

perpetual inventory records as being so convoluted that it was impossible for anyone to establish reliable inventory figures at any given time. Ironically, the proposed acquisition of Gitto Global's compounding business by VitroTech, as discussed extensively below, foundered due to the inability of VitroTech and its auditors to determine the true value of the company's inventory.

The overstatement of inventory values was further effected by "substituting" higher values or quantities for inventory that Gitto Global actually did purchase. Ms. Merchant advised the Examiner that Mr. Minardi would deliver a month-end inventory report to Maria Miller. Ms. Miller would then review the report and instruct Ms. Merchant as to what quantities or prices of inventory to adjust in the computer inventory system. As an example, Ms. Merchant stated that she was instructed by Maria Miller to adjust in the company's records the value of a product named FR720 from \$2.25 a pound to \$17.50 per pound. Ms. Merchant also described increasing at various time the costs of Teflon and reclassifying Vitrolite 325 as Vitrolite 800, a higher cost product. Other finished products whose prices Ms. Merchant increased at the direction of Ms. Miller included FC569R, FC683, GPE80 and GPE80405.

Ms. Merchant further stated that after she made these upward adjustments in the system, she would give the revised reports to Mr. Deakin, who would then tell her if further adjustments were necessary to increase inventory values. Mr. Deakin would often tell her that he had to check with Frank Miller to see if further adjustments were necessary to ensure compliance with the company's bank requirements. If further adjustments were needed, Mr. Deakin would tell Ms. Merchant. Ms. Merchant in turn would tell Maria Miller, who would then instruct Ms. Merchant as to which inventory values or quantities to change.

### **3. Deception of Bank Auditors**

The manipulation of Gitto Global's internal records was effected so that the company could report a higher borrowing base to LaSalle and its prior lenders, all of whom would periodically send auditors to test the accuracy of the reported amounts. In preparation, Gitto Global would take remarkable steps to mask the alteration of its inventory records.

Ms. Powell-Kotoch, Mr. Slattery and Mr. Deakin advised the Examiner in separate interviews that prior to an auditor visit, boxes of existing inventory or newly-created inventory were relabeled to reflect products with higher unit values. In the latter case, new inventory with low unit values would be manufactured, but labeled with the name of a higher value product to increase the reported overall value of the company's inventory. During his interview with the Examiner, Mr. Minardi described a notebook that he kept to record these activities and how he had been taught to keep this notebook by his predecessor at the company. The so-called "Minardi notebook" was kept by hand so that when boxed inventory was renamed or repriced, the nature of the relabeling was recorded so that any changes could be reversed after the auditors left. Minardi stated that he provided copies of his notes to Frank Miller. In his interview, Mr. Slattery stated that Frank Miller would direct Maria Miller to alter inventory identifiers and she would, in turn, organize and personally apply labels to boxes of inventory to increase their purported value.

Ms. Merchant also stated that when LaSalle auditors were expected, a physical inventory count was made on the weekend before the visit and the inventory in the computer system was changed to match the physical count. The new inventory reports would then be given to Frank Miller and Maria Miller so they could prepare for their interactions with the auditors.

## **F. Misrepresentation of Accounts Receivable Values**

### **1. Overview**

Accounts receivable represented the other category of assets included in Gitto Global's borrowing base. According to Mr. Deakin, the company has overstated the value of its accounts receivable to lenders since at least 1998. As with its overstatement of inventory, Gitto Global manipulated its internal accounting records in several different ways to inflate the value of its accounts receivable. Amounts due from actual customers were arbitrarily increased; separate entities controlled by the Gitto Principals that apparently conducted no actual business operations were listed as material account debtors; and vendors were also listed as customers that owed significant sums to Gitto Global. It appears that, as with inventory records, Frank Miller was directly involved in the day-to-day manipulation of the company's accounts receivable records. Further, it again appears that purposeful steps were taken to deceive auditors attempting to verify the company's reported account balances.

### **2. Manipulation of Internal Accounts Receivable Records**

The overall process by which the accounts receivable manipulation worked generally remained unchanged over time, regardless of which entity Gitto Global used to create its fictional accounts receivable. Maria Miller would enter a false sale into the company's computer system. Mr. Childs, who managed the company's shipping department, would then create a false shipping document indicating that the product "sold" by Maria Miller had in fact been shipped. An invoice was then generated and a corresponding receivable created and entered into the company's general ledger. Once in the general ledger, the manufactured account would be included in borrowing base certificates provided to LaSalle and other lenders.

Mr. Deakin advised the Examiner that the fraudulent nature of these accounts receivable could only be discovered if an auditor asked to see the specific details of a fictitious sales

transaction during the course of an audit. At least from December 2001 forward, moreover, when an auditor requested supporting documentation for a fraudulent transaction, Gitto Global had the technological capability simply to print fictitious invoices and shipping documentation from its Wang computer system. Separately, as discussed below, the Gitto Principals appear to have caused the company to disburse substantial sums of money to legal entities directly or indirectly controlled by them, which would promptly remit back to Gitto Global most or all of the funds. The remitted funds were characterized by Gitto Global as "sales receipts" and applied as payment of fictitious or overstated invoices. The receipts allowed Gitto Global both to turn its accounts receivable in a timely fashion and to pay down the company's loan obligations.

Frank Miller appears to have played a central, hands-on role in causing false documentation to support fictitious accounts receivable. Mr. Deakin stated that Mr. Miller installed Versacheck software on Mr. Deakin's computer to enable him to create checks from third parties payable to Gitto Global to match up with fictitious invoices in the event of a verification request from an auditor. V&L confirmed on December 6, 2004, that this program was installed in Mr. Deakin's computer. Unfortunately, Mr. Deakin did not store any Versacheck files on his hard drive, making it impossible to ascertain the exact nature of the documents created.

Mr. Deakin also stated that a software program named "Paper Port" was installed on Mr. Miller's computer to enable the creation of other false documents. He further stated that computers in the offices of both Mr. Miller and Mr. Deakin had scanners so that documents, including genuine checks received from customers, could be scanned into a computer and altered as needed as "back-up" for a challenged receipt. Notwithstanding Mr. Deakin's memory, the Examiner did not locate Paper Port software on Mr. Miller's computer. However, Mr. Miller's

computer “crashed” in the spring of 2004 and he began operating with a new laptop computer. It is possible that his previous computer did contain Paper Port files.

Mr. Deakin identified to the Examiner one John Moritz, who now resides in Blue Bell, Pennsylvania, as an individual who formerly worked at Gitto Global and who taught Mr. Miller how to scan documents into a computer so that the documents could subsequently be altered. Mr. Deakin stated he was not proficient at creating false documents and that Mr. Miller sought Mr. Moritz’s advice in this regard. After Mr. Moritz left Gitto Global, he allegedly continued to assist Mr. Miller with the falsification of documents. The Examiner has received a copy of a September 20, 2000 communication from Mr. Miller to Mr. Moritz, a copy of which is submitted herewith as Exhibit 21. The document contained approximately 20 pages of invoices to Gitto Global from suppliers and the typewritten portion of the fax states as follows: “I wrote the changes on one invoice and sent an extra invoice for you to work your magic.” Underneath that entry and written in black print is: “John: My home phone is 978-779-2913. Thanks. Frank. My email is [mijen@mediaone.net](mailto:mijen@mediaone.net).” Mr. Moritz received numerous “commission” payments from Gitto Global. He is listed as vendor #52003 in the Debtor’s general ledger, which reflects that between January 15, 1997 and December 22, 2003, the company paid to him a total of \$65,009.12.

Steven Snyder, an investigator for LaSalle, has spoken with Mr. Moritz and reports that Mr. Moritz describes himself as a chemist who developed over 1,000 chemical formulas for Gitto Global between 1996 and 2001. Mr. Moritz acknowledged to Mr. Snyder that since 2001, he has worked for Gitto Global as a consultant. Mr. Snyder asked Mr. Moritz whether he used a scanner to create checks and other false documents to reflect artificially inflated sales by Gitto

Global. Mr. Moritz did not deny that he had but stated that he wanted to seek advice of counsel before making further comment in this regard.

### **3. Deception of Bank Auditors**

In addition to the day-to-day manipulation of the company's internal accounts receivable records, Gitto Global would periodically need to take steps to reply to audit requirements imposed by its lenders. The Examiner has been provided with a number of account verification letters dated January 15, 2004 that purportedly were sent to various of Gitto Global's customers, copies of which are collectively submitted herewith as Exhibit 22. It appears that LaSalle required that Gitto Global obtain these confirmation in an effort to verify the reported value of the company's accounts receivable. Each of the customers was asked in the form to confirm the accounts receivable figures listed in the letter. Although each of the accounts receivable verifications appeared to have been executed on behalf of the company's customers, the Examiner has substantial doubts that all of the signatures are genuine. Among other things, the figures contained in the letters are vastly higher than what appear to be the Company's actual sales (if any) to the listed customers.

The Examiner noted that the verification forms appeared to have been transmitted by facsimile from Mr. Pellegrine's business office. In his initial interview with the Examiner, Mr. Pellegrine (after initially denying that he had any role in sending the verifications out) acknowledged that Mr. Miller had asked him to send out some receivable verifications in January 2004. He advised that Gitto Global filled out the address and the amount of the receivable and sent them to Mr. Pellegrine, who in turn sent the verifications out and asked that they be returned to him. Among the customers to whom verifications were directed was Hemisphere Distribution Corporation, which is discussed extensively in the Appendix to this Report. The verification produced to the Examiner reflects that Hemisphere owed Gitto Global

in excess of \$2 million. Mr. Pellegrine advised the Examiner that Hemisphere conducted essentially no business operations and could not possibly owe that sum to Gitto Global. After this initial interview, Mr. Pellegrine invoked his Fifth Amendment rights and refused to speak further with the Examiner.

Generally, it appears that the accounts receivable verification process was manipulated by Mr. Miller and possibly, at Mr. Miller's apparent direction, Mr. Pellegrine. The Examiner is of the view that Mr. Pellegrine's role in the verification process should be investigated further.

From interviews with Ms. Powell-Kotoch, Mr. Slattery and Mr. Deakin, it appears that Gitto Global also "pre-billed" its customers as a means of inflating its accounts receivable since the early 1990's. "Pre-billing" describes a practice whereby a legitimate order is received from a customer but, before the product is produced and shipped, records are purposefully altered to reflect an invoice submitted to the customer for that purchase as if the product has been produced and shipped. By pre-billing, Gitto Global generated a fictitious receivable that could be included on borrowing base certificates.

Mr. Deakin identified to the Examiner a problem with pre-billing that initially limited its usefulness. If a customer called to cancel an order that had been pre-billed, Gitto Global either had to cancel the invoice (which, if it happened too often, might alert an auditor) or somehow show that this pre-billed invoice had been paid. As noted earlier, Mr. Deakin has stated that scanning devices and computer software were used to create customer checks to reflect "payment" of fictitious invoices. Such technology also could be used to demonstrate that questioned pre-bill invoice had been paid, despite the fact that the customer had cancelled the order. In addition, by routing Gitto Global funds to third party companies who in turn submitted

funds back to Gitto Global, Gitto Global could generate the flow of funds necessary to pay the cancelled “pre-bills.”<sup>17</sup>

Although it appears that pre-billing played a relatively minor role in the manipulation of accounts receivable values, the problem with pre-billing identified by Mr. Deakin was emblematic of a more general problem resulting from the overstatement of inventory and accounts receivable values. The manipulation of inventory and accounts receivable records to reflect a desired value at any particular time was largely an internal process of creating fictitious documents and data entries, with periodic additional steps as necessary to fend off auditor inquiries. For Gitto Global’s borrowing base to withstand to even modest scrutiny, however, it was imperative that the company show large sums of actual cash being received as sales proceeds and being disbursed by the company for inventory purchases. These imperatives required substantial external transactions with third-parties that were more difficult for the Gitto Principals to mask and control.

#### **G. False Reporting of Sales and Purchases**

V&L and the CRO have advised the Examiner that due to the corruption of the company’s records it would be a Herculean task to determine with precision Gitto Global’s actual annual sales or profits and losses for the years immediately prior to the Petition Date. In the course of its investigation, the Examiner was provided with dramatically conflicting sales reports generated by the Company. The company’s financial statements for the years ending June 30, 2001 and June 2002, as audited by Mr. Pellegrine, reflect annual sales of approximately

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<sup>17</sup> This pre-billing activity seemingly required the support of Mr. Childs because he had to generate false production and shipping documents to enable the invoice to be created. Mr. Childs has declined to be interviewed, citing his Fifth Amendment privilege.

\$91 million and \$121 million, respectively. Its financial statements for the fiscal year ended June 30, 2003 reflect annual sales in excess of \$160 million. Gitto Global's 2001, 2002 and 2003 financial statements are collectively attached hereto as Exhibit 23.<sup>18</sup>

There appears to be little doubt that the sales figures contained in the 2001, 2002 and 2003 financial statements are grossly overstated. As noted above, the company's controller, Mr. Deakin, and sales manager, Mr. Grimley, both advised the Examiner in separate interviews that Gitto Global's actual annual sales never exceeded approximately \$56 Million and dropped precipitously after September 11, 2001 and aggregated approximately \$40 Million per year after that. Moreover, the Elimination Report that V&L located on Mr. Deakin's computer and submitted herewith as Exhibit 6 allocates sales reported on the company's financial statements between its "compounding" business (which appear to approximate actual sales) and "brokerage" business (which appear to be fictitious sales). On the Elimination Reports, annual sales in the compounding business do not exceed \$50,100,000 for any fiscal year but are as high as \$84,000,000 in the brokerage business. The Examiner also has been provided with a letter dated October 11, 2002 from Mr. Miller to Legg Mason, a financial institution in Baltimore, Maryland, a copy of which is submitted herewith as Exhibit 24. The letter, which indicates that it was copied to Charles and Gary Gitto, states as follows:

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<sup>18</sup> There is some dispute as to whether Mr. Pellegrine audited the Company's 2003 statements or otherwise played a role in preparing those statements. The Examiner has been provided with a copy of the statements that bear an unsigned cover letter from Mr. Pellegrine, on his firm's letterhead, dated November 12, 2003. A copy of that letter is included in Exhibit 23. Mr. Deakin advised the Examiner that he observed a conversation during which Mr. Miller requested that Mr. Pellegrine prepare falsified 2003 audited financial statements that could be submitted to VitroTech in connection with its proposed acquisition of Gitto Global. Mr. Deakin further advised that Mr. Pellegrine complied with the request. Mr. Pellegrine denied Mr. Deakin's allegations and stated that he did not audit Gitto Global's 2003 financial statements but only "compiled" certain information to be included in those statements. He also claimed to have no knowledge of how the unsigned November 12, 2003 letter came to be attached to those statements.

We feel there is a strong synergy between Legg Mason and Gitto/Global Corporation. I have enclosed for your review the forecasted financial statement for the next (5) years going forward, and I have given you the past (3) years of financials using actual sales and margins and using restated expenses eliminating excess expenditures. We can back up how we arrived at this point to any third party. I have also enclosed a list of assets with the assumption that the bank debt and equipment debt will be retired at closing.

Attached to the cover letter are Gitto Global's income statements for the years ended June 30, 2001 and June 30, 2002 "Using Gross Margin & Excesses Eliminated." The statements reflect total sales of \$47,440,784 and \$36,494,885 for 2001 and 2002, respectively. Forecasted total sales for 2003 are shown as \$51,287,836, increasing to \$63,707,518 for fiscal 2007.

Gitto Global's internal records, stored on its Wang computer system, reflect annual sales amounts that are even more drastically overstated:

<u>Year</u>	<u>Sales</u>
1995	\$38,636,670.50
1996	\$42,866,143.37
1997	\$49,168,153.32
1998	\$52,635,223.88
1999	\$45,721,941.35
2000	\$52,235,190.63
2001	\$38,717,947.09
2002	\$95,402,321.60
2003	\$360,692,676.23
2004	\$688,800,392.61

The Examiner lacks sufficient information to reconcile fully the differences among the sales figures reported in the company's financial statements, the Eliminations Report, Mr. Miller's October 11, 2002 correspondence and its own accounting system.<sup>19</sup> From the

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<sup>19</sup> It is of note that the company's records reflect strikingly implausible sales *increases* beginning in 2002, the time at which, the Examiner has been advised, the company's actual sales materially *decreased* after the telecommunications industry weakened and the events of September 11, 2001 occurred. This is consistent with the Examiner's view that the contraction of Gitto Global's legitimate business operations, and presumably a corresponding decrease in cash flow and profitability, forced the Gitto Principals to take more and more extreme steps to mask the company's true financial condition and the sums being diverted to them.

information reviewed to date, however, it appears beyond question that the Company's internal sales records were purposefully manipulated to support the inflated inventory and accounts receivable balances that were included in borrowing base reports submitted to LaSalle and presumably other lenders. The Examiner has further determined that the company's internal sales figures were artificially inflated primarily by recording fictitious sales to the following seven (7) companies: Color Compounds and Consultants Inc. ("CCC"), Hitachi Cable Manchester Inc. ("Hitachi Cable"), J-Tan Sales and Marketing ("J-Tan"), Lake Electronic Cable ("Lake Cable"), Velco Chemicals, Inc. ("Velco"), Zebulon Industries Inc. ("Zebulon") and Hemisphere Distribution Corporation ("Hemisphere").

For the period 2001 to the Petition Date, Gitto Global recorded in its internal accounting system total sales of \$1,052,645,958.62 to these seven companies. It appears that CCC, Hitachi Cable and Lake Cable in fact were customers of Gitto Global, but the amounts actually sold to them were artificially inflated by vast sums. Velco and Zebulon appear to have been vendors to Gitto Global but were not customers. Nonetheless, Gitto Global's records reflect hundreds of millions of dollars in sales to those two companies. Hemisphere appears to have been incorporated and controlled at the direction of Frank Miller through Kathleen Carland, an associate of Mr. Miller and Mr. Pellegrine. While Hemisphere never appears to have conducted business operations, Gitto Global's internal records reflect sales to Hemisphere in excess of \$177,000,000 in fewer than three (3) years, all of which appear to be fictitious.<sup>20</sup> A detailed summary of Gitto Global's sales records in respect of the six companies, together with other

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<sup>20</sup> The creation and apparent manipulation of Hemisphere is discussed at some length in the Appendix.

information that the Examiner compiled that relates to the companies, is attached to this Report as the Appendix.

The manipulation of the company's internal sales records tracks the manipulation of its accounts receivable records, as discussed above, and was apparently directed by Frank Miller with substantial assistance by Maria Miller, Mr. Deakin and Ms. Chaisson. It appears that to keep track of the fictitious sales entered into the Company's records, Ms. Chaisson began to maintain a separate Excel spreadsheet that recorded bogus sales. The internal manipulation of sales records, however, led inexorably to the need to demonstrate both that the company was disbursing sufficient funds to purchase needed inventory and receiving actual cash to apply against recorded but fictitious sales.

The disbursement and receipt of actual cash by Gitto Global was, of course, more complicated than simply manipulating internal sales records. It required that the Gitto Principals establish separate entities which they could direct and control. Beginning as early as 1998, it appears that Gary Gitto began to establish separate legal entities which had no valid business purpose. Instead, he would cause Gitto Global to disburse funds to the entities and then direct the recipients to disburse such funds back to the company or for his personal benefit. Mr. Miller also directed that entities be established for the same purposes either directly under his control or through persons with whom he was associated. As discussed in the Appendix, the Examiner believes that each of the following entities (and possibly others) served in these roles: K&D Plastics; Direct Wood and Paper Products, Inc.; Direct Chemical; Direct Equipment; Equitech Technologies; Terracat; and Kingsdale Corporation d/b/a J&J Chemical Distributors. During the period from 2001 through the Petition Date, Gitto Global's internal records reflect payments to these entities in a combined amount in excess of \$1 billion. Kingsdale / J&J Chemical was of

particular importance to the activities directed by the Gitto Principals and the commencement of Gitto Global's Chapter 11 case and is discussed at length in Section V.G.1. below.

The cycling of funds to and from these entities closes the circle of Gitto Global's borrowing base deceptions. Payments disbursed by the company were primarily listed as being for the payment of inventory from vendors, which in turn supported artificially inflated inventory values against which the company would borrow. Payments received back from these entities were then applied to selected fictitious or overstated invoices that had been booked as accounts receivable. This allowed for the "payment" of accounts receivable before they became ineligible under the governing loan documents. Further, as cash was received by Gitto Global, its secured obligations were reduced to create borrowing availability. The cycle could then begin again. As additional benefits, the cycling of funds facilitated (and likely masked) the diversion of cash to the Gitto Principals for their personal benefit and generally allowed for the portrayal of the company as a far healthier enterprise than it actually was.<sup>21</sup>

#### **1. Kingsdale d/b/a J&J Chemical Distributors**

Kingsdale was incorporated in Massachusetts on January 25, 2001 by Thomas J. Sullivan, who also was listed as the corporation's sole officer and director. Kingsdale's principal place of business was listed as 77 Snead Drive, Mashpee, Massachusetts 02649. The company's

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<sup>21</sup> The Examiner also has been advised that the company's accounts payable were dramatically understated in its accounting system. Upon the CRO's arrival, accounts payable were recorded in the general ledger as totaling \$770,000. After determining that accounts payable for chemical suppliers were not being entered into the Gitto Global accounting system, and after a physical search of the Gitto Global premises for all vendor invoices, the CRO determined that actual accounts payable were at least \$14.6 Million. The Examiner was advised that Mr. Miller and Mr. Deakin directed Ms. Bartlett not to enter certain vendor invoices into the accounting system, but instead to simply place them in the bottom drawer of a filing cabinet that was initially located in Mr. Deakin's office and later in Ms. Bartlett's office. These invoices remained in this bottom drawer until Mr. Miller or Mr. Deakin instructed Ms. Bartlett which invoices could be paid. It was only after these invoices were paid that they would be entered into the computer system as actual accounts payables or a cost of sale. This drawer came to be known as the "secret garden," a nickname coined by Ms. Bartlett. While accounts payable were not a part of the borrowing base *per se*,

charter was filed by Todd N. Gleason of Bowditch & Dewey. Kingsdale apparently utilized the trade name "J&J Chemical Distributors," the name which appears in Gitto Global's records and on hundreds of checks payable to Gitto Global that were obtained by the Examiner

Mr. Sullivan is married to a niece of Frank Miller (Mr. Sullivan's father-in-law, Marvin Miller, is Frank Miller's brother) and resides on Cape Cod. Kingsdale appears to be at least the second company nominally controlled by Mr. Sullivan that appears as a vendor in Gitto Global's accounting system. According to Gitto Global's general ledger, it made multiple payments to "Sullivan Co." during the period December 7, 1998 to March 31, 1999 totaling \$2,936,009. The Examiner has been provided with documentation that strongly suggests Sullivan Co. was controlled by Mr. Sullivan and was utilized to receive payments from, and to return the same funds back to, Gitto Global. It also appears that Mr. Sullivan received a "consulting" fee for facilitating the cycling of funds. The relationship between Gitto Global and Sullivan Co. is discussed in more detail in the Appendix.

It appears that Kingsdale rapidly became the primary fictitious vendor utilized to funnel funds out of Gitto Global, as "inventory purchases," and then back to the company, as "sales receipts." Gitto Global's general ledger, in which J&J Chemical appears as Vendor No. 2713, reflects the following aggregate annual amounts of payments to Kingsdale/J&J Chemical:

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the understatement of accounts payable would have the effect of exaggerating the liquidity and general health of Gitto Global's business

<u>Year</u>	<u>Amount</u>
2000	\$ 0
2001	\$ 45,452,553.75
2002	\$ 91,748,975.82
2003	\$ 324,658,354.50
2004	\$ 658,608,397.50
<b>TOTAL PAYMENTS</b>	<b><u>\$1,120,468,281.57</u></b>

It is not clear whether all of the above ledger entries reflect actual cash transfers by Gitto Global to Kingsdale. There is no question, however, that very substantial sums of cash were in fact paid by Gitto Global to Kingsdale and deposited in the J&J Chemical Account at Clinton Savings Bank, as discussed at length in Section V.H. Some of these funds were diverted from the J&J Chemical Account to Mr. Miller personally or for his personal benefit. The remaining funds, in extraordinary amounts, appear simply to have been repaid to Gitto Global, often on the same day they were deposited in the J&J Chemical Account, for deposit in Gitto Global's "lockbox" account at Fleet National Bank. Those funds were then transferred from the lockbox to LaSalle and used to pay-down Gitto Global's secured loan obligations. LaSalle has alleged that the total amount paid from Kingsdale to Gitto Global during the period July 2002 – September 2004 exceeds \$1.1 billion. LaSalle Complaint at ¶65. The Examiner has not reviewed any credible evidence that Kingsdale ever conducted actual business operations.

On October 25, 2004, the Examiner conducted a brief telephone interview with Mr. Sullivan. Mr. Sullivan advised that Frank Miller approached him in or about January 2001 and asked if Mr. Sullivan were interested in becoming involved with a company that would import and export plastics. Mr. Sullivan agreed to become involved and signed incorporation papers that were prepared for him by, to his recollection, Mr. Miller or Mr. Miller's attorney. He requested that Mr. Miller keep him up-to-date on the progress of the venture. Mr. Sullivan

advised, however, that to his knowledge the venture did not go forward and that he requested some time later that Mr. Miller remove him as an officer of the corporation. He further stated he knew nothing else about Kingsdale's activities.

The Examiner asked if Mr. Sullivan had opened a depositary account on Kingsdale's behalf. Mr. Sullivan responded that he recalled that Frank Miller had made a stamp of Mr. Sullivan's signature and that he thought the signature stamp of his name "may have been used to open a bank account." Mr. Sullivan advised that he never worked for Gitto Global or had any financial interest in the company. After this initial interview with the Examiner, both Mr. Sullivan and his father-in-law, Marvin Miller, invoked their Fifth Amendment rights and declined to be further interviewed or examined.

Mr. Deakin advised that when Kingsdale was formed, Charles Gitto made an initial deposit of \$1,5000,000 into the J&J Chemical Account at Clinton Savings Bank.<sup>22</sup> In exchange, Mr. Deakin further advised, Frank Miller and Gary Gitto each executed a promissory note payable to Charles Gitto in the principal amount of \$1,500,000 and granted mortgages on their homes to secure repayment of such notes. Mr. Deakin also advised that the payments from Gitto Global to J&J Chemical were recorded as a "cost of chemicals" and that payments received by Gitto Global from J&J Chemical were treated as sales receipts and applied against invoices previously recorded as fictitious sales to various entities, primarily the seven companies discussed in the Appendix. He further stated that the amount of funds cycled through the J&J Chemical Account increased exponentially over time because the company's actual sales had decreased significantly but expenses had not been reduced, erasing any ability to generate

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<sup>22</sup> Clinton has denied, through its counsel, that Charles Gitto made such deposit. Clinton instead asserted that the initial deposit to the account was in the amount of \$250,000 and was drawn on a Gitto account at Guaranty.

profits, while the Gitto Principals continued to misappropriate corporate funds for their personal benefit.

Ms. Bartlett, Gitto Global's accounts payable manager, stated to the Examiner that she never saw an invoice from Kingsdale or J&J Chemical. She further stated that initially Gitto Global might issue one check per day to J&J Chemical, but by 2004, the company was writing 45 to 50 checks a day to J&J Chemical. Ms. Bartlett typically gave these checks to Mr. Deakin or Ms. Chaisson. Ms. Bartlett stated that she did not think that J&J Chemical was a "real" company but did not want to verify that suspicion. She once asked Mr. Deakin why they were writing so many checks to J&J and he responded by saying that multiple checks allowed J&J Chemical to receive quicker credits to its account. Ms. Bartlett believed that his explanation did not make sense.

#### **H. Clinton Savings Bank**

From the date of the Examiner's appointment, it was apparent that the depositary account established at Clinton by Kingsdale / J&J Chemical (the "J&J Chemical Account") was central to Gitto Global's borrowing base fraud. The Examiner, consequently, devoted substantial resources in an effort to ascertain the nature of the Kingsdale/Clinton Savings/Gitto Global relationship and whether Clinton Savings understood the manner in which the J&J Chemical Account had been manipulated and took any steps to intervene. The Examiner interviewed the following representatives of Clinton:

- a. Michael D. Tenaglia, Senior Vice President;
- b. Robert J. Paulhus, Jr., Vice President Commercial Lending; and
- c. David A. Harmon, Assistant Vice President Commercial Lending

The Examiner also reviewed records produced by Clinton in response to a subpoena.

From the three interviews and the review of records, the Examiner has determined that some years ago Frank Miller personally had a loan from and an account at Clinton Savings and also served as an "incorporator" for the Bank. This is an honorary title which, according to Clinton, has no significance in Clinton's day-to-day operations. Incorporators apparently serve as goodwill ambassadors on behalf of Clinton in the local community. There are approximately 115 incorporators for Clinton. They gather once a year for an annual meeting which is a social as well as a business gathering.

In early 2001, Mr. Miller presented a document purporting to be a board vote of Kingsdale Corporation authorizing the opening of the J&J Chemical Account. The document was signed by a Thomas Sullivan as President, Treasurer and Clerk. An account signature card was signed on February 12, 2001 naming Frank Miller and Thomas J. Sullivan as authorized signatories on the J&J Chemical Account. Sullivan and Miller remained the signatories on the account until September 26, 2002 at which time Sullivan was removed as a signatory and John Tersigni was inserted as an authorized signatory.<sup>23</sup>

There is no evidence that Clinton did any kind of due diligence on Kingsdale Corporation to verify independently its corporate status. Clinton apparently did not require any documentation from Frank Miller showing that he maintained an ownership interest in the entity or what authority he held to act on behalf of Kingsdale, other than to file a corporate vote to authorize the opening of the account and naming authorized signatories.

Clinton allegedly had a policy to allow commercial checking account customers to draw on uncollected funds. Clinton did not have an established limit on the dollar value of a check for

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<sup>23</sup> The relationships among Mr. Tersigni, certain corporations controlled by him, Gitto Global and the Gitto Principals are discussed in the Appendix.

which they would allow a draw on uncollected funds and offered this procedure as an incentive for business clients to establish checking accounts at Clinton. Mr. Tenaglia stated that his introduction to the J&J Chemical Account occurred in April of 2002 when there were five or six checks drawn on account of Gitto Global and payable to J&J Chemical that were returned to Clinton for insufficient funds.

As a result of those returned checks and the level in the J&J Chemical Account, Clinton's operations manager, Bobby Jo Williams, contacted Clinton loan officer Joseph Guercio. Ms. Williams went to Mr. Guercio because he had acted as the loan officer for Mr. Miller's prior loan from Clinton. Mr. Tenaglia stated that both Mr. Guercio and Ms. Williams met with Frank Miller and discussed the dishonored checks. Mr. Miller told Guercio and Ms. Williams that Gitto Global was having problems with its then-current bank, Guaranty Business Credit, and that Guaranty had mistakenly failed to honor certain checks written by Gitto Global to Kingsdale and deposited in the J&J Chemical Account. Miller also told them that Gitto Global would be changing banks soon and that this would not be an ongoing problem.<sup>24</sup>

Mr. Tenaglia stated that this explanation satisfied Guercio and Williams; however, for the next six months Ms. Williams monitored the J&J Chemical Account closely and did not allow Kingsdale to draw on uncollected funds during that period of time. For that six month period,

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<sup>24</sup> Mr. Miller's statement is consistent with Mr. Deakin's, discussed in Section V.D.2. above, that Guaranty intentionally dishonored some Gitto Global checks to convince Mr. Miller to find another lender after Guaranty apparently had discovered indicia of inventory and/or accounts receivable fraud.

the account activity appeared relatively ordinary.<sup>25</sup> Toward the end of 2002, Clinton allowed Kingsdale to resume the practice of drawing on uncollected funds in the J&J Chemical Account.

Clinton's next significant observation of the J&J Chemical Account occurred in October of 2003 when Mr. Tenaglia was conducting a general review of Clinton's business deposit accounts. During that review, he noticed that substantial deposits to the J&J Chemical Account via checks written by Gitto Global were made on almost a daily basis. He further noted that substantial amounts were also paid by Kingsdale back to Gitto Global on a daily basis by checks written on the J&J Chemical Account. He stated that while the individual checks deposited into and, then drawn against, the J&J Chemical Account might be in different amounts, the aggregate dollar volume was roughly equal each day. He also observed that the checks payable to Gitto Global and drawn on the J&J Chemical Account were deposited at Fleet Bank. Mr. Tenaglia advised that, at the time, he did not know that the Fleet Bank account was a "lockbox" for LaSalle.

It was Mr. Tenaglia's memory that the volume he observed in October 2003 was \$2 Million to \$2.5 Million per day in checks deposited into and then drawn upon the J&J Chemical Account. Mr. Tenaglia went to Ms. Williams and advised her of what he observed and Ms. Williams stated she had observed substantial funds cycling through the J&J Chemical Account but she had not been alarmed because she had monitored the account herself for six months and Clinton had not suffered any loss. After speaking with Ms. Williams, Mr. Tenaglia brought the activity in the J&J Chemical Account to the attention of Steven Cash, the former President of

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<sup>25</sup> Within the same period – on July 25, 2002 – Gitto Global entered into its new credit facility with LaSalle and discharged its obligations to Guaranty

Clinton Savings.<sup>26</sup> Mr. Tenaglia advised Mr. Cash that he observed \$2.5 Million per day going into the account and going right back out of the account in a manner in which he described as a “high level” of activity. They jointly decided that Frank Miller needed to explain the activity.

Mr. Tenaglia stated that in early December 2003 he and Ms. Williams met with Mr. Miller and asked him to explain the level of activity in the J&J Chemical Account. Mr. Miller told them that one company, either Gitto Global or Kingsdale, had a license to acquire raw materials and the other had a license to produce plastic compounds. He further explained that it was necessary to separate the licenses to two separate legal entities for “competitive and licensing issues.” Mr. Miller also told them that Gitto Global was in the process of selling its business operations to a company in California named VitroTech. Mr. Tenaglia explained to Mr. Miller that the account was creating credit exposure for Clinton and was not profitable for Clinton, and that Clinton therefore intended to close the J&J Chemical Account.

Mr. Miller responded by repeating that Gitto was being sold to VitroTech and requesting that Clinton refrain from closing the J&J Chemical Account because the sale would be completed by the end of January 2004. After this meeting, Mr. Tenaglia informed Mr. Cash of what Mr. Miller said and both Mr. Tenaglia and Mr. Cash agreed they should allow the J&J Chemical Account to remain open at Mr. Miller’s request because of the anticipated sale of Gitto Global.

During the Examiner’s interview of Robert J. Paulhus, Jr., Mr. Paulhus stated that he also attended the above-referenced December 1, 2003 meeting with Mr. Tenaglia, Ms. Williams, and

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<sup>26</sup> On December 11, 2004, the *Worcester Telegram & Gazette* reported that Mr. Cash resigned as Clinton’s president at the request of the bank’s board of directors. In the same article, the newspaper reported that Clinton “lost more than \$1.8 million because of accounting regularities and an alleged check-kiting scheme perpetrated by Gitto/Global.”

Mr. Miller. It is his memory this was the first time that he, Ms. Williams and Mr. Tenaglia had ever met Mr. Miller in person. Mr. Paulhus stated he was asked to attend this meeting because of his expertise in the area of commercial lending. Mr. Paulhus was to try to understand what the level of activity was in the J&J Chemical Account and why it had such a high dollar volume. Prior to the meeting, the Clinton officials had also discussed whether Clinton needed to take any action to satisfy applicable regulatory or statutory requirements in regard to the J&J Chemical Account and thus Mr. Paulhus was there to hear first-hand Mr. Miller's explanation.

According to Mr. Paulhus, Mr. Miller explained the role Kingsdale played with Gitto Global and why they seemed to be switching the same money back and forth. Mr. Paulhus stated to the Examiner that it was difficult for him to repeat this explanation because he did not feel that he understood it even when Mr. Miller was telling him. Mr. Paulhus was not satisfied as a result of this meeting. He told the Examiner that Mr. Miller's explanation made no sense to him, based on Mr. Paulhus' experience as a commercial lender, and that is what he told others at Clinton following the meeting. Mr. Miller also made it very clear that when Gitto Global was sold to VitroTech the J&J Chemical Account would be "closed and go away." At the December 1, 2003 meeting, Mr. Miller agreed to send a letter to Clinton explaining the basis for the check transactions. Mr. Paulhus wanted such a letter in the file in the event an auditor reviewed the J&J Chemical Account at a later date. After the meeting, the relevant parties at Clinton concluded that they would obtain the letter of explanation from Mr. Miller, would continue to monitor the Account and let it remain open until January, 2004 pending the sale negotiations with VitroTech.<sup>27</sup>

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<sup>27</sup> It appears that Clinton decided not to take any action to satisfy regulatory or statutory requirements immediately after the meeting. Clinton advised the Examiner, however, that it did take such action in May 2004.

After the December 1, 2003 meeting, Mr. Tenaglia continued to talk with Mr. Miller to monitor the proposed sale of Gitto Global. In January 2004, Mr. Miller told Mr. Tenaglia that the sale was not ready yet, efforts were continuing, and they would get the sale done as quickly as possible but not until March 2004. Mr. Miller explained the delay by stating that VitroTech had just become a public company and now had to comply with SEC regulations that required an audit of Gitto Global.

By the end of January 2004, according to Mr. Tenaglia, the amount of daily activity in the J&J Chemical Account had increased from \$2.5 Million per day the previous year to \$3.5 Million per day. He discussed the increase in dollar volume with Mr. Miller and instructed Mr. Miller to reduce the activity in the account and to increase the account's cash balances. Mr. Tenaglia stated that he recognized in January 2004 that Clinton's credit exposure on the Account could be as high as \$3.5 Million because Clinton still was allowing Kingsdale to draw on uncollected funds. Asked why he permitted Kingsdale to draw on uncollected funds in the Account, with all he knew at the time, Mr. Tenaglia stated that he had never had a check returned on the J&J Chemical Account and Mr. Miller had asked Clinton to work with him to make the sale to VitroTech possible.<sup>28</sup> Mr. Tenaglia also stated that Mr. Miller made it very clear to him during their conversations that, if Clinton terminated Kingsdale's ability to draw on uncollected funds, such a decision would be "disruptive" to Gitto Global and its potential sale to VitroTech. Because of these reasons, Clinton decided not to restrict draws on uncollected funds.

In March 2004, Mr. Miller informed Mr. Tenaglia that the Gitto Global sale had been delayed until May 2004. Mr. Tenaglia asked Mr. Miller for documentation to support what he

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<sup>28</sup> Mr. Tenaglia's explanation appears to contradict his earlier statement that Ms. Williams first grew concerned when checks written against the J&J Chemical Account were dishonored in 2002.

claimed to be the pending sale of Gitto Global which was the basis of Clinton's forbearance from closing the Account. Mr. Miller provided Mr. Tenaglia with a copy of the sale agreement between VitroTech and Gitto Global as well as a financial statement for Gitto Global.

Mr. Tenaglia identified a financial statement from Clinton's records for Gitto Global for the fiscal year ending June 30, 2003, which statement bears a cover letter from Louis J. Pellegrine, dated November 12, 2003.<sup>29</sup> Mr. Tenaglia stated he wanted this statement as proof of the financial health of Gitto Global. He furnished both the sale agreement and financial statement to Mr. Cash, Clinton's President. The financial statement seemed to be a certified financial statement and Mr. Tenaglia saw that Gitto Global had a credit line with LaSalle for \$27 Million. He also noted that Gitto Global reported annual sales of \$160 Million during fiscal 2003. The financial statement provided by Miller indicated to Messrs. Tenaglia and Cash that Gitto Global was a profitable, growing company. Mr. Tenaglia did not observe until it was pointed out to him by the Examiner that the letter attached to the financial statements was not signed by Mr. Pellegrine.

Mr. Miller agreed with Mr. Tenaglia's request that, by the middle of May 2004, Mr. Miller would deposit up to \$1 million in the J&J Chemical Account. In May, however, Mr. Miller advised that he was having trouble raising cash and was busy working on the sale of the company to VitroTech. While Mr. Miller was unable to put additional cash into the J&J Chemical Account, Mr. Miller offered, as collateral, equipment owned by Gitto Global and presented Clinton with a certified appraisal stating the value of the Gitto Global equipment was \$21 Million and had a liquidation value of \$14 Million. Mr. Tenaglia stated that Clinton was

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<sup>29</sup> See footnote 18 *supra*, concerning this letter and Gitto Global's 2003 financial statements

aware that there were other liens against the equipment of Gitto Global of approximately \$6.5 Million, but with the equipment valued at \$14 Million, they had approximately \$8 Million left in equity to serve as collateral.

Mr. Paulhus states that from approximately January to June 2004 he kept abreast, through general office conversation, of what was happening in the J&J Chemical Account. However, he had no formal role in directing or handling this account during that period. Mr. Paulhus did state that Clinton understood that there was a business relationship between Gitto Global and Kingsdale/J&J Chemical and had been told that if Clinton closed down the J&J Chemical Account before Gitto Global was sold, it would do harm to the sale and thus Gitto Global might suffer financial hardship.

By June 2004 there was approximately \$4 Million in checks per day being drawn against and deposited into the J&J Chemical Account and Mr. Paulhus took on a larger role in managing Clinton's relationships with Kingsdale and Gitto Global. Mr. Paulhus agreed with the Examiner that Clinton had "unsecured exposure" and that if payment were stopped on the Gitto Global checks being deposited into the J&J Chemical Account, Clinton's loss could be as much as \$4 Million per day. Considering that there was a two-day "float," Clinton's total loss could be as much as \$8 Million. Mr. Paulhus stated that he was aware Gitto Global was offering its equipment as collateral to secure Kingsdale's obligations and convince Clinton to allow the Account to remain open. Mr. Paulhus stated he did nothing to look into the background of Kingsdale, J&J Chemical or their officers and directors, or review their financial statements. Mr. Paulhus stated his only job was to secure Kingsdale's obligations to Clinton and that is what he did. His priority was not to look into Kingsdale, he explained, but to secure Clinton's position and reduce its credit exposure. Mr. Paulhus stated to the Examiner he did not think the J&J

Chemical Account was being used as part of a criminal activity. He was then asked if he was aware that Clinton had made a regulatory filing in May 2004 and he stated yes. Asked why, Mr. Paulhus stated that had to do with the high volume of checks, the frequency they were presented, and the amounts Clinton was exposed to in uncollected funds.

The Examiner requested that Mr. Tenaglia explain a letter written to him, dated June 25, 2004, in which Miller explains why Gitto Global is writing checks to J&J and J&J is in return writing checks back to Gitto Global. Mr. Miller's letter, a copy of which is submitted herewith as Exhibit 25, reads as follows:

Per our recent conversations, I wanted to give the bank a better understanding of what J & J Chemicals does for us. Gitto Global Corporation is licensed to sell a chemical additive that we are not licensed to put into our own compounds for competitive reasons. For this reason we sell some of our compounds to J & J Chemical Distributors who then processes this additive into our compounds and then sells our compounds back to us with this additive included in the product. We have been advised that this is the appropriate way to handle these transactions in order to get proper accounting treatment for it. We appreciate the bank's understanding and the account will be closed after the acquisition of Gitto Global Corporation within the next few weeks.

Mr. Tenaglia agreed that this was the response given to him by Miller orally in the fall of 2003 and which Mr. Miller agreed to provide him by letter after the December 1, 2003 meeting. Asked why it took six months to obtain this letter from Mr. Miller, Mr. Tenaglia stated Clinton was putting more pressure on Mr. Miller to stop the volume and dollar amount of the checks being written and Mr. Tenaglia again asked Mr. Miller to confirm in writing what he had said in the fall of 2003. Mr. Tenaglia stated the request for this letter from Mr. Miller was not connected to any examination by the FDIC or other regulatory purpose.

Mr. Tenaglia did state that Clinton discussed its exposure on the J&J Chemical Account with the FDIC during an audit of Clinton in late June 2004. During its June 2004 audit, the FDIC determined that the J&J Chemical Account "should be terminated." Gitto Global,

however, again advised Clinton that a sale of Gitto Global to VitroTech was imminent and provided correspondence from Stonefield Josephson, VitroTech's auditor, as proof.<sup>30</sup> The outcome of these discussions was an agreement whereby Clinton allowed the continued use of the J&J Chemical Account until July 15, 2004, so long as Gitto Global agreed to guaranty the J&J obligations and secure that guaranty with a lien on its machinery and equipment. Such Guaranty and Security Agreement, each dated June 16, 2004, are submitted herewith as Exhibit 26.

When the sale of Gitto Global did not take place by July 15, 2004 and Clinton's exposure remained high, Mr. Miller continued to assure Clinton that a sale to VitroTech was in the offing. Clinton agreed to forbear for another month, until August 15, 2004, so long as Kingsdale entered a \$8.4 million line of credit agreement with respect to the overdrafts that existed in the J&J Chemical Account and paid a \$40,000 fee, and the following parties delivered guaranties and collateral:

1. Gary C. Gitto, whose guaranty was secured by \$500,000.00 of cash collateral;
2. Tradex Corp., whose guaranty was to be secured by (i) a mortgage encumbering real property known and numbered as 140 Leominster-Shirley Road, Lunenburg, Massachusetts (the "Real Estate"), and (ii) a security agreement granting Clinton a security interest in Vitrolite inventory purportedly owned by Tradex and located at Casey Transportation and Warehouse, 241 Willard Street, Leominster, Massachusetts; and
3. Frank Miller, whose guaranty was secured by \$500,000.00 cash.

Gitto Global's existing guaranty, dated June 16, 2004 and secured by its equipment pursuant to a security agreement dated June 16, 2004, was further secured by the pledge of

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<sup>30</sup> See Section V.I., *infra*

3,000,000 shares of VitroTech common stock. By its terms, the line of credit agreement expired on August 15, 2004.

Mr. Harmon, who assisted Mr. Paulhus, never saw any documentation showing that Tradex Corp. owned or bought the VitroLite inventory it was pledging. With Mr. Paulhus, Mr. Harmon went to the warehouse in Leominster with Mr. Childs of Gitto Global and was shown the Vitrolite inventory in shrink-wrapped bags on a pallet. He never saw any records at the warehouse which identified Tradex Corp. as the owner of the inventory.<sup>31</sup>

While the transaction was originally scheduled to be closed on July 15, 2004, the closing documents prepared by counsel still had Thomas Sullivan listed as an officer at an address in Mashpee, Massachusetts. This information was erroneous. Kingsdale had changed its corporate officers and Clinton was not aware of the changes. The closing was therefore delayed to allow Clinton's counsel to redraft the closing documents. The transaction eventually closed on July 23, 2004.

Mr. Paulhus was asked by the Examiner how he felt about learning at a closing that Clinton did not have the basic corporate data regarding Kingsdale, including the identity of its officers, directors, and address. Mr. Paulhus stated he found it "unsettling and uncomfortable." Mr. Paulhus further stated he would not let a commercial loan account be in that condition; however, this was a checking account and not a commercial loan. This distinction does not appear meaningful to the Examiner; regardless of its categorization, the Bank's relationship with Kingsdale and its maintenance of the J&J Chemical Account created substantial credit exposure for Clinton, which it urgently sought to secure through the transaction described above.

On August 18, 2004, the sale to VitroTech still not having occurred, the Maturity Date of Kingsdale's line of credit was extended to September 15, 2004.<sup>32</sup> It appears that Clinton and Gitto Global stayed in almost daily contact as during late August and the first few weeks of September. Ultimately, as discussed in more detail below, it became clear that the sale to VitroTech would not occur. Finally, on September 24, 2004, the Petition Date, Clinton's counsel made written demand for immediate payment of amounts due under Kingsdale's line of credit. A copy of Clinton's demand letter is submitted herewith as Exhibit 27.

### **I. VitroTech**

It appears that the Gitto Principals were well aware throughout late 2003 and all of 2004 that Clinton's threats to close the J&J Chemical Account directly imperiled Gitto Global's existence. The cycling of extraordinary sums through the J&J Chemical Account allowed Gitto Global to submit deceptive borrowing base reports to LaSalle. Indeed, it appears that Clinton's impending decision to close the J&J Chemical Account in September 2004 ultimately became the primary, precipitating factor in the resignation of the Gitto Principals and the company's Chapter 11 filing. The decision by Clinton finally to close the Account, moreover, appears to have been a direct result of VitroTech terminating its proposed acquisition of Gitto Global's compounding business.

Given the interrelationships among Gitto Global, Clinton and VitroTech and the significance of those relationships to Gitto Global's demise, the Examiner devoted considerable resources to reviewing the Debtor's lengthy pre-petition relationship with VitroTech. For a

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<sup>31</sup> It appears that the Vitrolite inventory either was owned or held on consignment by Gitto Global. See Section V.I.2 and footnote 39, *infra*. If owned by Gitto Global, of course, the Vitrolite inventory was encumbered by LaSalle's security interest.

<sup>32</sup> The Examiner notes that September 15, 2004 was 91 days after the date, June 16, 2004, that Gitto Global guaranteed Kingsdale's obligations and granted to Clinton a security interest in its assets.

period of approximately fifteen months, beginning in May 2003 and continuing almost immediately prior to the Debtor's bankruptcy filing in September 2004, VitroTech and Gitto Global engaged in negotiations with respect to a transaction whereby VitroTech would acquire a substantial portion of Gitto Global's business assets and the Gitto Plant and abutting real estate owned by Tradex Corp. The circumstances of these negotiations were, from the evidence reviewed by the Examiner, far outside the commercial mainstream and the Examiner believes persuasive evidence exists showing that VitroTech knew of the fraudulent activities being conducted by the Gitto Principals. The Examiner also believes that the Gitto Principals, with substantial assistance by VitroTech, used the sale negotiations to prolong Gitto Global's existence, to the likely detriment of its creditors.

#### **1. Formation of the VitroTech Business**

VitroTech is "engaged in the materials technology business which includes but is not limited to, the mining, processing, marketing and sale of a family of proprietary amorphous aluminosilicate (the "Mineral") based products designed to improve performance and quality of a broad array of manufacturing applications." VitroTech SEC Form 10-QSB for the Quarter ended June 30, 2004 (the "VitroTech 10-QSB for 2Q/2004"). VitroTech's business was formerly conducted by a separate but affiliated legal entity named Hi-Tech Environmental Products, LLC ("Hi-Tech"), a Nevada limited liability company that was apparently formed in May 1997 by the following individuals: Jess Rae Booth, Walter Carlson, John Keller, William Martin, Greg Yaris, James Kangas and Kristen Johnson (collectively, the "VitroTech Principals"). It appears that Mr. Booth was the principal founder and owner of Hi-Tech. He later served as VitroTech's chief executive officer and president throughout the time it negotiated the potential purchase of Gitto Global's business operations.

The VitroTech Principals formed Hi-Tech to extract the Mineral from certain mines in Calaveras County, California. Separate business entities known as Enviro Investment Group, LLC, Red Rock Cannon Mineral, LLC and Valley Springs Mineral, LLC (the “Mining Companies”), owned the mines. The VitroTech Principals, however, founded, owned and controlled all of the Mining Companies.

Hi-Tech and the Mining Companies entered into a series of purchase agreements under which Hi-Tech acquired the exclusive right to purchase the Mineral from the Mining Companies until the purchase agreements expire in 2017. VitroTech 10-QSB for 2Q/2004. Hi-Tech then began to market a variety of Mineral-based products—the largest of which are sold under the names Vitrolite and Vitrocote—to plastic and paint/coating manufacturers. Hi-Tech itself did business under the trade name “VitroCo.”

It appears that Hi-Tech had only limited success marketing its products to other manufacturers. The Mineral purchase agreements impose on Hi-Tech a minimum purchase requirement; Hi-Tech and VitroTech (which eventually assumed most of Hi-Tech’s assets and liabilities, as discussed below) apparently have not satisfied these minimum purchase requirements and consequently have accrued substantial liabilities to the Mining Companies. Eventually, Hi-Tech retained Steven Merry of the firm Golden International Group (“GIG”) of Los Angeles, California, to act as its business consultant. Mr. Merry recommended that Hi-Tech pursue a “vertical integration” strategy whereby Hi-Tech would acquire companies in the plastics compounding and painting/coating industries. Hi-Tech could then supply the acquired business with Vitrolite and/or Vitrocote for use in their own products, rather than Hi-Tech continuing to attempt sell to unaffiliated manufacturers. Mr. Merry apparently was of the view that Hi-Tech would be much more appealing to investors and financing sources if Hi-Tech executed such a

vertical integration strategy. In addition, the vertical integration strategy likely would increase demand for the Mineral, thereby benefiting the Mining Companies and their owners, the VitroTech Principals. The VitroTech Principals agreed with Mr. Merry's recommendation and began searching for potential acquisition targets for Hi-Tech.

## **2. Introduction To Gitto Global**

In approximately the Spring of 2002, an individual named Gil Donatelli introduced the VitroTech Principals to the Gitto Principals. Mr. Donatelli is a manufacturer's representative who at different times appears to have been employed by both Gitto Global and VitroTech. He is also related to Michael Angelini.<sup>33</sup> Hi-Tech considered Gitto Global's plastic compounding business to be a good strategic fit in to its vertical integration strategy and began to explore an acquisition of Gitto Global. In the spring of 2003, Hi-Tech and GIG issued at least two written proposals to acquire substantially all of Gitto Global's business assets. The Gitto Principals initially rebuffed Hi-Tech's offers and advised that they would only be interested in selling Gitto Global via a stock transaction pursuant to which Hi-Tech would assume all of Gitto Global's existing obligations and liabilities. Substantial negotiations appear to have been conducted among the parties throughout the summer of 2003. Ultimately, Hi-Tech and Gitto Global entered into a Purchase and Sale Agreement under which Gitto Global agreed to purchase substantial quantities of Vitrolite, a Mineral-based product. In consideration for the purchase, Gitto Global issued to Hi-Tech a series of promissory notes in an aggregate principal amount in excess of \$12 million. The notes, however, contained an unusual "conversion" feature pursuant to which Hi-Tech obtained the right to convert its notes into approximately two-thirds of the

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<sup>33</sup> Mr. Donatelli's sister is married to Mr. Angelini's brother. (Angelini Exam. at 2-18)

capital stock of Gitto Global. It appears that during this same time frame Hi-Tech was in negotiations to acquire an unrelated company named Seegott, Inc. ("Seegott"), a distributor of raw materials and chemicals to paint and coating manufacturers.

In September of 2003, Hi-Tech issued a newsletter titled "VitroCo News" in which the company claimed to have signed letters of intent to acquire Gitto Global and Seegott. It is not clear to whom Hi-Tech provided this newsletter, which states at the top that it is confidential in nature. Gitto Global would later assert that Hi-Tech provided the newsletter or similar materials to a wide variety of people in the plastics industry and to potential investors in Hi-Tech. In any event, the provision of the newsletter that referred to a letter of intent to acquire Gitto Global was at least moderately misleading. Hi-Tech, in fact, had not signed a traditional letter of intent to acquire Gitto Global. Instead, it had purportedly sold inventory to Gitto Global in return for promissory notes that in certain circumstances could be converted to a majority equity interest in the company.

### **3. Fall/Winter 2003 "Due Diligence" by Hi-Tech**

The Examiner has been advised that representatives of Hi-Tech conducted an extensive, on-site due diligence review at Gitto Global in the later months of 2003. John Keller, one of the VitroTech Principals, and Alex Kabatoff, an executive of Hi-Tech and later VitroTech, apparently spent several weeks at the Gitto Plant during this period. Mr. Booth also visited the Gitto Plant headquarters at least once. Hi-Tech remained highly interested in acquiring Gitto Global's business assets, although it is unclear whether the parties still intended to effect the acquisition through the convertible notes issued to Hi-Tech in the summer of 2003. The importance of acquiring Gitto Global significantly increased when Seegott—Hi-Tech's other acquisition target—experienced severe financial difficulties and eventually liquidated, derailing Hi-Tech's attempt to acquire that company. Indeed, by the end of 2003, it appears that the

success of Hi-Tech's vertical integration strategy wholly depended on completing the Gitto Global acquisition.

William Deakin has advised the Examiner that, at Mr. Miller's request, he personally met with Mr. Kabatoff and Mr. Keller in the fall of 2003 and explained in detail the fraudulent schemes that Gitto Global employed to defraud its creditors. In particular, Mr. Deakin alleged that he explained the various mechanisms by which Gitto Global artificially inflated the value of its inventory and accounts receivable to allow it to borrow significant funds from LaSalle. Mr. Deakin has also alleged that Mr. Miller told him that Mr. Miller had explained Gitto Global's fraudulent activity to Mr. Booth.

Mr. Deakin's allegations are somewhat at odds with statements made to the Examiner by Mr. Booth and Mr. Carlson. While acknowledging that they were aware by no later than the end of 2003 that Gitto Global's books and records contained various "idiosyncrasies," they deny being told specifically that Gitto Global was defrauding its creditors. Instead, Mr. Booth and Mr. Carlson claimed that they analyzed Gitto Global as essentially having two businesses: (i) a compounding business that was legitimate and valuable, and (ii) a so-called "brokerage" business that purportedly sold polymers to various customers.<sup>34</sup> Mr. Booth in particular claimed that, while he suspected that Gitto Global's brokerage business was not wholly legitimate, Hi-Tech was solely interested in acquiring Gitto Global's compounding business, which he considered to be of strategic value. Hi-Tech, therefore, took no real interest in the health or legitimacy of the brokerage business. He directed his subordinates at Hi-Tech to determine the

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<sup>34</sup> While distinguishing between the two business types, Mr. Booth and Mr. Carlson acknowledged that they knew Gitto Global was operated as a single legal entity and was managed by the same individuals, *i.e.*, the Gitto Principals. The distinction between Gitto Global's compounding and brokerage businesses is made in the Elimination Reports found on Mr. Deakin's computer and submitted herewith as Exhibit 6. Mr. Deakin confirmed

actual value of Gitto Global's compounding business on a stand-alone basis, isolated from the brokerage business.

The weight of the evidence suggests that Mr. Deakin's account is more plausible. VitroTech representatives had already expended substantial due diligence efforts by the end of 2003. On January 22, 2004, Mr. Booth sent an unusual e-mail to Frank Miller, a copy of which is submitted herewith as Exhibit 28, in which Mr. Booth references the various "surprises" which Hi-Tech had discovered during its due diligence review at Gitto Global. In the e-mail, Mr. Booth acknowledges that Gitto Global's bank (which Mr. Booth has acknowledged he knew to be LaSalle) had various problems due to its loan relationship with Gitto Global. He then suggested to Mr. Miller that a full audit of Gitto Global be performed with the results to be turned over to LaSalle for the purpose of determining if it would support and finance an acquisition of Gitto Global by Hi-Tech.

The next day, Mr. Miller and Gary Gitto sent a letter to Mr. Booth, a copy of which is submitted herewith as Exhibit 29 (the "January 23 Letter"), in which they emphatically reject Mr. Booth's suggestions. Mr. Miller and Mr. Gitto state in part:

Your proposal in your e-mail is completely unacceptable. I am sure this is no surprise to you.

We have been completely open with you from the very beginning of our discussions regarding our relationship to the Bank. You know all about it and about our Company's financial situation.

Because of the sensitive nature of our Bank relationship, and with your advice, we have carefully structured this transaction to avoid any fall-out. You have given us advice and direction and you have been involved with us in managing our Bank relationship to allow for our transaction. The proposal in your e-mail completely disregards what you

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to the Examiner that Gitto Global had only a minimal brokerage business and used that category as a repository for fictitious sales and mischaracterized expenses.

and others at your company have known for a long time, and would create a big problem for those of us at Gitto Global, and also for those of you at VitroCo.

Mr. Miller and Gary Gitto then outlined in the January 23 Letter a proposal by which Hi-Tech (referred to in the January 23 Letter by its trade name, VitroCo) could acquire the assets of Gitto Global. They inquire as to whether VitroCo is interested in moving forward on the proposed acquisition, “rather than creating substantial problems which would otherwise result,” and close with the following sentences:

We must make a decision NOW, or it will be made for us all. This is an arrangement that works for all of us, and allows us all to work hard to make lots of money together.  
[capitals in original]

The Examiner has not been provided with any evidence that Mr. Booth responded in writing to the January 23 Letter. As discussed below, Hi-Tech and its successor, VitroTech, pressed on with its efforts to acquire Gitto Global after the delivery of the January 23 Letter.

The written exchange among Messrs. Booth, Miller and Gitto, especially when considered with Mr. Deakin’s statements and in light of subsequent events discussed below, gives rise to a strong inference that Hi-Tech and the VitroTech Principals were aware of substantial improprieties at Gitto Global by no later than the end of 2003 or very early 2004, and possibly months earlier. When asked to explain the exchange, Mr. Booth replied that while the surprises referenced in his January 22 e-mail related to “unstated liabilities” that were not recorded on Gitto Global’s books, he understood Gitto Global’s “problem” with LaSalle simply to be that the company had no further borrowing availability under its line of credit. He also continued to make a definitive distinction between Gitto Global’s compounding business, which he considered wholly legitimate and healthy, and its brokerage business, which he suspected was illegitimate. Further, Mr. Booth claimed not to understand the statements in the January 23 Letter that he had helped Gitto Global in managing its bank relationship.

The Examiner, however, does not consider those responses to be credible, given the substantial due diligence Hi-Tech had already conducted during 2003, Mr. Deakin's statements that Gitto Global's fraudulent schemes had been fully disclosed to Mr. Booth and his subordinates, the serious allegations in the January 23 Letter written by two of the Gitto Principals, and Mr. Booth's apparent failure to respond in writing to the conspiratorial and accusatory tone of the January 23 Letter. Instead, the Examiner infers from the evidence available that Hi-Tech, under Mr. Booth's direction, decided that the potential acquisition was of such importance to its own business strategy that it was worth pursuing notwithstanding its actual knowledge of Gitto Global's ongoing defalcations and precarious financial condition.

#### **4. Exchange of Assets Between Hi-Tech and VitroTech**

While continuing its negotiations with Gitto Global, the VitroTech Principals considered other means to make Hi-Tech more appealing to investors. They concluded that placing Hi-Tech's operations under the control of a publicly traded corporation would create an opportunity to grow the business and attract capital. On February 3, 2004, Hi-Tech completed a complicated transaction (referred to herein as the "Exchange") whereby Hi-Tech spun off its assets and liabilities to a subsidiary of a public company named Star Computing Limited, which in turn changed its name to VitroTech Corporation (and is the legal entity referred to in this Report as "VitroTech") and appointed Jess Rae Booth as its chief executive officer, president and sole director.<sup>35</sup> Star Computing Limited had very limited operations and apparently was not affiliated with Hi-Tech or the VitroTech Principals prior to the Exchange.<sup>36</sup>

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<sup>35</sup> The Exchange is discussed in substantially more detail in, among other places, VitroTech's Form 10-QSB filed with the SEC for the Quarter ended March 31, 2004.

<sup>36</sup> Following the Exchange, VitroTech's stock began to trade in the Over-the-Counter bulletin board under the symbol "VROT.OB".

Following the Exchange, VitroTech continued Hi-Tech's existing business operations and its pursuit of Gitto Global as an acquisition target. Hi-Tech itself has continued in existence following the Exchange as a private company and is still controlled by the VitroTech Principals. As part of the Exchange, and as a condition to Hi-Tech's transfer of its assets to VitroTech, Hi-Tech and Vitro-Tech entered into a Royalty Agreement pursuant to which VitroTech agreed to pay to Hi-Tech a royalty with respect to all Minerals acquired from the Mining Companies and then sold. It is unclear to the Examiner whether Hi-Tech presently holds other material assets or conducts substantial other business operations.<sup>37</sup>

##### **5. VitroTech Agrees to Acquire Gitto Global's Assets**

Following the Exchange, negotiations over the acquisition of Gitto Global's assets continued apace, with VitroTech now established to act as the acquiror. By mid-February 2004, the parties reached an agreement on the material acquisition terms and VitroTech, Gitto Global and the Gitto Principals in their individual capacities executed a "Letter of Intent-Asset Purchase," a copy of which is submitted as Exhibit 30 (the "LOI"). In the LOI, VitroTech agreed to pay \$42,000,000 for the "Purchased Corporate Assets" and \$3,200,000 for the Gitto Plant in Lunenberg, Massachusetts, which is owned by Tradex Corp. The LOI was subject to a number of contingencies, including the execution of definitive documentation, VitroTech's completion of due diligence and its receipt of sufficient financing to complete the acquisition. The LOI provides that it is "not contemplated" that VitroTech would retain any of the Gitto Principals as employees following the acquisition. The LOI does provide, however, that closing was conditioned on the execution of a consulting contract between Frank Miller and VitroTech

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<sup>37</sup> See Footnote 39 below concerning Hi-Tech's claim to certain VitroLite inventory held by Gitto Global.

and an Independent Manufacturer's Representative Agreement between Gary Gitto and VitroTech.

The acquisition terms were subsequently memorialized in an Asset Purchase Agreement dated March 31, 2004, by and between Gitto Global, as seller, Gary Gitto and Frank Miller as seller shareholders, and Charles Gitto, and VitroTech, as Purchaser (the "Purchase Agreement," a copy of which is submitted as Exhibit 31). Therein, VitroTech agreed to pay \$50,400,000 for the "Purchased Assets," subject to certain adjustments. VitroTech's purchase obligations remained subject to the satisfaction of a number of conditions, however, including due diligence and financing contingencies, the execution of the contracts with Frank Miller and Gary Gitto referenced above, and the execution by Charles Gitto of a real estate purchase agreement pursuant to which VitroTech would purchase the Gitto Plant for \$3,300,000.<sup>38</sup> The Purchase Agreement also required that Gitto Global provide to VitroTech certain disclosure schedules and financial statements within thirty (30) days of the execution of the agreement. VitroTech retained the right to terminate the Purchase Agreement if Gitto Global failed to deliver such information on a timely basis.<sup>39</sup>

Following the execution of the Purchase Agreement, VitroTech re-commenced its due diligence on Gitto Global's operations. Alex Kabatoff and John Keller—who had spearheaded

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<sup>38</sup> It is the Examiner's understanding that the Gitto Plant is owned by Tradex Corporation. The Purchase Agreement, for reasons not clear to the Examiner, suggests that Charles Gitto individually owned the Gitto Plant. It also appears that Charles Gitto was negotiating an arrangement to be employed in some capacity by VitroTech after closing. In a April 7, 2004 letter from Charles Gitto to Mr. Booth, a copy of which is submitted herewith as Exhibit 32, Mr. Gitto expresses disappointment with an undefined "contractual arrangement" and argues that "\$8,000 per month just doesn't recognize my value."

<sup>39</sup> At the time the Asset Purchase Agreement was executed, the convertible promissory notes executed and delivered by Gitto Global to Hi-Tech remained outstanding. As noted above, the notes nominally were executed in connection with Gitto Global's purchase of Vitrolite inventory from Hi-Tech. Mr. Carlson advised the Examiner that, following the execution of the Purchase Agreement, Hi-Tech and Gitto Global entered into a Consignment and Settlement Agreement, pursuant to which Gitto Global agreed that the Vitrolite inventory purchased from Hi-Tech would be

Hi-Tech's due diligence efforts during 2003—spent “weeks” at the Gitto Plant in the spring of 2004. By this time, William Deakin advises, both Mr. Kabatoff and Mr. Keller were fully aware of the fraudulent schemes that Gitto Global was using to manipulate its creditors. Mr. Deakin further advises the Examiner that he and Mr. Kabatoff together expended substantial efforts during this time to determine the true value of Gitto Global's inventory and accounts receivable and its actual sales volume.

Walter Carlson, a corporate vice president of VitroTech and one of the VitroTech Principals, also spent significant time analyzing Gitto Global in connection with the proposed acquisition, although he apparently never traveled to the Gitto Plant. Mr. Carlson acknowledged to the Examiner that VitroTech's due diligence revealed that Gitto Global was experiencing substantial financial distress, reflected by the following:

- Gitto Global's liabilities to its trade creditors were substantially higher than would be expected for a company of its size;
- the Gitto Principals were being compensated in amounts far greater than would be expected for a company of Gitto Global's size and type;
- “extraneous” members of the Gitto and Miller families were on the company's payroll; and
- Gitto Global did not have sufficient working capital to maintain itself as a going concern.

In addition, Mr. Carlson confirmed that VitroTech knew that Gitto Global had advised its lenders that a sale was being negotiated with VitroTech that would result in the pay-off of Gitto Global's loan obligations. At this time, LaSalle and Clinton were Gitto Global's principal financing sources.

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recharacterized as a consignment. It is the Examiner's understanding that either Hi-Tech or VitroTech has demanded that the Debtor return the Vitrolite inventory but does not know whether the Debtor has agreed to such demand.

Mr. Carlson further acknowledged that by the spring of 2004 VitroTech knew that Gitto Global's accounting records were materially inaccurate. Nonetheless, VitroTech remained intent on isolating Gitto Global's compounding business and closing the acquisition of the assets related to that business. VitroTech, therefore, advised Gitto Global that it would retain an independent certified public accounting firm to conduct an audit of the financial statements of Gitto's compounding business.<sup>40</sup> In March 2004, VitroTech contacted Stonefield Josephson, Inc., a public accounting firm located in California, to serve in that role.

Dean Skupen was the engagement partner at Stonefield Josephson with ultimate responsibility for the Gitto audit. He advised the Examiner that VitroTech knew of substantial accounting problems at Gitto Global at the time it retained Stonefield Josephson and that the company advised Mr. Skupen of those problems. Based on this information, Mr. Skupen selected one of his "strongest" colleagues, Nanette Miller, to travel with him to the Gitto Plant in April or May of 2004.<sup>41</sup> While there, Mr. Skupen dealt primarily with Mr. Miller and Mr. Deakin. Stonefield Josephson also retained the services of a local accounting firm, Carlin, Charron & Rosen ("CCR"), to assist in the audit. Barbara Fuller, a CPA employed by CCR,

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<sup>40</sup> VitroTech also explained to the Examiner that it believed an audit of Gitto Global was necessary to satisfy certain requirements of the Securities and Exchange Commission, given VitroTech's new status as a public company.

<sup>41</sup> The Examiner has been provided with an engagement letter agreement dated May 19, 2004, among Stonefield Josephson, the audit committee of VitroTech's Board of Directors and the "management" of Gitto Global, a copy of which is submitted with Exhibit 39. The engagement letter provides in part:

Based on our initial planning and discussions with the Acquiror or VitroTech Corporation and the Company [*i.e.*, Gitto Global], it has come to our attention that there have been certain material improprieties in the historical reporting of the Company's financial information, specifically in the Company's audited financial statements for the years ended June 30, 2003 and 2002. Also, it is our understanding that the management and certain employees or representatives of VitroTech Corporation will be determining the effects of these issues as they relate to the financial statements of the compounding division and taking responsibility for the fair presentation of the financial statements of the compounding division of the Company. Based on this fact, we will be increasing our standard audit procedures and will be requiring that the management and certain employees or representatives of VitroTech, as well as the Company, sign the Company's representation letter to be addressed to us.

reportedly spent substantial time at the Gitto Plant and interacted at length with Mr. Deakin and Mr. Miller.

There appears to be no dispute that Mr. Miller and Mr. Deakin made extensive disclosures to Mr. Skupen and his colleagues about the fraudulent schemes that the Gitto Principals were employing. Mr. Deakin advised the Examiner that he fully described to Mr. Skupen and Ms. Fuller, Gitto Global's fraudulent activities and the attempts by him and Mr. Kabatoff to identify Gitto Global's true financial condition to help facilitate the proposed acquisition. Mr. Skupen himself told the Examiner that someone at Gitto Global—he believed it to be Mr. Deakin, but was not sure—advised him that Gitto Global in essence maintained “two sets of books.”<sup>42</sup> The second set of books, Mr. Skupen was told, reflected inflated values of accounts receivable and inventory and was used to “scam” Gitto Global’s banks into lending additional amounts of money. Mr. Skupen advised the Examiner that he relayed this information to VitroTech.<sup>43</sup>

## **6. Obstacles to Completion of Sale**

The audit conducted by Stonefield Josephson and CCR extended through the late spring and summer of 2004. Both Stonefield Josephson and VitroTech advised the Examiner that the primary obstacle to completing the audit was the chaotic state of Gitto Global’s inventory records. While Stonefield Josephson by now was aware of the fraudulent schemes existing at

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<sup>42</sup> The Examiner’s forensic accountants, V&L, have explained to the Examiner that the term “two sets of books,” which has been used by other parties during this case, is not precisely accurate. Gitto Global did not literally maintain an “accurate” set of books and a “fraudulent” set of books. Instead, voluminous amounts of both legitimate and fictitious information were entered into a single accounting system at the company while other information was not entered at all. Certain individuals at Gitto Global apparently had the ability to cull from the system some estimation of the company’s true financial system, as reflected in the Elimination Reports.

<sup>43</sup> When asked about Mr. Skupen’s statements, neither Mr. Booth nor Mr. Carlson would specifically confirm having such a conversation with Ms. Skupen. Mr. Booth did acknowledge, however, that Stonefield Josephson advised him that Gitto Global’s brokerage business was “not right.”

Gitto Global, it remained concerned that an accurate determination of Gitto Global's inventory value had not been achieved. Nonetheless, VitroTech remained determined to complete the sale and took several steps in July 2004 that had the effect of prolonging Gitto Global's life and maintaining the possibility that the sale would occur.

VitroTech was aware of the increasing pressure placed by Clinton on Gitto Global and Kingsdale to close the J&J Chemical Account. Although Mr. Booth and Mr. Carlson explained to the Examiner that they did not know of the precise relationship between Clinton and Gitto Global, they understood that adverse action by Clinton could imperil Gitto Global's continued existence and therefore the possibility of closing the sale. They recalled that Mr. Miller requested that VitroTech participate in a conference call with Clinton and Gitto Global to provide some assurance to Clinton that the sale, in fact, was likely to occur.

On July 14, 2004, Mr. Carlson and Mr. Kabatoff of VitroTech participated in the requested conference call with Mr. Miller and a number of parties from Clinton and Clinton's counsel. Mr. Carlson's recollection was that Clinton "badgered" VitroTech to provide cash or some other form of collateral on Gitto Global's behalf to secure Clinton's exposure under the J&J Chemical Account. The parties discussed that VitroTech had not yet posted a deposit under the Purchase Agreement due to the fact that Gitto Global had not satisfied its requirement to provide disclosure schedules and audited financial statements. Ultimately, the parties agreed that VitroTech would pledge 3,000,000 shares of its capital stock to Clinton to serve as collateral. In exchange, Gitto Global executed and delivered to VitroTech a Subordinated Promissory Note in the amount of \$2,250,000, the approximate market value of the pledged shares. Both the shares and the Subordinated Promissory Note would be placed in escrow pending either the completion of the sale or a default by Gitto Global and Kingsdale on their obligations to Clinton. Mr.

Angelini of Bowditch & Dewey ultimately agreed to serve as Escrow Agent in respect of the pledged shares and promissory note.<sup>44</sup>

The pledge of shares by VitroTech—to secure an obligation of Gitto Global that arose from a company, Kingsdale, which VitroTech had no plans to acquire—was highly unusual. In discussing the pledge with the Examiner, Mr. Carlson and Mr. Booth advised that VitroTech had “serious heartburn” about pledging 3,000,000 shares of VitroTech’s publicly traded capital stock. Both Mr. Carlson and Mr. Booth argued that VitroTech had no obligation to post the deposit due to Gitto Global’s own failure to satisfy the terms of the Purchase Agreement; rather the pledge was an accommodation to keep the proposed acquisition alive, which they still believed would occur. The decision to post such shares would appear to reflect both VitroTech’s continued intense desire to complete the Gitto Global transaction and, even at this relatively late stage, its belief that the acquisition would in fact close. Ultimately, the pledge of the VitroTech shares, together with other steps taken by the Gitto Principals, temporarily mollified Clinton and prevented the immediate closure of the J&J Chemical Account.

Mr. Booth also advised that Mr. Miller requested in early July 2004 that Mr. Booth provide an update on the sale negotiations to LaSalle. On July 8, 2004, Mr. Booth accommodated Mr. Miller’s request by sending a letter to Thomas F. Furst, a Vice President at LaSalle, a copy of which is submitted herewith as Exhibit 33. Therein, Mr. Booth confirmed that VitroTech had entered into the Purchase Agreement to acquire Gitto Global’s compounding assets for a price in excess of \$50 million and a separate agreement to purchase the Gitto Plant.

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<sup>44</sup> There appears to have been some degree of confusion among the parties as to the nature of the escrow. Both VitroTech and Clinton produced draft escrow agreements which had materially different terms concerning the release of the shares and the promissory note. Mr. Carlson advised the Examiner that while VitroTech believes the

Mr. Booth also noted that VitroTech had entered into an investment banking relationship to assist in obtaining \$35 million in convertible financing and that "the final leg of the due diligence activities is currently being completed." Mr. Booth further said that while the parties expected to complete the acquisition as of July 15, it appeared that the closing would take place in early August. Mr. Booth also stated: "It is our understanding that your institution intends to conduct its regular periodic bank audit during the week of July 12. Any interruption to the audit process underway by Stonefield Josephson will only delay the closing of our acquisition."

Notwithstanding the assistance that VitroTech had provided, strains began to develop between VitroTech and the Gitto Principals. Mr. Booth and Mr. Carlson advised the Examiner that following the July 14, 2004, conference call with Clinton, Mr. Miller and Gary Gitto vigorously challenged VitroTech's unwillingness to waive the audit requirements as a condition to closing the sale. The strain increased in late July and early August as Stonefield Josephson continued to advise VitroTech that it had not completed its audit and could not assign a firm number to the value of Gitto Global's inventory. On August 4, 2004, Gary Gitto wrote to Mr. Booth and advised that he believed it crucial that Mr. Booth travel to Gitto Global on the following Monday "so that we can further discuss the critical dates that are quickly approaching and how resolution of the issues will be brought about within the allotted time." Gary Gitto went on to say: "as you know, time is of the essence and I am appealing to you for some answers." Mr. Booth advised the Examiner that he was unable to travel to the Gitto Plant in the requested time frame, but continued to be hopeful that the acquisition would close.

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Subordinated Promissory Note should have been released from escrow on the termination of the sale negotiations, Mr. Angelini to date has refused to do so.

On August 16, 2004, Mr. Skupen wrote to Mr. Booth that Stonefield Josephson was in the final stages of the audit but that a few outstanding items remained, “the most important item being our inventory procedures.” Mr. Skupen advised that he anticipated his firm would complete the audit within two weeks from the date of receipt of “the inventory roll back schedule” prepared by Gitto’s staff. The following date, August 17, 2004, Mr. Booth wrote to Gary Gitto and Mr. Miller reporting in summary fashion that Stonefield Josephson hoped to complete its audit within two weeks. He said that once the audit was completed, he would take it to VitroTech’s board and continue with the acquisition negotiations.

Mr. Booth advised the Examiner that by late August 2004 he became concerned that the “wheels were coming off” at Gitto Global. On August 24, 2004, Charles Gitto wrote to Mr. Booth and noted that he had been unable to reach him by phone over the last two days but that he and Michael Angelini had made plans to travel to the West Coast at the end of August. Charles Gitto requested a meeting with Mr. Booth to discuss the closing of the acquisition. Mr. Booth and Mr. Carlson advised the Examiner, however, that by late August VitroTech had largely concluded that the acquisition would not close. Among other things, VitroTech did not believe that it could obtain the necessary financing to complete the acquisition. As a result, Mr. Booth requested that Michael W. Sanders, VitroTech’s corporate counsel, analyze the Purchase Agreement and determine if Gitto Global was in breach of its obligations. By letter dated August 26, 2004, Mr. Sanders provided to Mr. Booth “a partial list of areas in which known breaches appear to exist under the [Purchase Agreement].” Mr. Sanders listed, among other things, that Gitto Global had failed to “preserve the value of [its] business” and that “substantial funds have been paid out of Gitto [Global] to Gary Gitto.”

By letter dated August 27, 2004, in turn, Mr. Booth advised the Gitto Principals and Mr. Angelini that “following exhaustive due diligence and a review of the representations, warranties and covenants of Gitto in the APA, we have determined that Gitto is in material breach of a substantial number of representations, warranties and covenants under the APA. Based on those breaches, VitroTech hereby exercises its rights, as set forth in Section 11.1(c) and (d) of the APA, to terminate the APA effective immediately.” A copy of Mr. Booth’s August 27, 2004, letter is submitted herewith as Exhibit 34.

#### **7. Gitto Global’s Failed Attempt to Salvage the VitroTech Sale**

Notwithstanding Mr. Booth’s letter, the planned meeting among Mr. Booth, Mr. Angelini and Charles Gitto took place on August 30, 2004. Mr. Booth advised the Examiner that the meeting was extremely contentious, with Mr. Angelini in particular vociferously arguing that VitroTech had breached its obligations to Gitto Global. Mr. Angelini, according to Mr. Booth, demanded that VitroTech withdraw its sale revocation and complete the acquisition or face a lawsuit by Gitto Global and perhaps Mr. Angelini himself. Mr. Booth advised the Examiner that he was insulted by Mr. Angelini’s threats and demeanor, cut short the meeting and ordered Mr. Angelini and Charles Gitto to leave VitroTech’s office.

Subsequently, Mr. Angelini wrote a stinging letter to Mr. Booth dated September 8, 2004, a copy of which is submitted herewith as Exhibit 35. Mr. Angelini argued that Mr. Booth’s August 27, 2004, letter terminating the proposed acquisition was “pretextual, intended to disguise continuing and actionable misconduct by you, your company and its related companies, including VitroCo, Hi-Tech Environmental Products and Golden International Group.” He further wrote:

I have been informed that for more than fourteen months you and other representatives of your company have been intimately familiar with the financial affairs of Gitto Global, including its relationship with its lenders. You have induced Gitto

Global to continue those relationships, and to increase borrowing based on those relationships. While you disingenuously claim breach of various written agreements by Gitto Global and assert recent knowledge of Gitto Global's financing arrangements, these were fully disclosed to you more than a year ago, and you have not only approved but have supported and facilitated Gitto Global's financings.

While criticizing Gitto Global for not making timely payments to suppliers and for the alleged loss of certain customer relationships, you are the cause of the circumstances which have affected these relationships. While complaining about the pledge of Gitto's equipment to Clinton Savings Bank, you and your colleagues have created the circumstances necessitating that pledge and, moreover, you specifically approved of that pledge. All of the six items set forth in Mr. Sanders' letter of August 26 and which apparently form the basis of your letter of August 27 result directly or indirectly from the improper actions of you and your colleagues and VitroTech.

From documents prepared at VitroTech and made available to your client, your long-term knowledge of and countenance of Gitto Global's financial situation is obvious.

VitroTech was unmoved was Mr. Angelini's letter. By a brief letter dated September 10, 2004, to Mr. Angelini, Attorney Sanders responded that "I will not address the same [*i.e.*, Mr. Angelini's September 8 letter] other than to state that your allegations are wholly without merit or factual basis and to reiterate that VitroTech has conducted itself entirely in accordance with the terms of the [Purchase Agreement]." Soon thereafter, Mr. Booth resigned as VitroTech's President and Chief Executive Officer. Mr. Booth advised the Examiner that his resignation was, in large part, the result of the failed Gitto Global acquisition.

As discussed more fully in Section VI(B)(3) below, the Examiner conducted a Rule 2004 Examination of Mr. Angelini and inquired about his September 8, 2004, letter. Mr. Angelini replied that "really what was going on was they [Vitro Tech] had used their relationship with Gitto/Global as a way to try to raise money and they hadn't" (Angelini Exam. At 1-153) and that "they were looking to hike their stock . . . [and] . . . were using Gitto Global as a way to do it. . ." (Angelini Exam. at 2-75).

### **J. Removal and Possible Destruction of Corporate Records**

As noted above, VitroTech's termination of its proposed acquisition led directly to Clinton's closure of the J&J Chemical Account and the resignation of the Gitto Principals on September 18, 2004. Although the Bankruptcy Court appointed the CRO one day earlier, it appears that the Gitto Principals took advantage of the company's chaotic state to remove a substantial number of records and other items from the Gitto Plant prior to the CRO's arrival at the Gitto Plant at the end of the business day on September 17, 2004.

Mr. Deakin stated that he had been informed by Ms. Chaisson that Frank Miller and Maria Miller were at Gitto Global on the night before the arrival of the CRO "packing up" their desks. Ms. Chaisson also informed Mr. Deakin that a drawer in her office area had been cleaned out and that the statements related to the J&J Chemical Account had been removed. Ms. Chaisson also informed Mr. Deakin that Mr. Miller and Ms. Miller shredded documents prior to the arrival of the CRO.

Ms. Bartlett stated that she had not personally witnessed any shredding of Gitto Global documents prior to the arrival of the CRO, but she did hear "rumors" that Ms. Kozak shredded Gitto Global records before she left. Ms. Bartlett stated in a later affidavit that the day before the CRO arrived at the Gitto Plant, she personally observed Ms. Kozak in Mr. Deakin's office putting records into four or five storage boxes. She later observed Oren White, a maintenance employee of Gitto Global, removing these boxes from the Gitto Plant.

Matthew Stilwell, Regional Audit Manager for LaSalle, and Kevin P. Durkin, another representative of LaSalle, advised the Examiner that when they arrived at Gitto Global after the CRO had taken over they found a number of invoices and bills of lading related to J&J Chemical sitting next to the shredding machine at the back of the accounting department. It appeared to them as if the above documents had been brought there to be shredded but that there had not

been enough time to complete the task. Ms. Chaisson informed them that Ms. Kozak in fact had been shredding documents.

In an affidavit provided on November 19, 2004, Roger Delisle, Gitto Global's Vice President of Engineering, stated that on Tuesday, September 14, 2004, Ms. Kozak telephonically contacted him and requested that he assign Mr. White to remove boxes from Gary Gitto's office on Wednesday, September 15th. Mr. Delisle made the arrangements and late in the day on Wednesday, September 15th, he went to the second floor offices at Gitto Global because he heard rumors that the Gitto Principals were "moving out." Mr. Delisle stated that he saw approximately twenty white file boxes lined up against the window in Gary Gitto's office. Mr. White entered Gary Gitto's office with a hand truck and began hauling the boxes out. Part of Ms. Kozak's instructions to Mr. Delisle were to have Mr. White deliver the boxes to the residence of Charles Gitto at 18 Nancy Court, Leominster, Massachusetts. Mr. Delisle further testified that upon exiting the office of Gary Gitto, he observed Maria Miller just outside of Frank Miller's office on the second floor. Ms. Miller asked for Mr. Delisle's assistance in moving eight or nine boxes on the floor that were packed with material flowing over the tops of the boxes. While engaged in this conversation with Ms. Miller, Mr. Miller walked into his office and Mr. Delisle asked him if this was "good-bye," to which Mr. Miller responded "no, it's just in case." Mr. Delisle assisted Mr. Miller and Ms. Miller in removing the above-described boxes to the lobby area of Gitto Global.<sup>45</sup> Mr. Delisle further stated it was also his memory that on

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<sup>45</sup> Debtor's counsel contacted the Examiner during the Examiner's investigation and advised that Frank Miller had turned ten boxes of documents over to Debtor's counsel. The Examiner obtained and copied most of the documents and returned the originals to Debtor's counsel. The Examiner has no means of determining if these boxes were the ones that Mr. Delisle helped Mr. Miller and Ms. Miller remove from Gitto Global.