

**UNITED STATES DISTRICT COURT  
FOR THE DISTRICT OF MINNESOTA**

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IN RE PEMSTAR, INC.  
SECURITIES LITIGATION

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CIVIL ACTION NO.:  
05-CV-01182-JMR-FLN

**CONSOLIDATED COMPLAINT**

Lead Plaintiff Dr. Brian Cromwell (“Plaintiff”), on behalf of himself and all others similarly situated, alleges the following facts for this Consolidated Class Action Complaint (the “Complaint”), based upon the investigation conducted by Lead Counsel, including, among other things, a review and analysis of press releases, news reports, public filings with the United States Securities and Exchange Commission (the “SEC”), and interviews with former employees of Defendant Pemstar, Inc.

**NATURE OF THE ACTION**

1. This is a class action on behalf of all persons who purchased the common stock (the “Shares”) of Defendant Pemstar, Inc. (“Pemstar” or the “Company”) from January 30, 2003 through and including January 12, 2005 (the “Class Period” and the “Class”). Excluded from the Class are Defendants, members of Defendants’ immediate families, any entity in which any Defendant has a controlling interest, and the legal representatives, heirs, successors or assigns of any such excluded person (the “Class”).

2. This class action arises primarily out of Pemstar’s failure to write-off non-existent, excess, obsolete, or otherwise non-saleable inventory and the failure to record the purchase of inventory, which resulted in the material understatement of accounts payable and costs of goods sold and the material overstatement of inventory, accounts receivable, and

earnings. Pemstar has admitted some of the misrepresentations and restated financial statements – claiming that there were accounting errors at its Mexican manufacturing and order fulfillment facility. As discussed more fully below, the misrepresentations of Pemstar’s financial results and condition were the result of intentional actions.

### **JURISDICTION AND VENUE**

3. This Court has jurisdiction over this action pursuant to (i) Section 27 of the Securities Exchange Act of 1934, 15 U.S.C. § 78aa et seq. (the “Exchange Act”); and/or (ii) 28 U.S.C. §§ 1331 and 1337. The claims asserted in the Complaint arise under and pursuant to Sections 10(b) and 20(a) of the Exchange Act (15 U.S.C. §§78j(b), 78t(a)) and Rule 10b-5 (17 C.F.R. § 240.10b-5) promulgated by the SEC.

4. Venue is proper in this District pursuant to Section 27 of the Exchange Act and 28 U.S.C. § 1391(b). Pemstar’s principal executive office was located during the Class Period at 3535 Technology Drive N.W., Rochester, Minnesota 55901, and a substantial part of the events or omissions giving rise to the claims complained of herein occurred in this District.

5. In connection with the wrongs alleged herein, Defendants used the instrumentalities of interstate commerce, including the United States mails, interstate wire and telephone facilities, and the facilities of the national securities markets.

### **THE PARTIES**

6. Lead Plaintiff Dr. Brian Cromwell purchased Shares during the Class Period, as set forth in a Certification of Named Plaintiff previously filed with the Court, and has suffered losses that were caused by the wrongdoing more particularly described herein.

7. At all relevant times to this litigation, Defendant Pemstar was a corporation

organized under the laws of the State of Minnesota.

8. At all relevant times to this litigation, Defendant Allen J. Berning (“Berning”) was employed by Pemstar as its Chairman of the Board of Directors and Chief Executive Officer. Defendant Berning also served as President of the Company from the beginning of the Class Period until December 16, 2004.

9. At all relevant times to this litigation, Defendant Greg S. Lea (“Lea”) was employed by Pemstar as its Chief Financial Officer, and was a member of the Company’s Board of Directors.

10. At all relevant times to this litigation, Defendant Roy Bauer (“Bauer”) was employed by Pemstar as its Chief Operating Officer. From December 16, 2004 through the end of the Class Period, Defendant Bauer also served as President of the Company, and was a member of its Board of Directors.

11. Defendants Berning, Lea and Bauer are sometimes hereinafter collectively referred to as the “Individual Defendants.”

**CONFIDENTIAL WITNESSES**

12. Many of the factual allegations contained in this Complaint are attributable to the results of interviews with the following former employees of Pemstar, who provided information on a confidential basis:

a. Confidential Witness "A": Confidential Witness "A" was employed by Pemstar Mexico as a Consultant to Mexican General Manager Jorge Ramirez from approximately November 2003 to April 2004. Confidential Witness “A’s” duties as a Consultant involved analyzing the finances of Pemstar Mexico. Confidential Witness "A" also served as a

Controller and Finance Director for Pemstar Mexico for a four-year period from approximately 1999 to May 2002. During the employment of Confidential Witness "A" at Pemstar during the Class Period, the confidential witness was responsible for preparing a detailed financial analysis of Pemstar Mexico, including, inter alia, an analysis of the propriety of Pemstar Mexico's accounting. Confidential Witness "A" reported to Pemstar's Chief Operating Officer and Executive Vice President (Paul Singh), who was responsible for Pemstar's international operations.

b. Confidential Witness "B": Confidential Witness "B" was employed by Pemstar as the Vice President of Worldwide Supply Chain from approximately December 2001 to January 2005. During the employment of Confidential Witness "B" at Pemstar, the confidential witness was responsible for, inter alia, purchasing and working with suppliers of Pemstar Mexico, and directly reported to Paul Singh, Defendant Al Berning (Pemstar's Chief Executive Officer), and Defendant Roy Bauer (who replaced Singh as Pemstar's COO).

c. Confidential Witness "C": Confidential Witness "C" was employed by Pemstar as an International Program Management Director from approximately 1999 to December 2003. During the employment of Confidential Witness "C" at Pemstar, the confidential witness was responsible for setting up and establishing the Pemstar Mexico facility, and subsequently prepared an analysis of Pemstar Mexico's current and future profitability. The confidential witness reported to Paul Singh, and then to Defendant Bauer (who replaced Singh as Pemstar's COO).

d. Confidential Witness "D": Confidential Witness "D" was employed by Pemstar from approximately November 2000 to March 2005, and he served as Pemstar's International

Financial Controller from approximately November 2000 to August 2003. Confidential Witness “D” continued with some of the duties of International Financial Controller after August 2003, including trips to Pemstar Mexico with Controller Larson through approximately April 2004. During the employment of Confidential Witness “D” at Pemstar as International Financial Controller, the confidential witness was responsible for, inter alia, the finances of all Pemstar international business units, including Pemstar Mexico. Confidential Witness “D” reported directly to Defendant Greg Lea.

### **FACTUAL BACKGROUND**

#### **The Company’s Business and Products**

13. At all times relevant to this litigation, the Company designed and manufactured products for customers in the communications, computing and data storage, industrial equipment and medical industries. The Company manufactured its product worldwide, including at a plant in Guadalajara, Mexico. In the Guadalajara, Mexico facility, Pemstar manufactured products for such companies as Efficient Networks, Inc. (later purchased by Siemens), Logitech, Welch-Allyn, and Valence Technology, according to Confidential Witness “A.”

### **THE MATERIAL MISREPRESENTATIONS DURING THE CLASS PERIOD**

#### **Misrepresentations In Pemstar’s Income Statements and Balance Sheets**

14. According to Confidential Witness “A,” there were rampant problems with accounting controls and financial reporting at Pemstar Mexico, both before and throughout the Class Period. Pemstar Mexico Controller Luz Maria Gonzalez told Confidential Witness “A” that, in approximately November 2002, she was asked by the General Manager of Pemstar

Mexico, Marcio Pavageua, to sign and acknowledge the propriety of financial statements that contained false and inaccurate financial information, which caused Gonzalez to resign rather than sign financial documents that she knew were false and inaccurate, and which were reflected in the publicly reported financial results of Pemstar.

15. On January 29, 2003, after the close of trading, Pemstar issued a press release (listing Defendant Lea as the contact person) announcing the Company's financial results for the third fiscal quarter ended December 31, 2002 ("Third Quarter Fiscal 2003"). On or about February 14, 2003, the Company filed its quarterly report for the fiscal quarter ended December 31, 2002 on Form 10-Q with the SEC (the "February 2003 10-Q"), repeating and providing more detail concerning the results for the third fiscal quarter contained in the January 29, 2003 Press Release. The February 2003 10-Q was signed by Defendants Berning and Lea. The financial results reported for the Third Quarter Fiscal 2003 (which contained the financial information that Gonzalez refused to sign) were false and misleading when issued because Defendants overstated inventory, accounts receivable, and committed other accounting misstatements, as further described below.

16. On May 7, 2003, after the close of trading, Pemstar issued a press release (listing Defendant Lea as the contact person) announcing the Company's financial results for both the fourth fiscal quarter and fiscal year ended March 31, 2003 ("Fourth Quarter Fiscal 2003"). On or about July 10, 2003, the Company filed its annual report for the fiscal year ended March 31, 2003 on Form 10-K with the SEC (the "Fiscal 2003 10-K"), repeating and providing more detail concerning the results for the fourth fiscal quarter and fiscal year contained in the May 7, 2003

Press Release. The Fiscal 2003 10-K was signed by Defendants Berning and Lea. The financial results reported for the Fourth Quarter Fiscal 2003 (which confirmed the financial information that Gonzalez refused to sign) were false and misleading when issued because Defendants overstated inventory, accounts receivable, and committed other accounting misstatements, as further described below.

17. On July 23, 2003, Pemstar issued a press release (listing Defendant Lea as the contact person) announcing the Company's financial results for the first fiscal quarter ended June 30, 2003 ("First Quarter Fiscal 2004"). On or about August 7, 2003, the Company filed its quarterly report for the First Quarter Fiscal 2004 on Form 10-Q with the SEC (the "August 2003 10-Q"), and repeated the results for the First Quarter Fiscal 2004 contained in the July 23, 2003 Press Release. The August 2003 10-Q was signed by Defendants Berning and Lea. The financial results reported for the First Quarter Fiscal 2004 were false and misleading when issued, as set forth in the Company's restatement of the First Quarter Fiscal 2004 financial results contained in the Company's February 14, 2005 filing with the SEC, as follows:

Quarter Ended (In thousands, except per share data)	June 30, 2003 (As issued in August 2003)	June 30, 2003 (As Restated)
Net sales	145,500	145,500
Cost of goods sold	138,918	140,088
	-----	-----
Gross profit	6,582	5,412
Selling, general and administrative expenses	12,280	12,483
Restructuring costs	3,455	3,455
	-----	-----
Operating (loss) income	(9,153)	(10,553)

Other expense		
(income) – net	(286)	(287)
Interest expense	2,039	2,039
	-----	-----
Loss before income taxes		
and cumulative		
effect of		
accounting		
change	(10,906)	(12,305)
Income tax expense	80	80
	-----	-----
Loss before cumulative		
effect of		
accounting		
change	(10,986)	(12,385)
Cumulative effect of		
accounting		
change	–	–
	-----	-----
Net loss	(10,986)	(12,385)
	-----	-----
Basic and diluted loss per		
common share:		
Loss before cumulative		
effect of		
accounting change	(0.29)	(0.33)
Cumulative effect of		
accounting change	–	–
	-----	-----
Net loss	(0.29)	(0.33)

18. In August 2003, after the Company filed the August 2003 10-Q, the Company completed a Secondary Offering of approximately 7.5 million shares of Company stock, resulting in the Company receiving proceeds of approximately \$20.1 million. The Prospectus for the Secondary Public Offering (the “SPO Prospectus”) contained, inter alia, the financial information previously reported for the fiscal year ended March 31, 2003 and the first fiscal quarter ended

June 30, 2003, described in paragraphs 15-17 above. The Registration Statement, of which the SPO Prospectus was a part, was signed by, inter alia, Defendants Berning and Lea. The financial results reported for the fiscal year ended March 31, 2003 and for the first fiscal quarter ended June 30, 2003 were false and misleading when issued for the reasons set forth in paragraphs 16-17 above.

19. On October 28, 2003, Pemstar issued a press release (listing Defendant Lea as the contact person) announcing the Company's financial results for the second fiscal quarter ended September 30, 2003 ("Second Quarter Fiscal 2004"). On or about November 10, 2003, the Company filed its quarterly report for the Second Quarter Fiscal 2004 on Form 10-Q with the SEC (the "November 2003 10-Q"), and repeated the results for the Second Quarter Fiscal 2004 contained in the October 28, 2003 Press Release. The November 2003 10-Q was signed by Defendants Berning and Lea. The financial results reported for the Second Quarter Fiscal 2004 were false and misleading when issued, as set forth in the Company's restatement of the Second Quarter Fiscal 2004 financial results contained in the Company's February 14, 2005 filing with the SEC, as follows:

Quarter Ended (In thousands, except per share data)	September 30, 2003 (As issued in November 2003)	September 30, 2003 (As Restated)
Net sales	150,550	150,550
Cost of goods sold	138,665	139,321
	-----	-----
Gross profit	11,885	11,229

Selling, general and administrative expenses	12,039	12,065
Restructuring and impairment charges	4,757	4,757
Operating loss	(4,911)	(5,620)
Other income (expense) – net	(411)	(411)
Interest expense – net	2,111	2,111
Loss before income taxes and cumulative effect of accounting change	(6,611)	(7,320)
Income tax expense	198	198
Loss before cumulative effect of accounting change	(6,809)	(7,518)
Cumulative effect of accounting change	–	–
Net loss	(6,809)	(7,518)
Basic and diluted loss per common share:		
Loss before cumulative effect of accounting change	(0.17)	(0.19)
Cumulative effect of accounting change	–	–
Net loss	(0.17)	(0.19)

20. On January 28, 2004, Pemstar issued a press release (listing Defendant Lea as the

contact person) announcing the Company's financial results for the third fiscal quarter ended December 31, 2003 ("Third Quarter Fiscal 2004"). On or about February 17, 2004, the Company filed its quarterly report for the Third Quarter Fiscal 2004 on Form 10-Q with the SEC (the "February 2004 10-Q"), and repeated the results for the Third Quarter Fiscal 2004 contained in the January 28, 2004 Press Release. The February 2004 10-Q was signed by Defendants Berning and Lea. The financial results reported for the Third Quarter Fiscal 2004 were false and misleading when issued, as set forth in the Company's restatement of the Third Quarter Fiscal 2004 financial results contained in the Company's February 14, 2005 filing with the SEC, as follows:

Quarter Ended (In thousands, except per share data)	December 31, 2003 (As Issued in February 2004)	December 31, 2003 (As Restated)
Net sales	187,346	187,346
Cost of goods sold	173,605	175,730
	-----	-----
Gross profit	13,741	11,616
Selling, general and administrative expenses	12,656	12,630
Restructuring costs	(546)	(546)
	-----	-----
Operating (income) loss	1,631	(494)
Other income (expense) – net	(187)	(187)
Interest expense	1,772	1,772
	-----	-----
Income (loss) before income taxes and cumulative effect of accounting change	46	(2,079)

Income tax expense	22	22
	-----	-----
Income (loss) before cumulative effect of accounting change	24	(2,101)
Cumulative effect of accounting change	—	—
	-----	-----
Net income (loss)	24	(2,101)
	-----	-----
Basic and diluted net income (loss) per common share:		
Income (loss) before cumulative effect of accounting change	0.00	(0.05)
Cumulative effect of accounting change	—	—
	-----	-----
Net income (loss)	0.00	(0.05)

21. On May 18, 2004, Pemstar issued a press release (listing Defendant Lea as the contact person) announcing the Company's financial results for both the fourth fiscal quarter and fiscal year ended March 31, 2004 ("Fourth Quarter Fiscal 2004"). On or about June 14, 2004, the Company filed its annual report for the fiscal year ended March 31, 2004 on Form 10-K with the SEC (the "Fiscal 2004 10-K"), which was signed by Defendants Berning and Lea, repeating and providing more detail concerning the results for Fourth Quarter Fiscal 2004 and the fiscal year ended March 31, 2004 contained in the May 18, 2004 Press Release. The financial results reported for the Fourth Quarter Fiscal 2004 and the fiscal year ended March 31, 2004 were false and misleading when issued, as set forth in the Company's restatement of the Fourth Quarter

Fiscal 2004 and fiscal year ended March 31, 2004 financial results contained in the Company's

February 14, 2005 filing with the SEC, as follows:

Quarter Ended (In thousands, except per share data)	March 31, 2004 (As Issued in June 2004)	March 31, 2004 (As Restated)
Net sales	186,050	186,050
Cost of goods sold	170,442	171,693
	-----	-----
Gross profit	15,608	14,357
Selling, general and administrative expenses	15,128	15,128
Restructuring	295	295
Amortization	27	27
	-----	-----
Operating income (loss)	158	(1,093)
Other income (expense) – net	91	91
Interest expense – net	(1,893)	(1,893)
	-----	-----
(Loss) income before income taxes and cumulative effect of an accounting change	(1,826)	(3,077)
Income tax expense (benefit)	203	203
	-----	-----
(Loss) income before cumulative effect of accounting change	(2,029)	(3,280)
Cumulative effect of accounting change	–	–
	-----	-----
Net (loss) income	(2,029)	(3,280)

Basic and diluted (loss)		
income per common		
share:		
(Loss) income before		
cumulative effect of		
accounting change	(0.04)	(0.07)
Net (loss) income	(0.04)	(0.07)

22. On July 27, 2004, Pemstar issued a press release (listing Defendant Lea as the contact person) announcing the Company's financial results for the first fiscal quarter ended June 30, 2004 ("First Quarter Fiscal 2005"). On or about August 13, 2004, the Company filed its quarterly report for the First Quarter Fiscal 2005 on Form 10-Q with the SEC (the "August 2004 10-Q"), and repeated the results for the First Quarter Fiscal 2005 contained in the July 27, 2004 Press Release. The August 2004 10-Q was signed by Defendants Berning and Lea. The financial results reported for the First Quarter Fiscal 2005 were false and misleading when issued, as set forth in the Company's restatement of the First Quarter Fiscal 2005 financial results contained in the Company's February 14, 2005 filing with the SEC, as follows:

Statement of Operations – Restatement

	For the Three Months Ended June 30, 2004	
	As Previously Reported	As Restated
Sales	200,645	196,680
Cost of sales	183,776	180,520
Gross profit	16,869	16,160
Operating income (loss)	2,094	1,386
Income (loss) before income taxes	1,455	747
Net income (loss)	1,234	525
Basic and diluted income (loss) per common share	0.03	0.01

## Balance Sheet – Restatement

	For the Three Months Ended June 30, 2004	
	As Previously Reported	As Restated
Cash and cash equivalents	11,738	11,778
Accounts receivable, net	124,424	120,026
Recoverable income taxes	1,075	689
Inventories, net	93,589	96,158
Prepaid expenses and other	12,591	13,595
Other assets	6,128	6,001
Cash overdraft	3,885	3,057
Accounts payable	99,401	105,108
Accrued expenses and other	21,234	21,250
Accumulated deficit	(93,494)	(99,687)
Total shareholders' equity	164,457	158,264
Total assets/total liabilities and shareholders' equity	392,553	391,255

23. According to the restated Form 10-Q for the period ended June 30, 2004, filed with the SEC on February 14, 2005, the financial statements originally reported for the First Fiscal Quarter ended June 30, 2004 were materially misleading because they overstated sales revenue by approximately \$4 million, reflecting \$4 million of product that was sold and repurchased by the Company during the quarter in a sham transaction designed to create the appearance of revenue but without any legitimate economic substance. On May 18, 2004, during the quarter that would end on June 30, 2004, Defendants projected estimated revenue of \$180-190 million for that quarter, and analysts' estimates of revenue ranged as high as \$195 million.

**Misrepresentations Concerning Pemstar's Internal Controls**

24. In each annual report on Form 10-K and quarterly report on Form 10-Q filed during the Class Period, each of which was signed by Defendants Berning and Lea, Defendants

represented that the Company had conducted an evaluation of the effectiveness of the design and operation of the Company's disclosure controls and procedures, and that this evaluation was conducted under the supervision and with the participation of the Company's Chief Executive Officer (Defendant Berning) and its Chief Financial Officer (Defendant Lea). Each of these SEC filings on Form 10-K and Form 10-Q further stated that based upon this evaluation, Defendants Berning and Lea had concluded that the Company's disclosure controls and procedures were effective in timely alerting them to material information relating to the Company (including its consolidated subsidiaries) required to be included in the Company's periodic SEC filings.

25. However, at a minimum, at least Defendant Berning was aware of controls and procedures problems related to Pemstar Mexico. Indeed, according to Confidential Witness "C," one telephone conference call took place prior to the Class Period between Defendant Berning and senior managers and employees at Pemstar Mexico concerning the fact that the general ledger in Mexico was out of balance with the perpetual records and permanent data records. The variances were described as "huge" by Confidential Witness "C," who participated in these telephone conferences with Defendant Berning. Further, when Ernst & Young, Pemstar Mexico's auditor at that time, sought to resolve this issue, General Manager Ledesma intimidated the Mexican Ernst & Young auditors into not properly reflecting the financial information.

26. Other internal accounting controls also were awry in Mexico. For example, the results of inventory counts conducted at Pemstar Mexico did not agree with the Company's financial records, according to Confidential Witness "A," and as discussed in detail below.

27. Defendants' representations concerning Pemstar's internal controls, the evaluation

by Defendants of those procedures, and the conclusions reached by Defendants concerning the effectiveness of the Company's disclosure controls and procedures contained in each annual report on Form 10-K and quarterly report on Form 10-Q filed during the Class Period, alleged in paragraph 24 above, were materially false and misleading when issued. Specifically, in the restated annual report on Form 10-K for the fiscal year ended March 31, 2004 (the "Restated 2004 10-K") and the restated quarterly report on Form 10-Q for the fiscal quarter ended June 30, 2004 (the "Restated June 2004 10-Q"), Defendants made the following admissions concerning the Company's controls:

#### ITEM 9A. CONTROLS AND PROCEDURES

##### Disclosure Controls and Procedures

\* \* \*

Based on an investigation of these discrepancies conducted at the direction of the audit committee by an independent third party, the Company determined that these discrepancies resulted from various improper accounting practices engaged in by its accounting staff in Mexico, including not properly posting transactions, inappropriate journal entries, standard costing errors and improper account reconciliations. As a result of these discrepancies the Company is restating its previously reported financial statements for the fiscal year ended March 31, 2004 and quarter ended June 30, 2004 (see Note 17 to the Company's Consolidated Financial Statements (audited) for the fiscal year ended March 31, 2004 and Note H to the Company's Consolidated Financial Statements (unaudited) for the fiscal quarter ended June 30, 2004 for more information concerning the nature and scope of the restated items in each period). **The Company also determined that the errors in its Consolidated Financial Statements were due in part to material weaknesses in its disclosure controls and procedures with respect to its Mexico operations which prevented the necessary information from being accumulated and**

**communicated to the Company's management as appropriate to allow for timely decisions regarding required disclosure.**

\* \* \*

#### Internal Control Over Financial Reporting

During the fiscal quarter ended March 31, 2004, there were no changes made in our internal control over financial reporting (as defined in Rule 13a – 15(f) under the Securities and Exchange Act of 1934, as amended) that materially affected, or are reasonably likely to materially affect, our internal control over financial reporting.

**In the light of restatement [sic] of the Company's previously issued financial statements for the fiscal year ended March 31, 2004 and fiscal quarter ended June 30, 2004, the Company's management has concluded that there were significant deficiencies in the design or operation of its internal control over financial reporting in its Guadalajara, Mexico operation which did adversely affect the Company's ability to record, process, summarize and report financial data. Management believes that such deficiencies represented material weaknesses in its internal control over financial reporting that resulted in misstatements in its financial statements for fiscal year ended March 31, 2004 and quarter ended June 30, 2004.**

(emphases added)

#### **Misrepresentations Concerning Pemstar's Relationships With Its Suppliers**

28. The 2003 10-K also stated the following concerning the Company's relationships with its suppliers:

We have strong relationships with a broad range of materials and component suppliers and distributors based on our commitment to use them on a preferred basis. In addition, our product design and volume procurement capabilities enhance our ability to secure supplies of materials and components at advantageous pricing.

29. Defendants' representations alleged in paragraph 28 above were materially false and misleading when made because Defendants failed to disclose the fact that the Company's vendors repeatedly refused to ship components to Pemstar due to Pemstar's significant problems paying vendors on time, as reported by Confidential Witness "B" and discussed in detail below.

**Strong Inference of Scienter for Pemstar and Individual Defendants**

30. The following additional facts, individually and/or collectively, give rise to a further strong inference that the Defendants issued the materially false and misleading statements identified in paragraphs 15-23 above knowingly or recklessly.

**Confidential Witness "A"**

31. In September or October 2003, Pavageua was fired by Pemstar. Pavageua's replacement, Jorge Ramirez, hired Confidential Witness "A" to perform a Financial Analysis of Pemstar Mexico. The report, which was issued in December 2003 (the "December 2003 Report"), stated that Pemstar assets were overstated by at least \$3.5 million for the following reasons:

- a. Pemstar Mexico created invoices for product that never shipped.

Pavageua had a secret agreement with a customer that allowed Pavageua to inflate Pemstar Mexico's accounts receivable and revenue, without a corresponding increase in cost of goods sold. Pavageua used these phony invoices to reach quarterly revenue goals. For example, in February or March 2004, Confidential Witness "A" discovered a \$500,000 invoice that had not been collected and for which no shipments ever had been made, and which was dated immediately prior to the end of the March or June 2003 quarter. Confidential Witness "A"

showed this phony invoice to Controller Larson and General Manager Ramirez. According to Confidential Witness "A," Ramirez said that Controller Larson then showed the phony invoice to Defendant Bauer. Confidential Witness "A" also discovered two or three additional phony invoices, for amounts smaller than \$500,000, just prior to the end of the March or June 2003 quarter. (Indeed, according to Confidential Witness "A," in mid-2003, responsibility for Pemstar Mexico's accounts receivable and accounts payable was moved to Pemstar's international headquarters in Minnesota.)

b. Cycle inventory counts were conducted and variances were noted with respect to the inventory records, but the variances were not recorded in the financial records. The unrecorded variances resulted in approximately \$0.8 million to \$1 million of excess inventory in Pemstar's financial statements. After the issuance of the December 2003 Report, a physical audit was conducted at the insistence of General Manager Ramirez and Confidential Witness "A."

c. Worthless scrap material had not been reported for one year, and the report concluded that an excess of approximately \$500,000 was carried on Pemstar's books attributable to this scrap. Worthless scrap was counted as inventory, even though it was clearly identified within the Pemstar Mexico factory and was segregated from the remainder of the inventory. During the Class Period, Confidential Witness "A" spoke to Jaime Sandoval, a financial analyst who reported directly to Pemstar Mexico Controller Gonzalez, about the scrap issue. Sandoval told Confidential Witness "A" that General Manager Pavageua had personally told him not to separately list worthless scrap on his financial reports. This falsified the balance sheet by making the carrying value of inventory appear higher than it actually was, and by making the cost of

sales, as reflected in the income statement, appear lower than it actually was.

d. Pemstar Mexico possessed approximately \$400,000 of obsolete material that was improperly being carried as inventory. Mark Malde, Pemstar's Vice President of Material, drafted a monthly report showing all material in Pemstar's inventory, and he visited Mexico in connection with those duties.

e. Inventory was not reduced (nor cost of goods sold increased) by an amount that represented the full cost of items shipped to customers, including products made for customer Efficient Networks, Inc. If a company sells (uses) inventory, it must reflect as costs of goods sold the entire original cost of the inventory. However, when Pemstar sold (used) inventory at a lower price than the original cost, it reflected only the lower price as part of costs of goods sold, thereby leaving the difference as (phantom) inventory, resulting in overstated inventory and understated costs of goods sold.

32. According to Confidential Witness "A," in 2003, General Manager Pavageua had asked Ernst & Young's Mexican accountants to sign documentation confirming that Pemstar Mexico followed GAAP, and when the Mexican Ernst & Young auditors refused to sign the form, Pavageua fired the firm and replaced it with a local Mexican accounting firm.

33. Around February 2004, after Confidential Witness "A" issued the December 2003 Report, he began reporting directly to Kevin Larson, Pemstar's Controller who was based in international headquarters in Rochester, Minnesota. Larson reported directly to Defendant Lea, Pemstar's CFO. According to Confidential Witness "A," he was told that his monthly reports to Controller Larson, which also were sent to General Manager Ramirez, were shared by

Controller Larson with his boss, Defendant Lea.

34. From February to April 2004, Confidential Witness "A" also made lists of action items that Confidential Witness "A" e-mailed to Controller Larson and regularly discussed with him. The lists contained approximately 25 action items, including the issues from the December 2003 Report prepared by Confidential Witness "A" and set forth above, as well as other issues uncovered by Confidential Witness "A."

35. In addition, Confidential Witness "A" also prepared a monthly financial plan that was sent to both General Manager Ramirez and Controller Larson. General Manager Ramirez prepared the "Monthly Operational Report" (described below in further detail by Confidential Witness "D") that was sent to his boss, Defendant Bauer. General Manager Ramirez told Confidential Witness "A" that he rolled all of the information in Confidential Witness "A's" monthly financial plans into the "Monthly Operational Report" that he sent directly to Defendant Bauer each month by e-mail. Controller Larson also passed the information in the monthly financial plans on to his boss, Defendant Lea.

36. Confidential Witness "A" also met several times with Defendant Lea in Mexico, from November 2003 to April 2004, concerning the financial statements. Confidential Witness "A" was told that Defendant Lea was a former member of Pemstar's Board of Directors who had taken the CFO position to solve the problems in Mexico.

37. In March 2004, Pemstar Vice President and Principal Accounting Officer Larry Degen told Confidential Witness "A" that he was extremely angry when he learned that General Manager Pavageua had fired the Mexican Ernst & Young accountants. That same month, the

Mexican Ernst & Young accountants were re-hired as Pemstar Mexico's outside accountants.

38. Eventually, in May 2004 (just one month before Ernst & Young resigned as Pemstar's outside auditors), the Mexican Ernst & Young accountants refused to sign off on Pemstar Mexico's financial data, according to Confidential Witness "A."

39. In April 2004, Confidential Witness "A" met with Doug Titus, a Vice President of Operations who had come from international headquarters in Minnesota to review Pemstar Mexico's operations. Based on Confidential Witness "A's" reports, Titus agreed that Pemstar Mexico's financial records were overstated by at least \$3 million. As a result, according to Confidential Witness "A," Titus fired General Manager Ramirez and others in April 2004.

**Confidential Witness "B"**

40. Confidential Witness "B" attended the Company's "Executive Meetings," which were held on either Monday or Tuesday each week, starting at either 3 or 4 p.m. The meetings were 60-90 minutes in length, and were attended by the following Pemstar executives: Defendant Al Berning (CEO); Defendant Gregory Lea (CFO); Defendant Roy Bauer (COO); Bill Lind (Head of Sales); Larry Degen (Vice President and Principal Financial Officer); Gary Miller (Vice President of Sales); Mark Malde (Vice President of Material); Gary Moore (Vice President of Sales); Shayn Carlson (Executive Director of Financial Planning and Investor Relations); Confidential Witness "B" and others.

41. In the "Executive Meetings," according to Confidential Witness "B," those in attendance reviewed and analyzed weekly and monthly reports, broken down by site and by customer, that included information on inventory and gross margins. In addition, on numerous

occasions during the Class Period, those in attendance began to discuss the issue of the financial and accounting problems at Pemstar Mexico with the Individual Defendants, but the Individual Defendants tabled the discussion of those issues in the “Executive Meetings” and instead considered the issue only in either meetings limited to only the most senior Pemstar executives, referred to as the “Super Honcho” meetings, or a special breakout meeting attended only by the Individual Defendants and a very limited number of other Pemstar executives.

42. The “Super Honcho” meetings (as they were called by Pemstar’s non-executive employees) were held in a conference room at Pemstar’s international headquarters in Rochester, Minnesota, and Confidential Witness “B” was able to see who was in the meeting. Near the end of the Class Period, according to Confidential Witness “B,” the Company installed fogged glass to obscure the attendees and their presentations.

43. The “Super Honcho” meetings were attended by Defendant Berning, Defendant Lea, Defendant Bauer, and Lind. These meetings also occurred every week, and according to Confidential Witness “B,” the financial results reviewed at the “Super Honcho” meetings two weeks prior to the public release of financial results were materially worse than the financial results that were subsequently publicly announced by the Company.

44. Every day from February 2003 through February 2004, Confidential Witness “B” spent half of his time at work attempting to convince vendors to keep open Pemstar’s credit lines. According to Confidential Witness “B,” Defendant Lea and Confidential Witness “B” also made these calls side-by-side from February 2003 through February 2004, with Defendant Lea calling all vendors that were owed \$10 million or more. Confidential Witness “B” also personally

watched as Defendant Lea proactively called larger accounts in an attempt to keep the credit lines open. Even though Confidential Witness “B” stopped making these calls after February 2004, Defendant Lea continued to make these calls, according to Confidential Witness “B.”

45. According to Confidential Witness “B,” from February 2003 through January 2005, Pemstar was forced – every month – to close production lines because vendors were refusing to send parts to Pemstar until they were paid.

46. For example, according to Confidential Witness “B,” between February 2003 and February 2004, Pemstar owed a supplier named Arrow as much as \$50-\$60 million. Pemstar’s contract with Arrow called for payment within 45 days, but Pemstar never paid on time from February 2003 through February 2004, according to Confidential Witness “B.” With respect to other vendors, if Pemstar owed payment within 60 days, Pemstar would routinely not pay for 80-90 days, according to Confidential Witness “B.”

**Confidential Witness “C”**

47. Confidential Witness “C,” who was responsible for the supply chain and inventory at Pemstar Mexico, authored a “Breakeven Report” in April 2002 concerning the projected profitability of Pemstar Mexico for the period from April 2002 through June 2003. This inaptly named “Breakeven Report” concluded that Pemstar Mexico would run at an operating loss of at least \$1.2 million per year during that time period.

48. The so-called “Breakeven Report” was shared with then-COO Paul Singh, who set up a meeting of the team that ran Pemstar’s Mexico operations, as well as other Pemstar leaders including Confidential Witness “D,” Pemstar’s International Financial Controller (also

based in Minnesota), who had responsibility for the Company's profit and loss figures. At the meeting, Confidential Witness "C" disclosed to Confidential Witness "D" and the others in attendance that it would be impossible for the Mexican facility to ever become profitable. Confidential Witness "C" said that Confidential Witness "D" gave the "Breakeven Report" – and the information concerning Pemstar Mexico's inability to ever show a profit – to his boss, Defendant Lea, the Company's CFO.

49. Among other things, the "Breakeven Report" concluded that Pemstar Mexico's overhead was too high for the facility to ever show a profit, according to Confidential Witness "C." Indeed, the "Breakeven Report" described the spiraling labor and management costs as "out of control."

50. According to Confidential Witness "C," Defendant Berning spoke on a telephone conference call in 2002 with Confidential Witness "C" and a Senior Manager in Mexico during which Defendant Berning complained that Pemstar Mexico had been concealing accurate financial data from Defendant Berning.

51. The bonus for the Director of Manufacturing at Pemstar Mexico was directly tied to producing non-defective work product. The Director of Manufacturing received unwarranted bonuses because Pemstar did not have an effective quality control process in place. Confidential Witness "C" performed an analysis of the defective product in inventory in May 2002, and concluded that approximately \$1 million of such inventory needed to be written off.

52. According to Confidential Witness "C," all of Pemstar Mexico's senior executives knew about the profitability issues in Mexico. Confidential Witness "D" was told by Curt

Anderson, Pemstar's Director of Engineering, that Defendant Berning and Singh had also met regularly and discussed Pemstar Mexico's operations.

53. In addition to Defendant Berning, Defendant Lea also was involved in the accounting processes for Pemstar Mexico because, according to Confidential Witness "C," it was required that both Defendant Berning and Defendant Lea review Pemstar Mexico's financial data. Defendant Lea also attended the bi-annual meetings of General Managers and International Program Management Directors, which were attended by 30-50 Pemstar managers from around the world, and which were held in Minnesota, Mexico, and other locations. The leadership from the host country always attended these meetings, so that the managers could learn from one another. Financial issues always were discussed at these meetings, and at a July 2002 meeting that Defendant Lea attended in Rochester, Minnesota, Confidential Witness "C" watched as Defendant Lea confronted the Pemstar Mexico General Manager Pavageua concerning the Mexican facility's financial issues.

**Confidential Witness "D"**

54. Confidential Witness "D," Pemstar's International Financial Controller, had responsibility for reviewing the Company's profit and loss. Confidential Witness "D" received a "Monthly Financial Report" each month from each business unit in the Company, including Pemstar Mexico. According to Confidential Witness "D," the document was sent by e-mail as a Microsoft Excel Spreadsheet.

55. After Confidential Witness "D" reviewed the "Monthly Financial Report," Confidential Witness "D" sent this spreadsheet to the office of Controller Kevin Larson, where

the data was included in the “Monthly Consolidated Report.” According to Confidential Witness “D,” the “Monthly Consolidated Report” was read by Defendant Lea, Controller Larson, and Confidential Witness “D.”

56. After Defendant Lea, Controller Larson, and Confidential Witness “D” read and analyzed the “Monthly Consolidated Report,” the Pemstar business units, including Pemstar Mexico, were contacted for more information. As part of Confidential Witness “D’s” normal duties, Confidential Witness “D” was asked by Defendant Lea to follow up on specific items related to Pemstar Mexico and other business units.

57. According to Confidential Witness “D,” when Defendant Bauer became Chief Operating Officer in 2001, he recognized that the information provided by the General Managers of Pemstar’s business units, including Pemstar Mexico, contained information presented in multiple formats. Therefore, Defendant Bauer created a new report, called the “Monthly Operational Report,” that every Pemstar business unit, including Pemstar Mexico, was required to send to him each month, according to Confidential Witness “D.” Confidential Witness “D” identified the six “Dashboards” of information that were included in every “Monthly Operational Report” – Material/Inventory, Finance, Operations, Quality, Human Resources, and Issues. According to Confidential Witness “D,” the Material/Inventory Dashboard included data on scrap rate, obsolete inventory, work in progress, finished goods, out of stock, and other data; the Finance Dashboard included gross margin trends, aging of accounts receivable, sales trends, and other data; the Operations Dashboard included manufacturing yield, utilization of equipment, re-work levels, rejects, customer returns, and other data; the Quality Dashboard included on-time

delivery, red flags (indicating a problem area that needs to be addressed), green flags (indicating a problem area that has been fixed), and other data; the Human Resources Dashboard included head count and other data; and the Issues Dashboard included problems that needed to be addressed but were not associated with another Dashboard (one example is an account receivable problem with a particular customer).

58. Each month, Confidential Witness “D” witnessed Defendant Bauer talking to each business unit’s General Manager, including the General Manager of Pemstar Mexico, to discuss the contents of the unit’s “Monthly Operational Report.” According to Confidential Witness “D,” this thorough analysis would consume an entire work day for Defendant Bauer each month.

59. Confidential Witness “D” also discussed with Defendant Lea the June 2004 resignation of Ernst & Young as Pemstar’s outside accountants, about which Ernst & Young informed Pemstar just eight days after the filing of the 2004 10-K that was subsequently restated. Defendant Lea told Confidential Witness “D” that Ernst & Young was resigning because the amount of money it was receiving for serving as Pemstar’s accountants did not sufficiently compensate it given the potential exposure for the accounting issues at Pemstar Mexico and other business units. Defendant Lea also told Confidential Witness “D” that Ernst & Young was aware that Arthur Andersen had a client with a problem similar to Pemstar’s Mexico problem, and Arthur Andersen subsequently went out of business, so Ernst & Young saw resigning from the Pemstar account as a method of reducing risk.

#### **Additional Scierter Allegations**

60. In addition to the facts alleged above, the following additional facts individually

and/or collectively, give rise to a further strong inference that the Defendants issued the materially false and misleading statements identified in paragraphs 15-23 above knowingly or recklessly.

**Pemstar's April 2003 Credit Line**

61. Defendants were motivated to issue their financial statement misrepresentations in order to obtain critical financing for Pemstar, which was necessary to pay vendors, as failure to pay vendors was causing vendors to stop shipping materials to the Company. Because vendors were ceasing shipments to Pemstar, the Company was forced to stop manufacturing products every month, as set forth above.

62. As reported by the Company in an SEC filing filed on May 2, 2003 on Form 8-K, (and signed by Defendant Lea), on April 25, 2003, the Company entered into a Loan and Security Agreement by and among the Company, Turtle Mountain Corporation, Pemstar Pacific Consultants, Inc., Gentlelife, Inc., Congress Financial Corporation, and Fleet Capital Corporation, which provided Pemstar with a revolving line of credit of up to \$90 million (the "Loan Agreement"). The Loan Agreement provided, *inter alia*, that the amounts that Pemstar was permitted to borrow under the Loan Agreement were determined by the Company's "eligible collateral." The criteria for determining "eligible collateral" included amounts of Pemstar's inventory and accounts receivable, which as discussed below, were materially overstated by the Company during the Class Period.

63. In addition, the Loan Agreement required the maintenance of certain minimum cash flow levels, which would not have been achieved if Pemstar had paid vendors when amounts were due, as set forth above.

64. The inventory overstatement in the Form 10-Q for the period ended June 30, 2003, enabled the Company to report \$4.9 million of borrowing available under its new credit facility. If Defendants had not overstated inventory by this amount, the Company would not have had additional credit available, production lines would be closed, and other events that would cripple the Company would have occurred.

65. By misrepresenting the Company's financial results and by manipulating vendor payments, as set forth above, Defendants were able to obtain loans and maintain their credit lines.

#### **Pemstar's August 2003 Secondary Offering**

66. Defendants were also motivated to misrepresent Pemstar's financial condition and results in order to permit Pemstar to sell stock at artificially high prices in a Secondary Public Offering.

67. In August 2003, the Company received proceeds of approximately \$20.1 million from a Secondary Offering of approximately 7.5 million shares of Company stock. The Registration Statement and Prospectus for the Secondary Offering reported, inter alia, the false and misleading financial information previously reported for the fiscal year ended March 31, 2003 and the first fiscal quarter ended June 30, 2003, described in paragraphs 15-17 above. By misrepresenting the Company's financial results, cash flow, and internal controls in the Registration Statement and Prospectus, as described above, Defendants were able to receive a material, necessary cash infusion.

#### **Defendants' Further Access to Information**

68. In addition to the regular and special reports provided to Pemstar management, as

discussed above, management – and especially Defendants and other senior executives – had access to all information about inventory (including Mexico) through the Company’s enterprise resource planning (“ERP”) systems. Indeed, Defendants touted Pemstar’s ERP system in the Company’s SEC filings, specifically stating that it monitored “quality data” (i.e., scrap and worthless inventory data), provided “product and production information,” and provided Defendants “with real-time financial and materials management data.”

69. The inventory problems discussed above also were known to Defendants because they were closely monitoring the Company’s important Mexico facility.

a. Inventory in Mexico amounted to approximately \$12 million, according to Confidential Witness “A,” and total inventory at the end of the fiscal year ended March 31, 2004 was \$101.694 million.

b. The Pemstar Mexico facility constituted a “core” business operation. It served as a primary order fulfillment center, enabling the Company to provide low-cost manufacturing and order fulfillment services for its customers on a global basis, according to the SPO Prospectus.

c. As discussed above, Defendants had access to the information in the Company’s ERP system.

d. Creation of sales invoices and the recordation of vendor invoices (and, therefore, all information about the fictitious invoices and accounts payable) were controlled by the corporate offices in Minnesota. According to Confidential Witness “A,” in mid-2003, responsibility for Pemstar Mexico’s accounts receivable and accounts payable was moved from

Mexico to Pemstar's international headquarters in Minnesota.

**Loss Causation**

70. Defendants' material misrepresentations described in paragraphs 15-23 above caused Plaintiff and the Class to suffer losses.

71. On June 24, 2004, after the market closed, the Company filed a current report on Form 8-K with the SEC, which was signed by Defendant Lea, and stated that the Company had been informed by Ernst & Young on June 22, 2004 that the accounting firm would resign as the Company's independent auditor effective upon the completion of the quarterly review of the Company's fiscal quarter ending June 30, 2004. On June 25, 2004, the trading day after the announcement, Pemstar stock dropped to a price of \$1.97 per share, more than a 12 percent drop from the previous day's closing price, on extremely heavy volume of over 5.5 million shares – more than seven times the previous day's trading volume.

72. On November 3, 2004, after the market closed, Pemstar issued a press release (listing Defendant Lea as the contact person) announcing that the Company had launched an investigation of certain accounting discrepancies related to its Guadalajara, Mexico facility, due to difficulty in obtaining satisfactory explanations for specific items, which were identified during the company's normal reconciling process. On November 4, 2004, the trading day after the announcement, Pemstar stock plummeted to a price of \$1.17 per share, more than a 21 percent drop from the previous day's closing price, on nearly five times the previous day's trading volume.

73. On January 13, 2005, before the market opened, the Company filed a current report

on Form 8-K with the SEC, which was signed by Defendant Lea, stating the following:

On January 11, 2005, PEMSTAR Inc. and its management concluded that, due to certain accounting discrepancies at its Mexico facility, its previously filed financial statements for the year ended March 31, 2004, should no longer be relied upon. As previously disclosed, PEMSTAR has been conducting an investigation of accounting discrepancies at its Mexico facility since late October 2004 and has now turned over the results of its inquiry to Grant Thornton LLP and Ernst & Young LLP, its current and former independent audit firms, respectively, for their review and consultation with management in determining the impact on the company's financial results. Management's conclusion regarding continued reliance upon these previously filed financial statements was also discussed with and confirmed by the Audit Committee of the company's Board of Directors. The Company continues to estimate the amount involved as approximately \$6.0 million and currently believes that the majority of that amount will impact the operating results included in its previously filed financial statements for the year ended March 31, 2004. The Company is still considering whether its previously reported financial results for fiscal year 2003 and for the quarter ended June 30, 2004 will be impacted by the results of the Mexico investigation and may need to be restated as well.

74. On January 13, 2005, the trading day following the announcement, Pemstar stock fell more than 13 percent from the previous day's closing price, on more than three times the previous day's trading volume.

#### **Post-Class Period Admissions and Announcements**

75. On February 14, 2005, the Company issued a press release (listing Defendant Lea as the contact person) announcing the conclusion of the investigation into accounting discrepancies related to its Guadalajara, Mexico facility. In the press release, the Company admitted that inappropriate and irregular accounting entries were made at its Mexico facility, and

that the inconsistencies occurred in recording certain expenses, taxes, product costing and asset valuations, and impacted both the statement of operations and the balance sheet of its Mexico operations. As a result of the investigation's findings, Pemstar announced that it was forced to restate and increase its fiscal year 2004 loss by \$5.5 million to (\$25.3) million from (\$19.8) million, and adjusted the fiscal quarter ended June 30, 2004 by \$0.7 million to income of only \$0.5 million from \$1.2 million.

76. On February 14, 2005, the Company issued a restated annual report on Form 10-K for the fiscal year ended March 31, 2004 (the "Restated 2004 10-K"), as well as a restated quarterly report on Form 10-Q for the fiscal quarter ended June 30, 2004 (the "Restated June 2004 10-Q"), all as more particularly alleged above.

77. The Restated 2004 10-K contained the following statements concerning the Company's restatement of its financial results:

#### EXPLANATORY NOTE

This Form 10-K/A of Pemstar Inc. (together with its subsidiaries collectively referred to as "we", "us" and "our") is being filed for the purpose of amending and restating Part II—Items 6, 7, 8 and 9A, Part IV—Item 15, Schedule II, Exhibit 12.1 (Computation of Ratio of Earnings to Fixed Charges) and Exhibit 13.1 (Annual Report Part II) of our Form 10-K for the fiscal year ended March 31, 2004, to reflect the restatement of our Consolidated Financial Statements as of and for the fiscal year ended March 31, 2004. The Company has restated its Consolidated Balance Sheet, Consolidated Statement of Operations, Consolidated Statement of Shareholders' Equity and Consolidated Statement of Cash Flows as of and for the year ended March 31, 2004 to reflect corrections for errors identified as a result of its investigation of certain accounting discrepancies related to its Guadalajara, Mexico operation. Findings of this investigation resulted in increased charges in costs of goods sold and selling,

general and administrative expenses related to fully recording materials costs and expenses, certain taxes, and asset valuations. Accounts payable and inventory were the primary balance sheet accounts affected, with various other accounts being less significantly affected.

See Note 17 to the Consolidated Financial Statements for a discussion of the effect of the restatement.

\* \* \*

#### Note 17. Restatement

Restatement – The Company has restated its Consolidated Balance Sheet, Consolidated Statement of Operations, Consolidated Statement of Shareholders' Equity and Consolidated Statement of Cash Flows as of and for the year ended March 31, 2004 to reflect corrections of errors identified as a result of its investigation of certain accounting discrepancies related to its Guadalajara, Mexico operation. Findings of this investigation resulted in increased charges in costs of goods sold and selling, general and administrative expenses related to fully recording materials costs and expenses, certain taxes, and asset valuations. Accounts payable and inventory were the primary balance sheet accounts affected, with various other accounts being less significantly affected. The effects of the restatement is summarized as follows.

#### Statement of Operations – Restatement

	Year Ended March 31, 2004	
	As Previously Reported	As Restated
Cost of sales	\$621,630	\$626,832
Gross profit	47,816	42,614
Selling, general and administrative expenses	52,023	52,306
Operating loss	(12,275)	(17,760)
Other income (expense) – net	793	794
Loss before income taxes and cumulative effect of accounting change	(19,297)	(24,781)

Net loss	(19,800)	(25,284)
Basic and diluted loss per common share	(0.47)	(0.60)

## Balance Sheet – Restatement

Year Ended March 31, 2004

	As Previously Reported	As Restated
Cash and cash equivalents	\$9,792	\$9,832
Accounts receivable, net	127,583	127,823
Recoverable income taxes	1,122	870
Inventories, net	94,482	93,661
Prepaid expenses and other	14,609	14,806
Other assets	6,477	6,351
Cash overdraft	7,296	7,130
Accounts payable	101,694	106,644
Accrued expenses and other	22,947	22,925
Accumulated deficit	(94,728)	(100,212)
Total shareholders' equity	163,793	158,309
Total assets/total liabilities and shareholders' equity	394,855	394,133

78. On May 24, 2005, the Company issued a press release, which, inter alia, included a statement from Defendant Bauer that the Company was reviewing its options for the Guadalajara, Mexico facility, which would likely include a sale or downsizing.

79. Subsequently, on or about June 22, 2005, the Company filed a current report on Form 8-K with the SEC, which was signed by Defendant Lea, and stated that the Company had decided to exit its manufacturing facilities in Guadalajara, Mexico, resulting from the Company's continued losses from operations in that site. The Company expected to complete its exit by June 30, 2005.

80. In a current report on Form 8-K, filed with the SEC on August 9, 2005 (and signed by Defendant Lea), the Company admitted that in order to exit its Mexico facility by June 30,

2005, it had recorded charges of \$4.333 million (including \$3.272 million of asset write-downs to estimated liquidation value, \$0.912 million for severance costs, and \$0.149 million for associated other costs).

81. In the quarterly report on Form 10-Q for the second fiscal quarter ended September 30, 2005, which was signed by Defendants Berning and Lea and filed on November 9, 2005, Pemstar updated the charges recorded for closing the Mexico facility to at least \$5.026 million (including \$3.282 million of asset write-downs to estimated liquidation value, \$0.916 million for severance costs, \$0.420 million for expected losses on lease commitments, and \$0.408 million for associated other costs).

#### **No Safe Harbor**

82. The statutory safe harbor provided for “forward-looking statements” under certain circumstances does not apply to the misrepresentations identified in this Complaint because the statements were misrepresentations of historical facts or current or past conditions.

83. To the extent any of the misrepresentations identified in this Complaint are deemed to be forward-looking statements, the statutory safe harbor does not apply because Pemstar and the Individual Defendants did not specifically identify those statements as forward-looking statements and the statements were not accompanied by meaningful cautionary statements identifying important factors that could cause actual results to differ materially from those in the purportedly forward looking statements.

84. To the extent that the statutory safe harbor does apply to any statements pleaded herein, Pemstar and the Individual Defendants are liable for those false forward-looking

statements because at the time each of those forward-looking statements was made, Pemstar and the Individual Defendants knew that the particular forward-looking statement was false, and/or the forward-looking statement was authorized and/or approved by an executive officer of Pemstar who knew that those statements were false when made.

### **Class Action Allegations**

85. Plaintiff brings this action as a class action pursuant to Rule 23 of the Federal Rules of Civil Procedure, individually and on behalf of the Class.

86. The members of the Class are so numerous that joinder of all members of the Class is impractical. While the exact number of Class Members is unknown to the Plaintiff at this time and can only be ascertained through appropriate discovery, Plaintiff reasonably believes that there are thousands of members of the Class located throughout the United States. As of June 7, 2004, approximately 45,146,253 Shares were issued and outstanding. During the Class Period, the Shares were actively traded on the NASDAQ National Market under the designation "PMTR."

87. Plaintiff's claims are typical of the claims of the other members of the Class because the damages suffered by Plaintiff and all Class Members arise from and were caused by the same or similar misrepresentations and omissions made by or chargeable to the Individual Defendants as alleged herein. Plaintiff does not have interests antagonistic to, or in conflict with, the Class.

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

- a. whether the federal securities laws were violated by the acts alleged herein;
- b. whether the Defendants misrepresented and/or failed to disclose material facts in the Company's press releases, annual reports, and quarterly reports, as more particularly described above;
- c. whether the market price of the Company's Shares was artificially inflated during the Class Period due to the material misrepresentations and/or nondisclosures complained of herein; and
- d. whether the members of the Class have sustained damages, and, if so, the proper measure of such damages.

89. Plaintiff will fairly and adequately protect the interests of the other members of the Class, and Plaintiff has retained counsel competent and experienced in class and securities litigation to further ensure such protection and intend to prosecute this action vigorously.

90. A class action is superior to other available methods for the fair and efficient adjudication of this controversy. The Class is so numerous and geographically dispersed that it would be impracticable for each member of the Class to bring a separate action or to be joined in an individual action. The individual damages of any member of the Class may be relatively small when measured against the potential costs of bringing this action, and thus make the expense and burden of this litigation unjustifiable for individual actions. In this class action, the Court can determine the rights of all members of the Class with judicial economy.

91. Plaintiff will rely, in part, upon the presumption of reliance established by the fraud-on-the-market doctrine in that:

- a. Defendants made public misrepresentations or failed to disclose material facts during the Class Period;
- b. the omissions and misrepresentations were material;
- c. the stock of the Company traded in an efficient market, as it traded at a high weekly volume, was followed and reported on by securities analysts, had numerous market makers, was eligible to file SEC registration form S-3, and there are empirical facts showing a cause and effect relationship between unexpected corporate events or financial news and an immediate response in the stock price;
- d. the misrepresentations and omissions alleged would tend to mislead a reasonable investor concerning Pemstar's business and/or financial condition; and
- e. Plaintiff and members of the Class purchased their Pemstar stock at prices that were artificially inflated due to Defendants' material misrepresentations and omissions.

92. There will be no difficulty in the management of this litigation which would preclude its maintenance as a class action. The names and addresses of the record owners of the Shares purchased during the Class Period are available from the Company's transfer agent. Notice can be provided to such record owners and all Class Members by a combination of published notice and first-class mail, using techniques and a form of notice similar to those customarily used in class actions arising under the federal securities laws.

**CLAIMS FOR RELIEF**

**COUNT I**

(Against the Defendants for Violations of  
Section 10(b) and Rule 10b-5 Promulgated Thereunder)

93. Plaintiff repeats and re-alleges each and every allegation contained in the foregoing paragraphs as if fully set forth herein.

94. This Count is asserted against the Defendants and is based upon Section 10(b) of the Exchange Act, 15 U.S.C. § 78j(b), and Rule 10b-5 promulgated thereunder by the SEC.

95. During the Class Period, the Defendants engaged in a plan, scheme, conspiracy, and course of conduct, pursuant to which they knowingly or recklessly engaged in acts, transactions, practices and courses of business which operated as a fraud and deceit upon Plaintiff and the other members of the Class; made various untrue statements of material facts and omitted to state material facts necessary in order to make the statements made, in light of the circumstances under which they were made, not misleading; and employed devices, schemes and artifices to defraud in connection with the purchase and sale of securities. Such scheme was intended to, and, throughout the Class Period, did: (a) conceal the adverse facts concerning the Company's operations, particularly with respect to its business and financial condition; (b) artificially inflate and maintain the market price of Pemstar common stock; and (c) caused Plaintiff and the other members of the Class to purchase Pemstar common stock at inflated prices, thus causing injury to Plaintiff and the other members of the Class.

96. Pursuant to the above plan, scheme, conspiracy and course of conduct, each of the

Defendants participated directly or indirectly in the preparation and/or issuance of the SEC filings, press releases and other statements and documents described above, all of which were designed to and did influence the market for Pemstar common stock. Such reports, filings, releases, and statements were materially false and misleading in that they failed to disclose material adverse information and misrepresented the truth about Pemstar's business and financial results.

97. The Defendants had actual knowledge of the materially false and misleading statements and material omissions alleged herein or, in the alternative, the Defendants acted with reckless disregard for the truth in that they failed or refused to ascertain and disclose such facts as would reveal the materially false and misleading nature of the statements made, although such facts were readily available to defendants. Said acts and omissions of the Defendants were committed willfully or with reckless disregard for the truth. In addition, each Defendant knew or recklessly disregarded that material facts were being misrepresented or omitted as described above. As alleged herein, the Defendants acted with scienter in that defendants knew that the public documents and statements issued or disseminated in the name of the Company were materially false and misleading; knew that such statements or documents would be issued or disseminated to the investing public; and knowingly and substantially participated or acquiesced in the issuance or dissemination of such statements or documents as primary violations of the federal securities laws. As set forth elsewhere herein in detail, by virtue of their receipt of information reflecting the true facts regarding Pemstar, their control over, and/or receipt and/or modification of the Company's allegedly materially misleading misstatements and/or their associations with the Company which made them privy to confidential proprietary information

concerning Pemstar, participated in the fraudulent scheme alleged herein.

98. As a result of the dissemination of the aforementioned false and misleading reports, releases and public statements, the market price of Pemstar common stock was artificially inflated throughout the Class Period. In ignorance of the adverse facts concerning Pemstar's business and financial condition that were concealed by the Defendants, Plaintiff and the other members of the Class purchased Pemstar common stock at artificially inflated prices and relied upon the price of the stock, the integrity of the market for the stock and/or upon statements disseminated by the Defendants and were damaged thereby.

99. The misrepresentations and misconduct directly and proximately caused losses, injury and damages to Plaintiff and the Class. The price of Pemstar stock was artificially inflated throughout the Class Period, and the price of Pemstar stock decreased upon disclosure of true facts which had been misrepresented and/or concealed. Plaintiff and the Class purchased their Pemstar stock when the price of that stock was artificially inflated, and held stock at the time of the disclosures of the true facts. The losses suffered by Plaintiff and the Class were caused by the misrepresentations by the Defendants. Had Plaintiff and the other members of the Class known the truth, they would not have purchased said shares or would not have purchased them at the inflated prices that were paid. At the time of the purchases by Plaintiff and the Class, the true value of Pemstar stock was substantially lower than the prices paid by Plaintiff and the other members of the Class.

100. By reason of the conduct alleged herein, the Defendants knowingly or recklessly, directly or indirectly, have violated Section 10(b) of the Exchange Act and Rule 10-5 promulgated

thereunder and caused injury and damages to Plaintiff and the other members of the Class.

**COUNT II**

(Violations of Section 20(a) of the Exchange Act  
Against the Individual Defendants)

101. Plaintiff repeats and re-alleges each and every allegation contained in the foregoing paragraphs as if fully set forth herein.

102. During the Class Period, because of their position of control and authority as senior officers and directors of Pemstar, the Individual Defendants were able to, and did, control the contents of the various reports, press releases and public filings that Pemstar disseminated in the marketplace during the Class Period concerning the Company's results of operations. Throughout the Class Period, the Individual Defendants exercised their power and authority to cause Pemstar to engage in the wrongful acts complained herein. Therefore, the Individual Defendants were "controlling persons" of Pemstar within the meaning of Section 20(a) of the Exchange Act. In this capacity, they participated in the unlawful conduct alleged that artificially inflated the market price of Pemstar common stock.

103. As controlling persons of Pemstar, the Individual Defendants are liable pursuant to Section 20 of the Exchange Act for the violations of Pemstar.

**COUNT III**

(Violations of Section 11 of the Securities Act and  
Item 303 of Regulation S-K Promulgated Thereunder  
Against the Defendants)

104. Plaintiff repeats and re-alleges each and every allegation contained in the foregoing paragraphs as if fully set forth herein, except that Plaintiff expressly excludes and disclaims any

allegations that could be construed as alleging intentional or reckless misconduct or fraud.

Plaintiff asserts only strict liability or negligence claims in this cause of action.

105. This claim is brought pursuant to Section 11 of the 1933 Act, 15 U.S.C. § 77k, on behalf of the Class, against Defendants, and is based upon Defendants' negligence or theories of strict liability.

106. The Registration Statement and Prospectus for Pemstar's August 2003 Offering was contained untrue statements of material facts, and omitted to state material facts required by SEC regulation to be stated therein or that were necessary to make the statements therein not misleading, and failed to adequately disclose material facts, as described above.

107. Pemstar is the issuer of the stock sold via the Registration Statement and Prospectus, and therefore is strictly liable under Section 11 of the Securities Act and Item 303 of Regulation S-K promulgated thereunder.

108. Defendants Berning and Lea, inter alia, signed the Registration Statement and Prospectus filed with the SEC, and therefore are strictly liable under Section 11 of the Securities Act and Item 303 of Regulation S-K promulgated thereunder. None of these defendants made a reasonable investigation or possessed reasonable grounds for the belief that the statements contained in the document were not true, did not omit any material fact, and were not misleading.

109. Defendants violated Subsection (a)(1) of Item 303 of SEC Regulation S-K by failing to identify any known trends or any known demands, commitments, events or uncertainties that would result in or that were reasonably likely to result in the registrant's liquidity increasing or decreasing in any material way. Defendants did not make any disclosure in the Registration

Statement and Prospectus concerning their inability to make timely payments to vendors.

110. Defendants violated Subsection (a)(3)(ii) of Item 303 of SEC Regulation S-K by failing to describe any known trends or uncertainties that had or that the Company reasonably expected would have a material favorable or unfavorable impact on net sales or revenues or income from continuing operations, including disclosing known events that would cause a material change in the relationship between costs and revenues (such as known future increases in costs of labor or materials or price increases or inventory adjustments). Defendants did not disclose in the Registration Statement and Prospectus that the Company's inventory figures were false and therefore needed to be adjusted.

111. By reason of the conduct alleged herein, each Defendant identified in this Claim violated Section 11 of the Securities Act.

112. At the time they purchased Pemstar shares, which purchases were traceable to the Secondary Offering, Plaintiff and the members of the Class were without knowledge of the facts concerning the false or misleading statements or omissions alleged herein. Less than one year has elapsed from the time that Plaintiff and the members of the Class discovered, or reasonably could have discovered, the facts upon which this complaint is based, to the time that Plaintiff filed his complaint. Less than three years have elapsed from the time that the securities upon which this claim is brought have been offered to the public, to the time Plaintiff filed his complaint.

WHEREFORE, Plaintiff demands judgment against Defendants as follows:

A. Determining that the instant action may be maintained as a class action under Rule

23, Federal Rules of Civil Procedure, and certifying the named class Plaintiff;

B. Requiring the Defendants to pay damages sustained by Plaintiff and the Class by reason of the acts and transactions alleged herein;

C. Awarding Plaintiff and the other members of the Class prejudgment and post-judgment interest, as well as their reasonable attorneys' fees, expert fees and other costs; and

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

**JURY DEMAND**

Plaintiff demands a trial by jury.

Dated November 28, 2005

**SCHATZ & NOBEL, P.C.**

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