

IN THE UNITED STATES DISTRICT COURT  
FOR THE SOUTHERN DISTRICT OF NEW YORK

IN RE EVCI CAREER COLLEGES  
HOLDING CORP. SECURITIES  
LITIGATION

Master File No. 05 Civ. 10240 (CM)

JURY TRIAL DEMANDED

CONSOLIDATED AMENDED CLASS ACTION COMPLAINT

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Court-appointed Lead Plaintiff Arkansas Teacher Retirement System (“Arkansas Teachers”) brings this federal securities class action under sections 10(b) and 20(a) of the Securities Exchange Act of 1934 (the “Exchange Act”) on behalf of itself and all other persons and entities, other than Defendants and their affiliates as specified in ¶¶ 13-24 below, who purchased or acquired the publicly traded common stock of EVCI Career Colleges Holding Corp. (“EVCI” or the “Company”) during the period of August 14, 2003 through and including December 6, 2005 (the “Class Period”), and based upon the conduct asserted herein, were injured thereby.

### **I. NATURE OF THE ACTION**

1. Defendant EVCI is the publicly traded holding company for three “commercial” colleges: Interboro Institute (“Interboro” or the “Institute”), the Technical Career Institute (“TCI”), and the Pennsylvania School of Business (“PSB”). Throughout the Class Period, however, almost all of the Company's revenues were derived from Interboro. In its public filings, EVCI was quite explicit about its business model: the Company looks to recruit disadvantaged, inner city students to attend its schools, and makes approximately 94% of its money through the federal and state grants that those students receive. Thus, EVCI's success depends on its ability to get students in the door, and get them approved for federal and state grants.

2. Throughout the Class Period, the Company represented to investors that it was doing just that -- and doing it extremely well. Indeed, in every single quarterly filing with the Securities and Exchange Commission (the “SEC”) and in press releases, EVCI maintained that Interboro’s enrollments were increasing exponentially, and that the Company's revenues were growing accordingly. At the same time, however, the Company professed that it was not only concerned with getting students in the door: it was also supposedly focused on keeping them in

school. Thus, according to EVCI's public statements, the Company was making an enormous investment in its facilities and had developed successful "retention strategies" designed to assist students in graduating from Interboro. Because Interboro had taken these steps to purportedly "provide a quality and caring educational experience," graduation and retention rates were increasing throughout the Class Period. Put simply, EVCI repeatedly assured investors that it had built a business model that attracted and retained ever increasing numbers of qualified students (and ever increasing revenues) through a caring, proactive and legitimate program. Unfortunately, for those students -- and for the investors in EVCI -- that business model was a lie.

3. The lie began to unravel on October 19, 2005, when the Company announced that it had received a draft report of a compliance review conducted by the New York State Education Department ("NYSED"), during which the State had discovered irregularities in Interboro's admissions practices and would thus be denying extension center status for Interboro's Yonkers site. As set forth at ¶ 39 below, without approval as an "extension center," a campus is very limited in the number of students it can accept. According to the Company's press release, the NYSED would also require that Interboro increase the number and quality of its faculty, and improve its libraries, facilities and equipment resources. EVCI chose not to disclose the full contents of the State's draft report at this time, however, as doing so would have revealed that the NYSED had directed Interboro to immediately cease *all* expansion until it was in full compliance with the State regulations.

4. In immediate reaction to the disclosure of some -- but not all -- of this bad news, EVCI's stock plummeted over 50% from its previous day's closing price of \$5.53 to \$2.45.

5. Approximately six weeks later, on December 6, 2005, the Company filed a Form 8-K that attached a copy of NYSED's final report. The final report stated that NYSED had definitively determined to deny extension center status to Interboro's site in Yonkers. More significantly, the final report noted that the State would be requiring EVCI to submit within 30 days a “satisfactory plan to *reduce* enrollment at all locations so that resources [could] be better targeted to serve students with serious academic deficiencies to effectively meet the academic standards of a collegiate program.” (Emphasis added.) Finally, the final report expressed concern as to the “severity” of its findings concerning Interboro's practices; namely, that, among other things, (i) prospective students' answer sheets had been altered to produce passing grades at both the Yonkers and Flushing campuses; (ii) a prospective student had been encouraged to falsify income so as to be eligible for financial aid at the Yonkers campus; and (iii) there was a “total disregard for administering the ability-to-benefit examination with integrity” at the Flushing campus. In response to this additional disclosure, EVCI's stock price fell by roughly another third, from \$2.60 to \$1.80, on ten times normal trading volume. All told, the price of EVCI had declined by over 70% from its pre-October 19, 2005 price.

6. As set forth at ¶¶ 47-56 below, Lead Plaintiff's investigation has confirmed the State's findings -- and more. Thus, defendants' repeated statements during the Class Period regarding Interboro's soaring enrollment rates were misleading -- at best -- because those enrollments were generated through fraud, not the Company's “retention strategies.” What is more, the defendants were well aware during the Class Period that the Company was not in compliance with the state and federal regulations, and that the consequence of that non-compliance was a reduction in enrollments as the State ultimately prescribed. As a former Dean

of Interboro admitted to Lead Counsel during the course of their investigation, “the shareholders were given a bag of goods. Interboro was not as good as they were led to believe.”

7. While shareholders were given a “bag of goods,” the three principal officers at EVCI, Arol A. Buntzman, John J. McGrath, and Richard Goldenberg (together, the “Individual Defendants”), were helping themselves to a bag of gold as they paid themselves extraordinary annual salaries for a Company with limited capitalization. For instance, effective January 1, 2005, Buntzman's salary was \$630,000 plus bonus; McGrath's was \$490,000, plus bonus; and Goldenberg's was \$210,000. Further, these officers had a powerful incentive to increase revenues at EVCI. If EVCI's income increased 25% over the previous year, Buntzman was entitled to a bonus of \$790,000 with an option grant of 288,032, and McGrath a bonus of \$490,000 with options totaling 172,414. Finally, as set forth at ¶¶ 17, 20, 23, 44, 45, 46 below, Buntzman, McGrath and Goldenberg also took advantage of the Company's inflated stock price during the Class Period by disposing of the vast majority of their holdings in EVCI stock, garnering total proceeds of nearly \$7 million.

8. The NYSED report and the practices discovered in the course of Lead Plaintiff's investigation are a blistering indictment of how these defendants exploited economically disadvantaged students for personal gain. This lawsuit, of course, is brought on behalf of a different set of victims: the defrauded investors of EVCI.

## **II. JURISDICTION AND VENUE**

9. This Court has jurisdiction over the subject matter of this action pursuant to Section 27 of the Securities Exchange Act of 1934 (the “Exchange Act”), 15 U.S.C. § 78aa. The claims arise under Sections 10(b) and 20(a) of the Exchange Act, 15 U.S.C. §§ 78j(b) and 78t(a); and the rules and regulations promulgated thereunder, including SEC Rule 10b-5, 17 C.F.R. 240.10b-5. Venue is proper in this District pursuant to Section 27 of the Exchange Act, and 28

U.S.C. § 1391(b) and (c). At all times relevant to this complaint, EVCI's principal executive offices were located in this District, in Westchester County, at One Van Der Donck Street, Yonkers, New York. In addition, many of the acts and transactions giving rise to the violations of law complained of herein, including the preparation and dissemination to the public of materially false and misleading public filings, occurred in this District.

10. In connection with the wrongful acts and conduct alleged herein, the Defendants, directly and indirectly, used the means and instrumentalities of interstate commerce, including the United States mail and the facilities of a national securities market.

### **III. PARTIES**

#### **A. Lead Plaintiff**

11. Lead Plaintiff Arkansas Teacher Retirement System is a public pension fund organized in 1937 for the benefit of the current and retired public school teachers of the State of Arkansas. Arkansas' Teachers is located in Little Rock, Arkansas, and has total assets of approximately \$10.039 billion.

12. Arkansas Teachers purchased 320,480 shares of EVCI common stock during the Class Period as set forth in the Certification previously filed with the Court, and suffered damages as a result of the violations of the federal securities laws as alleged herein. By Order dated May 9, 2006, this Court appointed Arkansas Teachers Lead Plaintiff in this action in accordance with Section 21D(a)(3)(B) of the Exchange Act, 15 U.S.C. § 78u-4 and Section 27(a)(3) of the Securities Act, 15 U.S.C. § 77z-1.

#### **B. EVCI Career Colleges Holding Corp.**

13. EVCI Career Colleges Holding Corp. ("EVCI" or the "Company") is a Delaware corporation with its principal executive offices at One Van Der Donck Street, Yonkers, New York. EVCI changed its name from EVCI Career Colleges Incorporated during the Class

Period, on August 12, 2004. EVCI is a for-profit provider of on-campus career college education through its subsidiaries Interboro Institute, Inc. (“Interboro”), Technical Career Institutes, Inc. (“TCI”), and Pennsylvania School of Business (“PSB”). Interboro provides over 90% of EVCI’s revenues. In late 2003, *Investor’s Business Daily* (“IBD”) ranked EVCI ninth in its listing of “Who’s Who in Commercial Schools” as determined by the combined earnings-per-share (“EPS”) and IBD’s “Relative Strength” calculation.

14. During the Class Period, the Company’s common stock was traded on the NASDAQ under the symbol “EVCI” and the Company filed annual reports on Form 10-KSB and quarterly reports on Form 10-QSB and Form 10-Q with the SEC. As of December 6, 2005, there were 12,596,000 shares of EVCI common stock outstanding. EVCI operated on a fiscal year that ended on December 31.

**C. Individual Defendants**

15. **Arol I. Buntzman**. Defendant Arol I. Buntzman was a founder of EVCI and has been the Chairman of the Board since the Company’s inception in March of 1997 and the Chairman of the Board of Interboro since EVCI acquired it in 2000. In addition, Buntzman served as EVCI’s Chief Executive Officer (“CEO”) from March 1998 through December 2002, and Interboro’s CEO from January 2000 through December 2002. Buntzman has also been Chancellor of Interboro since January 1, 2003. Buntzman served as Chairman of TCI from September 2005 through March 2006, and continues to serve as a TCI director. He has also been on the Board of PSB since January 2005.

16. During the Class Period, Buntzman signed each of the Company’s Forms 10-KSB filed with the SEC. In direct communications with investors, Buntzman was also one of the Company’s principal spokespersons, and was frequently quoted in the press releases challenged herein.

17. Throughout the Class Period, Buntzman was one of the largest shareholders of the Company, owning or controlling, as of April 2005, almost 630,000 shares, or approximately 4.85% of EVCI's common stock issued and outstanding. On November 12, 2003, Buntzman sold 300,000 shares of his EVCI common stock for proceeds of \$1.2 million. Just five months later, on April 2, 2004, Buntzman sold 80% of his remaining EVCI common stock -- 310,000 shares -- at \$11.50 per share, reaping proceeds of \$3.56 million.

18. **John J. McGrath**. Defendant McGrath ("McGrath") was a founder of EVCI, and has been EVCI and Interboro's CEO since January 1, 2003. In addition, McGrath has been EVCI's President, and a member of the Board, since the Company's inception in March of 1997. McGrath has also been the Vice-Chairman of the Board of Interboro since January 2000.

19. McGrath signed each of the Company's Forms 10-KSB filed with the SEC during the Class Period, as well as the Form 10-Q for the third quarter of 2005. McGrath was also one of the Company's principal spokespersons, and was frequently quoted in the press releases challenged in this litigation.

20. Prior to his disposition of 310,000 shares in April 2004, Mr. McGrath was one of the Company's largest shareholders, holding or controlling approximately 5.8% of EVCI's common stock. On April 2, 2004, McGrath sold 81.5% of his EVCI common stock -- 150,000 shares -- at \$11.50 per share, reaping proceeds of \$1.72 million.

21. **Richard Goldenberg**. Defendant Goldenberg ("Goldenberg") served as Chief Financial Officer ("CFO") of EVCI from March 1997 until October 2005, and as Interboro's CFO during the entire Class Period. Goldenberg also recently served as Interim CFO of EVCI following the May 31, 2006 resignation of Joseph Looney. In addition, Mr. Goldenberg has been a director of EVCI since its inception, and a director of Interboro since January 2000.

22. Goldenberg signed each of the Company's Forms 10-KSB, 10-QSB, and 10-Q filed with the SEC during the Class Period, with the exception of the Form 10-Q for the third quarter of 2005.

23. During the Class Period, on April 2, 2004, Goldenberg sold 65% of his EVCI common stock – 40,000 shares – at \$11.50 per share for proceeds of \$460,000.00.

24. The Complaint collectively refers to Buntzman, McGrath, and Goldenberg as the “Individual Defendants.”

#### **IV. CLASS ACTION ALLEGATIONS**

25. Lead Plaintiff brings this action on its own behalf and as a class action pursuant to Rules 23(a) and 23(b)(3) of the Federal Rules of Civil Procedure on behalf of all persons or entities (the “Class”) who purchased securities of EVCI during the period of August 14, 2003 through and including December 6, 2005 (the “Class Period”), and who suffered damages thereby. Excluded from the Class are (i) the Defendants; (ii) members of the immediate family of each of the Individual Defendants; (iii) any entity in which any of the Defendants has a controlling interest; (iv) any parent, subsidiary, or affiliate of EVCI; (v) any person who was an officer or director of EVCI or any of its subsidiaries or affiliates during the Class Period; and (vi) the legal representatives, agents, heirs, predecessors, successors, or assigns of any of the excluded persons or entities specified in this paragraph.

26. The members of the Class are so numerous that joinder of all members is impracticable. EVCI common stock was actively traded on the NASDAQ, an efficient market, throughout the Class Period. While the exact number of Class members can only be determined by appropriate discovery, Lead Plaintiff believes that Class members number in the thousands. As of December 6, 2005, there were approximately 12,596,000 shares of EVCI common stock outstanding. Based upon the volume of trading of EVCI common stock during the Class Period,

it is believed that hundreds, if not thousands, of investors purchased EVCI common stock on the open market during the Class Period, rendering joinder of all such purchasers impracticable.

27. Common questions of law and fact exist as to all members of the Class and predominate over any individual questions affecting members of the Class and predominate over any questions solely affecting individual Class Members. Among the questions of law and fact Common to the Class are:

- (a) whether Defendants' acts as alleged herein violated the federal securities laws;
- (b) whether documents, including Registration Statements, press releases and public statements made by Defendants during the Class Period contained misstatements of material fact or omitted to state material facts necessary to make the statements made, in light of the circumstances under which they were made, not misleading;
- (c) whether Defendants acted with the requisite state of mind in omitting and/or misrepresenting material facts in the documents filed with the SEC, press releases and public statements;
- (d) whether the Individual Defendants are liable as control persons under the federal securities laws;
- (e) whether the market price of EVCI common stock during the Class Period was artificially inflated due to the material misrepresentations complained of herein; and
- (f) whether the members of the Class have sustained damages and, if so, what is the proper measure of damages.

28. Lead Plaintiff's claims are typical of the claims of other members of the Class. Lead Plaintiff and all Class members sustained damages arising out of Defendants' wrongful conduct in violation of Sections 10(b) and 20(a) of the Exchange Act.

29. Lead Plaintiff will fairly and adequately protect the interest of the members of the Class and has retained counsel competent and experienced in class actions and securities litigation. Lead Plaintiff has no interest antagonistic to or in conflict with the Class.

30. A class action is superior to other available methods for the fair and efficient adjudication of the controversy, since joinder of all members of the Class is impracticable. Furthermore, because the damages suffered by the individual Class members may be relatively small, the expense and burden of individual litigation make it virtually impossible for the Class members individually to redress the Defendants' wrongful conduct. There will be no difficulty in the management of this action as a class action.

31. The names and addresses of the record owners of EVCI's common stock purchased during the Class Period are obtainable from information in the possession of the Company's transfer agent(s). Notice can be provided to the record owners of EVCI stock via first class mail using techniques and a form of notice similar to those customarily used in securities class actions.

## **V. SUBSTANTIVE ALLEGATIONS**

### **A. EVCI's Business Model**

32. As set forth at ¶ 1 above, EVCI is the publicly-traded holding company for three so-called "commercial colleges": Interboro Institute; Technical Career Institutes, Inc.; and the Pennsylvania School of Business. Interboro, a two-year college that provides an Associates Degree upon graduation, is by far EVCI's most substantial asset, accounting for over 90% of its revenues. During certain quarters during the Class Period, Interboro accounted for *all* of EVCI's

revenues. Its main campus is in mid-town Manhattan and it has extension center campuses in Flushing, New York and in the Washington Heights section of Manhattan. It also has a site in Yonkers, New York, for which it was seeking extension center status during the Class Period.

33. Nearly all -- approximately 95% -- of Interboro's revenues are derived from federal Pell grants and New York State Tuition Assistant Program ("TAP") grants. Accordingly, Interboro's business model is to aggressively recruit economically disadvantaged students who will receive these grants and then pay that money over to Interboro. Most New Yorkers are well-familiar with Interboro's powerful advertising crusade in the New York City subways. A typical advertisement showed a young mother holding an infant. It read: "My baby will hold onto someone who can support her. Me." Interboro does not permit its students to borrow federal subsidized or unsubsidized loans to pay for school because, according to the Company, "that would subject it to liability or scrutiny as a result of defaults by its students."

34. More than 90% of Interboro's students do not have a high school diploma -- or even a GED degree. Without such a degree, a prospective student must pass what is known as an "ability to benefit" ("ATB") test to gain admission into Interboro and qualify for a Pell and/or a TAP grant. The "ATB" test is designed as a means to gauge a prospective student's intelligence and ability to perform college work. The ABT testing process is highly regulated and only certain tests approved by the United States Department of Education may be used for admission and/or financial aid. The approved test administered by Interboro during the Class Period was known as the "Career Programs Assessment Test" (or "CPAt"). All schools providing ATB testing must, pursuant to the Federal Regulations, certify that the tests are being administered by a professionally-trained, independent test administrator so that the test results will not be compromised.

**B. NYSED's Board of Regents Accreditation**

35. When EVCI first acquired Interboro in 2000, the NYSED's Board of Regents put the college's accreditation on probationary status. Accreditation is required for an institution's students to be eligible for Title IV student aid programs, such as Pell grants. Because, as set forth above, EVCI's revenues depended heavily -- if not almost entirely -- on Interboro students receiving these grants, Interboro's accreditation was vital to EVCI.

36. Shortly before the Class Period, on June 9, 2003, the State granted Interboro accreditation subject to the following conditions:

- That Interboro provide the NYSED with a plan to assure that its graduation rate would increase to at least 25%;
- That Interboro provide the NYSED with a plan to increase job placement in or related to a student's field of study to meet a goal of 65% by spring of 2006; and
- That Interboro fully document its faculty's training, experience, and performance.

(NYSED Board of Regents Memorandum, "Interboro Institute: Confirmation of Compliance with the Standards for Accreditation in Part 4 of the Rules of the Board of Regents and Renewal of Institutional Accreditation with Conditions," June 9, 2003.)

37. At this time, Interboro's graduation rate was under 20%. Thus, to increase its graduation rate to the requisite 25%, Interboro would have to retain a higher percentage of its students, which meant, *inter alia*, that Interboro would have to accept students legitimately capable of finishing its program.

38. Apart from the conditions specific to Interboro, Interboro also had to comply with the standard minimum level of quality required by the State to obtain and maintain institutional accreditation, including, but not limited to:

- Having a plan in place to assess student achievement such as graduation rates, state licensing examination results, and job placement rates and providing this information to the NYSED when making applications to the NYSED for accreditation or renewal of accreditation;
- Ensuring the integrity of the educational credits it provides;
- Maintaining a competent faculty with appropriate credentials (“the faculty should be sufficient in number to assure breadth and depth of instruction and the proper discharge of all other faculty responsibilities”);
- Providing adequate resources sufficient to support its students, which includes facilities, equipment, supplies, and libraries administered by “professionally trained staff supported by sufficient personnel”; the libraries must “possess and maintain collections and technology sufficient in depth and breadth to support the mission of the institution and each curriculum”;
- Having adequate administration, which includes maintaining clearly established institutional policies and programs, having learning objectives and methods of assessing student achievement, and, among other things, providing academic advice to students;
- Providing adequate support services that take into account the school’s mission and “the needs of its students”;
- Determining admissions through “an orderly process using published criteria that shall be uniformly applied” and that must “take into account the capacity of the student to undertake a course of study and the capacity of the institution to provide the instructional and other support the student needs to complete the program”; and
- Providing accurate consumer information on available financial assistance, the cost of attending, refunds, and the instructional programs offered; furthermore, the institution’s advertising “shall not be false, misleading, deceptive, or fraudulent.”

(New York State Board of Regents and the Commission Education, Handbook of Institutional Accreditation, March 2005 Ed.)

39. For approval of an institution as an “extension center,” the NYSED also requires that more than fifteen credit-bearing courses be offered. In order to meet the NYSED minimum educational standards, an institution must offer more courses when its existing course load is

filled to capacity. Unless and until a site is approved as an “extension center, it is very limited in the number of students it can accept. This is relevant because, as discussed, *infra* at ¶¶ 63, 93, on September 24, 2004, Interboro asked that the NYSED grant its Yonkers location extension-center status in order to support the enrollment of additional students at that site.

**C. EVCI Reports Exploding Enrollment Figures and Increasing Revenues Due To Its “Successful Retention Strategies”**

40. Beginning on August 14, 2003, and throughout the Class Period, EVCI reported to the investing public that Interboro’s enrollments were continuously increasing at phenomenal rates and that the Company's revenues were soaring as a result, as follows:

- August 14, 2003: summer enrollments up 15% over the summer of 2002 and revenues up 37% in the first six months of 2003 as compared to the same period in 2002 (Press Release and Form 10-QSB);
- October 22, 2003: enrollments for the fall semester up more than 30% over the fall of 2002, and increasing much faster than EVCI's peer group average of growth between 15-20% (Press Release);
- November 14, 2003: due to the enormous increase in enrollments announced on October 22, revenues for the third quarter of 2003 up 40% over the same period in 2002 (Press Release and Form 10-QSB);
- February 23, 2004: enrollments for 2003 up 28% over 2002, and 2003 revenues 31% higher than 2002 (Press Release and Form 10-KSB);
- February 24, 2004: spring semester 2004 enrollments up 56% over the 2003 spring semester (Press Release and Form 10-KSB);
- May 11, 2004: due to 56% increase in enrollments, EVCI's revenues for the first quarter of 2004 up 41% over the same period in 2003 (Press Release and Form 10-QSB);
- May 27, 2004: summer 2004 enrollments up an astounding 85% over the summer semester of 2003 (Press Release);
- August 12, 2004: based on dramatic increase in summer semester enrollments, second quarter 2004 revenues up 49% over the second quarter of 2003 (Press Release and Form 10-QSB);

- September 30, 2004: enrollments for the fall semester up 70% over the summer semester and revenues for the third quarter of 2003 up 45% over the third quarter of 2002 (Form 10-QSB);
- October 20, 2004: enrollments for the fall 2004 semester up 70% over the fall 2003 semester (Press Release);
- November 15, 2004: enrollments up 70% for the 2004 fall semester and revenues for the third quarter of 2004 up 45% over the same period in 2003 (Press Release and 10-QSB);
- February 22, 2005: spring semester 2005 enrollments up 32% over the previous year (Press Release);
- March 23, 2005: 2004 enrollment up 65% over 2003 and revenues up 63% over 2003 (Press Release and Form 10-KSB);
- May 12, 2005: as a result of the 32% increase in enrollments for the 2005 spring semester, revenues for the first quarter of 2005 up 21% over the same period in 2004 (Form 10-Q);
- June 14, 2005: summer semester enrollments up 35% over the 2004 summer semester (Press Release);
- August 12, 2005: due to the 35% increase in enrollments for the 2005 summer semester, revenues for the second quarter of 2005 up 66% over the second quarter of 2004 (Form 10-Q); and
- November 22, 2005: enrollments for the fall semester of 2005 up 94.9% over the same period in 2004, and revenues up 55% for the third quarter of 2005 over the same period in 2004 (Form 10-Q).

41. In their public statements, defendants attributed these extraordinary results to their “carefully developed strategies...designed to meet the unique needs of economically disadvantaged students” and to Interboro's “greater retention of existing students.” Thus, defendants said, because Interboro had taken steps to “provide a quality and caring educational experience,” graduation and retention rates were also increasing throughout the Class Period. For instance, in the Company's November 14, 2003 press release, McGrath reported a decline in the drop-out rate at Interboro during the first few weeks of the fall 2003 semester from 8% to just

3%, and in EVCI's 2004 Form 10-KSB, the Company stated that “[i]mproved retention and graduation rates continue to be a top priority at Interboro,” and that “[i]t considers student retention the responsibility of the entire college personnel.”

42. Analysts following the Company were dazzled by EVCI's dramatic performance during the Class Period. For instance, CJS Securities rated EVCI stock as “outperform” in light of the fact that the Company's “organic growth” in enrollments was “2x-4x faster than larger public peers.” Roth Capital Partners similarly rated EVCI a “Buy” and praised the Company for its initiatives designed to increase student retention and graduation rates. Based on defendants' representations, Barrington Research reported that “[s]tudent retention has been an important part of the success of Interboro” and that “EVCI takes student retention very seriously...” Finally, analysts uniformly believed that the Company's acquisition of Technical Career Institutes in September 2005 would further bolster EVCI's revenues because, as explained in Roth Capital Partners' September 22, 2005 report, the Company would likely utilize the same “guerilla marketing' focused on target communities to attract new students” that had been so successful in attracting new students to Interboro.

**D. The Individual Defendants Cash In On the Reported Success of the Company**

43. Individual Defendants Buntzman, McGrath and Goldenberg quickly took advantage of the increased valuation of EVCI stock as a result of the Company's great success during the Class Period, selling the vast majority of their shares in EVCI and reaping total proceeds of nearly \$7 million.

44. For instance, on November 12, 2003, EVCI issued a press release reporting that Buntzman had sold a block of 300,000 shares of EVCI stock, garnering him profits of \$1.2 million. As explained by the Company, Buntzman was not selling the stock because of any concerns he harbored with respect to the viability of the Company, but rather “to raise money in

anticipation of the equitable distribution of marital assets in a pending divorce.” That was apparently news to Buntzman's wife, however, as a recent opinion rendered in the Buntzmans' divorce reveals that Buntzman's November 12, 2003 sale of Company stock was made “without [his wife's] consent and in violation of the interim order limiting the transfer of the parties assets.” *Mahoney-Buntzman v. Buntzman*, 11 Misc.3d 869, 813 N.Y.S.2d 874, 876 n. 1 (Sup. Ct. Westchester Co. Feb. 8, 2006).

45. Later, on April 2, 2004, Buntzman, McGrath, and Goldenberg dumped the vast majority of their holdings in EVCI common stock at \$11.50 per share for proceeds of over \$5 million. On that day, Buntzman sold 80% of his stock, 310,000 shares, for \$3.56 million; McGrath 81.5% of his stock, 150,000 shares, for \$1.72 million; and Goldenberg 65% of his stock, 40,000 shares, for \$460,000. Again, defendants had a ready explanation for the sales, as McGrath stated in a press release that:

Institutional demand was extremely high, but EVCI is not willing to incur additional dilution to its existing shareholders at this time. We made the decision, with regard to each of our personal situations, to meet this demand with a portion of our personal holdings.

46. As set forth at paragraphs ¶¶ 59-60 below, beyond being suspicious in amount, the Individual Defendants' April 2, 2004, sales were also suspicious in timing as they occurred just days after the Company received from the NYSED a letter stating that the State expected that its imposition of an additional screening mechanism in connection with Interboro's admissions process would “result in the acceptance of a lower percentage of students than is [Interboro’s] current practice,” and that NYSED “expect[s] this reduction in admitted students to continue until [Interboro’s] graduation rate reaches 25 percent and remains at that percentage or higher for two years.”

**E. Interboro's Extraordinary Increase in Enrollments Was Not the Result of the Company's "Retention Strategies," But Rather Fraudulent Admissions Practices**

47. Lead Counsel's investigation has revealed that the dramatic increase in Interboro's student enrollment -- and consequently, EVCI's revenues -- resulted not from Interboro's retention strategies and the great "care" it provided to its disadvantaged students, but instead from fraudulent and coercive admissions processes. These practices put EVCI at serious risk of sanctions with the NYSED -- most notably enrollment reductions as made clear by NYSED in its communications with the Company during the Class Period.

48. As explained by a former Dean at Interboro during the Class Period, referred to herein as Confidential Witness # 1 ("CW # 1"), when McGrath became CEO of EVCI and Interboro in 2003, the Company's drive to escalate Interboro's enrollment became extremely aggressive. CW # 1 said that the orders from McGrath were to increase admissions by at least 20% every semester. Thus, for example, the spring semester should have 20% more students admitted to Interboro than the fall semester had. Two former Admissions Officers interviewed during Lead Counsel's investigation, Confidential Witnesses #2 and #3 ("CW#2" and "CW#3"), similarly reported that McGrath imposed a required admissions quota of 120 new students a semester or face dismissal. In fact, CW#2 was terminated when CW#2 was not able to meet the quota.

49. The senior officers of the Company -- including McGrath, Goldenberg, Interboro's Admissions Director, the Controller, and CW#1 -- would meet every Monday morning to discuss the number of potential students who had taken the CPA test and the number who had passed. According to CW#1, these Interboro officials were "very aggressive in doing whatever they needed to do to make the numbers."

50. CW#1 reported that, among other tactics, McGrath dramatically increased the frequency of admissions testing at Interboro's campuses. Whereas Interboro had previously administered the CPA test a few times a week under controlled conditions, pursuant to McGrath's orders, "[t]hey wanted us to conduct tests five to seven times per day, and they wanted the results back as soon as possible . . . they wanted the scores back yesterday."

51. An Interboro Testing Associate, who will be referred to herein as Confidential Witness # 4 ("CW#4), confirmed that the admissions testing staff was expected to conduct an unduly high volume of tests: "They pressured us to do a lot of testing."

52. Because of the pressure to conduct CPA testing at this frenetic pace, admissions officials often and openly used students to grade the tests -- in blatant derogation of the regulatory provisions described above. Another Confidential Informant ("CW#5") who worked in testing at Interboro knew that it was improper for students to monitor and grade the tests, but said that "students checking other students' CPA exams was part of the daily routine." This led, CW#5 explained, to a total corruption of the testing process because student workers would routinely change answers on completed exams. CW#5 said that full-time employees of Interboro also openly changed grades: "They wouldn't make it too extreme . . . they changed just enough answers to get them in there [Interboro]." CW#5 also saw proctors leaving examination rooms during the tests -- again in violation of the strict testing protocol that was supposed to be in place. CW#5 said that the test administrators were "well aware" of the fraudulent activity surrounding the ATB examination process. According to CW#5, "[t]hey would walk in and see it . . . they didn't care; they just wanted their money."

53. CW#5 reported that representatives of the Admissions Office actively directed the cheating with respect to the ABT testing because of the tremendous institutional pressure placed

on them to produce higher enrollments at Interboro. According to CW#5, Interboro Admissions Officers would, for example, pay examination graders bribes of \$50 to pass three or five students on the test when they otherwise would have failed, or give them Interboro merchandise such as T-shirts. As CW#5 explained, altering the ABT test scores was not difficult because the test answer key was actually attached to the examination form, so one only had to tear the perforation, remove the answer key, and place the answers side-by-side to see what the correct answers were.

54. According to the former Interboro Dean, CW#1, people were aware that the Director of Admissions at Interboro at this time employed “very unscrupulous” practices to meet McGrath's demands. Like CW#5, CW#1 also saw instances of CPAt test scores being changed, and further reported instances of seeing copies of the CPAt test on Admissions Officers' desks - thus making it possible for them to prepare applicants for the CPAt test with the actual test in hand.

55. CW#1 said that McGrath and the Admissions Officers seemed far more intent on recruiting students than retaining them. The reason was clear: “If a student showed up just one day before week four of the semester, then the student was locked in and the state was on the hook for paying the student’s tuition.”

56. CW#5 also said that Interboro misled CW#5 when CW#5 first spoke to an Interboro Admissions Officer about enrolling. The Admissions Officer assured CW#5 that CW#5 could complete the program at Interboro in 16 months and that Interboro would help CW#5 obtain full-time employment after CW#5 graduated -- neither of which happened.

**F. The New York State Education Department's Investigation Reveals Interboro's Fraudulent Admissions Practices and Inability to Retain and Support Students**

57. As set forth at ¶¶ 34-39 above, for-profit colleges such as those owned by EVCI, are subject to strict regulation by the state and federal governments, both in terms of obtaining accreditation and receiving grants. Indeed, EVCI admitted as such in all of its public filings. For instance, in its 2004 Form 10-KSB, EVCI stated that:

Interboro is subject to extensive regulation by government agencies that administer Title IV and TAP and by the NYSED. As a result, Interboro must comply with a complex framework of laws and regulations and is subjected to frequent compliance and financial reviews and detailed oversight.

As set forth in that Form 10-KSB, Interboro could lose its eligibility to participate in the Pell grant program if: (i) it was found to have paid “any commission, bonus, or other incentive payment, based directly or indirectly on success in securing new student enrollments or financial aid, to any person or entity engaged in any domestic student recruitment, admission or financial aid awarding activity”; and (ii) it could not demonstrate that it has “capable and sufficient personnel to administer its Title IV program and advise students about financial aid, satisfactorily measure its students' academic progress, and timely submit all reports and financial statements as required” by the United States Department of Education (the “DOE”). Similarly, Interboro could be removed from the TAP program if, for instance, it “certified ineligible students to receive TAP grants.” According to EVCI, loss of either of these sources due to misconduct would have a materially adverse effect on the Company because more than 90% of its revenues were derived from those two grant pools. However, this would not happen, because as set forth in EVCI's 2004 Form 10-KSB, “Interboro has policies and procedures that are designed to assure its compliance with Title IV regulations.”

58. Documents obtained by Lead Plaintiff through the New York State Freedom of Information Law (“FOIL”) reveal that in mid-2003, Interboro applied to the NYSED for

extension center status for its location in Washington Heights. As set forth at ¶ 3 above, EVCI's ability to increase capacity and thereby accept more students was seen as an important driver for Company revenues. Interboro's request touched off months of negotiations with the State during which the State insisted that in order to obtain approval of the Washington Heights Extension Center, Interboro would have to achieve a graduation rate of 25% or higher by 2006 at the latest.

59. In a letter dated March 18, 2004, Interboro's President, Stephen H. Adolphus, wrote NYSED Coordinator Barbara Meinert, offering her Interboro's proposal to resolve the school's differences with the State. Mr. Adolphus expressed confidence that Interboro would be able to achieve "true three-year graduation rates... in the next academic year, and 25% either one or two years later," and proposed that in addition to requiring a second interview with prospective students, a further screening mechanism would be implemented through which the admissions officers would use a scripted series of "searching questions." In addition, it would be "made clear to [the] Admissions Department that this will result in our accepting a lower percentage of students than our current practice" which, he said, had "significant budgeting, planning, scheduling and revenue implications for the college..." Although, he said, the proposed compromise would "result in our turning away students we otherwise would have admitted," Interboro would implement the additional screening mechanism in exchange for "quick approval" of the Washington Heights Extension Center.

60. In a letter dated March 23, 2004, the State accepted Interboro's proposal as follows:

*We accept the Institute's plan for enhancing its strategies and monitoring system to address the Department's concern, including the addition of a further screening mechanism to the second interview with prospective students. We understand that the additional screening mechanism will result in the acceptance of a lower percentage of students than is the Institute's current practice. We expect this*

*reduction in admitted students to continue until the Institute's graduation rate reaches 25 percent and remains at that percentage or higher for two years.*

Letter dated March 23, 2004, from Barbara Meinert to Stephen H. Adolphus. (Emphasis added.)

61. Despite this agreement with the State to reduce the number of admitted students -- which Interboro acknowledged would have “significant” revenue implications -- as set forth at ¶ 59 above, EVCI continued to tout Interboro’s continuing growth to the investing public. For example, in the Company's May 11, 2004 press release, Defendant McGrath stated: “EVCI believes that Interboro will continue to realize substantial organic growth for the foreseeable future, including increases in year-over-year enrollment that is, on a percentage basis, much greater than the post-secondary education industry average.”

62. Moreover, within days of entering into this agreement with the State to reduce the number of admitted students, Individual Defendants Buntzman, McGrath, and Goldenberg each dumped the majority of their EVCI common stock for proceeds of over \$5 million.

63. Later that year, in September 2004, Interboro applied to the NYSED for approval of extension-center status of its Yonkers site. In its 2004 Form 10-KSB, the Company said that while it believed that its application should be granted, if it was not, there could be “significant limitations” on the amount of enrollments at the site. As part of assessing Interboro's request, the NYSED began an intensive review of Interboro's practices and facilities.

64. In a letter dated December 6, 2004, the Assistant Commissioner of Education notified Interboro's President, Stephen Adolphus, that the data submitted by Interboro to the Department for 2003-2004 made clear that the Company had been operating the Yonkers site as an extension center long before its application was even submitted. The letter further informed Interboro that the State would be paying a “comprehensive visit” to determine if Interboro had the capacity to expand and, if not, its Yonkers site would not be approved as an extension center.

65. An extensive peer review of Interboro followed in early to mid-2005, and in a letter dated June 15, 2005, the NYSED told the Institute that because its examination had identified numerous deficiencies, it was denying its Yonkers location extension-center status:

I must advise the institution that, given the current deficiencies, the State Education Department will not approve Yonkers as an extension center. In the judgment of the Department, the Institute is overextended in its ability to effectively serve the students it enrolls. However, the Department will be open to entering into conversations with the Institute with respect to agreeing upon an appropriate number of students that the Institute can serve given the educational needs of the students and the state of the facilities and services currently available.

EVCI did not disclose the denial of extension center status for Yonkers. To the contrary: in its Form 10-Q for the second quarter of 2005, the Company represented that the NYSED “may” withhold approval of its Yonkers site as an extension center, and that “[i]f the New York State Education Department does not give Interboro the requisite approval to open new college sites or to receive extension center status for its Yonkers site, Interboro's operations and growth could be materially and adversely affected.”

66. On October 7, 2005, the Company received the draft report of the NYSED investigation, which detailed the same fraudulent practices at Interboro about which Lead Plaintiff has learned in the course of its investigation.

67. The draft report was comprised of two parts: a “peer review” and an “admissions requirements review.” The peer review was designed to assess Interboro’s compliance with the laws, rules, and regulations governing New York State’s degree-granting programs, and the admissions requirements review examined Interboro’s procedures for admitting students based on unannounced inspection visits by NYSED staff.

68. A stern cover letter accompanied the draft report. It stated that “the Department has serious concerns based on the findings of the peer reviews and on the unannounced inspections. These concerns included: (i) “insufficient admission processes and student support

services to assure satisfactory institutional rates of student persistence and levels of academic attainment”; (ii) “too porous or incomplete quality assurance at the instructional level”; (iii) “insufficiency of faculty engagement in academic governance and the proper discharge of other program responsibilities”; and (iv) “inadequate library resources and facilities.”

69. The draft report, summarized below, confirmed that EVCI was engaged in fraudulent activities in order to get students admitted and have them qualify for financial aid; and that Interboro was not providing adequate resources and support for the number of increasing students it was accepting. In addition, the draft report noted that NYSED's review of EVCI's internal documents and data had revealed that "while the enrollment at Interboro and at its extension centers and sites has increased dramatically over the last few years," *"graduation and persistence rates have not increased and in some cases have decreased."* (Emphasis added).

#### **1. The Peer Review**

70. The draft report's peer review -- whose purpose was “to assess the scope and sufficiency of resources and services at each location and confirm information provided by [Interboro]” -- contained startling revelations. The NYSED team members conducted the review by visiting each of Interboro’s locations, where they interviewed staff, faculty, and students; observed classes; and reviewed student, faculty, and other administrative records. Team members examined course materials from more than 90 course sections of 31 different courses. The team also reviewed data regarding 7,000 Interboro students to confirm graduation rate figures and to examine data related to persistence and performance.

71. First, with respect to Interboro’s admissions, the Draft Report stated that Interboro had increased admissions nearly three fold between 2001 and 2004, while the industry average increase was only 26.4%. Moreover, in contrast to Interboro's representations that it was

focusing more on admitting committed and capable students through its admissions process, “the high attrition and poor performance of many students . . . suggests that admissions staff have too limited training or experience in effectively assessing applicant likelihood of persistence in study.” In a random sample of 100 students whose files were reviewed, 35 had dropped out before completing their first term.

72. Moreover, the State's investigation further revealed that most Interboro students who pursued substantial continuous study took at least twenty months to earn a degree, and only two in the sample finished the program in 16 months, which is what Interboro conveyed to students as the “time to degree.” The draft report stated that “it would be a misrepresentation to convey an expectation of a 16-month program to potential students.” As set forth above at ¶ 56, that is exactly what Interboro's admissions officers represented to applicants.

73. The State's review also found that many poorly performing students unlikely to complete Interboro's program were classified by Interboro as making satisfactory progress. The Review noted that making “satisfactory progress” under Interboro's definition only required that students completed three credits by the end of their first semester and have a GPA of 0.5; have completed nine credits and have a .75 GPA by the end of their second semester; and have completed 19 credits and have a 1.3 GPA by the end of their third semester.

74. Second, the State found that Interboro had failed to keep adequate records of its faculty. In fact, the students interviewed during the investigation did not recall ever being asked to evaluate faculty members. The State also found that teaching overloads were common during the period they studied. While the normal load for a teacher is 18 credits, or six sections, NYSED found that 31 of the 64 faculty teaching in the summer of 2005 had teaching loads in excess of the normal course load. Eleven faculty members taught nine to 12 separate sections

each. One person was teaching nine different course titles. The investigation further revealed that certain of Interboro's mathematics instructors appeared to have insufficient academic backgrounds for college-level instruction. The findings concluded that: “[F]or a few full-time faculty, there is an inappropriate match of expertise with assignments and, for quite a few others, there are very high teaching loads. A likely outcome is limited time for course preparation, assessment of higher-level skills and engagement with students. Overextension of faculty in teaching assignments and load may contribute significantly to the poor retention and performance of Interboro’s students.”

75. Third, the investigation found that all of Interboro’s libraries had substantial problems, and that Interboro had failed to increase its libraries’ physical space to accommodate the substantial increases in student enrollment. For instance, at Interboro’s main campus in Manhattan, the library was so crowded that instruction was going on where other students were trying to study and perform research. In addition, both the Washington Heights and Flushing libraries shared a space with Interboro’s Academic Resource Center, which detracted from the library as a place to study. The Washington Heights library had water leaking onto and damaging its books. Moreover, none of the libraries had adequate computer and Internet workstations, which were essential since the majority of Interboro students do not have computer access at home. The Review further noted that Interboro’s catalog claim that “the libraries hold over 3,000 periodical titles in both print and electronic formats,” was misleading because only 70 titles were available in print, which was wholly insufficient across four locations.

76. The draft report also stated that while Interboro had “attained profitability through rapid enrollment growth,” the reported enrollment expansion included growth at the Yonkers Extension Site, which was now “significantly greater than [was] permitted under the

Commissioner's Regulations." The Report made clear said that Interboro had been notified that it would have to cap enrollment at Yonkers at 300 students, and that the NYSED would not approve the Yonkers Extension Site, or any additional locations, "until Interboro details plans, satisfactory to the Commissioner, and shows evidence of implementing them for investments in staffing and other resources and concomitant changes in practices related to strengthened student persistence and high quality attainment, in the comprehensive institutional effectiveness plan, due February 1, 2006."

## **2. The Admission Requirements Review**

77. The State's "Admissions Requirement Review" involved undercover operatives going to Interboro posing as students in order to investigate Interboro's admissions practices. The NYSED stated that it conducted this review because enrollment at Interboro and its extension centers had increased dramatically over the prior couple years, while graduation and persistence rates had not increased, and in some cases had actually decreased. The State's admissions review was consistent with what Lead Counsel learned during their investigation: that EVCI required Interboro admissions staff to meet very demanding admission quotas or potentially face termination. In light of this practice, NYSED was examining whether Interboro was admitting qualified students.

78. The State's findings were unsettling to say the least. For instance, an Interboro financial advisor asked a NYSED undercover agent how much he made. When the operative told the advisor he made \$10,000 - \$12,000 per year off the books, the financial advisor directed the operative to obtain a notarized statement representing that he made \$4,500, so that the operative would qualify for financial aid.

79. Another operative took the CPA entrance examination on July 24 and 27, 2005, and purposely failed the test on both occasions. The first time, the Interboro representative told

the operative he had failed, but could redeem himself. The second time, the representative told the operative he had passed. The NYSED secured a copy of the operative's July 27 answer sheet and learned that four answers had been changed so that the agent passed the test when, in fact, he had failed.

80. Another student operative sat for the CPA test at Interboro's Flushing location on July 21, 2005. The operative reported that her test book was marked to indicate the correct answers. For example, some questions had the wrong answers crossed out so only the correct answer remained and the reading portion of the examination had underlines according to the questions that followed. While the operative sat for the exam, the proctor left the room several times, often for more than ten minutes at a time. This operative also purposely failed her examination, but Interboro provided her with instruction on "tricks about eliminating the wrong answer choice." The operative took the CPAT examination again on August 8, 2005, and again received a marked test booklet. The operative purposely failed the examination again, but an Interboro representative told her she passed. The NYSED secured a copy of the operative's July 21 answer sheet and learned that three answers had been changed. Later, the operative received a call from Interboro, saying that she had to retake the examination because Interboro had given her the wrong version. When the operative returned to Flushing on August 31, 2005, to retake the CPA test, she again received a marked up answer book. Again, she purposely failed, but when she went upstairs after the examination to get the results, Interboro informed her that she had passed.

81. At the conclusion of the draft report, the NYSED insisted that Interboro cease further expansion until the NSYED could confirm that the Institute was in compliance with the

State's regulations requiring qualified and trained and experienced faculty; and denied extension center status to Interboro's Yonkers site.

**G. EVCI Discloses Portions of The October 19, 2005 Draft Report**

82. On October 19, 2005, EVCI surprised the market when it announced its receipt of the draft report. According to the press release issued that day, "the draft report includes proposed findings, recommendations and determinations related to increasing admissions and improving academic standards and taking other measures to improve persistence and graduation rates." The release also reported that one of the proposed determinations was to deny extension center status for Yonkers, and that as a result, Interboro "may not be able to enroll new students at its Yonkers site unless and until the Department decides to grant this site extension center status." In addition, the release stated that draft report includes "assertions of irregularities in Interboro's admission practices," and that the Audit Committee of EVCI's Board of Directors had engaged supposedly "independent" experts to conduct an investigation of the admission practices at Interboro.

83. In response to the draft report, Defendant McGrath stated that Interboro was likely to accept many of the NYSED's changes because they would "strengthen Interboro and, accordingly, will be in the best interest of Interboro's students." He noted that while "some of the changes will slow Interboro's rate of enrollment growth and have an adverse impact on its margins, ... it will take time before we can properly assess the magnitude of the effect of these changes."

84. In immediate reaction to EVCI's announcement, EVCI's stock plummeted more than 50% from its previous day's closing price of \$5.53 to \$2.45, trading at a dramatically higher volume of 3.65 million shares as compared to the previous day's volume of approximately 29,000 shares.

85. Analysts' reaction to the news was instant as well. For example, on October 20, 2005, CJS Securities downgraded EVCI from "Market Outperform" to "Market Perform," citing the "surprise announcement" by EVCI that it had been undergoing a compliance review by the NYSED and that the NYSED had unearthed some "irregularities" in Interboro's admissions process. That same day, Barrington Research issued a report on EVCI with the heading: "Downgrading Rating to MARKET PERFORM on Adverse Compliance Review." Roth Capital Partners also downgraded the Company's stock to "Neutral."

86. On November 3, 2005, EVCI submitted its responses to the draft report, in which it agreed to implement changes at Interboro in order to work towards compliance with the NYSED regulations. Significantly, EVCI agreed to cease expansion and to cap enrollment at the fall 2005 level of 4,500 students until the NYSED determined that Interboro was in compliance with its regulations. At this time, EVCI did not issue a press release or otherwise announce these developments.

87. Instead, on November 22, 2005, EVCI issued a press release announcing the results of its own "independent" investigation. The release attributed the misconduct reported in the October 7, 2005 Draft Report to a few "rogue employees" despite the fact that the Company had a policy that its admissions representatives admit a certain number of students or face termination. On this reported positive news, EVCI's stock rose 33.3% from its opening price of \$2.15 that day to a close of \$3.13, trading at a dramatically higher volume of 2.1 million shares as compared to the previous day's volume of approximately 143,000 shares.

88. On November 22, 2005, EVCI also filed a form 10-Q with the SEC, in which it generally described the allegations in the draft report. The Company failed to disclose in its

filing that it had agreed to cease all expansion at Interboro and to keep the Company's enrollment at the Fall 2005 level.

89. On November 28, 2005, EVCI hosted a conference call with analysts to discuss its third-quarter 2005 earnings. McGrath and Buntzman participated in the call and stated that EVCI was "surprised by the draft report and its contents." During the call, Defendant McGrath downplayed the results of the State's undercover investigation, saying that the practices revealed were "isolated" and not "pervasive," and that the investigators had only identified a single instance of an admissions officer being terminated for not meeting a quota, and that that termination had resulted from "performance issues broader than the mere number of students admitted."

90. EVCI's Joseph Looney, who replaced Goldenberg as EVCI's CFO, effective October 1, 2005, also participated in the call. Looney spoke of gaps in EVCI's financial controls. He said:

[W]e've identified some gaps and some significant deficiencies in our internal control over financial reporting. Those may or may not rise to the level of material weakness. We haven't completed our financial assessment as of yet. We intend to complete that financial assessment sometime before December 31<sup>st</sup>. And once we do that, we need to actually bring our outside auditors in to complete their assessment and their testing of our system.

#### **H. Defendant's Fraud Is Fully Disclosed In NYSED's Final Report**

91. On December 6, 2005, the true extent and materiality of defendants' fraud became clear when EVCI filed a Form 8-K that attached a copy of NYSED's final report, which consisted of the draft report, Interboro's response, and the December 6, 2005 cover letter. The final report confirmed that the NYSED was denying extension-center status for Interboro's Yonkers location and required Interboro to reduce student enrollment at *all locations*.

92. The cover letter that the NYSED incorporated into the final report noted that the Company's investigation into the practices revealed during the course of the State's undercover investigation "affirms some of the findings of misconduct of the Department's investigation and is not able to refute any of the findings in the Department's report." The NYSED stated that it was "gravely concerned about the severity of the findings of its undercover investigation," including: (i) the alteration of prospective students' answer sheets to produce passing grades at both the Yonkers and Flushing campuses; (ii) a prospective student being encouraged to falsify his income to qualify for financial aid; and (iii) "[a] total disregard for administering the ability-to-benefit examination with integrity at its Flushing campus." The letter went on to explain that after "careful review of the peer review report and the response from Interboro, the Department believes that the institution is significantly out of compliance with part 52 of the Regulations of the Commissioner of Education for operating credit-bearing programs in New York State, specifically in the areas of admissions, faculty, libraries, curriculum, faculty governance and policies."

93. As stated, *supra*, in Interboro's November 3, 2005 response to the NYSED's draft report -- and in the November 28, 2005 conference call with investors -- defendants expressed "surprise" at the NYSED's findings. In the final report, however, NYSED said that it found defendants' surprise unconvincing, referencing the December 6, 2004 letter that followed Interboro's September 2004 request for extension-center status for its Yonkers site. That letter, the NYSED pointed out, notified Interboro that it would be subject to a comprehensive visit to determine if it was capable of expanding. More significantly, in its June 15, 2005 letter, NYSED told Interboro that it would deny extension-center status for its Yonkers campus "given the current deficiencies." Based on these facts, the NYSED concluded, "it is the Department's

determination that Interboro Institute was well aware of the concerns of the Department with its expansion at Yonkers and overall academic deficiencies of the institution.”

94. Along with confirming its denial of extension-center status for Interboro’s Yonkers site, the NYSED’s final report directed Interboro to produce a satisfactory plan to reduce enrollment at all of its locations “so that resources can be better targeted to serve students with serious academic deficiencies to effectively meet the academic standard of a collegiate program.”

95. As a result of the December 6, 2005 news, EVCI’s stock tumbled nearly another third to \$1.80 from the previous day’s closing price of \$2.60. Meanwhile, the volume of shares traded after the news spiked over the previous day’s volume of approximately 154,000 shares to a volume of approximately 2.1 million.

96. Analysts’ reaction to the final report further demonstrates the materiality of the defendants’ fraud. For example, a December 6, 2005 CJS Securities report announced that the “investment case on EVCI . . . driven by exceptional growth” was under “attack” due to the NYSED’s final report “forcing the company to have negative enrollment trends” while “demanding the company increase its spending to provide better services (libraries, full-time teachers, etc.).” The analyst report continued, “Negative enrollment trends and higher operating costs will likely have a severe impact on reported financial results” and that, in hindsight, “it now appears that financial results for the last few years reflect underspending on systems and needed infrastructure.” In its December 8, 2006 analyst report, Barrington Research similarly stated, “Taking this new information into account, we would expect Interboro enrollment to fall (rather than stay flat or grow), revenues to fall (perhaps, though, at a lesser rate due to previously

implemented tuition price increases) and earnings to fall significantly (given the lower expected enrollment numbers and increased costs associates [sic] with NYSED compliance).”

97. On June 13, 2006, NASDAQ notified EVCI that its common stock was not in compliance with the “Bid Price Rule” because the closing price per share had been below \$1.00 for thirty consecutive trading days. Accordingly, EVCI had 180 days – until December 11, 2006 – to regain compliance with the “Bid Price Rule.” To regain compliance, EVCI’s stock must trade at over \$1.00 per share for ten consecutive trading days.

#### **I. The U.S. Department of Education Investigation**

98. On April 10, 2006, EVCI announced that the United States Department of Education (“DOE”) had, like the NYSED, issued a draft report with the results of its own review regarding Interboro’s compliance with respect to approximately \$26 million of Title IV grants made to the school’s students during July - June of years 2002/2003, 2003/2004, and 2004/2005.

99. The Company's release revealed that the DOE sampled sixty student files and discovered that Interboro had accepted four students who had not passed the ATB test, and that 11 accepted students had passed the ATB tests, but Interboro had misgraded their exams. The DOE ordered that Interboro rescore all of the ATB tests for the three reviewed years. EVCI has asked the DOE to reconsider its request to rescore all the tests, contending that only three of the sixty tests were miscored so as to admit unqualified students. If, however, the DOE does not agree with EVCI, EVCI has estimated that Interboro would be liable to repay approximately \$1.3 million of Title IV funds to the DOE.

100. In the April 10, 2006 press release, EVCI further admitted:

If the liability to the DOE exceeds \$250,000, and becomes fixed at a time when our current bank debt has not been fully repaid, our bank would have the right to accelerate the due date of that debt. Accordingly, we may need the continued cooperation of our bank and may be under significant pressure to attempt to

refinance our remaining bank debt under circumstances that could be materially adverse to EVCI.

101. On April 13, 2006, EVCI issued a press release that reported the DOE had denied its request to reconsider its requirement that Interboro rescore all of its ATB tests for the three reviewed years. However, the DOE extended Interboro's deadline for rescoring the ATB test from the first week of June 2006 to October 15, 2006.

## **VI. DEFENDANTS' FALSE AND MISLEADING STATEMENTS ISSUED DURING THE CLASS PERIOD**

### **A. The August 2003 Press Release**

102. On August 14, 2003, the first day of the Class Period, EVCI issued a press release that said, in relevant part:

EVCI Career Colleges Incorporated (NASDAQ: EVCI), owner of Interboro Institute, reported a \$2.7 million increase in total revenue and a positive swing of approximately \$1.0 million in net income available to common stockholders for the six months ended June 30, 2003 as compared to the same period of 2002. New student enrollments, increased retention and the addition of new college sites were primarily responsible for this increase.

103. Defendants knew or should have known that the statements made by them and contained in EVCI's August 14, 2003 press release were materially false and misleading because while Interboro's new student enrollments and EVCI's revenues may have been up, it was not due to "increased retention," but rather a fraudulent admissions process as set forth at ¶¶ 47-56; 77-81 above. Defendants also knew or should have known that Interboro was not providing the resources to support and retain the massive number of new students it was admitting, putting its accreditation, and its ability to increase enrollment in jeopardy as set forth at ¶¶ 35-39; 57-81 above.

**B. Form 10-QSB For the Second Quarter of 2003**

104. In EVCI's Form 10-QSB for the second quarter of 2003, dated August 14, 2003, EVCI similarly reported that: (i) Interboro's "summer enrollment increased 15% to approximately 1080 full-time students from 947 full-time students in the summer of 2002"; (ii) net revenues for the second quarter 2003 increased 17%, or \$563,000, to \$3,878,000 from \$3,315,000 for the second quarter 2002"; and (iii) due to our expansion and progress in increasing new enrollment and retention of Interboro students, we had record enrollment for the spring and summer semesters."

105. Defendants knew or should have known that the statements made by them and contained in EVCI's Form 10-QSB for the second quarter of 2003 press release were materially false and misleading because while Interboro's new student enrollments and EVCI's revenues may have been up, it was not due to increased retention, but rather a fraudulent admissions process as set forth at ¶¶ 47-56; 77-81 above. Defendants also knew or should have known that Interboro was not providing the resources to support and retain the massive number of new students it was admitting, putting its accreditation, and its ability to increase enrollment, in jeopardy as set forth at ¶¶ 35-39; 57-81 above.

**C. October 2003 Press Release**

106. On October 22, 2003, EVCI issued a press release that stated in relevant part:

EVCI Career Colleges Incorporated (Nasdaq: EVCI) announced an enrollment increase of more than 30% for the fall 2003 semester at Interboro Institute's four college sites. The enrollment in the fall 2003 semester was approximately 2300 students as compared to 1,750 students in the fall 2002 semester.

Dr. John J. McGrath, Chief Executive Officer and President expressed great satisfaction with the increases in new student enrollments and in the success of the college's new retention strategies.

Percentage of enrollment increase, when comparing year over year semester enrollment, is a key valuation driver in the for-profit education sector. According

to [a sector research analyst], EVCI's peer group within the post secondary education industry has averaged between 15% and 20% growth in year-over-year semester enrollments. "Measured by this standard, it is our opinion that EVCI's stock is undervalued," stated Dr. Arol I Buntzman, Chairman of EVCI.

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According to Dr. McGrath, "It is noteworthy that EVCI's 30% plus growth rate results solely from internally generated enrollments at existing campuses rather than growth by adding new Interboro sites or acquisitions." Interboro demonstrated significant enrollment increases at each college site.

107. Defendants knew or should have known that the statements made by them and contained in EVCI's October 22, 2003 press release were materially false and misleading because while Interboro's new student enrollments and EVCI's revenues may have been up, it was not due to the Company's "retention strategies" but rather a fraudulent admissions process as set forth at ¶¶ 47-56; 77-81 above. Defendants also knew or should have known that Interboro was not providing the resources to support and retain the massive number of new students it was admitting, putting its accreditation, and its ability to increase enrollment, in jeopardy as set forth at ¶¶ 35-39; 57-81 above. Finally, Defendants also knew or should have known that even if they existed, the Company's "retention strategies" were not successful as Interboro's retention rates were not increasing.

**D. November 12, 2003 Press Release**

108. On November 12, 2003, EVCI issued a press release announcing that Buntzman had sold 300,000 shares of EVCI common stock at \$4.00 per share for proceeds of \$1.2 million. According to the release, Buntzman needed to make the stock sale "in order to raise money in anticipation of the equitable distribution of marital assets in a pending divorce."

109. Defendant Buntzman knew that this statement was false and misleading, as evidenced by a divorce proceeding decision where the court noted that the November 12, 2003 sale was "made without [Buntzman's former wife's] consent and in violation of an interim order

limiting the transfer of the parties' assets.” *Mahoney-Buntzman v. Buntzman*, 11 Misc.3d 869, 876 n.1 (NY Sup. Ct. Westchester County 2006).

**E. November 14, 2003 Press Release**

110. On November 14, 2003, EVCI issued the press release that stated in relevant part:

EVCI Career Colleges Incorporated (NASDAQ: EVCI) today reported record third quarter revenues and income from continuing operations. Net revenue for the quarter ended September 30, 2003 was \$4,321,000, a 40% increase over revenue of \$3,081,000 for the quarter ended September 30, 2002

Income from continuing operations was \$83,500 compared to a loss of \$609,000 in the same quarter a year ago. The net loss to common stockholders was \$188,400 (\$.03 per share) in the third quarter of 2003 versus a loss of \$2,354,300 (\$0.47 per share) for the third quarter of 2002.

\* \* \*

Our improved results were primarily driven by increased college enrollments. As EVCI reported on October 22nd, enrollments for the fall semester are up over 30% to approximately 2,300 full-time students from 1,7500 full-time students last fall. Enrollment growth was entirely organic. EVCI did not make any acquisitions and Interboro did not open new college sites during the previous 12 months.

“We are delighted with Interboro's record enrollments which include both new students and greater retention of existing students,” commented EVCI's CEO and President Dr. John J. McGrath. “I am pleased to see the response to our carefully developed strategies which are designed to meet the unique needs of economically disadvantaged students. A concrete results of this initiative was a dramatic reduction in the drop-out rate during the first few weeks of the fall 2003 semester; it was only 3% vs. our historical rate of 8%. This is a win both for our students and Interboro.”

111. Defendants knew or should have known that the statements made by them and contained in EVCI's November 14, 2003 press release were materially false and misleading because while Interboro's new student enrollments and EVCI's revenues may have been up, it was not due to the Company's “greater retention of existing students” but rather a fraudulent admissions process as set forth at ¶¶ 47-56; 77-81 above. Defendants also knew or should have known that Interboro was not providing the resources to support and retain the extraordinary

number of new students it was admitting, putting its accreditation, and its ability to increase enrollment, in jeopardy as set forth at ¶¶ 35-39; 57-81 above. Finally, Defendants also knew or should have known that even if they existed, the Company's "carefully developed strategies" were not successful as Interboro's retention rates were not increasing.

**F. Form 10-QSB for the Third Quarter 2003**

112. In EVCI's Form 10-QSB for the third quarter of 2003, dated November 14, 2003, EVCI similarly reported that: (i) Interboro's "fall enrollment increased 31% to approximately 2300 full-time students from 1750 full-time students in the fall of 2002"; and (ii) "net revenues for the third quarter 2003 increased 40%, or \$1,240,000, to \$4,321,000 from \$3,081,000 for the third quarter 2002."

113. Defendants knew or should have known that the statements made by them and contained in EVCI's Form-10QSB for the third quarter of 2003 were materially false and misleading because while Interboro's new student enrollments and EVCI's revenues may have been up, defendants failed to disclose that those new enrollments and increase in revenues resulted from a fraudulent admissions process as set forth at ¶¶ 47-56; 77-81 above. Defendants also knew or should have known that Interboro was not providing the resources to support and retain the extraordinary number of new students it was admitting, putting its accreditation, and its ability to increase enrollment, in jeopardy as set forth at ¶¶ 35-39; 57-81 above.

**G. January 2004 Press Release**

114. On January 6, 2004, EVCI issued a press release stated in relevant part:

YONKERS, N.Y.—(BUSINESS WIRE)—Jan. 6, 2004—The Journal News reported on January 1, 2004 that EVCI Career Colleges Incorporated (Nasdaq:EVCI – News) led the Journal News' Bloomberg Index for 2003 because EVCI shares rose 729 percent, closing out the year at \$5.39. This local index tracks 77 stocks with corporate headquarters or a major presence in Westchester, Rockland, and Putnam counties in New York State.

\* \* \*

Dr. John J. McGrath, CEO and President of EVCI, expressed his pleasure at EVCI's recognition. "We are gratified that shareholder value has increased dramatically over the past year and that the success of our business strategy is being recognized by the investing public."

Dr. Arol I. Buntzman, Chairman of EVCI, believes that EVCI's present stock price still does not reflect EVCI's fundamental value, particularly when compared to other companies in the post-secondary industry. He stated, "we are optimistic that the market will continue to see how favorable EVCI's ratios are when compared to others in the post-secondary industry."

115. Defendants knew or should have known that this statements made by them and contained in the January 6, 2004 press release were false and misleading because as set forth at ¶¶ 47-56; 77-81 above, EVCI's "business strategy" was a sham and relied on fraudulent practices. Moreover, within three months of telling investors that EVCI's stock was undervalued, Buntzman was dumping more than 80% of his holdings.

#### **H. February 23, 2004 Press Release**

116. On February 23, 2004, EVCI issued a press release that stated in relevant part:

Fourth quarter 2003 revenues were \$5.8 million, up from \$5.0 million last year. Fourth quarter net income available to common stockholders was \$2.2 million, or basic earnings per share of \$0.20 and diluted earnings per share of \$0.19. This represents a swing of \$2.6 million from last year's fourth quarter net loss of \$0.4 million.

Full year 2003 revenues were \$20.2 million, up 31% from \$15.4 million last year. Full year 2003 net income available to common stockholders was \$2.6 million, or basic earnings per share of \$.035 and diluted earnings per share of \$.031. This represents a swing of \$5.8 million from last year's net loss of \$3.2 million. In achieving these results, EVCI reduced total operating expenses as a percentage of revenue by 5% in 2003 versus 2002. EVCI also increased income from continuing operations by 287% from \$.4 million in 2002 to \$1.5 million in 2003. Net income for 2003 includes a \$2.0 million federal income tax benefit EVCI expects to realize upon utilization of its net operating loss carry-forward.

Dr. John J. McGrath, CEO and President, commented that 2003 was, by far, the best year ever and produced EVCI's first full year of net income. "Our operating results were outstanding and we substantially improved our balance sheet. We exceeded our goals."

Dr. McGrath further commented, “It is noteworthy that all of our 2003 growth was generated by an organic same site enrollment increase of 28% to 5,250 full time students from 4,110 in 2002. This enrollment growth represents an increase of new students and improved retention of existing students. The growth in 2003 did not occur by increasing tuition, adding new Interboro college sites, or through acquisition of other post-secondary institutions.

117. Defendants knew or should have known that the statements made by them and contained in EVCI’s February 23, 2004 press release were materially false and misleading because while Interboro’s new student enrollments and EVCI’s revenues may have been up, it was not due to the Company’s “improved retention of existing students” but rather a fraudulent admissions process as set forth at ¶¶ 47-56; 77-81 above. Defendants also knew or should have known that Interboro was not providing the resources to support and retain the extraordinary number of new students it was admitting, putting its accreditation, and its ability to increase enrollment, in jeopardy as set forth at ¶¶ 35-39; 57-81 above.

**I. February 24, 2004 Press Release**

118. On February 24, 2004, the Company issued another press release – this one reporting that EVCI’s “[s]pring semester enrollments were approximately 2,800 full-time students, an increase of approximately 56% from the 1,800 full-time student enrollments for the same semester 2003.” McGrath was quoted as saying, “It is extremely gratifying for us to follow our 2003 full year enrollment increase of 28% with a larger percentage same site enrollment increase for the Spring 2004 semester. Enrollments are the most significant driver of our revenue and profits.”

119. Defendants knew or should have known that the statements made by them and contained in EVCI’s February 24, 2004 press release were materially false and misleading because while Interboro’s new student enrollments and EVCI’s revenues may have been up, it was not due to the Company’s “improved retention of existing students” but rather a fraudulent

admissions process as set forth at ¶¶ 47-56; 77-81 above. Defendants also knew or should have known that Interboro was not providing the resources to support and retain the extraordinary number of new students it was admitting, putting its accreditation, and its ability to increase enrollment, in jeopardy as set forth at ¶¶ 35-39; 57-81 above.

**J. 2003 Form 10-KSB**

120. On March 5, 2004, EVCI filed its Form 10-KSB for the year ending December 31, 2003. The Company reported “significant 2003 accomplishments” including: (i) increasing total revenue of \$20.2 million, up 31% from \$15.4 million in 2002; (ii) a 28% increase in full-time student enrollments for the full year, from 4,110 in 2002 to 5,250 in 2003; (iii) an increase in full-time student enrollments each semester of 2003 over the same semester in 2002; (iv) accreditation from the N.Y. State Board of Regents for five years; and (v) a strengthening of Interboro's academic programs by raising the academic standards in English and Mathematics; and (vi) continuing to upgrade the library system and computer labs. In addition, the Company stated that it was committed to providing a “quality and caring educational experience” and to “improving student retention”:

Improving student retention is essential to the continuing success of Interboro and is one of Interboro's greatest challenges and opportunities. The retention process starts from the initial enrollment and continues through graduation. As is true throughout the country for disadvantaged students, a large number of Interboro's students never finish their degree programs for personal, financial or academic reasons. We recognize that our ability to retain students until graduation is an important indicator of our success and that modest improvements in retention rates can result in meaningful increases in revenue and profitability.

Interboro significantly increased its retention and graduation rates in 2003, in part by adding 350 additional hours of tutoring per week college wide. For 2004, Interboro has hired 10 full-time remediation and developmental specialists whose sole job is to work, in and outside the classroom, with students, faculty and tutors in order to provide students with the skill sets required for them to succeed in college. Notwithstanding the extra expense of intense tutoring intervention it generally has been more cost-effective for us to retain students than to recruit new students.

Improved retention and graduation rates continue to be a top priority at Interboro. We are proud of the progress, so far, of our student retention programs since we acquired Interboro. We consider student retention the responsibility of the entire college personnel.

In addition, the Company reported a 56% increase in enrollments for the spring 2004 semester over the spring 2003 semester and said that “Interboro has enhanced an strengthened its retention and graduation strategies and rates.” EVCI also reported:

We expect to grow in 2004 mostly by continuing to increase new student enrollment and improve retention of students at our existing sites. Continuing the pace of our same site growth will require us to increase capacity by the Fall 2004 semester.

121. EVCI and the Individual Defendants, each of whom signed the Form 10-KSB, knew or should have known that the statements made by them and contained in EVCI’s 2003 Form 10-KSB were materially false and misleading because while Interboro’s new student enrollments and EVCI’s revenues may have been up, it was not due to the Company’s retention of students but rather a fraudulent admissions process as set forth at ¶¶ 47-56; 7781 above. Defendants also knew or should have known that Interboro was not providing the resources to support and retain the extraordinary number of new students it was admitting, putting its accreditation, and its ability to increase enrollment, in jeopardy as set forth at ¶¶ 35-39; 57-81 above.

**K. March 8, 2004 Press Release**

122. On March 8, 2004, EVCI issued a press release that said, in relevant part, “Dr. John J. McGrath, CEO and President, said he anticipates EVCI achieving an annual average revenue growth of 35% during the year ending December 31, 2004. This revenue and earnings guidance is based on continued organic growth in enrollments at existing Interboro college sites.”

123. Defendants knew or should have known that the statements made by them and contained in EVCI's March 8, 2004 press release were materially false and misleading because Interboro's new student enrollments and revenues resulted from a fraudulent admissions process as set forth at ¶¶ 47-56; 77-81 above. Defendants also knew or should have known that Interboro was not providing the resources to support and retain the extraordinary number of new students it was admitting, putting its accreditation, and its ability to increase enrollment, in jeopardy as set forth at ¶¶ 35-39; 57-81 above.

**L. March 30, 2004 Press Release**

124. On March 30, 2004, EVCI issued a press release titled "EVCI Receives \$10,000,000 an Equity Private Placement." The release stated in relevant part:

EVCI Career Colleges Incorporated announced it has sold 1,038,962 shares of its common stock for \$10,000,000 to institutional investors.

The net proceeds can be used for working capital and general corporate purposes, including expanding Interboro Institute, enhancing the college's facilities and further improving its retention and graduation rates.

125. Defendants knew or should have known that the statements made by them and contained in EVCI's March 30, 2004 press release were materially false and misleading because EVCI did not use the money to improve retention and graduation rates because retention and graduation rates were not improved, as set forth at ¶¶ 69; 71 above.

**M. April 2004 Press Release**

126. EVCI issued a press release on April 2, 2004, regarding the stock sales by the Individual Defendants. The press release did not disclose the NYSED's mandate that Interboro reduce enrollments; nor did it announce that Buntzman, McGrath, and Goldenberg had sold a majority of the stock they held. Rather, it announced the amount of stock sold and the share price and explained the sales with the following statements:

Dr. McGrath said, “Institutional demand was extremely high, but EVCI was not willing to incur additional dilution to its existing shareholders at this time. We made the decision, with regard to each of our personal situations, to meet this demand with a portion of our personal holdings. Management continues to hold significant stakes in EVCI’s equity, representing our belief in the future prospects for EVCI and its business.”

Management believes that EVCI will achieve earnings of \$0.50 per share for 2004, notwithstanding the increase to 12,002,241 outstanding shares as a result of the \$10,000,000 received from the other institutional buyers. Dr. McGrath stated that “the additional capital raised by EVCI will give us the opportunity to increase enrollment capacity and enhance retention efforts, thereby enabling EVCI to generate additional revenue and profit.”

127. Defendants knew or should have known that the statements made by them and contained in EVCI’s April 2, 2004 press release were materially false and misleading because, among other reasons, they knew that Buntzman, McGrath, and Goldenberg were selling off a majority of their EVCI common stock and not continuing to “hold significant stakes in EVCI’s equity, representing [Management’s] belief in the future prospects for EVCI and its business.” Moreover, Defendants had actual knowledge and failed to disclose the March 23, 2004 letter from the NYSED confirming that Interboro was to reduce enrollments.

**N. May 11, 2004 Press Release**

128. On May 11, 2004, the Company issued a press release announcing its results for the first quarter of 2004, which stated, in relevant part:

On a revenue increase of 41% over the first quarter 2003, EVCI increased income from operations by 82% and net income by 83%. Income available to common stockholders increased by 143%. As a percentage of revenue, income available to the common stockholders grew to 25% as compared to 14% for the first quarter last year....Full-time enrollment was approximately 2800 in the first quarter of 2004 compared to approximately 1800 in the 2003 period, a 56% quarter-over-quarter increase.

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Dr. McGrath continued, “Based upon our first quarter results, we feel comfortable reaffirming our fully diluted earnings per share guidance of \$.050 for 2004.” In addition, he said, “While much of our record earnings are directly due to

continuing our robust enrollment growth, expense reductions and economies of scale substantially improved our margins. As a result, income from operations, as a percentage of revenue, was 29.6% in the first quarter of 2004 as compared to 22.8% for the same quarter last year.”

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Our stronger balance sheet enables EVCI to continue to aggressively pursue our plans to expand Interboro this year by adding four new annexes to the existing college sites and to develop a freshman admissions center.

Concluding his remarks, Dr. McGrath offered the following additional guidance: “EVCI believes that Interboro will continue to realize substantial organic growth for the foreseeable future, including increases in year-over-year enrollment that is, on a percentage basis, much greater than the post-secondary education industry average. In addition, we seek acquisitions to further enhance our growth.

129. Defendants knew or should have known that the statements made by them and contained in EVCI’s May 11, 2004 press release were materially false and misleading because Interboro’s new student enrollments and revenues resulted from a fraudulent admissions process as set forth at ¶¶ 47-56; 77-81 above. Defendants also knew or should have known that Interboro was not providing the resources to support and retain the extraordinary number of new students it was admitting, putting its accreditation, and its ability to increase enrollment, in jeopardy as set forth at ¶¶ 35-39; 57-81 above. Defendants also knew that Interboro could not continue to grow, but had to decrease its enrollments to stay in compliance with the NYSED’s mandates, as discussed at ¶¶ 58-60 above.

**O. Form 10-QSB For The First Quarter of 2004**

130. In EVCI’s Form 10-QSB for the first quarter of 2004, dated May 11, 2004, EVCI similarly reported that: (i) revenues for the first quarter 2004 increased 41%, or \$2,447,000 to \$8,488,000 from \$6,041,000 for the first quarter of 2003; and that (ii) Interboro’s full-time student enrollment rose by 56% to approximately 2800 students from approximately 1800 in 2003.

131. Defendants knew or should have known that the statements made by them and contained in EVCI's Form 10-QSB for the first quarter of 2004 were materially false and misleading because while Interboro's new student enrollments and EVCI's revenues may have been up, defendants failed to disclose that those new enrollments and increase in revenues resulted from a fraudulent admissions process as set forth at ¶¶ 47-56; 77-81 above. Defendants also knew or should have known that Interboro was not providing the resources to support and retain the extraordinary number of new students it was admitting, putting its accreditation, and its ability to increase enrollment, in jeopardy as set forth at ¶¶ 35-39; 57-81 above. Finally, Defendants knew that Interboro had agreed to take steps that were likely to decrease its enrollments to stay in compliance with the NYSED's mandates, as discussed at ¶¶ 58-60 above.

**P. May 2004 Press Release**

132. On May 27, 2004, EVCI again touted student enrollment in a press release entitled "Increase of Approximately 85% over the Summer 2003 Semester Continues Momentum of Enrollment Growth," that stated in relevant part:

EVCI Career Colleges Incorporated (Nasdaq: EVCI) announced its summer semester enrollments were approximately 2,000 full-time students, an increase of approximately 85% over the 1,080 full-time student enrollments for the same semester in 2003. The record high summer enrolment follows a 53% increase in spring 2004 enrollment and is part of Interboro Institute's consistent year-over-year growth since EVCI acquired the college in 2000.

Dr. John J. McGrath, CEO and President, commented, "Interboro's model for student enrollments is performing well beyond our expectations. In fact, we did not accept many students this semester, who we would have otherwise accepted in the past, because we wanted to further improve our prospects for higher retention and graduation rates."

McGrath added, "Part of the additional revenue from this increase in enrollment will be used to expand our infrastructure more than we originally anticipated. Additionally, we are increasing our marketing and retention budgets for the fall 2004 semester."

133. Defendants knew or should have known that the statements made by them and contained in EVCI's May 27, 2004 press release were materially false and misleading because while Interboro's new student enrollments may have been up, defendants failed to disclose that those new enrollments resulted from a fraudulent admissions process as set forth at ¶¶ 47-56; 77-81 above. Defendants also knew or should have known that Interboro was not providing the resources to support and retain the extraordinary number of new students it was admitting, putting its accreditation, and its ability to increase enrollment, in jeopardy as set forth at ¶¶ 35-39; 57-81 above. In addition, Interboro was not improving its prospects for higher retention and graduation rates, and contrary to defendants' statement, Interboro was accepting students that it otherwise should not have accepted since Interboro was employing fraudulent admissions practices at that time to admit unqualified students.

**Q. August 12, 2004 Press Release**

134. On August 12, 2004, the Company announced its 2004 second quarter financial results in a press release that stated:

Comparing the second quarters of 2004 and 2003, total revenue was \$5.8 million versus \$3.9 million, loss from operations was \$0.6 million versus \$0.1 million, and loss available to common stockholders was \$0.6 million versus \$0.3 million. Fully diluted loss per share was (\$0.05) for the second quarter of 2004 as compared to (\$0.05) for the second quarter last year.

Comparing the first six months of 2004 and 2003, total revenue was \$14.3 million versus \$10.0 million, income from operations was \$1.9 million versus \$1.3 million and income available to common 1478548/stockholders was \$1.5 million versus \$0.6 million. Fully diluted earnings per share was \$0.12 for the first six months of 2004, as compared to \$0.07 for the first six months of 2003.

Dr. John J. McGrath, Chief Executive Officer and President, commented, "Our second quarter 2004 results reflect the substantial investments Interboro has made since March 1, 2004 in its growth. Most of this investment has been for salaries and benefits of new personnel, including more qualified and seasoned personnel. In addition, while our 2004 summer semester enrollments increased by 83% over 2003 summer semester enrollments, because Interboro's revenue is recognized ratably, we were only able to recognize 54% of the revenue attributable to these

enrollments. The summer semester started May 10<sup>th</sup> and ends August 13<sup>th</sup>. As a result, summer semester revenues of \$3.6 million will be recognized in the third quarter.

Dr. McGrath continued, “Based upon our first six month results, and our expectations for the balance of the year, we are on target to meet our previously announced EPS guidance of fully diluted earnings per share of \$0.50 for 2004. To achieve our expected enrollment increases for the fall semester, four new college annexes should be ready for operation by the beginning of the fall semester.”

Concluding his remarks, Dr. McGrath offered the following additional guidance: “EVCI believes that the substantial investments being made in Interboro will permit it to continue to realize its previously announced goal of substantial organic growth for the foreseeable future, including significant increases in year-over-year enrollment that is much greater than the post-secondary education industry average on a percentage basis. In addition, we are seeking acquisitions that will further enhance our growth and be accretive to EVCI’s top and bottom line.

135. Defendants knew or should have known that the statements made by them and contained in EVCI’s August 12, 2004 press release were materially false and misleading because while Interboro’s new student enrollments and revenues may have been up, defendants failed to disclose that those new enrollments resulted from a fraudulent admissions process as set forth at ¶¶ 47-56; 77-81 above. Defendants also knew or should have known that Interboro was not providing the resources to support and retain the extraordinary number of new students it was admitting, putting its accreditation, and its ability to increase enrollment, in jeopardy as set forth at ¶¶ 35-39; 57-81 above. In addition, Interboro was not making “substantial investments” in Interboro that would improve its prospects for higher retention and graduation rates.

**R. Form 10-QSB For the Second Quarter of 2004**

136. EVCI’s second quarter 2004 10-QSB, dated August 12, 2004, similarly reported that (i) Interboro’s full-time student enrollments for its summer semester increased to 1975 in 2004 from 1080 in 2003, an 83% increase; (ii) In June, Interboro graduated 305 students, a 42% increase over its 215 graduates in June 2003; (iii) “in preparation for its anticipated growth,

Interboro made substantial investments in its academic, administrative and financial infrastructure and systems”; and (iv) that revenue for the second quarter 2004 increased 49%, or \$1,914,000 to \$5,833,000 from \$3,919,000 for the second quarter 2003. In addition, the Form 10-QSB also stated that: “Interboro’s growth strategy is not simply about increasing enrollments. Its significant growth requires personnel, senior management and other resources to ensure that the quality of Interboro’s academic and administrative operations continues to improve,” and that “Interboro is hiring more qualified and seasoned personnel...and adding new systems.” The 10-QSB further stated that “Interboro personnel are working to further improve retention rates by being more selective in admitting new students and providing intensive remedial instruction for its students. Furthermore, Interboro is seeking to enhance its reputation by obtaining additional regulatory academic approvals and college-wide accreditation.”

137. Defendants knew or should have known that the statements made by them and contained in EVCI’s Form 10-QSB for the second quarter of 2004 were materially false and misleading because while Interboro’s new student enrollments and revenues may have been up, Defendants failed to disclose that those new enrollments and increased revenues resulted from a fraudulent admissions process as set forth at ¶¶ 47-56; 77-81 above. Defendants also knew or should have known that Interboro was not providing the resources to support and retain the extraordinary number of new students it was admitting, putting its accreditation, and its ability to increase enrollment, in jeopardy as set forth at ¶¶ 35-39; 57-81 above. In addition, Interboro was not making substantial investments in Interboro that would improve its prospects for higher retention and graduation rates and Interboro was not being “more selective about admitting new students” but to the contrary was admitting students fraudulently to increase enrollment.

**S. August 2004 Press Release**

138. On August 26, 2004, EVCI issued a press release regarding a “routine” TAP audit being conducted by the State. McGrath stated, “I would like to assure the public that management is very confident that any TAP disallowance will not in any way result from intentional misconduct.”

139. Defendants knew or should have known that the statements made by them and contained in EVCI’s August 26, 2004 press release were materially false and misleading because Interboro’s admissions practices fraudulently admitted unqualified students – *i.e.*, the misconduct was intentional.

**T. Form 10-QSB For the Third Quarter of 2004**

140. In its press release and Form 10-QSB for the third quarter of 2004, dated September 30, 2004, EVCI reported that its fall semester enrollment had increased to approximately 3900 in 2004 from approximately 2300 in 2003, a 70% increase, and that its revenue for the third quarter 2004 increased 45%, or \$2,034,000, to \$6,509,000 from \$4,475,000.

EVCI’s Form 10-QSB also claimed that:

Interboro’s aggressive growth requires senior management personnel and other resources to ensure that the quality of Interboro’s academic and administrative operations continues to improve. Accordingly, Interboro has hired more qualified and seasoned personnel, is continuing to improve the operating efficiencies of its existing communications systems and is continuing to add new integrated systems. Interboro personnel are working to improve retention rates further by being more selective in admitting new students and providing intensive remedial instruction for students needing it. Furthermore, Interboro is seeking to enhance its reputation by obtaining additional regulatory academic approvals and additional college accreditation. While we expect that Interboro’s rate of growth will continue to exceed industry averages in 2005, Interboro plans to continue to increase its focus on improving its academic operations, administrative operations and operating efficiencies as well as its retention and graduation rates. We are always mindful of the increasing level of scrutiny we are subject to as we continue to grow aggressively.

141. Defendants knew or should have known that the statements made by them and contained in EVCI's Form 10-QSB for the third quarter of 2004 were materially false and misleading because while Interboro's new student enrollments and revenues may have been up, defendants failed to disclose that those new enrollments and increased revenues resulted from a fraudulent admissions process as set forth at ¶¶ 47-56; 77-81 above. Defendants also knew or should have known that Interboro was not providing the resources to support and retain the extraordinary number of new students it was admitting, putting its accreditation, and its ability to increase enrollment, in jeopardy as set forth at ¶¶ 35-39; 57-81 above. In addition, Interboro was not making substantial investments in Interboro that would improve its prospects for higher retention and graduation rates.

**U. October 2004 Press Release**

142. On October 20, 2004, EVCI issued a press release reaffirming year-end guidance and reporting that "enrollment for the fall 2004 semester at Interboro Institute is approximately 3,900 full-time students, a 70% increase over the approximately 2,300 students enrolled in the fall 2003 semester." McGrath stated: "We are very pleased that Interboro's model continues to make a positive contribution in New York City, especially for economically disadvantaged minorities that have limited educational opportunities."

143. Defendants knew or should have known that the statements made by them and contained in EVCI's October 20, 2004 press release were materially false and misleading because while Interboro's new student enrollments may have been up, defendants failed to disclose that those new enrollments resulted from a fraudulent admissions process as set forth at ¶¶ 47-56; 77-81 above. Defendants also knew or should have known that Interboro's "model" was *not* to provide the resources to support and retain the extraordinary number of new students

it was admitting, putting its accreditation, and its ability to increase enrollment, in jeopardy as set forth at ¶¶ 35-39; 57-81 above.

**V. November 2004 Press Release**

144. On November 15, 2004, the Company issued a press release concerning its third quarter 2004 results. It stated in relevant part:

Dr. John J. McGrath, Chief Executive Officer and President, commented:

“Our third quarter 2004 loss is consistent with our expectations. While we had a 70% increase in enrollments, representing an additional 1600 students for the fall 2004 semester as compared to fall 2003, there were nine fewer days of revenue recognition in the 2004 third quarter. This year’s third quarter recognized only 14 days of revenue because the 2004 fall semester started a week later than originally scheduled. We recognized 23 days of revenue in last year’s third quarter because the fall 2003 semester started a week earlier than typical in our academic calendar....”

145. Defendants knew or should have known that the statements made by them and contained in the November 15, 2004 press release were materially false and misleading because while Interboro’s new student enrollments may have been up, defendants failed to disclose that those new enrollments resulted from a fraudulent admissions process as set forth at ¶¶ 47-56; 77-81 above.

**W. December 2004 Press Release**

146. On December 13, 2004, EVCI announced the preliminary findings from a New York State “routine” audit of its TAP awards. The State determined that the Company had to return \$903,150 in grants the State made to Interboro from January 2000 to mid-2003. McGrath commented: “I am pleased that the TAP audit has been concluded with all disallowances related only to human error. The college has strengthened its internal compliance policies and procedures to reduce human error in the future.”

147. Defendants knew or should have known that the statements made by them and contained in EVCI's December 13, 2004 press release were materially false and misleading because, among other reasons, they attributed the TAP overpayment to "human error" when in fact they knew or should have known the overpayment was likely due to intentional acts rather than error due to the Company's fraudulent admission practices. The statements were also false and misleading because, in fact, the Company did not do anything to strengthen its internal compliance policies to avoid similar misconduct.

**X. 2004 Form 10-KSB**

148. In its 10-KSB filed for the year ended December 31, 2004, EVCI reported that its revenue was up 63% from 2002, to \$33.1 million and that enrollments were growing an average of 40% per year since EVCI acquired Interboro in 2000. The Form 10-KSB said, "At this rate, Interboro will continue to significantly exceed industry averages for enrollment." In addition, the Form 10-KSB also again touted the Company's efforts to "provide a quality and caring educational experience" and "improve student retention":

Most of Interboro's faculty members teaching career-based courses have direct work experience in the areas they teach. Interboro's full-time faculty is particularly effective in providing any necessary remedial education. Typically, full-time faculty members are hired after they have proven their effectiveness as adjunct instructors at Interboro.

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Interboro has increased its retention and graduation rates since EVCI acquired Interboro in January 2000 from less than 10% to approximately 20%. Interboro has hired full-time remediation and developmental specialists whose sole job is to work, in and outside the classroom, with students, faculty and tutors in order to provide students with the skill sets required for them to succeed in college. Notwithstanding the extra expense of intense tutoring intervention, it generally has been more cost-effective for Interboro to retain students than to recruit new students. Interboro has submitted to the New York State Education Department (NYSED) a plan to assure a graduation rate of 25% before Interboro's accreditation expires on September 30, 2008.

Improved retention and graduation rates continue to be a top priority at Interboro. It considers student retention the responsibility of the entire college personnel.

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We expect to grow Interboro's enrollments in 2005 at a rate that is consistent with its historical compounded annual growth rate of enrollments that has averaged approximately 40% per year since we acquired Interboro in 2000. At this rate, Interboro will continue to significantly exceed industry averages for enrollment growth at proprietary colleges owned by public companies. In order to meet Interboro's 2005 growth target, it will need to increase capacity by the fall 2005 semester.

149. EVCI and the Individual Defendants, all of whom signed the 10-KSB, knew or should have known that the statements made by them and contained in EVCI's 2004 10-KSB were materially false and misleading because while Interboro's new student enrollments and revenues may have been up, defendants failed to disclose that those new enrollments and increased revenues resulted from a fraudulent admissions process as set forth at ¶¶ 47-56; 77-81 above. Defendants also knew or should have known that contrary to its representations, Interboro was not providing the resources to support and retain the extraordinary number of new students it was admitting, putting its accreditation, and its ability to increase enrollment, in jeopardy as set forth at ¶¶ 35-39; 57-81 above. In addition, Interboro was not making substantial investments in Interboro or its students that would improve its prospects for higher retention and graduation rates, and its graduation and retention rates were not increasing as represented.

**Y. February 17, 2005 Press Release**

150. On February 17, 2005, the Company issued a press release announcing its fourth quarter financial results for year ended December 21, 2004. In the press release, EVCI stated:

Revenue for Q4 2004 was \$12.2 million, up from \$5.8 million for Q4 last year. Net income available to common stockholders for Q4 2004 was \$5.9 million as compared to \$2.2 million for Q4 2003. Diluted EPS for Q4 2004 was \$0.46 compared to \$0.26 for Q4 2004. Operating income per share for Q4 2004 was

\$0.32 compared to \$0.03 for Q4 2003 (which is determined by dividing operating income by the diluted weighted average number of shares per period).

Full year 2004 revenues were \$33.1 million, up 64% from \$20.2 million for 2003. Full year 2004 net income available to common stockholders was \$6.3 million, as compared to \$2.6 million last year, a 142% increase. Net income included a benefit for income taxes of \$2.8 million in 2004 as compared to \$1.9 million in 2003, resulting from a reduction in the valuation allowance of our deferred income tax asset, which was primarily derived from prior net operating losses. Diluted EPS was \$0.50 for 2004 versus \$0.31 for 2003.

Income from operations was \$4.6 million for 2004 as compared to \$1.6 million in 2003, a 188% increase. Operating income per share was \$0.37 for 2004 as compared to \$0.20 for 2003, an 85% increase

\* \* \*

Dr. John J. McGrath, EVCI's CEO and President, commented "Enrollment and Interboro Institute for 2004 was up approximately 65% over 2003. Our operating income increased dramatically. Our operating income, as a percentage of revenue, improved from 8% in 2003 to 14% in 2004. This improvement resulted from economies of scale and strengthening our operating efficiencies. We met our publicly issued guidance."

151. Defendants knew or should have known that the statements made by them and contained in EVCI's February 17, 2005 press release were materially false and misleading because while Interboro's new student enrollments and revenues may have been up, defendants failed to disclose that those new enrollments and increased revenues resulted from a fraudulent admissions process as set forth at ¶¶ 47-56; 77-81 above. Defendants also knew or should have known that contrary to its representations, Interboro was not providing the resources to support and retain the extraordinary number of new students it was admitting, putting its accreditation, and its ability to increase enrollment, in jeopardy as set forth at ¶¶ 35-39; 57-81 above.

**Z. February 22, 2005 Press Release**

152. On February 22, 2005, the Company issued a press release announcing that:

EVCI Career Colleges Holding Corp. (NASDAQ: EVCI) announced its Spring semester enrollments were approximately 3,700 full-time students, an increase of 32% from the 2,800 full-time student enrollments for spring semester 2004.

Dr. John J. McGrath, EVCI's CEO and President, commented, "This enrollment growth is in line with our plans and expectations. While we expect that Interboro's rate of growth will continue to significantly exceed industry averages in 2005, Interboro's plan is to continue to increase its focus on improving academic operations, administrative operations, operating efficiencies and retention and graduation rates.

153. Defendants knew or should have known that the statements made by them and contained in EVCI's February 22, 2005 press release were materially false and misleading because while Interboro's new student enrollments may have been up, defendants failed to disclose that those new enrollments resulted from a fraudulent admissions process as set forth at ¶¶ 47-56; 77-81 above. Defendants also knew or should have known that contrary to their representations, Interboro was not providing the resources to support and retain the extraordinary number of new students it was admitting, putting its accreditation, and its ability to increase enrollment, in jeopardy as set forth at ¶¶ 35-39; 57-81 above. In addition, Interboro was not making substantial investments in Interboro that would improve its prospects for higher retention and graduation rates.

**AA. Form 10-Q For The First Quarter of 2005**

154. EVCI's Form 10-Q for the first quarter of 2005 reported that enrollments had increased by 32% over spring 2004 and that its revenue had increased by 21% for the first quarter of 2005 versus the first quarter of 2004.

155. Defendants knew or should have known that the statements contained in EVCI's Form 10-Q for the first quarter of 2005 were materially false and misleading because while Interboro's new student enrollments may have been up, defendants failed to disclose that those new enrollments resulted from a fraudulent admissions process as set forth at ¶¶ 47-56; 77-81 above. Defendants also knew or should have known that contrary to their representations, Interboro was not providing the resources to support and retain the extraordinary number of new

students it was admitting, putting its accreditation, and its ability to increase enrollment, in jeopardy as set forth at ¶¶ 35-39; 57-81 above. In addition, Interboro was not making substantial investments in Interboro or Interboro's students that would improve the Company's prospects for higher retention and graduation rates.

**BB. May 2005 Press Release**

156. On May 12, 2005, the Company issued a press release announcing its financial results for the first quarter of 2005. The press release stated in relevant part:

Comparing the first quarters of 2004 and 2005, total revenue was \$10.2 million versus \$8.5 million, income from operations was \$0.9 million versus \$2.5 million, net income was \$0.7 million versus \$2.1 million. Diluted earnings per share was \$0.05 for the first quarter of 2005, compared to \$0.18 for the first quarter last year. Full-time student enrollment was approximately 2,800 in the 2004 period, a 32% quarter-to-quarter increase.

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Concluding Dr. McGrath remarks: “While Interboro continues to increase its focus on improving academic operations, administrative operations and operating efficiencies, EVCI still believes that Interboro will continue to realize substantial organic growth for the foreseeable future, including increases in year-over-year enrollment that is, on a percentage basis, much greater than the post-secondary education industry average. In addition, EVCI is seeking other acquisitions that we believe will further accelerate our growth and increase our stockholder value.”

157. Defendants knew or should have known that the statements made by them and contained in EVCI's May 12, 2005 press release were materially false and misleading because while Interboro's new student enrollments and revenues may have been up, defendants failed to disclose that those new enrollments and increased revenues resulted from a fraudulent admissions process as set forth at ¶¶ 47-56; 77-81 above. Defendants also knew or should have known that contrary to their representations, Interboro was not providing the resources to support and retain the extraordinary number of new students it was admitting, putting its accreditation,

and its ability to increase enrollment, in jeopardy as set forth at ¶¶ 35-39; 57-81 above. In addition, Interboro was not making substantial investments in Interboro or Interboro's students that would improve the Company's prospects for higher retention and graduation rates.

**CC. June 2005 Press Release**

158. On June 14, 2005 EVCI again touted its growth in a press release that announced “summer semester enrollments were approximately 2,660 full-time students, an increase of 35% over the 1,975 full-time student enrolments for the same semester 2004.”

159. Defendants knew or should have known that the statements made by them and contained in EVCI's June 14, 2005 press release were materially false and misleading because while Interboro's new student enrollments and revenues may have been up, defendants failed to disclose that those new enrollments and increased revenues resulted from a fraudulent admissions process as set forth at ¶¶ 47-56; 77-81 above.

**DD. Form 10-Q For The Second Quarter of 2005**

EVCI's Form 10-Q for the second quarter of 2005 reported a 34% increase in enrollment for its 2005 spring semester over 2004 and a 66% increase in revenue for the second quarter, or \$3,823,000, to \$9,656,000 from \$5,833,000 for the second quarter 2004. The Company also said that:

We expect that Interboro's rate of growth will continue to exceed industry averages in 2005. Interboro's aggressive growth requires senior management personnel and other resources to ensure that the quality of Interboro's academic, administrative and financial operations continues to strengthen. Interboro plans to continue to increase its focus to improve its academic operations and to improve further its retention and graduation rates. We are always mindful of the increasing level of scrutiny we are subject to as we continue to grow aggressively.

160. Defendants knew or should have known that the statements made by them and contained in EVCI's Form 10-Q for the second quarter of 2005 were materially false and

misleading because while Interboro's new student enrollments and revenues may have been up, defendants failed to disclose that those new enrollments and increased revenues resulted from a fraudulent admissions process as set forth at ¶¶ 47-56; 77-81 above. Defendants also knew or should have known that contrary to their representations, Interboro was not providing the resources to support and retain the extraordinary number of new students it was admitting, putting its accreditation, and its ability to increase enrollment, in jeopardy as set forth at ¶¶ 35-39; 57-81 above. In addition, Interboro was not making substantial investments in Interboro or Interboro's students that would improve the Company's prospects for higher retention and graduation rates.

**EE. October 19, 2005 Press Release**

161. On October 19, 2005, EVCI announced that it had received the NYSED's draft report. Through a press release, EVCI revealed, in relevant part:

The draft report includes proposed findings, recommendations and determinations related to increasing admissions and improving academic standards and taking other measures to improve persistence and graduation rates. The recommendations include increasing the number and percent of full-time faculty, improving Interboro's libraries, improving other facilities and equipment resources and assessing and improving the quality of student learning. One of the proposed determinations was to deny extension center status for Yonkers. Accordingly, Interboro may not be able to enroll new students at its Yonkers site unless and until the Department decides to grant this site extension center status.

The draft report also includes assertions of irregularities in Interboro's admission practices. In response, the Audit Committee of EVCI's Board of Directors has engaged independent experts to conduct an investigation of the admission practices at Interboro. EVCI will not release enrollment Numbers for Interboro's fall 2005 semester until the impact of the results of the investigation can be assessed.

162. The October 19, 2005 was only a partial disclosure of the truth because defendants failed to disclose that the NYSED had stated that Interboro should cease expansion at *all* of its campuses and maintain enrollment at Fall 2005 levels. The press release was also

incomplete because EVCI did not release the draft report and only disclosed selected portions of the report to the investing public.

**FF. Form 10-Q For The Third Quarter of 2005**

163. EVCI's Form 10-Q for the third quarter 2005 reported that enrollments for the fall 2005 semester had increased to approximately 7600 as compared to approximately 3900 for the fall semester and that revenue for the quarter had also increased from \$6,509,000 to \$10,100,000. The Form 10-Q also generally described the findings of the draft report. The Company included NYSED's allegation that Interboro had changed admissions test scores so that more students received passing grades and that a financial aid representative encouraged a student to alter his income in order to qualify for grants, but stated that its own internal investigation had found "no evidence to suggest that any of these allegations were caused by the admissions department, or any goals reflected in Interboro's union agreement regarding minimum numbers of student admissions representatives must enroll or face disciplinary action." The Company said that it would abolish its policy that admission representatives enroll a minimum number of students, that it would increase faculty and staff, and would improve its facilities.

164. Defendants knew or should have known that the statements contained in the Form 10-Q for the third quarter of 2005 were materially false and misleading because while Interboro's new student enrollments and revenues may have been up, defendants failed to disclose that those new enrollments and increased revenues resulted from a fraudulent admissions process as set forth at ¶¶ 47-56; 77-81 above. In addition, as set forth at ¶¶ 47-56 above, the fraudulent admissions practices did, in fact, involve the admissions department and were the direct result of the quotas set by the executive officers of the Company - most notably, McGrath.

**GG. November 22, 2005 Press Release**

165. On November 22, 2005, EVCI issued a press release announcing the results of its internal “investigation” conducted by a law firm hired by defendants. The press release attributed the misconduct reported in the October 7, 2005 draft report to a few “rogue employees” despite the fact that the Company had a policy that its admissions representatives admit a certain number of students or face discipline. On this reported positive news, EVCI’s stock rose 33.3% from its opening price of \$2.15 that day to a close of \$3.13, trading at a much higher volume of 2.1 million shares as compared to the previous day’s volume of approximately 143,000 shares.

166. Defendants knew or should have known that the statements made by them and contained in EVCI’s November 22, 2005 press release were materially false and misleading because a few “rogue employees” were not responsible for the irregularities in EVCI’s admissions process. Rather, as set forth at ¶¶ 47-56 above, the fraudulent practices in the admissions process were widespread and well-known.

**HH. November 28, 2005 Conference Call**

167. On November 28, 2005, EVCI hosted in a conference call with analysts to discuss its third-quarter 2005 earnings. McGrath and Buntzman participated in the call. Buntzman represented that EVCI was “surprised by the draft report and its contents,” a contention that McGrath seconded. McGrath spoke about the investigation:

The investigation concluded that up to seven admissions test scores were changed by one tester at Interboro’s Yonkers site to permit students to pass. She claimed that she felt sorry for the prospective students who were trying to pass the admissions test. The investigations could not corroborate or refute, other than by receiving a verbal denial, the State Education Department’s allegation that a tester at Interboro’s Flushing Extension Center changed a test score.

\* \* \*

The investigation also concluded a financial aid representative at Interboro's Yonkers site appears to have participated in improper or inappropriate discussion, which he believed he had with a prospective student. The financial aid officer, in multiple interviews with investigators, repeatedly denied the State Education Department's claim that he told an individual to produce a notarized statement which would misrepresent his income so he would be eligible for financial aid. The investigators believed, however, that the evidence provided by the SED and that the financial aid representative's demeanor and description of his work raised serious questions as to his reliability. Assuming the State Education Department's allegation to be true, the investigators concluded that it was an isolated event and that it is not a pervasive problem at Interboro.

Furthermore, the investigation found no evidence to suggest that any of these allegations were caused by the admissions department or any goals reflected in Interboro's union agreement regarding minimum numbers of student admissions representatives must enroll or face disciplinary action. That provision of the union agreement is being deleted.

The investigators found only one instance in which an admissions representative was terminated for poor performance, and further, that this termination resulted from performance issues broader than the mere number of students admitted.

EVCI's Joseph Looney, who replaced Goldenberg as EVCI's CFO when he relinquished his position on October 1, 2005, also participated in the call. Looney spoke of gaps in EVCI's financial control:

[W]e've identified some gaps and some significant deficiencies in our internal control over financial reporting. Those may or may not rise to the level of material weakness. We haven't completed our financial assessment as of yet. We intend to complete that financial assessment sometime before December 31<sup>st</sup>. And once we do that, we need to actually bring our outside auditors in to complete their assessment and their testing of our system.

168. Defendants knew or should have known that the statements made by them on the November 28, 2005 conference call were materially false and misleading because it was not just a few "rogue employees" who were responsible for the irregularities in EVCI's admissions process. Rather, as set forth at ¶¶ 47-56 above, the fraudulent practices in the admissions process were widespread and well-known. Moreover, as set forth at ¶¶ 47-56 above, the fraudulent

admissions practices did, in fact, involve the admissions department and were the direct result of the quotas set by the executive officers of the Company - most notably, McGrath.

## **VII. DEFENDANTS' SCIENTER**

169. The facts set forth herein raise a strong inference that each EVCI and the Individual Defendants acted with scienter. Buntzman, McGrath, and Goldenberg (i) knew or should have known that the statements they made, or were responsible for making, were false and misleading and (ii) had motive and opportunity. Additionally, circumstantial evidence raises a strong inference of scienter.

### **A. Defendants Knew or Should Have Known of the Fraudulent Manner in which Interboro Increased Its Enrollments**

170. As set forth in detail above at ¶¶40-4; 47-56; 77-81, defendants knew or should have known about the fraudulent manner in which Interboro increased its enrollments during the Class Period. During the Class Period, EVCI aggressively enrolled an extraordinary number of students based on an express policy that its admissions officers meet a quota or face potential termination. As a result of the policy – which defendants were responsible for carrying out and overseeing – fraud in admissions at Interboro became so prevalent that NYSED operatives posing as potential students received false passes at two separate locations, Yonkers and Flushing. These practices were confirmed by Lead Counsel's investigation as set forth at ¶¶47-56 above. As CW#1 said, “[T]hey were very aggressive and did whatever they needed to do to make their numbers.”

171. Defendants’ pass rate for acceptance into Interboro was the minimum ATB pass rate to qualify for federal grants, which Interboro needed its students to obtain in order for Interboro to get paid. Defendants would give prospective students multiple opportunities to pass the ATB exam, underscoring that Interboro’s goal was quantity over quality of students.

Defendants claimed later that a “few rogue employees” were responsible for the admissions irregularities; however, it was the Individual Defendants, and not their employees, who threatened to punish Interboro’s admissions representatives if they failed to admit a certain number of students.

**B. Defendants Knew or Should Have Known of the Risk of Sanctions**

172. The Individual Defendants, as senior officers of the Company, knew or should have known that Interboro was at risk of facing sanctions from the NYSED if it did not comply with the state and federal regulations.

173. First, the Board of Regents Handbook of Institutional Accreditation laid out what the minimum expectations of the NYSED included. Defendants knew or should have known that they were not in compliance with these minimum standards. Moreover, and underscoring that the defendants knew or should have known that they were not in compliance with the NYSED’s requirements, are the conditions imposed upon Interboro by the NYSED prior to the Class Period, when the Board of Regents granted Interboro accreditation on June 9, 2003. The conditions included increasing Interboro’s graduation and job placement rates significantly. Defendants knew or should have known that lowering Interboro’s admission standards to admit more students – many of whom did not even pass the ATB test – and failing to adequately support its increased student body -- would result in a lower percentage graduation rate. Defendants knew or should have known that having a less capable student body with fewer resources available to it, would not increase its job placement percentage as per the conditions, but would likely decrease job placement. The conditions also included documenting faculty. The NYSED investigation found no evidence that Interboro ever documented faculty. The Individual Defendants' positions within the Company dictated that they were responsible for

ensuring that this condition was carried out. By wholly ignoring this condition and the others, defendants knew or should have known that they were putting Interboro's accreditation at risk.

174. Defendants also knew that the NYSED would be investigating Interboro. In fact, in the NYSED's final report, the State points to a letter dated December 6, 2004, in which it notified EVCI that Interboro would be subject to a thorough review to see if it was capable of expanding. As such, defendants knew or should have known that there was no way that Interboro would pass muster under any review in the condition that it was in because it was not providing the minimum support the NYSED required for the extraordinary number of students it was admitting.

175. Defendants also knew or should have known that Interboro's Yonkers site would be denied extension-center status on or shortly after June 15, 2005, when the NYSED sent Interboro a letter stating as much, according to the final report. Significantly, this was over four months before the Company ever disclosed to the market that this was a risk and nearly six months before it announced that extension-center status had, in fact, been denied for the Yonkers site. Furthermore, defendants knew or should have known that the NYSED would not approve Interboro's Yonkers site as an extension center throughout the Class Period. Defendants knew that the Institute was not complying with the NYSED's minimum standards and that Interboro would not measure up under scrutiny. Defendants knew that they were not providing proper support nor retaining students at the minimum levels set forth by the NYSED.

176. The Defendants also knew or should have known that Interboro's projected growth that EVCI continually announced and upon which analysts relied in favorably rating EVCI common stock, was impossible to sustain due to the NYSED constraints. Defendants also knew or should have known that announcing Interboro's increased enrollments through press

releases and financial filings would attract the attention of the NYSED, who would then be alerted to the fact that Interboro was not in compliance with its mandates, including its expectation that Interboro decrease enrollment until it could increase its graduation rate, which would ultimately lead to sanctions. In fact, defendants were reminded that the NYSED expected it to reduce its enrollment in the letter dated March 2004, when the NYSED informed Interboro's President of that fact.

**C. Defendants Had Motive and Opportunity to Commit Fraud**

177. The Individual Defendants all owned EVCI stock and, therefore, had significant pecuniary interest in the price of stock and therefore had motive to artificially inflate its price and then sell it.

a. Insider Selling

178. Buntzman, McGrath, and Goldenberg all engaged in insider selling of their EVCI common stock, raising a strong inference of scienter. In total, these defendants disposed of approximately 960,000 shares of stock during the Class Period for proceeds of nearly \$7 million.

179. On March 23, 2004, the NYSED sent a letter to Interboro's President that confirmed that Interboro had agreed to use a new screening mechanism that would result in decreased enrollments. Defendants knew or should have known at this time that decreased enrollments would negatively affect the price of Interboro's stock because, among other things, analyst reports pointed to growing enrollments when recommending EVCI stock and most of EVCI's revenues come from enrollments at Interboro.

180. On April 2, 2004 – just days after learning that it was to decrease enrollments – Buntzman, McGrath, and Goldenberg dumped 500,000 shares of their EVCI common stock, for \$11.50 a share for proceeds of over \$5 million. On April 2, 2004, Buntzman sold 80% of his

stock, 310,000 shares, for \$3.56 million; McGrath sold 81.5% of his stock, 150,000 shares, for \$1.72 million; and Goldenberg sold 65% of his stock, 40,000 shares, for \$460,000.

181. Buntzman made another sale of his stock earlier in the Class Period. On November 12, 2003, Buntzman sold 300,000 shares of EVCI common stock at \$4.00 per share for proceeds of \$1.2 million. According to a press release issued by EVCI that day, Buntzman needed to make the stock sale “in order to raise money in anticipation of the equitable distribution of marital assets in a pending divorce.” However, in a divorce decision, the court noted that the November 12, 2003 sale was “made without [Buntzman’s former wife’s] consent and in violation of an interim order limiting the transfer of the parties’ assets.” *Mahoney-Buntzman v. Buntzman*, 11 Misc.3d 869, 876 n.1 (NY Sup. Ct. Westchester County 2006).

**D. Circumstantial Evidence Raised a Strong Inference of Scienter**

182. There is also overwhelming circumstantial evidence raising a strong inference of scienter that the Individual Defendants knew that the projections of EVCI in their public statements were unreasonable and unattainable; and that Interboro was facing devastating sanctions from the NYSED of which they were aware.

183. Repeatedly, the Company and Individual Defendants took action and made statements contrary to the reality of Interboro’s situation. For example, in its press releases and financial statements touting its enrollment growth, defendants never mentioned that Interboro could not retain or sustain its growth and at the same time be in compliance with the NYSED.

184. Defendants also failed to make several other material disclosures. For instance, they failed to disclose that the NYSED expected them to decrease enrollment and that it had confirmed so in a letter to Interboro’s President in a letter dated March 23, 2004. Defendants also failed to disclose that the NYSED told defendants in a June 15, 2005 letter that given the deficiencies the NYSED had found, it would not grant extension-center status for Interboro's

Yonkers location. Defendants, in fact, waited until the NYSED's issued its final report on December 6, 2005 to share this news with the investing public, which was nearly half a year after defendants had actual knowledge.

185. Defendants also failed to correct analyst reports that predicted continuing increased enrollments at Interboro. Defendants did not disclose or correct analysts' reports after they were informed in December 2004 that the NYSED would be investigating; and they did not disclose nor did they correct analysts' reports after they learned that NYSED expected Interboro to reduce enrollments in March of 2005. To the contrary, the Individual Defendants dumped their stock, as the investing public was encouraged to hold onto its stock. Finally, among other things, defendants did not disclose or correct analysts' reports after learning on June 15, 2005 that the NSYED had identified deficiencies and would be denying extension-center status to Interboro's Yonkers site.

## **VIII. CLAIMS FOR RELIEF**

### **COUNT ONE**

#### **For Violations of Section 10(B) of the Exchange Act and Rule 10b-5 Promulgated Thereunder**

186. Lead Plaintiff repeats and realleges each and every allegation contained above as if fully set forth herein.

187. Throughout the Class Period, defendants, directly and indirectly, by the use of means and instrumentalities of interstate commerce, the United States mails, and a national securities exchange, employed a device, scheme, and artifice to defraud, made untrue statements of material fact, and omitted to state material facts necessary in order to make the statements made, in light of the circumstances under which they were made, not misleading, and engaged in

acts, practices, and a course of business which operated as a fraud and deceit upon the Lead Plaintiff and Class members.

188. EVCI and the Individual Defendants, as the most senior officers of EVCI during the Class Period, are liable as direct participants in all of the wrongs complained of herein. Through their positions of control and authority, the Individual Defendants were in a position to and did control all of the Company's false and misleading statements and omissions, including the contents of all its public filings and press releases as more particularly set forth above. In addition, the false and misleading statements made in the Company's published documents (including its press releases and publicly issued financial statements) constitute "group published information," which the Individual Defendants were responsible for creating. The Individual Defendants had direct involvement in the daily business of the Company and participated in the preparation and dissemination of the Company's "group published" documents. The Company is liable for each of the statements of the Individual Defendants through the principles of respondent superior.

189. As detailed above, the defendants had actual knowledge of the misrepresentations and omissions of material facts set forth herein, or acted with reckless disregard for the truth in that they failed to ascertain and to disclose such facts, even though such facts were available to them. Such material misrepresentations and/or omissions were made knowingly or recklessly and for the purpose and effect of concealing EVCI's operating condition, finances, and present and future business prospects from the investing public and supporting the artificially inflated price of its securities.

190. Lead Plaintiff and other members of the Class relied upon the defendants' statements and upon the integrity of the market in purchasing shares of EVCI common stock at artificially inflated prices.

191. In bringing these claims, Lead Plaintiff and the members of the Class are entitled to the presumption of reliance established by the fraud-on-the-market doctrine. At all times relevant to this Complaint, the market for EVCI common stock was an efficient market for the following reasons, among others:

- a. EVCI common stock traded on the NASDAQ, a highly efficient market. The average weekly trading volume through the Class Period was 685,212 shares;
- b. As a regulated issuer, EVCI filed periodic public reports with the SEC;
- c. Numerous securities analysts followed EVCI and wrote reports that were distributed and publicly available and entered the public marketplace;
- d. EVCI regularly issued press releases, which were carried by national news wires. Each of these releases was publicly available and entered into the public marketplace; and
- e. The market price of EVCI common stock reflected the news disseminated in the market.

192. As a direct and proximate cause of the wrongful conduct described herein, Lead Plaintiff and the other members of the Class suffered damages in connection with their purchases of EVCI common stock. Had Lead Plaintiff and the other members of the Class known of the material adverse information not disclosed by the defendants, or had been aware of the truth behind the defendants' material misstatements; they would not have purchased EVCI stock at artificially inflated prices.

193. This claim was brought within two years after the discovery of the fraud and within five years of the making of the statements alleged herein to be materially false and misleading.

194. By virtue of the foregoing, the defendants violated Section 10(b) of the Exchange act and Rule 10b-5 promulgated thereunder and are liable to Plaintiff and the members of the Class, each of whom has been damaged as a result of such violations.

## **COUNT TWO**

### **For Violations of Section 20(a) of the Exchange Act**

195. Plaintiff repeats and realleges each and every allegation contained above as if fully set forth herein.

196. Throughout the Class Period, the Individual Defendants, by virtue of their positions, stock ownership, and/or specific acts described above were controlling persons within the meaning of Section 20(a) of the Exchange Act.

197. The Individual Defendants had the power to, and did, directly and indirectly, exercise control over EVCI and Interboro, including the content and dissemination of statements which the Lead Plaintiff allege are false and misleading. The Individual Defendants were each provided with and had access to reports, filings, press releases and other statements alleged to be misleading prior to and/or shortly after they were issued and had the ability to prevent the issuance or to correct the statements. The Individual Defendants had direct and supervisory involvement in the day-to-day operations of the Company and induced EVCI to engage in acts constituting violations of the federal securities laws, as set forth in Count One above.

198. Individual Defendant Buntzman exercised control over the Company through his position of Chairman of the Board of EVCI and Chancellor of Interboro. Additionally, as

alleged above, Buntzman had the ability to control the Company's financial statements, public statements, and operations, and exercised such control throughout the Class Period, both adopting and directly disseminating false information to the market through signing financial statements, such as the 10-KSBs, Form 8-Ks, and Form S-3s, or by causing such information to be disseminated through press releases and analyst calls. Buntzman also exercised control over EVCI's financial reporting through his management responsibilities and his certification of the Company's fraudulent statements. Moreover, Buntzman was under an executive employment contract for the entire class period.

199. Individual Defendant McGrath exercised control over the Company through his position as CEO of EVCI and Interboro, and Vice Chairman of Interboro. Additionally, as alleged above, Buntzman had the ability to control the Company's financial statements, public statements, and operations, and exercised such control throughout the Class Period, both adopting and directly disseminating false information to the market through signing financial statements, such as the 10-KSBs, 10-Qs, Form 8-Ks, and Form S-3s, or by causing such information to be disseminated through press releases and analyst calls. McGrath also exercised control over EVCI's financial reporting through his management responsibilities and his certification of the Company's fraudulent statements. Moreover, McGrath was under an executive employment contract for the entire class period.

200. Individual Defendant Goldenberg exercised control over the Company through his position as CFO of EVCI throughout the Class Period and Interboro until October 1, 2005 for the majority of the Class Period. Additionally, as alleged above, Goldenberg had the ability to control the Company's financial statements, public statements, and operations, and exercised such control throughout the Class Period, both adopting and directly disseminating false

information to the market through signing financial statements, such as the 10-KSBs, 10-QSBs, 10-Qs, and S-3s or by causing such information to be disseminated through press releases. Goldenberg also exercised control over EVCI's financial reporting through his management responsibilities and his certification of the Company's financial statements. Moreover, Goldenberg was under an executive employment contract for the entire class period.

## **IX. LOSS CAUSATION**

201. Defendants' wrongful conduct, as alleged herein, directly and proximately caused the damages suffered by Lead Plaintiffs and the Class.

202. During the Class Period, Lead Plaintiff and the Class purchased securities of EVCI at artificially inflated prices and were damaged thereby. The prices of EVCI securities declined when the misrepresentations made to the market, and/or the information alleged herein to have been concealed from the market, and/or the effects thereof, were revealed, in whole or in part, causing investors' losses.

## **X. INAPPLICABILITY OF STATUTORY SAFE HARBOR**

203. The statutory safe harbor provided for forward-looking statements under certain circumstances does not apply to any of the allegedly false statements pleaded in this complaint. Many of the specific statements pleaded herein were not identified as "forward-looking statements" when made. To the extent there were any forward-looking statements, there were no meaningful cautionary statements identifying important factors that could cause actual results to differ materially from those in the purportedly forward-looking statements. Alternatively, to the extent that the statutory safe harbor does apply to any forward-looking statements pleaded herein, defendants are liable for those false forward-looking statements because at the time each of those forward-looking statements was made, the particular speaker knew that the particular forward-looking statement was false, and/or the forward-looking statement was authorized

and/or approved by an executive officer of EVCI who knew that those statements were false when made.

**PRAYER FOR RELIEF**

WHEREFORE, Lead Plaintiff prays for judgment as follows:

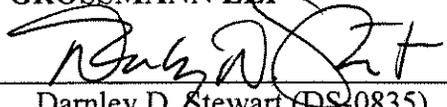
- A. Determining this action to be a proper class action pursuant to Rule 23 of the Federal Rules of Civil Procedure;
- B. Awarding Lead Plaintiff and members of the Class compensatory damages;
- C. Awarding Lead Plaintiff and members of the Class pre-judgment interest and post-judgment interest, as well as their reasonable attorneys' fees, expert witness fees, and costs;
- D. Awarding extraordinary, equitable and/or injunctive relief as permitted by law, equity and the applicable federal statutory provisions, pursuant to Rules 64 and 65 of the Federal Rules of Civil Procedure, and any appropriate state law remedies , to assure that the Class has an effective remedy; and
- E. Awarding such other relief as this Court deems just and proper.

**JURY TRIAL DEMANDED**

Lead Plaintiff hereby demands a trial by jury.

Dated: July 21, 2006

**BERNSTEIN LITOWITZ BERGER  
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By: 

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