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**UNITED STATES DISTRICT COURT  
DISTRICT OF NEW JERSEY**

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SECURITIES AND EXCHANGE COMMISSION	:
450 Fifth Street, N.W.	:
Washington, D.C. 20549,	:
	:
Plaintiff,	:
	:
vs.	: <b>Civil Action No.</b>
	:
JACK GAGLIO	: <b><u>COMPLAINT</u></b>
c/o Proskauer & Rose LLP	:
2049 Century Park East, Suite 3200	:
Los Angeles, CA 90067-3206,	:
	:
Defendant.	:

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The United States Securities and Exchange Commission (“Commission”) alleges:

**SUMMARY**

1. This action involves a financial fraud designed to falsely inflate the sales revenue, accounts receivable, and inventory of Suprema Specialties, Inc. (“Suprema”), a publicly-traded company based in Paterson, New Jersey that was formerly engaged in the

manufacturing, processing, and distribution of cheese and cheese products. The fraudulent scheme commenced in or around 1998 or earlier, and continued into February 2002, when Suprema filed for bankruptcy.

2. The fraudulent scheme was orchestrated by Suprema's management with the direct participation of Suprema's employees and certain vendors and customers of Suprema, and their owners and operators. During the relevant period, the named defendant, JACK GAGLIO ("GAGLIO"), operated and owned in part certain Suprema customers and vendors through which he participated in the fraudulent scheme.

3. The principal component of the fraudulent scheme involved fictitious circular "round-tripping" sales and purchase transactions between Suprema and certain of its customers and vendors, including those operated and owned in part by GAGLIO.

4. The fraudulent scheme resulted in material misstatements in Suprema's periodic reports filed with the Commission during its fiscal years 1998 through 2001 and the first quarter of 2002, as well as Suprema's registration statements filed with the Commission for its secondary public offerings in 2000 and 2001.

5. From fiscal year 1998 through and including the first quarter of 2002, which ended on September 30, 2001, the fictitious round-tripping transactions resulted in Suprema's reporting in its filings with the Commission of fictitious sales that represented approximately 60% of Suprema's total reported revenue of approximately \$1.13 billion. Suprema's fictitious sales accounted for approximately 30%, 65%, 85%, and 87% of accounts receivable reported by Suprema in its filings with the Commission at the end of fiscal years 1998, 1999, 2000, and 2001, respectively. Suprema's fictitious purchases

from vendors participating in the scheme also resulted in a corresponding inflation in Suprema's reported inventory at the end of fiscal years 1998, 1999, 2000 and 2001.

6. From 1998 through the bankruptcy filing in early 2002, the fictitious sales revenue on Suprema's books and records resulting from the round-tripping transactions totaled over \$700 million.

7. Approximately \$359 million, or 32%, of Suprema's \$1.13 billion in reported revenue during the period 1998 through the first quarter of Suprema's 2002 fiscal year was attributable to round-tripping transactions effected with entities operated and owned in part by GAGLIO. These fictitious transactions accounted for approximately 10%, 23%, 34%, 38% and 38% of the revenue reported by Suprema in its filings with the Commission for the fiscal years 1998, 1999, 2000, and 2001, and the first quarter of Suprema's 2002 fiscal year, respectively.

8. By knowingly or recklessly engaging in the acts alleged in this Complaint, GAGLIO violated, or aided and abetted violations of, the anti-fraud, reporting, books and records, internal controls, and lying-to-auditors provisions of the federal securities laws.

9. Unless enjoined by this Court, it is likely that GAGLIO will continue to engage in such violative conduct. Therefore, the Commission seeks this Court's injunction against future violations, an officer and director bar, as well as disgorgement of unjust enrichment, prejudgment interest, and statutory civil penalties as described in its prayer for relief.

### **JURISDICTION**

10. The Commission brings this action pursuant to Section 21(d) of the Securities Exchange Act of 1934 ("Exchange Act") [15 U.S.C. § 78u(d)].

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

12. The defendant has made use of the means or instrumentalities of interstate commerce, or of the mails, or the facilities of a national securities exchange in connection with the transactions, acts, practices, and courses of business alleged herein.

### **DEFENDANT**

13. JACK GAGLIO, age 46, resides in Rancho Mirage, California. From at least 1998 through February 2002, GAGLIO was the founder and president of and owned 50% of A&J Cheese Company; owned 50% of Noble J. G. Cheese, LLC and California Goldfield Cheese Trading, LLC; and owned 25% of Wall Street Cheese, LLC and Whitehall Specialties, Inc. During this same time period, GAGLIO also operated A&J Cheese Company, Noble J. G. Cheese, LLC, and California Goldfield Cheese Trading, LLC.

### **OTHER RELEVANT PERSON AND ENTITIES**

14. Founded in 1983, Suprema, a New York corporation based in Paterson, New Jersey, held itself out as a manufacturer, processor and distributor of “all natural” gourmet Italian cheeses. Suprema maintained three wholly owned subsidiary facilities in California, New York, and Idaho. Suprema held its initial public offering in 1991 and registered its securities with the Commission pursuant to Section 12(g) of the Exchange Act. As such, the company was required to file periodic reports with the Commission pursuant to Section 13 of the Exchange Act. The company adopted a fiscal year ending on June 30. Suprema’s common stock was traded on the over-the-counter market starting on April 25, 1991, as well as on the NASDAQ National Market System from March 22,

1993 until March 1, 2002, when the stock was delisted. Suprema is presently liquidating pursuant to a Chapter 7 proceeding in federal bankruptcy court.

15. Lawrence Fransen (“Fransen”), age 49, owns LNN Enterprises, Inc., and also owns a 25% interest in Wall Street Cheese, LLC, both of which he operates.

Fransen is also the founder and president of LNN Enterprises, Inc.

16. A&J Cheese Company (“A&J”), a non-public company registered as a corporation and located in California, was engaged in the purchase and sale of cheese products. A&J was placed in receivership in March 2002 and liquidated in September 2002.

17. California Goldfield Cheese Trading, LLC (“California Goldfield”) was a non-public company registered as a limited liability company (“LLC”) located at different times in California and in Colorado that purchased and sold cheese products. California Goldfield ceased operations after February 2002.

18. LNN Enterprises, Inc. (“LNN”) is a sole proprietorship incorporated and located in California that brokers cheese transactions.

19. Noble J. G. Cheese, LLC (“Noble”) was a non-public company registered as an LLC and located in California that purchased and sold cheese products. Noble ceased operations after February 2002.

20. Wall Street Cheese, LLC (“WSC”) is a non-public company registered as an LLC and located in California that purchases and sells cheese products.

21. Whitehall Specialties, Inc. (“Whitehall”) is a non-public company registered as a corporation and located in Wisconsin that purchases and sells cheese products.

## **THE FRAUDULENT SCHEME**

22. In every fiscal year from 1996 forward, Suprema claimed annual double-digit growth in sales and revenues. Beginning in 1994, the company borrowed against its accounts receivable and inventory to obtain a revolving credit line with a consortium of banks that rose to \$140 million by the end of 2001. Suprema held secondary public offerings in August 2000 and November 2001 that raised over \$8 million and \$48 million, respectively. In fiscal 2001, which ended on June 30 of the calendar year, Suprema reported over \$420 million in revenues, an increase of over 50% from the prior fiscal year, and reported \$8.9 million in net income.

23. From at least 1998 through the first quarter of 2002, however, Suprema's apparent success was the product of a fraudulent scheme orchestrated and managed by the company's management with the defendant's direct and knowing involvement. The principal component of the fraudulent scheme involved fictitious circular "round-tripping" transactions among Suprema and certain of its customers and vendors.

### **I. The False Transactions**

24. From at least 1998 through early 2002, Suprema engaged in circular round-tripping transactions that generated fictitious sales revenues and inflated accounts receivable and inventory. Each round-tripping "circle" in this scheme involved three parties: Suprema, a third-party "customer," and a "vendor." In most instances, the customer and vendor in these circles shared a common owner. With some exceptions as noted below, the fraud operated as follows: Fictitious paperwork was created purporting to represent sales of cheese products from Suprema to a customer involved in the fraud. The customer then purportedly sold those or other products to the related vendor. This

was followed by a fictitious sale of other products (often purporting to be the raw materials for cheese manufacturing) from the vendor back to Suprema. With rare exception, no goods were actually delivered, or otherwise changed hands, in these transactions.

25. On each leg of the circle – Suprema to the customer, customer to the vendor, and vendor back to Suprema – the entity purporting to sell goods created false invoices and bills of lading to document the false transaction, and the entity purporting to buy goods generated a check in payment for the same false transaction.

26. These circular round-tripping transactions resulted in a continuous flow of checks from Suprema to the vendors involved in the fraud, from the vendors to the related customers, and from the customers back to Suprema, all purportedly in payment for fictitious sales. Typically, the checks from Suprema to the vendors involved in the fraud were greater than the corresponding checks from the related customers back to Suprema. This difference in the checks represented a kick-back or “commission” paid to the common owner of the customer and vendor for his participation in the fraudulent scheme. Funds for the checks, including commissions, were drawn on Suprema’s line of credit with its consortium of banks, which increased as Suprema’s accounts receivable and inventory grew.

## **II. Gaglio’s Participation in the Round-Tripping Transactions**

27. From at least 1998 through the first quarter of 2002, Suprema engaged in round-tripping transactions with A&J, California Goldfield, Noble, and WSC as customers and several entities, including LNN and Whitehall, as vendors. All of these entities were operated and owned in part by defendant GAGLIO, or by his business

associates, including Fransen, whom he persuaded to participate in the scheme. During this period, Suprema recognized approximately \$359 million in fraudulent revenue from the round-tripping transactions with these entities.

28. Defendant GAGLIO, through the entities operated and owned in part by him, participated in the round-tripping fraud; received false invoices reflecting fictitious sales from Suprema to A&J, California Goldfield, and Noble; directed the generation of false invoices reflecting fictitious purchases by Suprema from its vendors; circulated checks purportedly in payment for these fictitious transactions; and signed false audit confirmations that were provided to Suprema's independent auditors purporting to confirm the existence of fictitious accounts receivable at the end of each fiscal year.

29. In addition to the foregoing, GAGLIO, through the entities owned and operated by him, shipped sizeable quantities of artificial cheese to Suprema at fiscal year end which Suprema then relabeled as higher priced cheese products and included in physical inventory. Suprema used this relabeled physical inventory to support the inflated fiscal year end inventory figures on its books and records during the year-end audit by its external auditors, and the invoices for GAGLIO's shipments were recorded on its books and records only after the close of the fiscal year.

30. For their participation in the fraudulent scheme to inflate Suprema's publicly reported revenues, the entities operated and owned in part by GAGLIO received a payment of one to two cents per pound of cheese. A&J also borrowed from banks against its own inflated accounts receivable and inventory.

31. In furtherance of the round-tripping fraud, one or more officers and directors of Suprema created false paperwork and instructed GAGLIO to sign the false

audit confirmations, all of which were provided to Suprema's independent auditors purporting to confirm the existence of fictitious accounts receivable.

32. GAGLIO knew, or was reckless in not knowing, that his conduct would result in Suprema materially misstating the financial statements that it filed with the Commission.

### **III. Suprema's Reporting of Fictitious Revenue from the Round-Tripping Transactions in its Filings with the Commission**

33. GAGLIO's participation in fictitious sales transactions with Suprema resulted in Suprema materially misstating its reported revenue by approximately 10%, 23%, 34%, 38%, and 38% in fiscal years 1998, 1999, 2000, and 2001, and the first quarter of 2002, respectively. As a consequence, the round-tripping scheme resulted in material overstatements of Suprema's revenue and total assets in the financial statement included in the following forms that the company filed with the Commission: a Form 10-K for each of its fiscal years 1998, 1999, 2000, and 2001; a Form 10-Q for the first three quarters of each of those fiscal years and for the first quarter of its fiscal year 2002; and a Form S-2 registration statement, and any amendments thereto, for each of the secondary public offerings in August 2000 and November 2001.

### **THE FRAUDULENT SCHEME COLLAPSES**

34. On December 21, 2001, after the close of trading, Suprema issued a press release announcing the resignations of its chief financial officer and its controller. The same press release also stated that the company had "initiated an internal investigation of its prior reported financial results and ha[d] instructed its auditors to review the Company's financial records."

35. Also after the close of trading on December 21, 2001, the Nasdaq halted trading in Suprema's common stock. The trading halt continued until the Nasdaq delisted Suprema's common stock on March 1, 2002.

36. On February 24, 2002, Suprema filed a voluntary bankruptcy petition for a Chapter 11 reorganization in the U.S. Bankruptcy Court for the Southern District of New York. On March 20, 2002, the bankruptcy was converted to a Chapter 7 liquidation. In re the Jointly Administered Estate of Suprema Specialties, Inc., et al., No. 02-10823 (CB) (Bankr. S.D.N.Y.).

### **FIRST CLAIM**

#### **Defendant Gaglio Violated Section 10(b) of the Exchange Act and Exchange Act Rule 10b-5**

37. Paragraphs 1 through 36 are realleged and incorporated herein by this reference.

38. Section 10(b) of the Exchange Act [15 U.S.C. § 78j(b)] and Exchange Act Rule 10b-5 thereunder [17 C.F.R. § 240.10b-5] prohibit a person from, *inter alia*, employing any device, scheme or artifice to defraud; making any untrue statement of a material fact or omitting 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 engaging in any act, practice, or course of business which operates or would operate as a fraud or deceit upon any person, in connection with the purchase or sale of any security.

39. By virtue of the conduct described above, defendant GAGLIO violated Section 10(b) of the Exchange Act and Exchange Act Rule 10b-5 thereunder.

## SECOND CLAIM

### **Defendant Gaglio Aided and Abetted Violations of Sections 13(a) and 13(b)(2)(A) and (B) of the Exchange Act and Exchange Act Rules 12b-20, 13a-1, and 13a-13**

40. Paragraphs 1 through 36 are realleged and incorporated herein by this reference.

41. Section 13(a) of the Exchange Act [15 U.S.C. § 78m(a)] and Exchange Act Rules 13a-1 and 13a-13 thereunder [17 C.F.R. §§ 240.13a-1 and 240.13a-13] require all issuers with registered securities to file with the Commission factually accurate annual and quarterly reports. Exchange Act Rule 12b-20 [17 C.F.R. § 240.12b-20] provides that in addition to the information expressly required to be included in a statement or report, there shall be added such further material information as may be necessary to make the required statements, in light of the circumstances under which they were made, not misleading.

42. Section 13(b)(2)(A) of the Exchange Act [15 U.S.C. § 78m(b)(2)(A)] requires issuers of registered securities to make and keep books, records, and accounts, which, in reasonable detail, accurately and fairly reflect the transactions and dispositions of the assets of the issuer. Section 13(b)(2)(B) of the Exchange Act [15 U.S.C. § 78m(b)(2)(B)] requires issuers to, among other things, devise and maintain a system of internal accounting controls sufficient to provide reasonable assurances that the company's transactions were recorded as necessary to permit preparation of financial statements in conformity with generally accepted accounting principles.

43. By reason of the conduct described above, Suprema violated Sections 13(a) and 13(b)(2)(A) and (B) of the Exchange Act and Exchange Act Rules 12b-20, 13a-1, and 13a-13.

44. Defendant GAGLIO knowingly provided substantial assistance to Suprema in connection with its above-described violations of the federal securities laws.

45. By virtue of the conduct described above in paragraphs 1 to 37 inclusive, and pursuant to Exchange Act Section 20(e) [15 U.S.C. § 78t(e)], defendant GAGLIO is liable as an aider and abettor of Suprema's violations of Sections 13(a) and 13(b)(2)(A) and (B) of the Exchange Act and Exchange Act Rules 12b-20, 13a-1, and 13a-13.

### **THIRD CLAIM**

#### **Defendant Gaglio Aided and Abetted Violations of Exchange Act Rule 13b2-2**

46. Paragraphs 1 through 36 above are realleged and incorporated herein by this reference.

47. Exchange Act Rule 13b2-2 [17 C.F.R. § 240.13b2-2] prohibits an officer or director, among other things, from making, or causing to be made, materially false statements or omissions to an accountant in connection with an audit or a filing with the Commission.

48. By virtue of the conduct described above, one or more Suprema officers and directors violated Exchange Act Rule 13b2-2.

49. Defendant GAGLIO knowingly provided substantial assistance to one or more Suprema officers and directors in connection with those officers' and directors' violations of Exchange Act Rule 13b2-2.

50. By virtue of the conduct described above, and pursuant to Exchange Act Section 20(e) [15 U.S.C. § 78t(e)], defendant GAGLIO is liable as an aider and abettor of violations of Exchange Act Rule 13b2-2 by one or more Suprema officers and directors.

**PRAYER FOR RELIEF**

WHEREFORE, the Commission respectfully requests that this Court enter an Order:

A. permanently restraining and enjoining defendant GAGLIO from violating Section 10(b) of the Exchange Act and Exchange Act Rule 10b-5 thereunder and from aiding and abetting violations of Sections 13(a), 13(b)(2)(A), and 13(b)(2)(B) of the Exchange Act and Exchange Act Rules 12b-20, 13a-1, 13a-13, and 13b2-2;

B. prohibiting defendant GAGLIO from acting as an officer or a director of any issuer that has a class of securities registered pursuant to Section 12 of the Exchange Act or that is required to file reports pursuant to Section 15(d) of the Exchange Act, pursuant to Section 21(d)(2) of the Exchange Act [15 U.S.C. § 78u(d)(2)];

C. requiring defendant GAGLIO to pay disgorgement of all unlawful gains and prejudgment interest;

D. imposing civil monetary penalties on defendant GAGLIO pursuant to Section 21(d) of the Exchange Act [15 U.S.C. § 78u(d)]; and

E. granting such other and additional relief as the Court may deem just and proper.

Dated: March 2, 2005

Respectfully submitted,

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