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UNITED STATES DISTRICT COURT

FOR THE SOUTHERN DISTRICT OF CALIFORNIA

SECURITIES AND EXCHANGE COMMISSION, Plaintiff, v. STEPHEN P. GARDNER, DOUGLAS S. POWANDA, GARY L. LENZ, BERDJ J. RASSAM, JOSEPH G. REICHNER, PETER J. O'BRIEN, DANIEL F. STULAC, LARRY A. RODDA, and MICHAEL D. WHITT, Defendants.	Case No. 04 CV 2002 JAH (RBB) **COMPLAINT**

Plaintiff Securities and Exchange Commission alleges:

SUMMARY

1. This case is about a massive financial fraud and its attempted cover up at Peregrine Systems, Inc., a publicly-traded San Diego-based software company, orchestrated by senior Peregrine officers with the knowing assistance of its outside auditor and certain of its customers. Together, over a period of three years, the defendants fraudulently inflated the product revenues Peregrine reported in its filings with the Securities and Exchange Commission (Commission) and elsewhere. The defendants employed deception and lies to portray Peregrine as a vibrant company with a constantly growing sales base while covering up Peregrine's persistent failure to fulfill revenue forecasts. At the same time, certain defendants who had received stock options unloaded their stock into the unsuspecting market, thereby enriching themselves at the expense of the investing public.

2. Peregrine filed materially incorrect financial statements with the Commission for 12 consecutive quarters between January 1, 1999 and December 31, 2001. The expanding fraud became impossible to conceal and was uncovered in April 2002. In February 2003, Peregrine restated its financial results for its fiscal years 2000 and 2001, and for the first three quarters of fiscal 2002. Peregrine reduced previously-reported revenue of $1.34 billion by more than $507 million.

3. The heart of the fraud was Peregrine's recording of millions of dollars of revenue on the improper basis of non-binding arrangements with resellers—companies that purchased software from Peregrine for resale to end users. In the parlance of the software industry, resellers are referred to as "channel partners" and company sales to them are called "channel sales," or simply the "channel." To meet revenue forecasts quarter after quarter, Peregrine unlawfully exploited certain of its channel relationships by entering into sham deals with some

channel partners who knowingly signed non-binding agreements under which the channel partners would have no legal obligation to pay Peregrine. Typically, these arrangements materialized around the end of a fiscal quarter, were improperly recorded as revenue, and often became uncollectible receivables. Peregrine executives referred to some of these arrangements as "parked" deals.

4. To perpetuate the accounting fraud, members of Peregrine's senior management team would communicate near the ends of quarters to determine how much additional revenue the company needed to book that quarter in order to meet or exceed analysts' expectations. They would then devise fraudulent and misleading transactions, as described herein, and the resulting "revenue" would be recognized in that quarter in order to mislead the analysts and the investing public into believing that Peregrine's financial condition was significantly better than it actually was and to maintain Peregrine's inflated stock price.

5. Peregrine's uncollectible receivables from the parked deals swelled on Peregrine's balance sheet. To make it appear that Peregrine was collecting cash on its channel deals in a timely manner, Peregrine devised a temporary solution. The uncollectible receivables were purportedly sold to banks, and Peregrine removed them from its balance sheet. These receivable financing transactions, however, were in reality loans and not sales because, under the terms of deals, the banks had recourse against Peregrine if the channel partners did not pay Peregrine. Peregrine's removal of the receivables from its balance sheet was therefore fraudulent.

6. To prevent the banks from discovering that the underlying sales were bogus, when channel partners did not pay for the parked deals, Peregrine often repurchased the receivables from the banks. Peregrine's management—with the knowledge of its lead outside

accountant—then improperly wrote off some of the repurchased receivables (and other unpaid receivables) as acquisition costs even though the receivables were wholly unrelated to acquisitions. These improper write-offs enabled them to remove the uncollectible channel receivables from Peregrine's books.

7. Peregrine's recognition of revenue from the parked deals violated the revenue recognition policies that Peregrine claimed to be following in its periodic filings with the Commission. It also violated the written "Revenue Recognition Policy" that Peregrine CFOs periodically distributed to the company's senior management, including its president and general counsel, and to members of Peregrine's finance and sales departments.

8. Peregrine's lead outside accountant, then a partner at Arthur Andersen LLP, was an indispensable contributor to Peregrine's fraudulent accounting. Among other things, he knew, or was reckless in not knowing, that Peregrine improperly recorded millions of dollars of revenue on channel transactions and improperly wrote off millions of dollars in uncollectible receivables as acquisition costs, and that, as a result, its fiscal 2001 financial statements were materially false and misleading. Despite this knowledge or reckless disregard, he caused Arthur Andersen to issue an unqualified opinion attesting to the accuracy and completeness of Peregrine's fiscal 2001 financial statements.

THE DEFENDANTS

9. Defendant Stephen P. Gardner, age 50, was hired by Peregrine in 1997 as Vice President of Strategic Acquisitions. He was promoted to Chief Executive Officer in April 1998 and became a member of the Board of Directors. Gardner became Chairman of the Board in July 2000. Gardner resigned from Peregrine on May 3, 2002. During Peregrine's accounting fraud, Gardner exercised options and sold Peregrine stock for proceeds of more than $11 million.

Gardner also received substantial salaries and bonuses during the fraud, awarded by Peregrine's Board in large part to reward him for Peregrine's deceptively strong financial performance.

10. Defendant Douglas S. Powanda, age 48, was hired by Peregrine in February 1992 as a Senior Account Executive. By January 1998, Powanda was Peregrine's Executive Vice President of Sales reporting directly to Gardner. Peregrine terminated Powanda on May 15, 2002. During Peregrine's accounting fraud, Powanda exercised options and sold Peregrine stock for proceeds of more than $24 million. Powanda also received salaries, bonuses, and sales commissions throughout his participation in the scheme based in part on sales Powanda knew, or was reckless in not knowing, were fraudulent.

11. Defendant Gary L. Lenz, age 57, was hired by Peregrine in May 2000 as its Executive Vice President of Business Development. In October 2000, Lenz became Peregrine's President and Chief Operating Officer. Peregrine terminated Lenz on March 31, 2002. During Peregrine's accounting fraud, Lenz received options, salaries, bonuses and an $800,000 interest-free loan from Peregrine based in part on the company's illusory financial performance.

12. Defendant Berdj J. Rassam, age 38, a certified public accountant, was hired by Peregrine in November 2000 as its Controller and was promoted in September 2001 to Vice President of Finance and Chief Accountant. Rassam was terminated by Peregrine in June 2002. During Peregrine's accounting fraud, Rassam received options, salaries and bonuses based in part on the company's illusory financial performance.

13. Defendant Joseph G. Reichner, age 57, was hired by Peregrine in September 2000 as its Senior Vice President for Alliances and Business Development after 31 years at Arthur Andersen LLP. While at Andersen, Reichner worked with Defendant Lenz, who eventually recruited Reichner to Peregrine. Reichner's employment was terminated in March 2002. During

Peregrine's accounting fraud, Reichner received options, salaries and bonuses from Peregrine based in part on the company's illusory financial performance.

14. Defendant Peter J. O'Brien, age 44, was hired by Peregrine in January 1998 as an Alliance Manager in the company's channel program. In October 2000, Peregrine promoted him to Director of Strategic Alliances. His employment at Peregrine ended in August 2002. While he participated in the fraud, O'Brien exercised options and sold Peregrine stock for proceeds of approximately $150,000. Also during Peregrine's accounting fraud, O'Brien received salaries and bonuses from Peregrine based in part on the company's illusory financial performance.

15. Defendant Daniel F. Stulac, age 40, a certified public accountant, was on the Arthur Andersen team for Peregrine audits and was the engagement partner on the Peregrine audit from September 2000 to September 2001.

16. Larry A. Rodda, age 54, was a partner at KPMG's consulting arm, one of Peregrine's channel partners.

17. Michael D. Whitt, age 59, was president and majority owner of one of Peregrine's channel partners, Barnhill Associates, Inc., until Peregrine acquired Barnhill in March 2000. After the acquisition, Whitt joined Peregrine and worked with its channel partners.

THE ISSUER

18. Peregrine Systems, Inc., a Delaware corporation with principal offices in San Diego, California, sells infrastructure management software. From its initial public offering in April 1997 to the present, Peregrine's common stock has been registered with the Commission pursuant to Exchange Act Section 12(g). It traded on the Nasdaq National Market System from its initial public offering until August 30, 2002, when it was delisted. On September 22, 2002, Peregrine filed a voluntary petition for reorganization under Chapter 11 of the U.S. Bankruptcy

Code. Since Peregrine emerged from bankruptcy on August 7, 2003, its common stock has traded in the over-the-counter securities market.

JURISDICTION AND VENUE

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

20. Venue properly lies in this Court pursuant to Section 27 of the Exchange Act [15 U.S.C. § 78aa] because the defendants transacted business in this judicial district, many of the defendants inhabit this judicial district, offers and sales of the securities at issue in this case took place in this judicial district, and certain of the acts and transactions constituting the violations in this case occurred within this judicial district.

21. The defendants made use of the means and instrumentalities of interstate commerce in connection with the acts alleged in this complaint.

22. The Commission requests that the Court permanently enjoin defendants Gardner, Powanda, Lenz, Rassam, Reichner, O'Brien and Stulac from engaging in further violations; enjoin them from aiding and abetting further violations; order an accounting; impose civil penalties upon them for participating in the accounting fraud; and order them to disgorge any other ill-gotten gains, plus prejudgment interest.

23. The Commission further requests that the Court bar defendants Gardner, Powanda, Lenz, Rassam, Reichner and O'Brien from acting as an officer or director of any reporting company. The Commission further requests that the Court order defendants Gardner, Powanda and O'Brien to pay disgorgement, plus prejudgment interest, and civil penalties for insider trading.

24. The Commission requests that the Court permanently enjoin defendants Rodda and Whitt from aiding and abetting violations and impose civil penalties upon them for participating in the accounting fraud. As to Whitt, the Commission further requests that the Court order an accounting and order him to disgorge any ill-gotten gains, plus prejudgment interest.

THE REVENUE INFLATION SCHEME: SHAM CHANNEL TRANSACTIONS

25. Following its initial public offering in April 1997, Peregrine reported 17 consecutive quarters of revenue growth through the quarter ended June 30, 2001. This trend gave a false impression that Peregrine's market share was dramatically increasing. It also falsely appeared that Peregrine's financial results met or exceeded analysts' expectations. During that time, the company's stock price increased from $2.25 per share (split-adjusted) to a high of $79.50 per share on March 27, 2000.

26. In reality, however, Peregrine's spectacular reported growth in revenue was due to the defendants' scheme to fraudulently inflate the company's revenues.

27. As the ends of quarters approached, Peregrine management was acutely aware that the company could not meet its revenue forecasts. Management also realized that the failure to achieve Peregrine's forecasts would have a deleterious effect on the price of the company's stock. As a result, defendants Gardner (Peregrine's CEO), Powanda (Executive Vice President/Sales), Lenz (President), Reichner (Senior VP), O'Brien (Director of Strategic Alliances) and other Peregrine officers schemed to backdate transactions and arrange sham transactions with certain channel partners to record revenue to meet analysts' expectations.

28. The scheme began no later than the March 1999 quarter. While Peregrine's written contracts with its channel partners appeared to bind them to pay Peregrine for software

sold to end users, the complicit channel partners' obligations frequently were subject to side agreements freeing them from payment obligations and making revenue recognition improper.

29. The side agreements took various forms and were both oral and written. In substance, however, the side agreements freed the channel partners from any enforceable obligation to Peregrine under the apparent sales contracts because, as senior Peregrine officers made clear: (a) channel partners could cancel the "sale" within a specified time despite the written contract's payment terms; or (b) the resellers did not have to pay because Peregrine would close a sale later with the end user identified in the channel partner's contract and Peregrine would collect from the end user; or (c) the resellers did not have to pay because Peregrine would find yet-to-be-identified end users, sell them software, and then credit the channel partner's account with these sales; or (d) if unable to sell or use Peregrine's software licenses internally, the channel partner could invoice Peregrine for "services" so that it would have cash to pay Peregrine.

30. The financial reporting of public companies in the United States must conform with Generally Accepted Accounting Principles (GAAP). GAAP, and in particular the American Institute of Certified Public Accountants' Statement of Position (SOP) 97-2, Software Revenue Recognition, prohibited Peregrine from recognizing revenue on software sales unless each of four criteria was met: (a) persuasive evidence of an arrangement exists; (b) delivery has occurred; (c) the fee is fixed or determinable; and (d) collectibility is probable.

31. In addition, if the payment terms of any sales transaction exceeded one year, GAAP presumes the fee is not fixed or determinable. Peregrine could overcome this presumption only by demonstrating a history of collections on similar contracts.

32. SOP 97-2 was not satisfied in the many instances where Peregrine officers excused channel partners' performance because, among other violations of the rule, collectibility was far from probable. Even absent the side agreements provided to channel partners, revenue recognition was inappropriate under GAAP because of Peregrine's historical failure to collect its channel receivables.

33. As the uncollected revenues from the faked channel sales mounted, Peregrine's senior management concocted another fraudulent scheme to remove them from the company's balance sheet. Rassam, Peregrine's Controller, with the knowledge and acquiescence of auditor Stulac, hid the true amount of Peregrine's aging receivables from public view by fraudulently writing them off as acquisition costs.

DEFENDANT POWANDA'S FRAUDULENT CONDUCT

34. Executive VP Douglas Powanda was a primary architect of Peregrine's revenue-inflation scheme. He parked deals so often at or after the ends of many quarters that the deals became known among Peregrine personnel as "Powanda Specials." Powanda told his colleagues that he pulled contracts from his "magic drawer" at quarter end to make Peregrine's revenue forecasts and spoke about a desire to start a company called "Quartermaker, Inc." to park deals to help companies meet their forecasts. Described below are some of the more egregious "Powanda Specials."

Powanda Parked Deals with Barnhill Associates, Inc. Through its Majority Owner, Defendant Michael Whitt

35. Defendant Whitt was the president of Barnhill Associates, Inc., a Colorado-based reseller. Beginning in spring 1999, Barnhill and Peregrine, through the knowing efforts of Whitt and Powanda, entered into a series of sham transactions to inflate Peregrine's revenue. Although the contracts appeared to bind Barnhill to pay Peregrine for software licenses, Barnhill had no

obligation to pay Peregrine on the contracts, and therefore never recorded them as payables. Whitt signed some of the agreements in April, but the contracts were backdated to March, and Peregrine recorded revenue from those contracts in the March 1999 quarter. For that quarter alone, Peregrine improperly recorded more than $1.4 million revenue on sham software license deals with Barnhill.

36. To compensate Whitt for his complicity in the fraud, Powanda caused Peregrine to pay Barnhill five percent of the dollar amounts of certain of the sham contracts, which, by agreement, Barnhill mischaracterized as "finder's fees" in its invoices to Peregrine.

37. Powanda and Whitt entered into similar sham contracts to enable Peregrine to meet its forecast for the next quarter, ending in June 1999. Peregrine improperly recorded approximately $4.4 million revenue on these deals. Barnhill invoiced Peregrine for a $25,000 "finder's fee" for some of these June deals.

38. In October 1999, Powanda again obtained Whitt's help in making Peregrine's revenue targets for the just-closed September 1999 quarter. This time, Whitt signed seven contracts totaling over $4.11 million. Whitt signed the backdated contracts, then invoiced Peregrine for five percent "finder's fees" for each of the seven sham deals. For the September 1999 quarter, Peregrine improperly recorded approximately $3.5 million revenue on sham deals with Barnhill.

Powanda Entered Into a Sham Deal with Another Customer in Fall 2000

39. Peregrine's outlook for achieving its revenue targets for the quarter ending in September 2000 appeared particularly bleak. In July, defendant Gardner warned the company's Board that the quarter's revenue goal "may be very difficult to reach" and that "we go into the always difficult September quarter essentially naked." Peregrine's General Counsel extended the

trading blackout applicable to certain Peregrine insiders because "there is some concern about the pipeline for this quarter. We do not want our Section 16 people selling stock in earnest during a quarter immediately preceding an earnings problem."

40. Powanda set out to solve the "earnings problem" in late September 2000, while entertaining major Peregrine customers at an all-expenses-paid weekend at the Indianapolis Motor Speedway. During the weekend, he told a channel partner he would need a favor. The following week, Powanda told the channel partner that Peregrine needed revenue for the September quarter, and asked the channel partner to sign a contract to make it appear that the company was purchasing $3.22 million in Peregrine software. Powanda assured the channel partner that his company would have no payment obligation to Peregrine. Powanda also told the channel partner that he wanted to start a business called "End-of-Quarter.com" that would sign sham deals for a fee to help companies meet their quarterly forecasts. The channel partner signed the contract, was never required to pay any of the $3.22 million due under it, and later was issued a "credit" invoice by Peregrine for the full amount allegedly owed. Peregrine, meanwhile, recorded revenue of $2.8 million in the September 2000 quarter.

Powanda Parked Deals with KPMG's Consulting Arm Through Defendant Larry Rodda

41. Even with Powanda's bogus $3.22 million contract, by early October 2000 Peregrine still fell short of its revenue goals for the quarter ending in September. Peregrine's sales force had failed to close a significant deal with a major financial services company within the quarter. In quarter-end communications, Powanda, Gardner and others in senior management decided to park this hoped-for revenue with a channel partner.

42. On October 3, 2000, Powanda and Peregrine Alliances (Channel) Manager Steven Spitzer parked an $11.5 million deal with KPMG's consulting arm through defendant Larry

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Rodda, identifying the financial services company as the end user in the transaction documents. Spitzer told Rodda, in connection with this and other parked deals, that KPMG would not be obligated to pay Peregrine and that the reason Rodda was being asked to sign the sham contract was to help Peregrine meet its quarterly revenue goals. Likewise, defendants Powanda and Gardner understood that—despite the binding language in the written contract—KPMG's consulting arm had no payment obligation to Peregrine. The contract was backdated to September 2000, and Peregrine recorded $10 million of this phantom revenue in its September 2000 quarter.

43. Peregrine reported total license revenue of $87.4 million for the September 2000 quarter. Almost $13 million of that revenue (about 15 percent) came from the two deals Powanda parked in that quarter.

44. In October 2000, CEO Gardner told Peregrine's Board that the September 2000 quarter had been a "nail-biter," in which forecasts were met only by "borrow[ing] from the future to make the present happen." He stated that Peregrine had been forced to grant "extraordinary terms" to achieve closings in September, which would "clearly impact" the next two quarters.

45. While the phantom revenue from the September 2000 quarter enabled Peregrine to meet its revenue forecast, it became a problem for the company's balance sheet. Important indicators of a company's financial strength are the total of its accounts receivable and how long the receivables have gone uncollected. To remove the $11.5 million KPMG consulting arm receivable from its balance sheet, Peregrine's finance department initially "sold" the sham receivable to a bank. Peregrine later repurchased the same receivable from the bank after failing to close the deal with the financial services company.

46. Defendant Rassam, Peregrine's controller—with auditor Stulac's knowledge—then improperly wrote off the receivable as an acquisition cost in the September 2001 quarter.

Powanda Parked a Deal with a United Kingdom Channel Partner in Early 2001

47. Peregrine's revenue woes continued into 2001, as did Powanda's fraudulent scheme to meet Peregrine's unattainable forecasts. Peregrine failed to achieve its quarterly forecast by the end of the March 2001 quarter. This time, Powanda parked a multi-million dollar deal with a United Kingdom channel partner in April, instructing a Peregrine salesman in the United Kingdom to backdate the deal documents to the March 2001 quarter. Peregrine improperly recorded approximately $3.5 million on this sham transaction in the March 2001 quarter.

48. Powanda knew that the United Kingdom channel partner was not obligated to perform its contract with Peregrine and that the fictitious obligation to Peregrine would be "cleansed" once Peregrine consummated its own deal with the contemplated end user. Powanda also knew, or was reckless in not knowing, that Peregrine improperly recorded revenue on this transaction in the March 2001 quarter.

49. In July 2001, a Peregrine sales manager advised Gardner and another Peregrine executive by email that Peregrine had "parked" the deal with the United Kingdom channel partner, but now needed to "cleanse this account." In August 2001, the sales manager again emailed Gardner and another executive: "We have to 'fix' [the channel partner's CEO], who passed $4 [million] of business of [end user] revenue that has not happened…." He then emailed the channel partner's CEO: "Steve Gardner is aware of the situation and Peregrine is mobilising to assist."

50. Within days Peregrine confirmed to the United Kingdom channel partner that its obligation to Peregrine had been satisfied by two completely unrelated transactions. In a process known as "burn cleaning," Peregrine eliminated this channel partner's purported obligation by using two of Peregrine's direct sales to erase the channel partner's receivable from its books.

Powanda Profited From the Fraud

51. During the fraud, Executive VP Powanda received salaries of more than $650,000, sales commissions of approximately $885,000, and bonuses of $225,000 based in part on his generation of phony revenues.

52. Additionally, during the time that Powanda was actively involved in Peregrine's fraud he exercised stock options and sold nearly 800,000 shares (split adjusted) of Peregrine stock for gross proceeds of approximately $24.7 million. On a single day in February 2001, Powanda sold more than $11 million worth of Peregrine stock. His gain on the exercise of options and sale of stock exceeded $20 million.

DEFENDANT GARDNER'S FRAUDULENT CONDUCT

53. Gardner was a full and knowing participant in Peregrine's accounting fraud. He was aware that Peregrine executives concocted sham sales at the ends of quarters and after the ends of quarters (and backdated them). Gardner understood revenue recognition requirements under GAAP, and knew Peregrine's financial statements were inflated with improperly-reported revenue from bogus software license sales.

54. For example, in the December 1999 quarter, Alliances Manager Spitzer parked a deal with KPMG's consulting arm, using a hospitality company as the supposed end user. Gardner contemporaneously understood that Peregrine (not KPMG) would bear the financial risk

if Peregrine was unable to close its contemplated sale to the hospitality company. Peregrine improperly recorded approximately $4 million revenue on the parked deal.

55. Gardner understood that Peregrine had recorded revenue on the sham sale. Indeed, in Gardner's January 18, 2000 "Fiscal Q3 2000 Review and Outlook" written for Peregrine's Board of Directors, he stated: "We had a bad forecast to begin with, a gradual improvement in the middle part of the quarter, and then a $4 million melt-down in the last week of the quarter. Only the KPMG deal with [the hospitality company] and [an unrelated deal] saved the US performance."

56. Much of the responsibility of covering up the revenue fraud fell to CFO Matthew Gless, who kept Gardner informed of deals that had not closed, but for which Peregrine had recorded revenue. For example, in October 2000, Gless learned that a Peregrine customer had exercised a 30-day money-back guarantee on a $2 million software license purchase from Peregrine, and that in response Peregrine's sales force had extended the money-back guarantee to 60 days. Gless emailed Gardner: "Here we go again! Need to make sure deal closes." Gardner knew, or was reckless in not knowing, that Peregrine had improperly recorded revenue on the deal.

57. In November 2000, Gless reminded Gardner about more than $30 million of Peregrine's software license "sales" from prior quarters, including the $11.5 million deal with KPMG's consulting arm, for which Peregrine had improperly recorded revenue. Gless warned Gardner: "We must close this business this quarter or otherwise risk potential exposure." Gardner knew, or was reckless in not knowing, that Peregrine had improperly recorded more than $30 million revenue on these unconsummated software license sales, and that the "potential exposure" was a revenue restatement.

Gardner Buried Uncollectible Barnhill Receivables

58. By December 1999, Peregrine's financial books and records reflected more than $12 million in uncollectible "receivables" from parked deals with Barnhill, the reseller owned by defendant Whitt. To eliminate the sham Barnhill receivables, Peregrine bought Barnhill and accounted for the unpaid receivables as acquisition costs. Gardner knew, or was reckless in not knowing, that a primary purpose of the Barnhill acquisition was to eliminate the uncollectible Barnhill receivables from Peregrine's balance sheet. Peregrine's Board of Directors approved the Barnhill acquisition on January 18, 2000, and the acquisition closed on March 30, 2000. Peregrine paid $32.2 million for Barnhill, and defendant Whitt received Peregrine stock that was then worth approximately $11 million.

Gardner Knew that Peregrine Fraudulently Booked $10 Million in Deals with Another Channel Partner

59. In the March 2000 quarter, Peregrine recorded $3.88 million revenue on a software license sale to a channel partner under a contract that did not close until after the quarter ended.

60. Gardner knew that the contract had been recognized as revenue but was not yet finalized. In May 2000—almost two months after Peregrine recorded the revenue—Gardner emailed other Peregrine officers: "I am not sure why we have no contract closure on an item that we booked last quarter and which we are now looking for payment on. This is going to place this payable in jeopardy, since [the channel partner] has already indicated that they are well aware of the lack of closure."

61. The channel partner eventually paid Peregrine for this contract. However, Gardner knew, or was reckless in not knowing, that Peregrine had violated the software revenue recognition rules by recording the revenue in the quarter before the contract was finalized.

62. In the September 2000 quarter, Peregrine improperly recognized more than $6 million of revenue from another software license "sale" to this same channel partner. However, the contract was both backdated and made subject to a contingency giving the channel partner the right to cancel the contract if Peregrine and the channel partner failed to implement certain "commercial objectives." These terms meant that the channel partner was not obligated to pay Peregrine.

63. On April 5, 2001—21 days before Peregrine announced its fiscal 2001 financial results—the channel partner informed Gardner that it had terminated the transaction, and therefore would not pay Peregrine. Although Gardner knew, or was reckless in not knowing, that Peregrine had improperly recorded the revenue, he did not ensure that Peregrine reversed the revenue. On April 26, 2001, Peregrine announced its year-end financial results that included the more than $6 million in revenue on the software license transaction that Gardner knew had been cancelled.

64. On April 30, 2001, Gardner tried to revive the cancelled transaction, entering into an agreement with the channel partner that attempted to resuscitate negotiations. Once again, the document did not bind the channel partner to pay Peregrine anything under the contract. The channel partner in fact never paid Peregrine, and defendant Rassam, with the knowledge of auditor Stulac, improperly wrote off the receivable as an acquisition cost as part of the scheme to conceal Peregrine's uncollectible receivables from the investing public.

Gardner Knew a Deal with a United Kingdom Company was Prematurely Booked

65. Peregrine failed to achieve its revenue forecasts for the December 2000 quarter. As in previous quarters, Peregrine kept its December 2000 books open into January 2001 so that

its executives could continue to search for sources of revenue that would be backdated to the December 2000 quarter.

66. On January 5, 2001, defendants Gardner, Powanda, and Lenz learned that Peregrine's United Kingdom sales force had just entered into a £10 million software license transaction with a United Kingdom telecommunications company. Peregrine provided the telecommunications company with two separate "out clauses": an unconditional money-back guarantee and the right to cancel if it failed to enter into an agreement with its own customer within 30 days. Peregrine improperly recorded $12.55 million revenue on this January 2001 transaction in the December 2000 quarter. This transaction comprised 12.5 percent of Peregrine's reported license revenue ($99.54 million) for the December 2000 quarter. Gardner, Powanda and other Peregrine executives knew, or were reckless in not knowing, that Peregrine had improperly recorded revenue on this transaction. When the 30-day period expired and the telecommunications company informed Peregrine it wished to cancel, Peregrine further extended the out clause period.

67. As demonstrated by the following exchange of emails with a Peregrine sales manager, Gardner knew in March 2001 that the transaction with the telecommunications company had not closed.

- March 20 email from sales manager to Gardner:

> Chasing everything for Q4 but still finalising [the deal with the telecommunications company]. Not completed yet after all . . .

- Gardner response:

> [T]his is clearly not good news.

- March 21 email from sales manager to Gardner and Powanda:

> We are struggling to move this forward. They [the United Kingdom telecommunications company] want to remove the payment profile so that on their books it does not look like a commitment . . . . Are we dead in the water here?

68. Despite the moribund outlook for the deal, Peregrine management—having included the revenue in its quarterly financial statement—schemed to remove the receivable from the company's balance sheet. In and around the time of Gardner's email exchange, Treasury manager Ilse Cappel first tried to sell the receivable to one bank, which she emailed:

> I have confirmed with our most senior sales executives and our CEO, and we are extremely confident that this deal will close this week. Please do everything you can to ensure that approval to purchase this receivable is in place, in anticipation of this deal closing. We are working toward closing and funding to our account this Friday, March 30th.

69. On March 30, however, the telecommunications company cancelled its negotiations with Peregrine. Peregrine's United Kingdom legal counsel emailed Cappel, CFO Gless, and defendants Powanda and Gardner:

> Matt, Ilse, there seems to be some confusion surrounding the financing of [the receivable from the telecommunications company]. I have just discussed with Steve and Doug and said that I would confirm this for everyone's benefit. The position is that, given the various commercial discussions still going on, we will not be able to get the necessary [bank] wording approved by [the telecommunications company] today (and probably not even very early next week) which would need to be slotted into the SLA [software license agreement]/schedule A. Therefore [the contacts at the bank] have confirmed that they will not be able to finance to get the money in today. Steve and Doug are aware of this and suggested that you might know of other alternatives for financing.

70. Despite the ongoing contract negotiations (i.e., "the various commercial discussions still going on"), Gardner instructed Cappel to sell the "receivable" to a different bank. Cappel executed Gardner's instructions and Peregrine eventually had to repurchase the purported receivable from the bank.

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Gardner Knew of Other Sham Sales

71. Gardner knew that Peregrine's sales force utilized side letters to give channel partners the right to nullify contracts, a practice that he knew, or was reckless in not knowing, made revenue recognition fraudulent. For example, Peregrine entered into a June 2001 software license contract that purported to bind a South African channel partner to pay Peregrine $12 million within two years. The contract, however, was made conditional by a side agreement prepared by a Peregrine employee. The side agreement stated that if the channel partner "falls behind in revenue sold vs. payment to [Peregrine] - Peregrine will provide relief to [the channel partner]. . . until the sales are back on target." As a result, the channel partner had no obligation to pay Peregrine yet Peregrine recorded $8.54 million revenue for the transaction in the June 2001 quarter. Gardner knew, or was reckless in not knowing, that Peregrine had recorded the revenue improperly since he discussed the side letter at the channel partner's offices in South Africa in or about November 2001. Gardner took no action to ensure that Peregrine reversed the revenue.

72. Gardner also knew of another side letter dated in June 2001 that made it improper for Peregrine to have recognized revenue on a software license transaction with a channel partner in Poland. Once again, the contract purported to bind the channel partner to pay Peregrine $12 million within two years and was subject to a side agreement excusing the channel partner from its payment obligation. Nevertheless, Peregrine recorded $9.3 million revenue for the transaction in the June 2001 quarter. Gardner learned of the side agreement in or about November 2001 and therefore knew, or was reckless in not knowing, that Peregrine had improperly recorded revenue on the transaction. Once again, he failed to ensure that Peregrine reversed the revenue.

73. Peregrine improperly recorded a total of $17.8 million revenue on the June 2001 transactions with the South African and Polish channel partners. Those transactions comprised about 18 percent of Peregrine's reported license revenue ($100 million) for the June 2001 quarter.

Gardner Made False Statements to Investors and to Peregrine's Auditors

74. Gardner was Peregrine's principal conduit to industry analysts and investors. In quarterly-earnings conference calls and in Peregrine's press releases in connection with earnings, Gardner trumpeted Peregrine's "record" financial results. As Chief Executive Officer, he also signed Peregrine's Forms 10-K, including the fiscal 2001 Form 10-K that falsely stated:

> Revenues from direct and indirect license agreements are recognized, provided that all of the following conditions are met: a noncancelable license agreement has been signed; the product has been delivered; there are no material uncertainties regarding customer acceptance; collection of the resulting receivable is deemed probable; risk of concession is deemed remote; and no other significant vendor obligations exist.

When Gardner signed Peregrine's fiscal 2001 Form 10-K, he knew, or was reckless in not knowing, that this statement falsely described Peregrine's established revenue-recognition practices.

75. Gardner signed at least nine management representation letters that Peregrine presented to its auditor, Arthur Andersen. Some of these letters contained the following false representations: (a) Peregrine's financial statements were in accordance with GAAP; (b) there were no material transactions that were not properly recorded in Peregrine's accounting records underlying its financial statements; and (c) there had been no fraud involving (i) management or employees who had significant roles in internal control, or (ii) others that could have a material effect on the financial statements. When Gardner signed the management representation letters, he knew, or was reckless in not knowing, that these representations were false.

Gardner Profited From the Fraud

76. Gardner profited from the fraudulent scheme at Peregrine. While Gardner was participating in the scheme, Peregrine paid him salaries of more than $1.1 million and bonuses exceeding $2.3 million. When Gardner received these payments he knew, or was reckless in not knowing, that Peregrine's publicly-disclosed revenues and income were fraudulently inflated.

77. In 2001—in the midst of the fraud—Gardner's salary and bonus were substantially increased largely due to the inflated financial picture created by the fraud. Peregrine's 2001 Proxy Statement stated:

> The board of directors substantially increased the amount of base salary and bonus paid to Mr. Gardner in fiscal 2001 compared to fiscal 2000. This increase reflects Peregrine's growth as a company and … reflects the determination of the board of directors that during fiscal 2001 Peregrine met certain objectives, including objectives relating to Peregrine's revenue growth and financial performance.

78. Gardner also exercised options and sold stock for gross proceeds exceeding $11 million during the fraudulent scheme.

DEFENDANT LENZ'S FRAUDULENT CONDUCT

79. Gary Lenz joined Peregrine in May 2000 as Executive Vice President of Development and Strategy and was promoted to President in October 2000. By that time, he was participating in the revenue-inflation scheme. Lenz participated in several sham revenue transactions, including two with a Peregrine consultant.

Lenz Authorized Spitzer to Park a Deal with the Peregrine Consultant

80. At the end of the September 2000 quarter, Peregrine once again needed revenue to meet its forecasts. Peregrine had pinned its earnings hopes on a sale of software licenses to an oil company, but could not complete the sale in September 2000. To record that revenue in the

September quarter, Lenz directed Alliances Manager Spitzer to park the oil-company deal with a Peregrine consultant. In accordance with Peregrine's familiar pattern, the contract documentation appeared to obligate the consultant to purchase software licenses from Peregrine for resale to the oil company; however, Spitzer assured the consultant that Peregrine would not enforce the contract. The Peregrine consultant signed the sham contract, dated September 29, 2000, purporting to bind him to pay Peregrine $572,000 for software.

81. Peregrine improperly recorded $476,850 revenue in the September 2000 quarter for this parked transaction. Lenz knew, or was reckless in not knowing, that the consultant's contract was a sham and that Peregrine had improperly recorded revenue in the September 2000 quarter.

Lenz Negotiated a Backdated Deal

82. After the end of the September 2000 quarter, Lenz and Powanda entered into a backdated contract with a Peregrine channel partner under which the channel partner agreed to a $3.6 million transaction on October 2, 2000. Powanda backdated the contract to September 29, 2000, gave the channel partner a 30-day written money-back guarantee and emailed the documentation to the channel partner on October 2 with a copy to Lenz.

83. Peregrine improperly recorded $3 million revenue in the September 2000 quarter on this backdated contract. Lenz and Powanda knew, or were reckless in not knowing, that Peregrine had improperly recorded revenue on this contract.

84. Controller Rassam, with auditor Stulac's knowledge, improperly wrote off the bogus receivable as an acquisition cost in the September 2001 quarter.

Lenz Authorized Spitzer to Park a
Second Deal with the Peregrine Consultant

85. At the end of the March 2001 quarter, Lenz directed Spitzer to park a second software license sale with the Peregrine consultant. This sham revenue transaction was more than twice the size of the one Lenz had directed Spitzer to park in the September 2000 quarter. Like the previous transaction, the March 2001 contract was for a hoped-for sale of software licenses by Peregrine to a third party and falsely purported to bind the consultant to pay Peregrine $1.14 million for software licenses.

86. Peregrine improperly recorded $993,000 revenue in the March 2001 quarter for this parked transaction. Lenz knew, or was reckless in not knowing, that the Peregrine consultant had signed a sham software purchase agreement with Peregrine, and that Peregrine improperly recorded revenue on it in the March 2001 quarter.

Lenz Signed a False
Management Representation Letter

87. On April 26, 2001, Peregrine announced its fraudulent financial results for fiscal 2001, which included the three improperly recorded transactions arranged by Lenz. Contemporaneously, Lenz and Gardner, among other Peregrine officers, signed a false management representation letter.

88. The representation letter contained the following misrepresentations, among others: (a) Peregrine's financial statements were in accordance with GAAP; (b) there were no material transactions that were not properly recorded in Peregrine's accounting records underlying its financial statements; and (c) there had been no fraud involving (i) management or employees who had significant roles in internal control, or (ii) others that could have a material effect on the financial statements. When Lenz and Gardner signed and issued this representation letter, they knew, or were reckless in not knowing, that it was false.

Lenz Profited From the Fraud

89. Lenz profited from the fraudulent scheme at Peregrine. Peregrine paid Lenz an annual salary of $250,000. He also received total cash bonuses of approximately $290,000 and an interest-free loan of $800,000. Lenz was terminated as Peregrine President in February 2002, but remained on the payroll "working from home" until March 31, 2003. As part of his severance package, he was paid $137,500 on March 31, 2002, bi-monthly payments of $12,500, and was granted continued interest-free status on the $800,000 loan for two years.

DEFENDANT RODDA'S FRAUDULENT CONDUCT

90. At all relevant times, defendant Rodda worked at KPMG's consulting arm. Between 1999 and late 2000, Rodda signed several sham software license purchase contracts at the request of Powanda, Spitzer and other senior Peregrine officers. Rodda knew that KPMG's consulting arm had no payment obligation under its contracts with Peregrine. He further understood that the purpose of these phony contracts was to enable Peregrine to improperly record revenue to achieve its quarterly forecasts. Peregrine improperly recorded approximately $22 million on the sham parking arrangements signed by Rodda.

91. Rodda willingly participated in these fraudulent transactions with the expectation that, in return, Peregrine would award KPMG's consulting arm lucrative services work. Peregrine never collected on the deals parked with Rodda, fraudulently "sold" some of the associated receivables to banks, and improperly wrote off many of the receivables as acquisition costs.

Rodda Agreed to Park the Deal Peregrine was Negotiating with a Hospitality Company

92. At the end of the December 1999 quarter, Peregrine was again short in achieving its revenue target. To enable the company to meet its goals, Rodda agreed to park a $4 million

deal for Spitzer using a hospitality company as the purported end user. Rodda entered into the contract with the understanding that KPMG's consulting arm had no payment obligation to Peregrine. Peregrine recorded approximately $4 million revenue on that parked contract, constituting 8.6 percent of Peregrine's reported license revenue ($46.5 million) for the December 1999 quarter.

93. Rodda later helped Peregrine hide the parked transaction by signing a false audit confirmation. On February 14, 2000, Rodda received a letter from Peregrine, addressed to KPMG's "Accounts Payable," stating in pertinent part:

> Our auditors, Arthur Andersen LLP, are now engaged in an audit of our financial statements. In connection therewith, they desire to confirm the balance due us on your account as of Dec. 31, 1999 and certain terms of your recent purchase . . . . Please state in the space below whether or not the enclosed information is in agreement with your records . . . . Also, please describe any unfulfilled obligations or contingencies under this contract at December 31, 1999.

Although he knew KPMG's consulting arm had no payment obligation to Peregrine, Rodda signed the audit confirmation, wrote "no exceptions," and returned it to Arthur Andersen.

94. Peregrine never collected the receivable. In September 2001, Controller Rassam, with Andersen partner Stulac's knowledge, improperly wrote off the receivable as an acquisition cost.

Rodda Parked Additional Deals for Peregrine
In the June 2000 Quarter

95. Rodda parked two more deals for Peregrine in the June 2000 quarter. Like his other sham contracts, he knew that Peregrine did not expect KPMG's consulting arm to pay Peregrine. Rodda also understood the purpose of the sham contracts was to enable Peregrine to achieve its revenue forecasts. The first of the transactions Rodda parked in the June 2000 quarter was a $7.1 million deal that Peregrine could not complete with a financial services company by

quarter end. Peregrine improperly recorded $6.1 million revenue on this parked deal in the June 2000 quarter.

96. After signing that sham contract, Rodda informed Peregrine that he wanted to find a way for KPMG's consulting arm to record revenue on the transaction. Accordingly, Spitzer and Rodda agreed that Peregrine would flow the $7.5 million (the $7.1 million deal plus tax) it expected from the end user—assuming Peregrine completed its aspired-to deal with the end user—through KPMG's consulting arm on its way to Peregrine.

97. Rodda then signed another contract, for $2.29 million, which Peregrine used to record $2 million revenue in the June 2000 quarter. Since KPMG never paid Peregrine on the parked contract, Peregrine improperly wrote off the receivable as an acquisition cost a year later.

98. This improperly recorded revenue was 12.9 percent of Peregrine's reported license revenue ($62.44 million) for the June 2000 quarter.

The September 2000 Quarter

99. In October 2000, Powanda and Spitzer asked Rodda to park an $11.5 million deal with a financial services company described as the end user.

100. Initially Rodda balked at the request because KPMG's consulting arm had not received the promised $7.5 million flow of money on the contract he parked for Peregrine in the June 2000 quarter. To induce Rodda to sign the sham $11.5 million software license transaction, Powanda and others at Peregrine agreed to wire KPMG's consulting arm the $7.5 million for the previously-parked transaction.

101. Powanda faxed Rodda the documents for the $11.5 million parked deal in October 2000 with the written pledge to: "follow up and have the wire confirmed with you today." Shortly thereafter, Peregrine wired $7.5 million to KPMG's consulting arm. Rodda then duped KPMG's consulting arm into wiring $7.5 million back to Peregrine. Thus, the transaction was

wholly without substance with the money circularly flowing from Peregrine to KPMG's consulting arm, and then back to Peregrine.

102. Rodda signed the $11.5 million software license purchase agreement with the understanding that the contract was a sham and backdated to September 2000 to enable Peregrine to record the revenue in that quarter.

DEFENDANT REICHNER'S AND DEFENDANT O'BRIEN'S FRAUDULENT CONDUCT

Reichner and O'Brien Parked Two Deals with KPMG's Consulting Arm in December 2000

103. During the fall of 2000, Rodda transferred his Peregrine practice to another partner at KPMG's consulting arm.

104. In December 2000, Senior VP Joseph G. Reichner and Director of Strategic Alliances Peter J. O'Brien parked two deals valued at more than $5 million at KPMG's consulting division. Reichner and O'Brien asked the KPMG consulting arm partner to sign a reseller agreement for two prospective deals that Peregrine's sales force had been negotiating with a global technology company and an international aerospace corporation that the sales force would be unable to close by the end of the December quarter.

105. Reichner told the KPMG consulting partner that if he agreed to sign for these deals, then Reichner would make it "worth his while." Reichner promised him: (a) a $250,000 "marketing development fund"; (b) 90-day cancellation terms, thereby eliminating any risk to KPMG's consulting arm during that period; and (c) a steeper reseller discount on the software when and if it was sold to the end users.

106. A few days later, as the quarter end grew closer, Reichner and O'Brien called the KPMG consulting arm partner to follow up on their request. During this second call, Reichner

promised the KPMG consulting arm partner that if he signed for the deals now and Peregrine did not close its prospective end-user deals with the two global companies, then he (Reichner) would "take care of it." Reichner assured him that Peregrine would not seek payment from KPMG's consulting arm if the end users did not buy the software.

107. The KPMG consulting arm partner then signed for the deals, returned them to O'Brien, but did not show his copy of the contracts to anyone at KPMG.

108. In the December 2000 quarter, Peregrine recorded $5 million in license revenue on the two deals Reichner and O'Brien parked with KPMG's consulting arm. Reichner and O'Brien knew, or were reckless in not knowing, that Peregrine improperly recorded revenue on the deals they parked with KPMG's consulting arm.

Reichner and O'Brien Were Involved in a Sham Deal with a Government Contractor in September 2001

109. As the end of the September 2001 quarter approached, Peregrine's public sector sales team was close to securing a $3 million contract with a government entity. O'Brien met with Peregrine's public sector sales vice president and representatives from the government entity, but the terms of the deal were subject to further negotiation. O'Brien reported the uncertain status of the transaction to Reichner.

110. Peregrine's public sector sales group sought a channel partner with which it could park the prospective deal with the government entity, and approached a government contractor in the information technology field for that purpose. O'Brien learned that Peregrine was offering the information technology contractor, among other things, a 30-day out clause. The information technology contractor agreed to sign for the deal at the end of September 2001. With the 30-day out clause, there was no risk to the channel partner.

111. Peregrine recognized $2.85 million in license revenue in the September 2001 quarter on the deal it parked with the information technology contractor. Reichner and O'Brien knew, or were reckless in not knowing, that Peregrine improperly recognized revenue on the deal parked with the information technology contractor.

112. During the next several weeks, Peregrine's public sector group still could not close the deal with the government entity. As a result, the information technology contractor informed Peregrine of its intention to exercise the 30-day out clause and cancel the contract.

113. O'Brien and Reichner discussed how to account for the channel partner's cancellation of the parked deal, and, despite the lack of closure on the prospective end-user deal with the government entity, Reichner issued a false "credit" letter to the information technology contractor in late October of 2001, informing it that "[y]our obligation has been satisfied by the [government entity] [c]ontract."

Reichner Profited from the Fraud

114. Peregrine hired Reichner in September 2000 as its Senior Vice President of Alliances and Business Development, paying him an annual salary of $250,000. In January 2001, immediately following the two parked deals with KPMG's consulting arm, Peregrine paid Reichner an incentive bonus of $31,250, and in July 2001, Peregrine paid him another incentive bonus of $125,000. The bonuses were based in part on his generation of phony revenues. Reichner's active employment was terminated by Peregrine in January 2002, and he received a severance payment of $34,500 on February 15, 2002, and the equivalent of a $125,000 salary through January 15, 2003.

O'Brien Profited from the Fraud

115. In October 2000, Peregrine promoted O'Brien to Director of Strategic Alliances, with an annual salary of $120,000. In February 2001—shortly after he and Reichner parked the deals with KPMG's consulting arm—O'Brien exercised options and sold Peregrine stock for gross proceeds exceeding $150,000. Several months later, in June 2001, Peregrine paid him a bonus of $54,780 that was related in part to his generation of phony revenues.

DEFENDANTS STULAC AND RASSAM COVERED UP THE FRAUD

116. Defendant Stulac is a certified public accountant who was a member of Arthur Andersen's audit team for the Peregrine engagement, first as audit manager, then as engagement partner from September 2000 to September 2001. As early as January 2000, Stulac knew that his direct supervisor—the then-engagement partner for Peregrine—was concerned about the company's sluggish collection of its channel sales. Stulac also knew that the Andersen engagement partner had instructed Peregrine that it should not recognize revenue on any channel sale with payment terms of more than 90 days.

117. In fall 2000, Peregrine hired defendant Berdj Rassam as its Controller. Like the Andersen auditors, Rassam quickly observed that Peregrine was not collecting on its channel sales. In January 2001, Rassam warned colleagues in Peregrine's finance department: "We book channel sales, no end user….The channel doesn't get burned, we never get paid….Not only do we lose from an acctg [sic] perspective, but a cash and shareholder value perspective….Please consider this as a real problem…." Within the next month, Rassam learned that KPMG's consulting arm did not consider its transactions with Peregrine to be "real sales." Rassam later learned of other "sales" Peregrine had improperly recorded as revenue.

118. Also in fall 2000, Stulac was promoted to engagement partner for Peregrine's fiscal year 2001. During fiscal year 2001, Stulac learned that, contrary to Peregrine's prior assurances to Andersen, it was wrongly recording revenue on channel sales with payment terms exceeding 90 days, and that Peregrine's channel was bursting with unpaid receivables. Stulac instructed Peregrine's finance department to "clean" Peregrine's channel because the situation was "giving him heartburn."

119. In late March or early April 2001, Rassam expressed concern to Stulac about the large dollar amount of Peregrine's channel receivables and told Stulac that Peregrine was about to write off channel receivables as acquisition costs. Rassam also told Stulac the write-offs would eliminate Peregrine's channel problem.

120. At or around that period, on March 28, 2001, Peregrine received a "Comment Letter" from the Securities and Exchange Commission's Division of Corporation Finance questioning certain aspects of its fiscal 2000 Form 10-K and Forms 10-Q it had filed for fiscal 2001. The Comment Letter asked Peregrine to describe its "concession" risk on its software license sales. A truthful answer—that the concession risk was enormous because Peregrine's channel partners were not paying Peregrine—likely would have exposed Peregrine's accounting fraud. To conceal the fraud, Peregrine's response falsely claimed, among other things, that Peregrine's only concession risk related to contracts with extended payment terms greater than one year; that Peregrine had an "excellent" history of collections on contracts with greater-than-one-year payment terms; and that Peregrine had successfully collected on all such extended payment term contracts. The Comment Letter response also misrepresented: "The Company does not have a history of offering concessions for any customers, products, or payment arrangements."

121. Stulac and another Andersen auditor helped prepare Peregrine's response to the Comment Letter, and Rassam and Gless reviewed it before sending it to the SEC on or about April 12, 2001.

122. Also around this time, Peregrine's improper revenue recognition practices were detected by a German affiliate of Andersen LLP that was auditing Peregrine's German subsidiary. On April 12, 2001, a German auditor emailed Stulac an "Early Warning" memorandum documenting, among other things, revenue apparently recorded improperly on three contracts with channel partners, in part because their payment terms exceeded one year. One of the three contracts was a $12 million software license sale to a certain German channel partner that had not paid Peregrine on previous software license sales. At the time, that channel partner had a multi-million dollar receivable balance with Peregrine.

123. As a certified public accountant, Stulac knew, or was reckless in not knowing, that software revenue recognition rules do not permit issuers to recognize revenue on these extended payment term contracts unless the vendor can demonstrate a history of collections on similar contracts. He also knew the opposite was true at Peregrine: the company had a history of failing to collect receivables. Stulac also knew that recognition of this revenue was in violation of Andersen's instructions to Peregrine that revenue should not be recognized on channel contracts if payment terms extended beyond 90 days.

124. To conceal both Peregrine's accounting fraud and his own complicity, Stulac mischaracterized the nature of the three channel contracts and falsely claimed to his German colleagues that Peregrine had a history of collections on similar contracts.

125. Unpersuaded by Stulac's response, the German auditor replied by email on April 17, 2001 stating, among other things: "So how in the world can revenue be recognized on these

[channel contracts with extended payment terms]??" Stulac then informed the German auditor that Andersen LLP would address his concerns "in consolidation." In fact, Stulac never properly addressed the German auditor's concerns in consolidation or otherwise, and instead allowed Peregrine to recognize revenue on the three German channel contracts.

126. The German auditor refused to give Andersen LLP an audit opinion on the financial statements of Peregrine's German subsidiary. Both Stulac and Rassam knew, or were reckless in not knowing, that the German subsidiary's financial results were material to Peregrine's worldwide consolidated financial results. Stulac and Rassam further knew, or were reckless in not knowing, that Andersen LLP should not have issued an unqualified opinion on Peregrine's fiscal 2001 consolidated financial statements, especially in light of the German auditor's refusal to issue a "clean" opinion on the material German subsidiary's financial statements.

127. The implications of the German auditor's refusal to "sign off" on the financial statements of Peregrine's German subsidiary were clear to Rassam. In May 2001, he informed others at Peregrine:

> Given that [the German subsidiary] is material to [Peregrine] it was imperative that [the German subsidiary] be materially audited ("signed-off") by April 24. It wasn't signed-off….As a result [Andersen LLP] did not have to give [Peregrine] an unqualified opinion….If Peregrine did not get an unqualified opinion our stock price [sic] would not legally be tradeable and therefore are [sic] stock price would be practically worthless.

128. Undaunted by the German auditor's objections, Stulac and Rassam met days before Peregrine's April 26, 2001 earnings release for fiscal 2001 to discuss $26.5 million of channel receivables Peregrine planned to write off as "Acquisition Costs and Other" in the March 2001 quarter. The list included a $2.3 million receivable from the same German channel partner with which Peregrine had just entered into a new $12 million agreement. Peregrine's list

also revealed it had written off a second receivable for approximately $653,000 with that same German channel partner.

129. Stulac and Rassam each knew, or were reckless in not knowing, that the receivables Peregrine intended to write-off were unrelated to acquisitions and that Peregrine's management had improperly characterized the write-offs as acquisition costs to cover up Peregrine's mountain of uncollectible receivables.

130. Stulac knew, or was reckless in not knowing, that Peregrine's 2001 financial statements improperly recognized millions of dollars of revenue from channel transactions, including the most recent $12 million agreement with the German channel partner. Nevertheless, Stulac caused Andersen to issue an unqualified audit opinion on Peregrine's fiscal 2001 financial statements after (a) preparing a false response to an SEC Division of Corporation Finance Comment Letter, (b) ignoring the German auditor's objections to Peregrine's revenue recognition practices, and (c) allowing Peregrine to misclassify channel-receivable write-offs as acquisition costs.

131. Among other things, Andersen's audit opinion misrepresented that Andersen conducted its audits in accordance with auditing standards generally accepted in the United States, and that the financial statements presented fairly, in all material respects, the financial position of Peregrine, the results of their operations and their cash flows in conformity with accounting principles generally accepted in the United States.

In Early Fiscal Year 2002, Rassam Learned of More Revenue Problems And Improperly Wrote Off Unpaid KPMG Receivables

132. During the September 2001 quarter, Rassam, with Stulac's knowledge, seized on Peregrine's acquisition of Remedy Corporation as an opportunity to improperly write off another $26.65 million of uncollectible receivables to the "Acquisition Costs and Other Expense" line

item and an additional $16.93 million to a balance sheet item called "Remedy Acquisition Accrual." Of these improperly written-off receivables, $21 million were sham sales to KPMG's consulting arm (which Rassam had been informed were not, in KPMG's view, "real" deals).

133. Rassam and Stulac knew, or were reckless in not knowing, that: (a) Peregrine had sold and repurchased at least some of the KPMG receivables from banks; (b) the repurchases of receivables demonstrated that Peregrine remained liable for the debts; and (c) consequently, that its sales of the receivables did not qualify for the off-balance-sheet treatment they had been accorded to cover up the accounting fraud. Rassam and Stulac also knew, or were reckless in not knowing, that Peregrine failed to disclose properly its off-balance-sheet financing in its financial statements. The last Form 10-Q Peregrine filed with the Commission before the fraud came to light (for the December 31, 2001 quarter) falsely disclosed only that "[t]he Company may at times market certain client receivable balances without recourse."

Rassam Profited From the Fraud

134. Rassam profited from the fraud. Peregrine paid him salaries of approximately $247,500 and bonuses totaling approximately $163,000 in part based on the company's fraudulently inflated financial performance.

FIRST CLAIM

Gardner, Powanda, Lenz, Rassam, Reichner, O'Brien and Stulac Violated Exchange Act Section 10(b) and Exchange Act Rule 10b-5

[Financial Fraud]

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

136. Defendants Gardner, Powanda, Lenz, Rassam, Reichner, O'Brien and Stulac knowingly or recklessly employed devices, schemes, or artifices to defraud, in connection with

the purchase or sale of securities, with the intent of materially misstating Peregrine's publicly-reported financial results.

137. Defendants Gardner, Powanda, Lenz, Rassam, Reichner, O'Brien and Stulac knowingly or recklessly made misrepresentations and omissions of fact, in connection with the purchase or sale of securities, with the intent of materially misstating Peregrine's publicly-reported financial results.

138. Defendants Gardner, Powanda, Lenz, Rassam, Reichner, O'Brien and Stulac engaged in acts, practices, or courses of business, in connection with the purchase or sale of securities, which operated or would have operated as a fraud or deceit upon analysts and the investing public.

139. By reason of the foregoing, defendants Gardner, Powanda, Lenz, Rassam, Reichner, O'Brien and Stulac violated Exchange Act Section 10(b) [15 U.S.C. § 78j(b)] and Exchange Act Rule 10b-5 [17 C.F.R. § 240.10b-5[1]].

SECOND CLAIM

Gardner, Powanda, Lenz, Rassam and O'Brien Violated Securities Act Section 17(a)

[Financial Fraud]

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

141. Defendants Gardner, Powanda, Lenz, Rassam and O'Brien knowingly or recklessly employed devices, schemes, or artifices to defraud, in the offer or sale of securities, with the intent of materially misstating Peregrine's publicly-reported financial results.

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[1] 2002 ed., p. 60, promulgated 12/22/48, as amended 8/11/51.

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142. Defendants Gardner, Powanda, Lenz, Rassam and O'Brien knowingly or recklessly made misrepresentations and omissions of fact, in the offer or sale of securities, with the intent of materially misstating Peregrine's publicly-reported financial results.

143. Defendants Gardner, Powanda, Lenz, Rassam and O'Brien knowingly or recklessly engaged in transactions, practices, or courses of business, in the offer or sale of securities, which operated or would have operated as a fraud upon purchasers of Peregrine securities.

144. By reason of the foregoing, defendants Gardner, Powanda, Lenz, Rassam and O'Brien violated Securities Act Section 17(a) [15 U.S.C. § 77q(a)].

THIRD CLAIM

Gardner, Powanda and O'Brien Violated Securities Act Section 17(a), Exchange Act Section 10(b) and Exchange Act Rule 10b-5

[Insider Trading]

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

146. Defendants Gardner, Powanda and O'Brien sold Peregrine stock on the basis of material nonpublic information concerning Peregrine's true financial condition, in breach of their fiduciary duty to Peregrine and its shareholders.

147. By reason of the foregoing, defendants Gardner, Powanda and O'Brien violated Securities Act Section 17(a) [15 U.S.C. § 77q(a)], Exchange Act Section 10(b) [15 U.S.C. § 78j(b)] and Exchange Act Rule 10b-5 [17 C.F.R. § 240.10b-5].

FOURTH CLAIM

Gardner, Powanda, Lenz, Rassam, Reichner and O'Brien Violated Exchange Act Section 13(b)(5) and Exchange Act Rule 13b2-1 and Aided and Abetted Violations of Exchange Act Sections 13(b)(2)(A) and 13(b)(2)(B)

[Books and Records and Internal Controls Violations]

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

149. Defendants Gardner, Powanda, Lenz, Rassam, Reichner and O'Brien deliberately circumvented existing internal accounting controls in place at Peregrine in order to falsify the company's books and records.

150. Gardner, Powanda, Lenz, Rassam, Reichner and O'Brien directly or indirectly falsified or caused to be falsified, books, records, or accounts of Peregrine described in Exchange Act Section 13(b)(2) [15 U.S.C. § 78m(b)(2)].

151. Gardner, Powanda, Lenz, Rassam, Reichner and O'Brien knowingly and substantially participated in a scheme to cause extensive false and misleading entries in Peregrine's books and records. By doing so, Gardner, Powanda, Lenz, Rassam, Reichner and O'Brien aided and abetted Peregrine's failure to make and keep books, records, and accounts, which, in reasonable detail, accurately and fairly reflected the company's transactions and dispositions of its assets.

152. Gardner, Powanda, Lenz, Rassam, Reichner and O'Brien knowingly and substantially contributed to Peregrine's failure to maintain its internal accounting controls. By doing so, Gardner, Powanda, Lenz, Rassam, Reichner and O'Brien aided and abetted the company's failure to devise and maintain a system of internal accounting controls sufficient to provide reasonable assurances that transactions were recorded as necessary to permit preparation of financial statements in conformity with GAAP.

153. By reason of the foregoing, Gardner, Powanda, Lenz, Rassam, Reichner and O'Brien violated Exchange Act Section 13(b)(5) [15 U.S.C. § 78m(b)(5)] and Exchange Act Rule 13b2-1 [17 C.F.R. § 240.13b2-1[2]], and aided and abetted violations of Exchange Act Sections 13(b)(2)(A) and 13(b)(2)(B) [15 U.S.C. §§ 78m(b)(2)(A) and 78m(b)(2)(B)].

FIFTH CLAIM

Gardner, Powanda, Lenz, Rassam, Reichner and O'Brien Aided and Abetted Violations of Exchange Act Section 13(a) and Rules 12b-20, 13a-1, and 13a-13 thereunder

[Reporting Violations]

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

155. Defendants Gardner, Powanda, Lenz, Rassam, Reichner and O'Brien knowingly and substantially participated in Peregrine's inclusion of financial statements that were not presented in conformity with GAAP in annual, quarterly, and other reports filed with the Commission.

156. By reason of the foregoing, defendants Gardner, Powanda, Lenz, Rassam, Reichner and O'Brien aided and abetted violations of Exchange Act Section 13(a) [15 U.S.C. § 78m(a)] and Exchange Act Rules 12b-20, 13a-1, and 13a-13 [17 C.F.R. §§ 240.12b-20[3], 240.13a-1[4], and 240.13a-13[5]].

SIXTH CLAIM

Gardner and Lenz Violated Exchange Act Rule 13b2-2

[Misleading the Auditors]

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

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[2] 2002 ed., p. 133, promulgated 2/23/79.
[3] 2002 ed., p. 112, promulgated 2/13/65.
[4] 2002 ed., p. 128, promulgated 7/24/97.
[5] 2002 ed., p. 132, promulgated 5/12/77, as amended 5/3/83, 7/9/85, 3/13/89, 3/27/92, and 6/14/96.

158. Defendants Gardner and Lenz made materially false statements to accountants in connection with their audits and quarterly reviews of Peregrine's financial statements.

159. By reason of the foregoing, defendants Gardner and Lenz violated Exchange Act Rule 13b2-2 [17 C.F.R. § 240.13b2-2[6]].

SEVENTH CLAIM

Stulac Aided and Abetted Violations of Exchange Act Section 13(a) and Exchange Act Rules 13a-1 and 13a-13

[Reporting Violations]

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

161. Defendant Stulac knowingly and substantially participated in Peregrine's inclusion of financial statements that were not presented in conformity with GAAP.

162. By reason of the foregoing, defendant Stulac aided and abetted violations of Exchange Act Section 13(a) [15 U.S.C. § 78m(a)] and Exchange Act Rules 13a-1 and 13a-13 [17 C.F.R. §§ 240.13a-1, and 240.13a-13].

EIGHTH CLAIM

Rodda and Whitt Aided and Abetted Violations of Exchange Act Section 10(b) and Exchange Act Rule 10b-5

[Financial Fraud]

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

164. Defendants Rodda and Whitt had actual knowledge that Peregrine's senior management knowingly or recklessly employed devices, schemes, or artifices to defraud, in connection with the purchase or sale of securities, with the intent of materially misstating Peregrine's publicly-reported financial results.

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[6] 2002 ed., p. 133, promulgated 2/23/79.

165. Defendants Rodda and Whitt had actual knowledge that Peregrine's senior management made misrepresentations and omissions of fact, in connection with the purchase or sale of securities, with the intent of materially misstating Peregrine's publicly-reported financial results.

166. Defendants Rodda and Whitt had actual knowledge that Peregrine's senior management engaged in acts, practices, or courses of business, in connection with the purchase or sale of securities, which operated or would have operated as a fraud or deceit upon analysts and the investing public.

167. Rodda and Whitt provided knowing and substantial assistance to Peregrine's senior management in connection with senior management's violations of Exchange Act Section 10(b) and Rule 10b-5 and were aware that their role was part of a fraudulent scheme by Peregrine executives to improperly recognize revenue from channel sales.

168. By reason of the foregoing, defendants Rodda and Whitt aided and abetted violations of Exchange Act Section 10(b) [15 U.S.C. § 78j(b)] and Exchange Act Rule 10b-5 [17 C.F.R. § 240.10b-5].

RELIEF REQUESTED

WHEREFORE, plaintiff Securities and Exchange Commission respectfully requests that this Court:

I.

Issue an order of permanent injunction restraining and enjoining defendants Gardner, Powanda, Lenz, Rassam, Reichner and O'Brien and their agents, servants, employees, attorneys, and assigns, and those persons in active concert or participation with them, and each of them, from violating Exchange Act Sections 10(b) and 13(b)(5) [15 U.S.C. §§ 78j(b) and 78m(b)(5)],

and Exchange Act Rules 10b-5 [17 C.F.R. § 240.10b-5], 13b2-1 [17 C.F.R. § 240.13b2-1], and from aiding and abetting violations of Exchange Act Sections 13(a), 13(b)(2)(A), and 13(b)(2)(B) [15 U.S.C. §§ 78m(a), 78m(b)(2)(A), and 78m(b)(2)(B)] and Exchange Act Rules 12b-20 [17 C.F.R. § 240.12b-20], 13a-1 [17 C.F.R. § 240.13a-1], and 13a-13 [17 C.F.R. § 240.13a-13].

II.

Issue an order of permanent injunction restraining and enjoining defendants Gardner, Powanda, Lenz, Rassam and O'Brien and their agents, servants, employees, attorneys, and assigns, and those persons in active concert or participation with them, and each of them, from violating Securities Act Section 17(a) [15 U.S.C. § 77q(a)].

III.

Issue an order of permanent injunction restraining and enjoining defendants Gardner and Lenz, and their agents, servants, employees, attorneys, and assigns, and those persons in active concert or participation with them, and each of them, from violating Exchange Act Rule 13b2-2 [17 C.F.R. § 240.13b2-2].

IV.

Issue an order of permanent injunction restraining and enjoining defendant Stulac, and his agents, servants, employees, attorneys and assigns, and those persons in active concert or participation with them, and each of them, from violating Exchange Act Sections 10(b) and Exchange Act Rules 10b-5 [17 C.F.R. § 240.10b-5], and from aiding and abetting violations of Sections 13(a), [15 U.S.C. §§ 78m(a)] and Exchange Act Rules 13a-1 [17 C.F.R. § 240.13a-1], and 13a-13 [17 C.F.R. § 240.13a-13].

V.

Issue an order of permanent injunction restraining and enjoining defendants Rodda and Whitt, and their agents, servants, employees, attorneys, and assigns, and those persons in active concert or participation with them, and each of them, from aiding and abetting violations of Exchange Act Sections 10(b) [15 U.S.C. § 78j(b)] and Exchange Act Rule 10b-5 [17 C.F.R. § 240.10b-5].

VI.

Order an accounting by defendants Gardner, Powanda, Lenz, Rassam, Reichner, O'Brien, Stulac and Whitt of all money, property, and other assets directly or indirectly derived from their unlawful activities at or concerning Peregrine.

VII.

Issue an order directing defendants Gardner, Powanda, Lenz, Rassam, Reichner, O'Brien, Stulac and Whitt to disgorge, with prejudgment interest, all ill-gotten gains resulting from their unlawful activities at or concerning Peregrine.

VIII.

Issue an order directing defendants Gardner and Lenz to pay civil monetary penalties under Section 21A of the Exchange Act [15 U.S.C. § 78u-1].

IX.

Issue an order directing defendants Gardner, Powanda, Lenz, Rassam, Reichner, O'Brien, Stulac, Rodda and Whitt to pay civil monetary penalties under Section 21(d)(3) of the Exchange Act [15 U.S.C. § 78u(d)(3)].

X.

Enter an order under Section 21(d)(2) of the Exchange Act [15 U.S.C. § 78u(d)(2)] prohibiting defendants Gardner, Powanda, Lenz, Rassam, Reichner and O'Brien 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 [15 U.S.C. § 78l] or that is required to file reports pursuant to Section 15(d) of the Exchange Act [15 U.S.C. § 78o(d)].

XI.

Grant such other and further relief as this Court may deem just and proper.

Dated: October 5, 2004

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