

**IN THE UNITED STATES DISTRICT COURT
FOR THE EASTERN DISTRICT OF MISSOURI
EASTERN DIVISION**

Securities and Exchange Commission,)	
)	
Plaintiff,)	
)	
vs.)	Civil Action No.
)	
Gary C. Gerhardt,)	
)	
)	Trial by Jury Demanded
Defendant.)	

COMPLAINT

Plaintiff, the United States Securities and Exchange Commission (“the Commission”), for its Complaint, alleges as follows:

SUMMARY

1. From 1997 through 2003, Gary C. Gerhardt participated in a fraudulent scheme intended to enrich certain officers, directors, and employees of Engineered Support Systems, Inc. (“Engineered Support” or “the Company”). Engineered Support’s management periodically issued stock options to officers, directors and certain employees as an incentive, purportedly tying the recipients’ compensation to the Company’s future stock price. Pursuant to Engineered Support’s stock option plans, the Company was required to grant these options “at-the-money,” which means that the option exercise price would be equal to the closing market price of the Company’s common stock on the date of the award. Thus, employees and directors would profit only if the Company’s stock price rose after options were awarded.

2. During this period of time, Engineered Support regularly issued proxy statements and annual reports which represented that the Company’s stock options were

issued with exercise prices equal to the closing market prices on the dates of the awards. However, these statements were false.

3. Gerhardt, who was Engineered Support's Chief Financial Officer ("CFO") during the relevant period, directed Steven Landmann ("Landmann"), his subordinate and Engineered Support's Controller, to backdate the grant dates of certain of Engineered Support's stock options to coincide with low points in the closing market price for the Company's common stock. This undisclosed practice resulted in grants of disguised in-the-money options, where the options had a lower exercise price than the market price of Engineered Support's common stock on the actual date of the award. Because the Company's stock options vested immediately, Gerhardt and the other option recipients could realize an immediate profit on the option grants which had not been authorized by shareholders.

4. As part of this scheme, on at least two occasions, Gerhardt directed Landmann to cancel and reissue previously issued Engineered Support options with a new backdated grant date and exercise price because the Company's stock price declined after the Company had granted those options. These efforts were intended to bring options that fell out-of-the-money back in-the-money, further thwarting the stock option plans' stated goal of tying compensation to increases in the Company's stock price.

5. As part of this scheme, Gerhardt also directed Landmann to improperly issue stock options to non-employee directors beyond what those directors were authorized to receive under Engineered Support's stock option plans. The Company never disclosed to shareholders that it had awarded this additional compensation to its non-employee directors in violation of the terms of the stock option plans.

16. The Company explicitly stated in both plans that all options were to be granted with an exercise price equal to the closing price of Engineered Support's common stock on the date that the options were awarded.

17. Michael F. Shanahan, Sr. ("Shanahan"), Engineered Support's Chief Executive Officer and Chairman of the Board of Directors, was ultimately responsible for authorizing stock option grants during the relevant period. However, Gerhardt actively participated in and approved nearly all options granting decisions. He was also responsible for overseeing the completion of the stock option certificates and award letters for Engineered Support's option grants. Gerhardt personally selected the specific grant dates to be used for many of those option grants.

Engineered Support's Backdating of Stock Option Grant Dates

18. From 1997 through 2002, Gerhardt engaged in several manipulative options granting schemes and practices at Engineered Support that were not disclosed in filings with the Commission.

19. Gerhardt repeatedly instructed Landmann to backdate Engineered Support's stock option grants, using false grant dates that corresponded to low points in the Company's stock price. In most cases, the grant dates for Engineered Support's options differed from the date those options were actually awarded. The backdated option grants included those purportedly issued on December 2, 1996; February 1, March 10 and September 4, 1998; July 1 and December 9, 1999; May 4, 2000; March 29, 2001; and, July 24 and October 17, 2002.

20. The intent and object of the backdating scheme was to grant undisclosed and unauthorized compensation to Company employees and directors through the use of in-the-

money stock options. Gerhardt and others intentionally concealed the fact that these options were granted at an exercise price that was lower than the closing price of Engineered Support's common stock on the date of the award.

21. Initially, Landmann informed Gerhardt that backdating options grants was prohibited by the express terms of the shareholder-approved stock option plans. Gerhardt did not dispute this fact. However, Gerhardt ordered Landmann to backdate the stock option grant dates and issue in-the-money stock options.

22. Because Engineered Support's options vested immediately, the backdating of options grants conferred an immediate monetary benefit to the option recipients. In total, grants of backdated options increased the compensation received by Engineered Support employees and non-employee directors by approximately \$20 million. Of that amount, top executives and outside directors received approximately \$15 million. Gerhardt personally received \$1,906,300 in additional compensation as a result of backdating. Nearly half of the unauthorized and undisclosed compensation derived from the options backdating, or approximately \$8.6 million, was received by Shanahan, who was the Company's chief executive.

23. Most of the backdating activity was documented in contemporaneous writings. For example, on March 10, 1998, Gerhardt created a list of Engineered Support stock prices from January 28 through February 27, 1998. Gerhardt highlighted January 30 and the corresponding stock price and wrote, "stock effective 2/1/98." Gerhardt initialed and dated the note, "GCG 3/10/98." By using February 1, 1998, which was a Sunday, as the grant date, Gerhardt obtained a January 30 closing price and was able to avoid dating the

option grant within Engineered Support's previous reporting period, which ended January 31.

24. Approximately one month later, on April 8, 1998, Gerhardt wrote Landmann a note, which stated, "IAW previous discussions with MFS Sr. please issue/authorize the following stock options," and provided a list of recipients, the number of shares for each recipient, and the "Effective Date" of the options, which was either February 1 or March 10.

25. On another occasion, on July 12, 2000, Gerhardt provided a list of potential option recipients to Michael Shanahan, Jr. ("Shanahan Jr."), who was Shanahan's son and one of the Company's outside directors. This list contained a date, "4-May-00," and a price, "10 13/16," which was the closing price of the stock on that date. Shanahan Jr. made changes to the number of shares certain recipients were to receive and faxed the list back to Gerhardt on July 17. Engineered Support subsequently issued options for 494,500 shares of Company stock with a May 4, 2000 grant date and corresponding exercise price, which was the lowest possible exercise price during that quarter.

Repricing of Engineered Support Stock Options

26. On a few occasions, Engineered Support's stock price fell shortly after the issuance of backdated stock options. The decline in the stock price meant that the options were no longer in-the-money, rendering them temporarily valueless. On two of these occasions, Gerhardt directed Landmann to reprice all of the stock options that had fallen out-of-the-money. This was done by cancelling and reissuing the options with a new grant date and lower corresponding exercise price, which restored the lost financial benefit. In these instances, both the original options issuance and the subsequent, repriced issuance contained backdated grant dates. This double-backdating provided

option recipients with the lowest possible exercise price for the options. These repriced options contained grant dates of September 4, 1998 and July 1, 1999. Engineered Support never disclosed its repricing of stock options to shareholders or its auditors, instead reporting only the reissuance as if it were the only issuance.

27. For example, on June 1, 1999, Shanahan instructed Landmann to issue stock options for 295,000 shares of Company stock to Engineered Support executives. These stock options were issued with an April 21, 1999 grant date and were in-the-money at the time of issuance. After June 1, Engineered Support's stock price fell below the previous April 21 low point, causing the stock options to fall out-of-the-money. On July 15, 1999, Gerhardt instructed Landmann to cancel and reissue the April 21 stock options with a new grant date of July 1, 1999 and the corresponding exercise price, which was the new low point for Engineered Support's common stock so far that year.

Additional Grants to Non-employee Directors

28. Gerhardt also instructed Landmann to issue additional stock options for thousands of shares of Company stock to non-employee directors beyond the number which had been authorized by shareholders under any of Engineered Support's stock option plans. These additional options also were backdated and contained grant dates of December 2, 1996; February 1, 1998; July 1, 1999; and March 29, 2001. In total, Engineered Support issued backdated options for 132,000 shares of Company stock to non-employee directors that were not authorized by shareholders. As a result, these directors realized approximately \$6 million in unauthorized compensation from the exercise of their additional stock options.

V.

Retain jurisdiction over this action in accordance with the principles of equity and the Federal Rules of Civil Procedure in order to implement and carry out the terms of all orders and decrees that may be entered, or to entertain any suitable application or motion for additional relief within the jurisdiction of this Court.

VI.

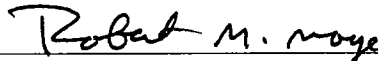
Grant such other relief as the Court may deem just and appropriate.

VII.

Pursuant to Rule 39 of the Federal Rules of Civil Procedure, Plaintiff demands that this case be tried to a jury.

Dated: February 6, 2007.

Respectfully submitted,



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