during the month, or in applicable instances to file a Form 5 within 45 days following the close of the issuer's fiscal year.

133. Moskowitz failed to timely file with the Commission on Forms 4 or Forms 5 sales of Ferrofluidics stock by the RPM Trust and by the other trusts described above.

134. By reason of the foregoing, Moskowitz violated Section 16(a) of the Exchange Act and Rules 16a-2 and 16a-3 thereunder.

ELEVENTH CLAIM

Aiding and Abetting Violations of Section 10(b) of the Exchange Act and Rule 10b-5 thereunder

[Against Defendant Moody]

135. Paragraphs 1 through 134 are realleged and incorporated herein by reference.

136. During the course of the fraudulent scheme, Moody sold at Moskowitz's direction, and permitted Moskowitz to sell directly, Ferrofluidics shares owned by the RPM Trust representing approximately 21% of the Ferrofluidics shares outstanding. In addition, the RPM Trust's Schedules 13D, for which Moody was responsible, affirmatively misrepresented that Moody controlled the Trust's shares when in fact, as Moody knew, Moskowitz controlled those shares. Moody also failed to disclose Moskowitz's line of credit in any of the Trust's filings. Accordingly, Moody knowingly provided substantial assistance to Moskowitz in connection with the fraudulent scheme by helping Moskowitz conceal his beneficial interest in the Ferrofluidics

shares held by the Trust, thus providing the vehicle through which Moskowitz profited from the scheme.

137. By reason of the foregoing, Moody aided and abetted Moskowitz's and the RPM Trust's violations of Section 10(b) of the Exchange Act and Rule 10b-5 thereunder.

TWELFTH CLAIM

Aiding and Abetting Violations of Section 13(d)
of the Exchange Act and Rule 13d-2 thereunder

[Against Defendant Moody]

138. Paragraphs 1 through 137 are realleged and incorporated herein by reference.

139. Defendant Moody prepared the Schedules 13D and amendments filed with the Commission by the RPM Trust. Those filings affirmatively misrepresented that Moody controlled the Trust's shares when, in fact, Moskowitz controlled those shares. Moreover, after Moody agreed with Moskowitz to vote the RPM Trust's shares against the shareholder's proposal, the RPM Trust's filings failed to include all shares beneficially owned by Moskowitz.

140. By reason of the foregoing, Moody aided and abetted the RPM Trust's violations of Section 13(d) of the Exchange Act and Rule 13d-2 thereunder.

* * * * *

WHEREFORE, plaintiff requests that this Court enter a final judgment:

(a) against defendant Ferrofluidics Corporation:

(i) enjoining it from violating Section 17(a) of the Securities Act, Sections 10(b), 13(a), 13(b)(2)(A), 13(b)(2)(B) and 14(a) of the Exchange Act and Rules 10b-5, 12b-20, 13a-1, 13a-13 and 14a-9 thereunder;

(b) against defendant Ronald Moskowitz:

(i) enjoining him from violating Section 17(a) of the Securities Act, Sections 10(b), 13(d) and 16(a) of the Exchange Act and Rules 10b-5, 13b2-1, 13b2-2, 13d-2, 16a-2 and 16a-3 thereunder;

(ii) ordering him to disgorge unjust enrichment and prejudgment interest thereon, and to pay civil penalties pursuant to Section 20(d) of the Securities Act and Sections 21(d)(3)(A) and 21A of the Exchange Act; and

(iii) prohibiting him from serving as an officer or director of a public company pursuant to Section 20(e) of the Securities Act and Section 21(d)(2) of the Exchange Act;

(c) against defendant Jan R. Kirk:

(i) enjoining him from violating Section 17(a) of the Securities Act, Sections 10(b) and 13(d) of the Exchange Act and Rules 10b-5, 13b2-1, 13b2-2 and 13d-1 thereunder;

(ii) ordering him to disgorge unjust enrichment and prejudgment interest thereon, and to pay civil penalties pursuant to Section 20(d) of the Securities Act and Section 21(d)(3)(A) of the Exchange Act; and

(iii) prohibiting him from serving as an officer or director of a public company pursuant to Section 20(e) of the Securities Act and Section 21(d)(2) of the Exchange Act;

(d) against defendant Jerome R. Allen:

(i) enjoining him from violating Sections 17(a) and 17(b) of the Securities Act, Section 10(b) of the Exchange Act and Rule 10b-5 thereunder;

(ii) ordering him to disgorge unjust enrichment and prejudgment interest thereon, and to pay civil penalties pursuant to Section 20(d) of the Securities Act and Sections 21(d)(3)(A) and 21A of the Exchange Act;

(e) against defendant Stephen P. Morin:

(i) enjoining him from violating Section 17(a) of the Securities Act, Sections 10(b), 13(b)(5) and 13(d) of the Exchange Act and Rules 10b-5, 13b2-1, 13b2-2 and 13d-1 thereunder;

(ii) ordering him to pay civil penalties pursuant to Section 20(d) of the Securities Act and Section 21(d)(3)(A) of the Exchange Act; and

(iii) prohibiting him from serving as an officer or director of a public company pursuant to Section 20(e) of the Securities Act and Section 21(d)(2) of the Exchange Act;

(f) against defendant Bruce S. Moody:

(i) enjoining him from violating Sections 10(b) and 13(d) of the Exchange Act and Rules 10b-5 and 13d-2 thereunder;

(g) against defendant RPM Trust:

(i) enjoining it from violating Section 17(a) of the Securities Act, Sections 10(b) and 13(d) of the Exchange Act and Rules 10b-5 and 13d-2 thereunder;

(ii) ordering it to disgorge unjust enrichment and prejudgment interest thereon, and to pay civil penalties pursuant to Section 20(d) of the Securities Act and Sections 21(d)(3)(A) and 21A of the Exchange Act; and

(h) granting such other relief as the Court deems appropriate.

Dated: Washington, D.C.

September 25, 1997

Respectfully submitted,

Paul V. Gerlach
William H. Kuehnle
Gregory S. Bruch
Laura B. Josephs
Scott W. Friestad (SF-8048)

Attorneys for Plaintiff
SECURITIES AND EXCHANGE COMMISSION
450 Fifth Street, N.W. (Stop 4-2)
Washington, D.C. 20549
(202) 942-4678 (Kuehnle)
(202) 942-9637 (fax)