



IN THE COURT OF CHANCERY OF THE STATE OF DELAWARE  
IN AND FOR NEW CASTLE COUNTY

In Re: INFOUSA, Inc. Shareholders  
Litigation

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:  
: Consol. C.A. No. 1956-CC  
:  
:

**PLAINTIFFS' ANSWERING BRIEF  
IN OPPOSITION TO DEFENDANTS'  
MOTION TO DISMISS**

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## **NATURE AND STAGE OF PROCEEDINGS**

Cardinal Value Equity Partners, L.P. ("Cardinal") filed its original complaint (C.A. No. 1956) on February 22, 2006, which it amended on May 1, 2006. On October 17, 2006, this Court dismissed Cardinal's amended complaint with leave to amend. Bench Ruling, Oct. 17, 2006 Tr. 16. Cardinal filed its second amended complaint on December 15, 2006.

Dolphin Limited Partnership I, L.P., Dolphin Financial Partners, LLC (collectively "Dolphin") and Robert Bartow (together with Cardinal, the "Plaintiffs") filed their complaint (C.A. No. 2486) on October 19, 2006. Over Plaintiffs' objections, on January 22, 2007, this Court ordered the consolidation of Dolphin's and Bartow's action and Cardinal's action. Plaintiffs filed a consolidated complaint (the "Complaint") on February 5, 2007, which the Defendants moved to dismiss. Defendants' filed their Opening Memorandum of Law in Support of Their Motion to Dismiss ("DOB") on March 5, 2007.

This is the Plaintiffs' Answering Brief in Opposition to Defendants' Motion to Dismiss.

## STATEMENT OF FACTS

The Defendants' so-called "Statement of Facts" consists of a recitation of the procedural history of the Cardinal action; a description of the Plaintiffs and the October 19, 2006 board of directors of infoUSA, Inc. ("IUSA" or the "Company"); and a one-paragraph summary of Defendant Vinod Gupta's 2005 attempt to take IUSA private. This abbreviated version of the facts ignores most of the detailed allegations in the Complaint all of which show a supine board whose members take their cue from V. Gupta, IUSA's Chairman, Chief Executive Officer and single largest shareholder. While the Defendants' brief does not address the facts pled in the Complaint, Plaintiffs' Statement of Facts summarizes the numerous particularized facts set forth in the Complaint which, for purposes of this motion, must be taken as true. Most of the allegations are based on IUSA's public filings and on the thousands of pages of documents obtained by Dolphin in an earlier §220 action.

### A. The Plaintiffs

Cardinal beneficially owns approximately 5.6% of the Company's common stock. Compl. ¶3. Dolphin owns 3.6% of the Company's sock and Bartow owns 2,000 shares. Id. In 2006, Dolphin waged a proxy contest which it lost by just a 1% swing notwithstanding V. Gupta's and his affiliates substantial 41% stock holdings. Id. ¶19. All three independent proxy advisory services supported Dolphin's candidates and one service went so far as to say it appears that V. Gupta "abused his position" as CEO. Id. During the course of the proxy contest, V. Gupta exercised options for 1.2 million shares (2.2%) which shares were a significant factor in management prevailing. Id. ¶120. Immediately prior to the proxy contest, the public learned of V. Gupta's beneficial ownership of an additional 4.4% of IUSA stock over and above what he

and IUSA, had been publicly reporting in IUSA's prior SEC filings. Id. ¶4. This repeated under reporting of V. Gupta's beneficial ownership violated the federal securities laws.

## B. The Defendants

Nominal Defendant IUSA is an Omaha, Nebraska based provider of business and consumer financial information products. Compl. ¶15. Its stock is traded on the NASDAQ Global Select Market. Id.

The primary Defendants are IUSA's eight current directors and three recent former directors. The current directors are V. Gupta, George F. Haddix, Vasant H. Raval, Bill L. Fairfield, Anshoo S. Gupta, Elliott S. Kaplan, Bernard W. Reznicek and Dennis P. Walker. The former directors are Martin F. Kahn, who resigned during these proceedings on February 2, 2007 (DOB 6); Harold W. Andersen, who served from 1993 until November 2005; and Charles W. Stryker, who served from May 2005 until January 2006. Id. ¶¶ 5-14.<sup>1</sup>

Most of the Defendants are Omaha businessmen or academics with longstanding ties to V. Gupta, the Company's Chairman, CEO and single largest stockholder. Haddix, a director since 1995, runs his software company in rent-free office space provided by IUSA. Id. ¶5. Haddix co-founded and was part of the original group of investors that led a leveraged buyout of CSG Systems from First Data Corp. DOB Ex. 5. The group included IUSA and former IUSA director, Donald Dixon and his venture firm Trident Capital. Id. ¶5. Haddix is a director at Creighton University in Omaha. V. Gupta has made substantial donations to Creighton and Creighton runs an exchange program with the Vinod Gupta School of Management at the Indian

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<sup>1</sup> Although unreasonably short by other measures, Stryker's 8-month stint on IUSA's board is typical of the tenure of many of IUSA's directors. IUSA has had 24 directors in the past 10 years many of whom have served very brief terms. Compl. ¶14. The board room's revolving door shows that much is amiss at IUSA. Directors who take their duties seriously either leave of their own accord or are forced out shortly after they join the board.

Institute of Technology ("IIT") in Kharagpur, India. Id. ¶¶5-6. V. Gupta graduated from IIT and donated \$2 million to it. Id. ¶8.

Defendant Raval, a director since 2002, is a professor and chair of the Accounting Department at Creighton University. Id. ¶6. His academic salary is materially supplemented by significant director and committee fees paid by IUSA. Id. In 2004 and 2005, Raval received \$96,000 and \$147,000, respectively, in director fees (id.) which fees exceed the average 2004 and 2005 salaries -- \$89,000 and \$91,000, respectively -- of a Creighton professor.<sup>2</sup> He and all other non-employee directors also received a vested option for 10,000 shares of Company stock. Id. ¶5.

Defendant Fairfield, a director since November 2005, runs a venture capital firm in Omaha. Id. ¶7. He is the former Chairman of one of IUSA's wholly-owned subsidiaries, businessCreditUSA.com. Id. He and V. Gupta are trustees of the University of Nebraska Foundation. Id.

Defendant Walker, a director since 2003, is President and CEO of a private jet aviation company in Omaha. Id. ¶12. IUSA gives him rent-free office space and, on at least one

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<sup>2</sup> Official Nebraska Government website: [http://www.ccpe.state.ne.us/PublicDoc/CCPE/reports/factlook/95-05/SectionC/FL\\_95-05\\_Sec\\_C\\_WEB\\_Workbook.xls](http://www.ccpe.state.ne.us/PublicDoc/CCPE/reports/factlook/95-05/SectionC/FL_95-05_Sec_C_WEB_Workbook.xls) Based on average salaries for Creighton professors in the period from 2002 to 2006, Raval received \$450,000 in the aggregate from Creighton; based on IUSA's proxy statements for this same period (Exhibit A hereto), he received a total of \$399,000 in director and committee fees (exclusive of stock options) from IUSA as illustrated in the following table:

Year	Creighton	IUSA
2002	\$88,000	\$12,000
2003	90,000	72,000
2004	89,000	96,000
2005	\$91,000	\$147,000
2006	\$92,000	\$72,000
	<u>\$450,000</u>	<u>\$399,000</u>

occasion, he flew with V. Gupta and V. Gupta's wife on personal travel paid by the Company. Id.

Defendant Reznicek, a director since March 2006, is the former Dean of the College of Business at Creighton University, which is where Defendant Raval teaches and Defendant Haddix is a director. Id. ¶11. Reznicek has been a director of CSG since 1997 and is currently its non-executive chairman. CSG is the company co-founded by Haddix and in which IUSA and former IUSA director Dixon invested. Id.

Defendant Anshoo Gupta, a director since 2005, graduated from IIT in Kharagpur, India as did V. Gupta. Id. ¶8. Anshoo Gupta serves on IIT's Advisory Board. Id. V. Gupta donated \$2 million to IIT and established its Vinod Gupta School of Management. Id.

Defendant Kaplan, a director since 1988, is a senior partner in Robins, Kaplan, Miller & Ciresi, LLP, which is the Company's principal outside law firm. Id. ¶9. Kaplan lists his IUSA board membership on his firm's website as one of only two corporations of which he is a director. Id. His firm has received and receives substantial legal fees from the Company: \$1.1 million in 2006<sup>3</sup> and an average of \$500,000 per year in 2003-2005. Id. ¶9. IUSA is, without doubt, a major client for Kaplan and likely important to his personal compensation.

Defendant Kahn, a director from 2004 until February 2, 2007, is former Chairman and CEO of a company which IUSA bought in 2004. Id. ¶10. Kahn was paid a \$184,000 topping fee in that acquisition. Id. Kahn chaired IUSA's short-lived Special Committee which was formed in June 2005 to consider a going private offer from V. Gupta and disbanded in August 2005 after V. Gupta withdrew his offer. Id.

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<sup>3</sup> IUSA's 2006 Form 10-K at p. 68 (Exhibit B hereto).

Defendant Andersen was a director from 1993 until November 2005. Id. ¶13. He is the former Publisher, President, CEO and Chairman of the Omaha World Herald Company. Id. Andersen was a member of the Company's Audit Committee from at least 1997 until his sudden resignation from it in July 2005 after the Company's shareholders began to question extensive and excessive related party transactions between the Company and V. Gupta. Id. While a director, Andersen also served as a director of two Everest Mutual Funds owned and run by V. Gupta as an investment vehicle for V. Gupta's family and friends. Id. In 2001, the Company invested \$1 million in an Everest Mutual Fund. Id. The Company also bought Everest's office building from V. Gupta for \$2.8 million and assumed the mortgage on it for which V. Gupta was personally liable. Id. Andersen was given rent-free office space, decorated at IUSA's expense, in the Everest building as well as many personal flights on private jets paid for by the Company. Id. At IUSA's expense, he also vacationed on the American Princess Yacht. Id.

Defendant Stryker, a director from May 2005 until January 2006, was Chairman and CEO of a company with which IUSA did business. Id. ¶14. He, too, resigned after IUSA's stockholders began making inquiries into the matters complained of in the Complaint. He was one of IUSA's five shareholders when it went public in 1992. Id.

### C. V. Gupta's Use of the Company's Treasury to Fund His, His Family's and His Friends' Lifestyles

Although a public company, V. Gupta has run IUSA as if he privately owns it. For many years, V. Gupta has used Company money to pay for his expensive and lavish lifestyle, including millions of dollars to pay for personal private jet travel; Gupta family owned homes; luxury cars (a Mercedes SL500R, Hummer, Lexus, Mini Cooper and a Jeep kept in Maui); a catamaran; and an 80-foot yacht docked in Florida called the American Princess. Based on documents produced

in the §220 action, there are no board minutes reflecting that IUSA's directors ever approved of these massive payments to V. Gupta.<sup>4</sup>

The underlying details of these payments first came to public light in 2005-06 when Dolphin exercised its §220 inspection rights and then waged a proxy contest in which it made many of these documents available on its website. *Id.* ¶62.<sup>5</sup> Although the Company's financial statements had very general references with respect to some, but not all, of the related party transactions between IUSA and V. Gupta's privately owned company, Annapurna, the true nature of these transactions, their extent, and other transactions had been concealed. For example, although its usage goes back to the mid-1990's, IUSA never revealed the existence of the American Princess yacht until August 2005 when it filed its second quarterly report. *Id.* ¶¶69, 95. Moreover, in its 2005 Annual Report, the Company stated that it had paid approximately \$1.5 million in 2004 to Annapurna for "usage of the aircraft and related services."<sup>6</sup> *Id.* ¶68. Only the §220 action revealed that a substantial portion of this \$1.5 million for 2004 alone had nothing to do with aircraft usage or related services. *Id.* Rather, it went to pay for personal residences (including a condo in Maui owned by V. Gupta's son), vacations on the American Princess yacht, undefined "travel services" charged and billed by Annapurna and contractor services to decorate the rent free office space which IUSA was giving to Haddix and Andersen.

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<sup>4</sup> IUSA did produce minutes showing that IUSA's Board approved the Company's purchase of a University of Nebraska football stadium skybox from V. Gupta. *Id.* ¶97. The Board approval, however, came *after* the purchase had occurred suggesting that this was a "rubberstamp" rather an independent review. *Id.*

<sup>5</sup> Dolphin initially obtained five years of IUSA records, but based on Dolphin's March 22, 2006 application to the Court, IUSA was required to permit inspection of records relating to V. Gupta's compensation and related party transactions going back to 1998. Dolphin Ltd. P'ship I, L.P. v. infoUSA, Inc., 2006 WL 1071518, \*1 (Del. Ch. Apr. 11, 2006).

<sup>6</sup> Prior to 2004, Annapurna directly owned interests in several private jets that were used by V. Gupta, his family and friends. Annapurna billed IUSA whenever V. Gupta, his family and his friends flew on Annapurna's jets.

Id. Between 2001 and 2005, the Company paid approximately \$8.2 million to Annapurna for these types of expenses. Id. ¶64.

An examination of the documents produced in the §220 action revealed that there was no legitimate business purpose for a vast amount of these expenses. Id. ¶66. For example, the American Princess logbook, the only document produced by IUSA to justify the usage of the yacht, does not evidence any business purpose for its use. Id. ¶66.<sup>7</sup> To the contrary, the log book appears to include pleasure trips taken by V. Gupta and/or his sons. Moreover, the Company's records show that V. Gupta routinely charged IUSA for his own personal private jet travel as well as that of his wife, sons and family friends to vacation in the Caribbean, Mexico and Hawaii. For example, in 2002, IUSA paid almost \$150,000 to fly V. Gupta, his family and a former high ranking government official and the official's family members to Acapulco for a New Year's vacation. Id. ¶78. The Company paid at least \$82,500 for this former official and eight companions (including two of V. Gupta's sons) to fly on a private jet to attend the 2005 World Economic Forum in Switzerland. Id. ¶73.<sup>8</sup>

V. Gupta is a close personal friend of this former high ranking government official. Id. ¶115. He has raised political contributions for both the official and the official's wife and donated a million dollars to the official's library as well as at least \$250,000 out of IUSA funds to his sponsored charity. Id. While this former official was in office, he offered V. Gupta a position of prestige and later appointed him to the board of a major cultural institution. Id.

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<sup>7</sup> The log book, which is referred to in the Complaint, is posted on Dolphin's website, at [www.iusaaccountability.com](http://www.iusaaccountability.com). It is attached to the brief as Exhibit C.

<sup>8</sup> Since 2001, the Company has paid approximately \$900,000 in private jet expenses for this former high ranking official and his family members. Id. ¶111.

V. Gupta has done much more than simply provide this official with private jet travel and charitable donations at IUSA expense. In 2002, he caused the Company to enter into a three year consulting agreement with this official which was renewed for another three years in 2005. Id. ¶¶111-112. Under the 2002 agreement, the Company paid the official \$1.2 million to provide "confidential advice and counsel" to V. Gupta for purposes of "strategic growth and business development." Id. ¶111. The 2002 agreement also gave the official an option for 100,000 shares under IUSA's 1997 Stock Option Plan without board or board committee approval in violation of the 1997 Plan. Id.

#### D. The Raval Report

In February 2005, Defendant Raval prepared a report that analyzed a portion of the payments made by IUSA to Annapurna and another V. Gupta company, Aspen Leasing, in 2004 (the "Raval Report") (Exhibit D hereto). Compl. ¶68. Although IUSA designated the Raval Report as confidential in the §220 action and never publicly disclosed it; this Court lifted IUSA's confidential designation of it (and many other records) in connection with Dolphin's proxy contest. Dolphin Ltd. P'ship I, 2006 WL 1071518 at \*1. The Raval Report admitted significant problems with the related party payments IUSA was making to Annapurna and Aspen Leasing.

Unfortunately, the analysis in the Raval Report was limited just to payments made in 2004. Raval did not investigate over \$14 million of related party transactions and direct payments going back to 1998 when V. Gupta re-installed himself as the Company's CEO. Raval also did not attempt to determine how much of the \$929,000 paid to Annapurna for private jet travel in 2004 was for non business purposes. Nevertheless, for the year 2004 alone, the Raval Report identified over \$600,000 of charges for personal and unsupportable items that Raval concluded "should be borne by V. Gupta." Compl. ¶103. This included payments for the

personal residences, the yacht, undefined "charges for travel services" and premiums on a personal insurance policy for V. Gupta.

Among other things, the Raval Report also stated that the Company's practice of paying fixed monthly amounts to Annapurna for the use of V. Gupta's personal residences was "difficult to support under any circumstances." Id. ¶103. It also advised that the Company should be compensated for the free office space provided to directors Walker and Haddix and former director Andersen (id. ¶104) and stated "[e]mployees affected should consider reporting unreimbursed employee expenses on the individual tax return to the IRS." Despite Raval's conclusions, remarkably there is no evidence in the Company's public filings or in the books and records produced pursuant to Dolphin's §220 demands that V. Gupta (or any other directors) ever reimbursed the Company for the personal expenses charged to IUSA.

Raval emailed his report to Defendants Kaplan, Haddix, Kahn and Walker. Id. ¶69. Although they were aware that IUSA was paying for V. Gupta's personal residences and the luxury yacht, they knowingly signed off on the Company's 2004 and 2005 Form 10-Ks, both of which misleadingly characterized the personal residence and yacht expenses as "usage of the aircraft and related services." Id. ¶69. Moreover, none of these directors asked Raval or the Company's accountants to determine the amount of similar inappropriate related party transactions for periods before or after 2004 that should be borne by V. Gupta or to examine his and his family's sizeable plane usage. Nor did they do anything to see that V. Gupta actually reimbursed IUSA for these clearly personal expenses. They did not examine the basis for any of the charges, including whether or not Annapurna was adding markups on its invoices to IUSA.<sup>9</sup>

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<sup>9</sup> Invoices produced in the §220 case show that Annapurna did charge IUSA a mark up on the costs of the private jets owned by Annapurna but used by V. Gupta, his family and friends. Id. ¶71.

On July 11, 2005, Raval prepared a "Tax Discussion" memo, which was subsequently provided to the board which, at the time consisted of V. Gupta, Haddix, Kaplan, Kahn, Walker, A. Gupta, Strykher and Andersen as well as Raval. Id. ¶109. The Tax Discussion memo noted changes in IRS regulations limiting business deductions when aircraft is used for entertainment. Id. It stated that "a more fundamental issue facing the Company is the proper determination of business use versus entertainment use". Id. ¶109. V. Gupta's W-2's and Forms 1099 obtained in the books and records action essentially tie to his salary, bonus and stock option amounts in IUSA's proxy statements. Id. Accordingly, these tax documents do not appear to reflect any income derived from V. Gupta's personal usage of the American Princess yacht, personal plane rides and other personal transactions. Id. Rather, it appears that all expenses of private jet travel, usage of the American Princess yacht and other expenses of a personal nature were all charged to IUSA and presumably deducted by it for book and tax purposes as business expenses. As such, the Company's financial statements and tax returns are likely inaccurate.<sup>10</sup>

#### E. V. Gupta's Unsuccessful Effort to Take the Company Private

In February 2005, V. Gupta told the Company's then second largest stockholder that he was committed to taking IUSA's stock to \$20 per share and higher in 2005. Id. ¶22. A month

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<sup>10</sup> The IRS has and has had extensive regulations governing the taxation of fringe benefits including personal and nonpersonal flights on employer-provided aircraft. E.g., 26 CFR §§1.61-21(g)(1)-(14) and 1.132-5. Personal flights, even those combined with business flights, must be separately accounted for and included in the employee's income. §1.61-21(g)(4). The IRS also requires detailed substantiation records for employee travel and entertainment. 26 CFR §1.274-5. To deduct for entertainment, for example, the taxpayer must substantiate the amount, date, business reason for the entertainment or the nature of the business benefit derived or expected to be derived, the nature of any business discussion or activity and the occupation of person entertained including name, title or other designation sufficient to establish the business relationship to the taxpayer. 26 CFR §1.274-5T(b)(3). Documents produced in response to the §220 demands, in fact, fail to supply any business support for a significant amount of the charges and, consistent with the Raval Report, show that a large amount appears to be for V. Gupta's personal use.

later, V. Gupta purchased 61,000 IUSA shares at an average price of \$10.13, bringing his then disclosed holdings to approximately 34.5%.<sup>11</sup> Id. ¶23. He stated in a public press release that he continued to believe that the stock was worth more than \$18 per share based on the Company's strong financial condition and earnings momentum. Id. ¶23. A few months later, in June 2005, IUSA issued an earnings warning, lowering its earnings guidance by about 5%. Id. ¶24. Its stock price fell on this news from \$11.94 to \$9.85 per share. Id. ¶24. Five days later, on June 13, 2005, V. Gupta made an offer to buy all of the Company's outstanding shares for \$11.75 per share. Id. ¶26. His opportunistic offer came on the heels of an earnings warning which V. Gupta knew would have a negative short term impact on the price of the Company's stock.

On June 24, 2005, the Company announced the formation of a Special Committee consisting of Defendants Kahn, Stryker, Raval and A. Gupta. Id. ¶28. The Company stated that the Special Committee had the authority to "review Mr. Vinod Gupta's proposal and *potential alternatives*." (emphasis added). Id. In fact, as the Company reiterated on July 22, 2005, the Special Committee was authorized to evaluate V. Gupta's proposal, including "negotiate, accept or reject" it, as well as to "solicit, consider or negotiate alternative proposals" and "take any other actions that the Committee deemed appropriate or necessary." Id. ¶30.

In connection with V. Gupta's offer, in July 2005, the Special Committee caused V. Gupta to enter into a standstill letter agreement pursuant to which V. Gupta would refrain from taking certain actions relating to the acquisition of the Company's stock. Id. ¶29.

At significant expense, the Special Committee hired outside legal counsel and an investment banker. Id. ¶35. On August 25, 2005, IUSA announced that the Special Committee

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<sup>11</sup> As noted above, prior to the 2006 proxy contest, V. Gupta had been under reporting his IUSA stock ownership in violation of the federal securities laws.

had determined that V. Gupta's \$11.75 per share proposal was inadequate. Id. ¶33. IUSA also announced that the Special Committee had determined it would continue to explore potential alternative strategic transactions for the Company. Id. In response, V. Gupta advised the Special Committee that he was withdrawing his offer and that he would not support a sale of IUSA or any other transaction. Id. ¶34. V. Gupta made these statements even though he was not the majority owner of IUSA and, therefore, could not necessarily block or prohibit any transaction. Id. ¶37. Despite V. Gupta's statements, the Special Committee issued a press release on August 25, 2006, stating that it would continue to explore a range of strategic alternatives for IUSA. Id. ¶34.

V. Gupta immediately took steps to prevent the Special Committee from considering any such strategic alternatives. At a board meeting on August 26, 2005, V. Gupta made it clear that IUSA was not for sale even though he was not the majority owner. Id. ¶43. Over the objection of three of the four members of the Special Committee, the other five directors, V. Gupta, Andersen, Haddix, Kaplan and Walker, voted to disband the Special Committee. Id. Special Committee members Kahn, A. Gupta and Stryker opposed the motion. Id. Raval curiously abstained from voting on it even though just one day earlier, the Special Committee of which he was a member had publicly announced it would continue to explore strategic alternatives for IUSA. Id. ¶45. The August 26, 2005 board minutes do not reveal any reasons for Raval's abstention. A fair inference from the abstention is that Raval, whose income is materially enhanced by IUSA director fees and whose University receives major support from V. Gupta, did not have the independence to oppose V. Gupta. Had he voted with the other members of the Special Committee, as he had done the day before, and had V. Gupta not been allowed to cast a

self-interested vote, the proposal to disband the Special Committee would have failed on a 4-4 vote.

The justifications made by the five directors who voted to disband the four person Special Committee directly contravened the Special Committee's express mandate which these same five directors had unanimously authorized just six weeks earlier. But, there was no new intervening business plan or strategy for their about face turn. The only changes that had occurred in the six-week interval was V. Gupta's withdrawal of his inadequate \$11.75 per share offer and the Special Committee's decision to continue to explore strategic alternatives – a development that V. Gupta opposed.

The unusual circumstances surrounding V. Gupta's unsuccessful going private offer and the abolishment of the Special Committee over the opposition of three of its four members shows that the creation of the Special Committee was a sham created as "window dressing." When the Special Committee tried to assert itself, V. Gupta and directors Haddix, Kaplan, Walker and former director Andersen dissolved it. The sham cost IUSA millions of dollars in fees for the members of the Special Committee, their attorneys and investment advisers. To add insult to injury, the Company even paid for V. Gupta's personal expenses, including flying V. Gupta and his own investment adviser around the country to meet with venture capitalists. On top of all of this, V. Gupta sent a letter to the IUSA board on September 7, 2006, in which he stated that the primary reason for his offer was to "support the stock" after it "got crushed" on the earnings guidance reduction.

#### F. IUSA's Shareholders Rights Plan

IUSA adopted a Shareholders Rights Plan on July 21, 1997. Id. ¶116. Pursuant to Section 1(a) of the Rights Plan, V. Gupta, members of his immediate family and entities

controlled by or established for the benefit of V. Gupta or his family, are excluded from the definition of "Acquiring Person" and thereby exempt from the Rights Plan. Id. The Rights Plan also provides that prior to a Distribution Date (i.e., after the triggering of the Rights), the Rights Plan may be amended or supplemented and, upon the delivery of a certificate of an appropriate Company officer, the Rights Agent is required to execute such supplement or amendment. Id. ¶117.

V. Gupta's and his affiliates' exemption from the Rights Plan is inconsistent with the stated purpose of the Rights Plan, which is to protect shareholders from change of control transactions that deprive them of fair value, including a "control premium." Indeed, the Company's press release issued on adoption of the Rights Plan stated that the Plan was intended to guard against control transactions effected "without paying all shareholders the fair value of their shares, including a 'control premium.'" Id. ¶118.

Notwithstanding this stated purpose, V. Gupta through option grants and stock purchases has steadily increased his control from approximately 35% in 1998 to his current beneficial ownership of over 41%. Id. ¶120. Indeed, at the 2005 Annual Meeting, stockholders voted to increase the number of shares available under the Company's 1997 Stock Option Plan from 5 million to 8 million shares. Id. ¶121. This increased the pool of options available to Company insiders, including V. Gupta who has received most of the options awarded to employees. The proxy statement soliciting shareholder approval of the increased number of option shares falsely represented the number of shares beneficially owned by V. Gupta at the time. Id. The proxy statements prior to Dolphin's 2006 proxy contest misleadingly (and in violation of the federal securities laws) under reported V. Gupta's stock ownership by omitting disclosure of 2.4 million shares (4.4%) held by his sons' trusts and his charitable foundation. Id.

After V. Gupta announced his proposed going private offer, the Company entered into a standstill letter agreement with V. Gupta, which it has subsequently renewed. Pursuant to a letter agreement dated July 26, 2006 (the "Standstill Letter"), V. Gupta will not directly or indirectly acquire any additional shares of the Company except that he may exercise his currently held options. Id. ¶128. The Standstill Letter is timed to expire when IUSA's Rights Plan expires. Id. The Standstill Letter further states that it is not applicable if the Company (a) announces that it has entered into an agreement with a third party that contemplates a merger, consolidation, sale, sale of substantially all of the Company's assets, or a business combination; or (b) announces it has entered into an agreement with a third party that contemplates a change of control of IUSA. Id. The Standstill Letter does not state that it applies to members of V. Gupta's family or other affiliates and associates and such family members, affiliates and associates have not signed the Standstill Letter. Id. The Company has no enforceable rights against them. Id.

The Standstill Letter further provides that so long as V. Gupta is in compliance with his obligations under it:

The Company shall not take any action to modify, extend or amend the Company's Preferred Share Rights Agreement with Northwest Bank N.A. Minnesota, (as amended the "Rights Agreement") to directly or indirectly include [V. Gupta] in the definition of "Acquiring Person" as such term is used in the Rights Agreement or take any action including amending the Rights Agreement or adopting any other Rights Agreement, plan or other arrangement that has the direct or indirect effect of including [V. Gupta] within the purview of the Rights Agreement or such other rights agreement, plan or arrangement." Id. ¶129.

Thus, the Standstill Letter purports to eliminate the Company's ability to amend the Rights Plan to make it applicable to V. Gupta. Because V. Gupta does not yet have majority control of IUSA, the special exemption in the Rights Plan for him and his affiliates gives him an

unfair tactical advantage over other prospective bidders and the ability through additional option grants and exercises to increase his creeping control.

## ARGUMENT

### I. PRE-SUIT DEMAND IS EXCUSED AS TO PLAINTIFFS' DERIVATIVE CLAIMS.

Defendants' Rule 23.1 motion should be denied because the Complaint sets forth numerous detailed, particularized and egregious facts showing that demand on IUSA's directors would be completely futile. The accumulation of the particularized factual allegations, together with the reasonable inferences that can logically be drawn from them, easily satisfy the demand futility test set forth in Aronson v. Lewis, 473 A.2d 805, 814 (Del. 1984). Under Aronson, demand is futile if the complaint contains particularized allegations that create a reasonable doubt that (1) a majority of the directors are disinterested and independent or (2) the challenged transaction was not otherwise the product of a valid exercise of business judgment. Id.

In considering a Rule 23.1 motion to dismiss, the Court must "review the complaint in detail to ascertain if the plaintiff has alleged with particularity facts which show that a pre-suit demand for redress of the alleged wrongs would have been futile." Kaufman v. Belmont, 479 A.2d 282, 284 (Del. Ch. 1984). While conclusory allegations are not sufficient, the Court must accept as true particularized facts and the Plaintiff is entitled to all reasonable inferences that logically flow from such facts. Beam v. Stewart, 845 A.2d 1040, 1050 (Del. 2004).

In making the required judgment, no single factor, such as the receipt of director compensation; social relationship; approval of the challenged transaction; or other relationships with the corporation is by itself dispositive. Harris v. Carter, 582 A.2d 222, 229 (Del. Ch. 1998). Rather, the question is whether, in the Court's sound discretion, the "accumulation of all factors" creates reasonable doubt under Aronson. Id. Here, an objective analysis of all the facts set forth in Plaintiffs' Complaint and the inferences reasonably drawn from such facts show that demand is excused under both prongs of Aronson.

**A. The Complaint Pleads That The Directors Have Not Acted Independently.**

1. The Specific Actions Challenged in the Complaint Create Ample Reasonable Doubt as to Independence.

Demand is excused under Aronson's first prong because the Complaint contains numerous detailed facts creating a reasonable doubt as to the independence of a majority of the IUSA directors from V. Gupta. Independence is not woodenly assessed based on a director's background and credentials. Directors should not simply be or appear to be independent. Rather, they "must act independently." Kahn v. Tremont Corp., 694 A.2d 422, 429 (Del. 1997). As stated in Kahn, "[i]t is the care, attention and sense of individual responsibility to the performance of one's duties ... that generally touches on independence." Id. at 430 (quoting Aronson, 473 A.2d at 816).

Plaintiffs' Complaint contains numerous particularized facts showing that a majority of IUSA's directors have not acted independently of V. Gupta. The Raval Report is prima facie evidence for what it says, for what it does not say and for the directors' failure to act on it. After the Raval Report, which detailed more than \$600,000 of inappropriate personal expenses in 2004 alone and concluded that they should be "borne" by V. Gupta, the directors, including Raval and the four directors who were given his report (Kaplan, Haddix, Kahn and Walker) chose not to pursue reimbursement from V. Gupta.<sup>12</sup> Likewise, these directors and former directors Andersen and Stryker chose not to investigate millions of dollars of similar personal expenses which V. Gupta had been charging to IUSA going back to at least 1998. The board's intentional decision to ignore millions of dollars of personal expenses improperly charged to IUSA creates

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<sup>12</sup> The Company's public SEC filings and the documents provided pursuant to §220 demands do not reveal any repayments of these charges made by V. Gupta. The lack of any substantiating documents creates a strong inference that repayment has not occurred. In re Tyson Foods, Inc. Consol. S'holder Litig., 2007 WL 416132, at \*7 and n.20 (Del. Ch. Feb. 6, 2007).

more than a reasonable doubt as to the directors' independence from V. Gupta. To the contrary, it shows that a majority of the directors believe that IUSA is V. Gupta's company and he can do as he pleases with it even to the point of ignoring his and IUSA's apparent violations of the tax laws and IUSA's own Code of Conduct.<sup>13</sup>

Similarly, Kaplan's, Haddix's, Kahn's and Walker's and former director Andersen's vote to disband the Special Committee, coupled with Raval's unexplained abstention from voting, is another act confirming the directors' lack of independence from V. Gupta. The vote to disband the Special Committee occurred because V. Gupta objected to the Special Committee's publicly announced decision to consider strategic alternatives for IUSA after V. Gupta withdrew his inadequate going private offer. The five directors who were not Special Committee members (V. Gupta, Kaplan, Haddix, Walker and Andersen) overrode the Special Committee and adhered to V. Gupta's position that the Company was not for sale simply because V. Gupta said so and even though he did not own a majority of the stock. Raval lacked the independence to vote, much less vote against V. Gupta. And none of the directors, not even Kaplan, an attorney whose firm represents IUSA, had the mettle to tell V. Gupta that he should abstain on this vote. In short, the five directors who were not considered sufficiently independent or disinterested to be members of the Special Committee, were allowed to close it down.

The board's lack of independence is further illustrated by its refusal to consider the fairness of continuing to exempt (and thereby entrench) V. Gupta, his family members and his

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<sup>13</sup> Paragraph 4 of IUSA's Code of Conduct states, in pertinent part, "Conflicts of interest may also arise when an employee, officer or director (or one of their family members) receives improper personal benefits as a result of the employee's, officer's or director's position in the Corporation." IUSA website: <http://ir.infousa.com/phoenix.zhtml?c=96263&p=irol-govConduct>. The Code of Conduct also states that the protection of corporate assets from misuse and waste is the responsibility of every employee, officer and director. *Id.* ¶7.

affiliates and associates from the Rights Plan. Rather than confront the issue, which was raised during Dolphin's proxy contest, the board instead entered into a Standstill Letter with V. Gupta.<sup>14</sup> The Standstill Letter does nothing to protect IUSA and its stockholders to whom the directors owe fiduciary duties from V. Gupta's "creeping takeover" because it is not even enforceable against V. Gupta's family members and his associates and affiliates. These associates and affiliates are exempt from the Rights Plan but they are not parties to the letter agreement. All the Standstill Letter does is continue to entrench V. Gupta by allowing his associates and affiliates to continue to acquire stock and by allowing V. Gupta himself to acquire more stock through existing and newly granted stock options.<sup>15</sup>

The directors' actions speak more loudly on the question of independence than the rote analysis in their brief. The brief tries to create an appearance of independence but neglects to address the critical question as to whether the directors are independent of V. Gupta for purposes of suing him on Plaintiffs' claims. As stated in Scattered Corp. v. Chicago Stock Exch., Inc., 701 A.2d 70, 74 (Del. 1997), "[a] board or a committee of the board may *appear* to be independent, but may not act independently." Here, the directors' actions create neither the appearance nor the reality of independence. This was readily apparent to Glass Lewis, an independent and objective proxy advisory service, which after reviewing the Company's track record and documents made public during the 2006 proxy contest concluded that V. Gupta had "abused his position" as CEO. The IUSA board has enabled such abuse.

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<sup>14</sup> The directors at the time of the 2006 Standstill Letter were V. Gupta, Raval, Haddix, Kaplan, Kahn, Walker, A. Gupta, Fairfield and Reznicek.

<sup>15</sup> V. Gupta's very narrow victory in Dolphin's 2006 proxy contest strongly indicates that a third party offer for IUSA's stock at an appropriate price could succeed if the Rights Plan was eliminated.

2. Other Actions Alleged in the Complaint Bolster the Directors' Lack of Independence.

In assessing the directors' independence with respect to the transactions challenged in that Complaint, the Court must view the Complaint as a whole. In so doing, the Court may consider other transactions described in the Complaint. Kells-Murphy v. McNiff, 1991 WL 137143, at \*2 (Del. Ch. July 12, 1991). Plaintiffs' Complaint is replete with other transactions that confirm that a majority of IUSA's directors are not independent of V. Gupta. For example, in October 2004, the then board of IUSA, which included Kaplan, Haddix, Raval, Walker and former director Andersen, voted to approve V. Gupta's self-interested proposal that existing stock options be repriced to reduce the exercise price by seventeen percent. Compl. ¶140. Not surprisingly, the primary beneficiary of this proposal was its proponent, V. Gupta, who, despite his sizeable stock interest, has received approximately seventy-five percent of all IUSA options issued to senior management since 2001. Id. Then, just a few months later on February 3, 2005, these same directors, who were now joined by Kahn, voted to give V. Gupta an additional option on 500,000 IUSA shares. Id. That approval came just one day after V. Gupta sent a memo to the Compensation Committee (Haddix, Walker and Andersen) urging that his compensation plan be approved "very quickly" so that he could receive his options before they became more expensive. Id. ¶140.

In 2001, directors Haddix and Kaplan and former director Andersen approved the distribution of 700,000 shares under IUSA's 1992 Stock Option Plan. Id. ¶120. They gave V. Gupta the sole authority to decide which employees, including himself, would receive such options. Not surprisingly, V. Gupta kept most of them for himself. Id. ¶120. All of the option grants have only served to expand V. Gupta's sizeable position, not to motivate him to increase the stock price for all stockholders as the stock price has done nothing for years. Id. ¶21.

The board's asserted independence is further undermined by the fact that directors Haddix and Walker and former director Andersen have had their own personal expenses paid by the Company. The Raval Report admitted that these payments casted doubt on the receiving directors' independence: "[t]he question of independence of a director may surface if the director or his organization is an occupant of InfoUSA premises and particularly, if no rental/lease agreement exists between InfoUSA, and the director or his organization." Defendants' brief ignores this critical admission just as it ignores most of the specific acts alleged in the Complaint that go directly to independence. And regardless of the dollar amount of the free rent or private jet travel, the fact that these directors have their own private related party arrangements casts serious doubt on whether they would cause IUSA to sue V. Gupta for his. See In re Tyson Foods, Inc. Consol. S'holder Litig., 2007 WL 416132, at \*11 (recognizing that directors may not be independent for purposes of challenging other directors' related party transactions when they have their own related party transactions to protect); Strougo v. Carroll, 1991 WL 9978, \*4 (Del. Ch. Jan. 29, 1991)(common sense suggests that directors accused of insider trading would not cause company to pursue co-directors for the same alleged wrongs).<sup>16</sup>

3. Defendants' Authorities Are Legally and Factually Inapposite.

Defendants do not cite any factually similar case in which a Rule 23.1 motion was granted. Indeed, Defendants do not even bother to analyze most of Plaintiffs' factual allegations. Instead, they rely on select and limited portions of the Complaint and snippets from case law to

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<sup>16</sup> Neither Haddix, Walker or Andersen have repaid IUSA for the free office space and/or private jet travel they received. There is nothing in the §220 production to suggest that they immediately offered to repay the Company and did so. Cf. Perlegos v. Atmel Corp., 2007 WL 475453 (Del. Ch. Feb. 8, 2007)(director who immediately offered to repay and did repay for personal air travel unknowingly charged to the company not conflicted because his actions allay any concern of divided loyalties or bias with respect to review of other directors who were abusing company travel policies).

try to argue the directors' independence. This type of a mechanical and inelastic approach was rejected in Grobow v. Perot, 539 A.2d 180, 186 (Del. 1988) overruled in part on other grounds, Brehn v. Eisner, 746 A.2d 244 (Del. 2000), where the Supreme Court stated that "[r]easonable doubt must be decided by the trial court on a case-by-case basis employing an objective analysis." Objectively viewed, the overwhelming number of particularized facts in the Complaint creates more than a reasonable doubt as to the independence of a majority of the board. This is not a case where the Complaint consists of nothing more than "a suspicion expressed solely in conclusory terms." Beam, 845 A.2d at 1050.

Defendants rely on Beam to argue that a mere outside business relationship or friendship is not sufficient to create a reasonable doubt as to a director's independence. DOB 19. In Beam, a shareholder of Martha Stewart Omnimedia ("MSO") brought a derivative suit arising out of Martha Stewart's sale of ImClone stock which allegedly harmed MSO. The complaint made conclusory allegations of Martha Stewart's domination and control of three outside directors based on her personal friendship with them. The Court rejected this "structural bias" argument and criticized the plaintiff for not making a §220 demand for documents that might have provided a factual predicate for pleading domination and control.<sup>17</sup>

Here, Plaintiffs do not and need not base their independence argument on conclusory allegations of domination and control derived from mere friendships or business relationships. It is true that most of the directors are Omaha businessmen with past and present business, philanthropic and personal ties to V. Gupta. They invest together, they sit on the same corporate

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<sup>17</sup> Litt v. Wycoff, 2003 WL 1794724 (Del. Ch. Mar. 28, 2003) and Highland Legacy Ltd. v. Singer, 2006 WL 741939 (Del. Ch. Mar. 17, 2006) (DOB 19) are also cases in which the plaintiffs did not make §220 demands.

and/or charitable boards and foundations, they have sold their companies to IUSA, and V. Gupta is a major donor of the University at which several directors work or have worked. These connections suggest a board beholden to V. Gupta. Oracle Corp. Derivative Litig., 824 A.2d 917, 938-39 (Del. Ch. 2003) (director may be beholden to an interested person based on personal or other relationships even if not beholden financially). Plaintiffs, however, do not rely merely on these connections. Rather, based on documents obtained pursuant to their §220 demands, Plaintiffs allege a myriad of particularized facts showing specific actions across a wide spectrum of activities taken by the board over a seven year period to comport with V. Gupta's wishes and financial interests.

Defendants' mischaracterization of Plaintiff's argument as the circular argument rejected in Tyson (DOB 21) is wrong. The wholly circular argument rejected in Tyson assumes that directors lack independence because they fail to exercise business judgment and that they fail to exercise business judgment because they lack independence. Here, Plaintiffs are not relying on the board's approval of challenged transactions to prove their lack of independence from V. Gupta. To the contrary, as alleged in the Complaint, in most instances there is no evidence from the §220 action that V. Gupta ever sought or obtained board approval of his self-dealing related party transactions. Instead, the massive number of related party transactions, V. Gupta's special exemption under the Rights Plan and the sizeable stock option grants to V. Gupta when he already owned 35% of IUSA show directors who have consistently permitted V. Gupta to run IUSA as if it were his own company. Even after at least four of the current directors learned in black and white that V. Gupta was using Company funds to pay for his and his friends' lavish lifestyles, they did nothing to stop it or to seek repayment from V. Gupta. Worse yet, they

covered the expenses up in false Form 10-Ks which described the lavish perks such as the yacht as "usage of aircraft and related services."<sup>18</sup>

**B. Demand is Excused Because a Majority of the Directors Are Interested.**

1. The Directors Benefit From the Related Party Transactions.

V. Gupta is clearly interested for purposes of a demand futility analysis because he has been charging millions of dollars of personal expenses to IUSA. Directors Walker, Haddix, Kaplan and Raval are also interested because of their own personal benefits that they receive from the Company. Walker and Haddix occupy office space rent free at IUSA. The Company has also paid for Walker's personal private jet travel. Kaplan's law firm receives significant and material legal fees from IUSA, including \$1.1 million in 2006 alone. IUSA pays Raval a material supplement to his academic salary in director fees. Under the circumstances and in light of the other significant facts alleged in the Complaint, it is more than reasonable to conclude that Walker, Haddix, Kaplan and Raval willingly tolerate V. Gupta's related party transactions in exchange for their own personal Company paid benefits. See In re Tyson Foods, 2007 WL 416132, at \*11.

2. The Board Faces the Risk of Substantial Liability.

A majority of the board is also interested because the directors face a substantial risk of personal liability arising out of the challenged transactions. V. Gupta has charged IUSA for millions of dollars of personal and unsupportable expenses. Walker, Haddix, Kaplan and Raval also face personal liability because they knew from the Raval Report alone that V. Gupta improperly charged massive amounts of personal expenses to IUSA, including but not limited to

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<sup>18</sup> Defendants mischaracterize Plaintiffs' Complaint stating that "Raval signed Forms 10-K allegedly approving some transactions challenged in the Consolidated Complaint." DOB 25. Raval and the others who signed Forms 10-K were not "approving" the challenged transactions. They were covering up their true nature.

private jet travel for himself, his family and his friends; personal residences (including a Maui condo owned by V. Gupta's son); luxury cars and a catamaran; vacations on the American Princess Yacht; and premiums on V. Gupta's personal life insurance policies. Compl. ¶102. Despite this knowledge, these directors and V. Gupta (five of the current eight directors) signed SEC filings that falsely and misleadingly characterized these personal residences, luxury cars and yacht expenses as "usage of aircraft and related services." Id. ¶68.

Walker, Haddix and Kaplan also rejected (or purposefully ignored) Raval's conclusion that V. Gupta should reimburse IUSA for substantial amounts of personal and unsupported items which he had charged to the Company. Raval himself did nothing to make sure his conclusion was carried out. Even after Raval's Tax Discussion memo, which highlighted IRS limitations on the deductibility of business use versus personal use of IUSA's assets, there is no evidence in the §220 document production or in the public filings that IUSA's financial statements or its tax position have been amended. One can reasonably conclude, however, from the abundant evidence that IUSA's statements likely contain improper deductions for expenses that should be properly characterized as income to V. Gupta. In short, the Complaint establishes doubt as to the interestedness of a majority of the board because it pleads extensive particularized facts showing that a majority of the directors may likely be exposed to substantial liability for securities and knowing violations of IRS regulations. See Ryan v. Gifford, 2007 WL 416162, at \*10 and n.38 (Del. Ch. Feb. 6, 2007).

The Defendants try to deflect this serious risk claiming that the board has taken action with respect to V. Gupta's improper personal expenditures. DOB 29. This contention is flatly contradicted by the very specific allegations of the Complaint showing that the board has enabled V. Gupta to abuse his position within IUSA. Although it is unclear, Defendants cryptic reference

to action taken by the board presumably refers to IUSA's mid-2004 purchase of Annapurna's interests in the private jets and its 2005 assumption of the lease for the American Princess yacht. There are, however, no minutes reflecting the board's approval of IUSA's purchase of and/or assumption of the leases for these pricey assets from Annapurna. Moreover, having IUSA purchase or directly lease these assets does not solve the underlying problem. All that it does is eliminate the need for IUSA to disclose its payments to Annapurna in the related party transaction footnote to IUSA's financial statements. It does not stop V. Gupta from charging IUSA for personal expenses.

**C. Demand is Excused Because the Business Judgment Rule is Inapplicable.**

Pre-suit demand is also excused under the second prong of Aronson because Plaintiffs have alleged extensive and particularized facts that create a substantial doubt that the challenged transactions were the product of valid exercise of business judgment.

1. The Complaint Pleads Waste.

Demand is excused where, as here, the Complaint states a claim for waste. Emerald Partners v. Berlin, 1993 WL 545409, at \*6 (Del. Ch. Dec. 23, 1993); see also Oct. 17, 2006 Tr. 13 ("And there may be a claim for waste related to all the lavish perks."). The standard for alleging waste is whether the consideration received by the corporation is so inadequate that no person of ordinary sound business judgment would deem it worth what the company paid. Grobow, 539 A.2d at 189; Emerald Partners, 1993 WL 545409, at \*6. The allegations in the Complaint easily satisfy that standard. In the exercise of ordinary sound business judgment, no person would conclude that IUSA should pay for V. Gupta, his family and his friends' private jet travel to luxury vacation destinations, their holidays on the American Princess yacht or V. Gupta's personal residences in resort locations and his family's luxury cars. Plaintiffs' allegations of waste are substantiated by the conclusion in the Raval Report that V. Gupta should

reimburse IUSA for a significant portion of the related party payments made by IUSA in 2004 to Annapurna and Aspen Leasing.<sup>19</sup> In light of this conclusion, no person of ordinary, sound business judgment would give V. Gupta unfettered access to the Company's treasury. Yet that is exactly what Haddix, Walker, Raval and Kaplan, all recipients of the Raval Report, did.

The Complaint also pleads waste in connection with the undisclosed consulting agreements signed by V. Gupta and a former high ranking government official. The consulting agreements require the Company to pay the former official \$3.3 million over a six-year period and to grant him an option on 100,000 shares in exchange for his providing "confidential advice and counsel" to V. Gupta for the purposes of "strategic growth and business development." There is no minimum amount of time which this former official must spend providing such confidential advice and the contract is not even clear as to whether the advice is for V. Gupta personally or on behalf of IUSA. This official could presumably spend five minutes suggesting nothing more than that V. Gupta upgrade the Company's private jet and still collect millions in fees and a 100,000 share option to boot. Moreover, the Company produced no documentation showing that this official ever actually provided any confidential advice about the Company's "strategic growth" or its "business development." Again, under these circumstances, it is appropriate to draw a negative inference that no such advice was provided. In re Tyson Foods, 2007 WL 416132, at \*7 and n.20.

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<sup>19</sup> The Raval Report, which is referred to in the Complaint, refutes Defendants' argument that Plaintiffs failed to allege that the expenditures were without a valid business purpose such as client development or entertainment. DOB 29. Moreover, the Complaint highlights the complete disconnect between the travel expenses in question and how V. Gupta characterized them when he unilaterally determined that IUSA should pay for these expenses. One glaring example, found in ¶86 of the Complaint, is a \$48,000 private jet charge so that V. Gupta, his wife, two of his sons and six friends could travel to Hawaii for Christmas and New Year's and which V. Gupta characterized as "business development."

The one-sided, illusory nature of the consulting agreements combined with the fact that V. Gupta, a close friend of this former official, signed the agreements without disclosure to or approval by IUSA's board show that the Company is not receiving adequate consideration. Rather, it is reasonable to infer that the agreements are a way for V. Gupta to continue to ingratiate himself with this former high ranking government official who, among other things, nominated V. Gupta to several prestigious posts.

2. Demand is Excused as to the Illegal and Ultra Vires Acts Alleged in the Complaint.

Demand is also excused because Plaintiffs allege illegal and ultra vires acts. Calif. Public Employees' Ret. Sys. v. Coulter, 2002 WL 31888343, at \*11 (Del. Ch. Dec. 18, 2002). As this Court stated in Coulter, "[a]ny action of the board that falls outside the rather broad scope of its authority is not entitled to the protection of the business judgment rule and demand is excused." Id. Here, the Complaint alleges that V. Gupta gave an option for 100,000 shares to a consultant in violation of the Company's 1997 Stock Option Plan which requires board or board committee approval of all option grants. This unauthorized action, which also violates 8 Del. C. §157, is an ultra vires gift as to which demand is excused.

Likewise, demand is excused because the Complaint alleges violations of 8 Del. C. §144. Under §144, a transaction between a corporation and one of its directors or officers in which the director or officer has a personal financial interest is void or voidable unless (1) approved by a majority of disinterested directors; (2) approved by the stockholders; or (3) it is fair to the corporation. As alleged in the Complaint, none of the three conditions set forth in §144 is satisfied with respect to V. Gupta's massive self-dealing related party transactions. Compl. ¶151. Accordingly, the business judgment rule is inapplicable and cannot be used to excuse demand. Aronson v. Lewis, 473 A.2d at 812 (citing §144(a) for the proposition that if self-dealing is

present and the transaction is not approved by a majority of disinterested directors, then the business judgment rule has no application in determining demand futility); see also HMG/Courtland Prop., Inc. v. Gray, 749 A.2d 94, 113 (Del. Ch. 1999) (compliance with §144 "should be a minimum requirement to retain the protection of the business judgment rule"); Edelman v. Phillips Petroleum Co., 1985 WL 11534, \*4 (Del. Ch. Feb. 12, 1985)(business judgment rule does not protect conduct alleged to be void under DGCL).

Demand is also excused because the Complaint alleges the invalidity of the Standstill Letter between the Company and V. Gupta. In the Standstill Letter, the board agreed not to terminate the exemption for V. Gupta in the Company's Rights Plan in exchange for V. Gupta's promise not to buy more IUSA stock (other than by exercise of his options). This agreement is invalid because it is inconsistent with the Rights Plan itself. The board has not complied with the procedures in the Rights Plan for amendments because the Rights Agent has not executed any amendment as required by the Rights Plan. Id. ¶117.

In addition, the Standstill Letter is invalid because it purports to preclude the IUSA board from amending the Rights Plan to eliminate V. Gupta's exemption from it even if it is in the stockholders' interests to do so. This limitation improperly deprives the current board, and any new directors, of their statutory duty under 8 Del. C. §141(a) to manage IUSA's business and affairs. See Quickturn Design Sys., Inc. v. Shapiro, 721 A.2d 1281, 1291-92 (Del. 1998); Carmody v. Toll Bros., Inc., 723 A.2d 1180, 1191 (Del. Ch. 1998).

3. Demand is Excused Because the Complaint Contains Extensive Particularized Allegations That the Directors Consciously and Intentionally Disregarded Their Fiduciary Duties Across a Wide Spectrum of Activities.

Demand is excused when a plaintiff alleges facts suggesting that the directors consciously and intentionally disregarded their fiduciary duties. In Re Walt Disney Co. Deriv. Litig., 825

A.2d 275, 289 (Del. Ch. 2003). Plaintiffs' allegations do so here. V. Gupta has engaged in massive self-dealing transactions over an extended period of time while Haddix, Raval, Kaplan and Walker (the recipients of the Raval Report) have consciously and knowingly turned a blind eye in letting V. Gupta charge his personal expenses to the Company in the first place and then in not seeking reimbursement even after the impropriety was set forth in the Raval Report. This bad faith excuses demand under Disney. Even if the directors were grossly negligent, demand would be excused. In re NVF Co. Litig., 1989 WL 146237, at \*5 (Del. Ch. Nov. 22, 1989).

4. The Directors Have Improperly Deferred to V. Gupta on Transactions in Which He Has a Personal Interest.

Aronson's second prong is satisfied where directors, even seemingly disinterested directors, defer to a CEO on a challenged transaction in which he is personally interested. Coulter, 2002 WL 31888343, at \*14. The Complaint pleads facts that show the board's repeated deference to V. Gupta on the challenged transactions and otherwise. As set forth above, the directors deferred to V. Gupta's interest when they refused to rectify these improper personal payments.

The board further deferred to V. Gupta in connection with the Special Committee. When it suited V. Gupta's interests, the board voted to establish the Special Committee and gave it full authority to pursue alternative transactions to V. Gupta's proposal. Then, after V. Gupta withdrew his offer, a majority of the board led by V. Gupta voted to disband the Special Committee before it had the chance to even begin to review alternatives that might further the interests of all IUSA stockholders. The board even let V. Gupta vote on the motion to disband notwithstanding his personal interests which clashed with the Special Committee's. Raval abstained from voting without explanation. The clear inference, however, is that Raval was unwilling to accept any retribution that might befall him for standing up to V. Gupta.

**D. Rales is Inapplicable But Even If It Does Apply, Demand is Still Excused.**

Contrary to Defendants' argument (DOB 28-29), this is not a failure to supervise or lack of oversight case. Accordingly, Rales v. Blasband, 634 A.2d 927 (Del. 1993) is inapplicable. Plaintiffs do allege that the IUSA board did not approve many of V. Gupta's self-dealing related party transactions and that such transactions are void or voidable under §144. E.g. Compl. ¶¶100, 151. Additionally, however, Plaintiffs challenge the board's decision to give V. Gupta a "free pass" notwithstanding the Raval Report's conclusion that he should pay IUSA for a substantial amount of personal and unsupportable items which he directed IUSA to pay in 2004. Thus, Plaintiffs allege in ¶105 that V. Gupta never reimbursed the Company for the amounts Raval said he should bear. Plaintiffs also challenge the board's decision to forego examining similar expenditures in other years. Likewise, the board, including Raval, misled stockholders as to the true nature of these personal and unsupportable items. Compl. ¶102. The directors are not simply charged with ineffective oversight. They are charged with active wrongdoing.

In a transparent attempt to deflect attention away from these damaging facts, Defendants claim that the "Board acting through its Audit Committee has investigated and taken action with respect to many of these same allegations of improper personal expenditures by the [CEO]." DOB 29. Defendants do not offer any record citation and there are no minutes in the §220 document production to support the statement. The Complaint pleads the contrary. E.g., Compl. ¶105 (no evidence in the Company's public disclosures or in the books and records produced in the §220 action revealing that V. Gupta has reimbursed the Company); see also Id. ¶106. Even Raval, who concluded that a substantial portion of the related party transactions between V. Gupta and IUSA in 2004 were personal and unsupportable, has not pursued V. Gupta for reimbursement.

Even if Rales does apply to some of Plaintiffs' allegations, Defendants' motion to dismiss should still be denied. As explained above, a majority of IUSA's directors are interested and not independent of V. Gupta.

**II. THE DEFENDANTS' RULE 12(b)(6) MOTION SHOULD BE DENIED BECAUSE EACH OF THE FIVE COUNTS IN THE COMPLAINT STATES A LEGALLY SUFFICIENT CLAIM**

The Defendants' Rule 12(b)(6) motion should be denied because Defendants have failed to show that Plaintiffs are not entitled to recover under any reasonably conceivable set of circumstances susceptible of proof. In re Gen. Motors (Hughes) S'holder Litig., 897 A.2d 162, 168 (Del. 2006) (quoting Savor, Inc. v. FMR Corp., 812 A.2d 894, 896-97 (Del. 2002)). As shown above, the Complaint alleges particularized facts sufficient to prove demand futility under the second prong of Aronson. These allegations, *a fortiori*, are sufficient to survive a Rule 12(b)(6) motion based on the business judgment rule. Ryan, 2007 WL 416162, at \*8.

**A. The Sham Special Committee Claim is Legally Sufficient**

The Defendants argue that the business judgment rule should apply to the claim that the Defendants created a sham Special Committee for the purpose of deceiving the shareholders and attempting to shield themselves from liability for V. Gupta's self-dealing going private transaction. DOB 36. The Defendants' sole argument is that Plaintiffs have not alleged any new fact beyond those which were dismissed in Cardinal's First Amended Derivative Complaint. Not only is the Defendants' characterization of the absence of any new allegations wrong, the Defendants' characterization of this Court's decision in dismissing Cardinal's First Amended Derivative complaint is also inaccurate.

The Court did not dismiss Cardinal's prior complaint because any substantive difficulties with the claim now asserted: that the Defendants engaged in a sham Special Committee process in order to deceive the shareholders into believing that an independent process existed when the

Defendants never intended that such a process would be independent and did not allow the process to be independent. This Court's substantive criticism of the prior claim was directed at the relief sought. The Court stated that it did not believe, as a matter of law, it would order the reinstatement of the Special Committee. Oct. 17, 2006 Tr. 11-12.

As to whether the creation of a sham Special Committee would constitute a breach of fiduciary duty, the Court suggested it could reach quite a different decision:

I do believe that a viable claim or claims can be found in this complaint. You have the beginnings of a claim that may give rise to different kinds of relief. It may, for example, give rise to claims of breach of fiduciary duty by the board in having – it created through pretext and a sham, really, a special committee whose real functions was merely to provide legal cover for Gupta's low ball offer to acquire the remaining shares in the company, and thus all the costs, if you can demonstrate that is – that that's the case and that that was done knowingly or in bad faith, then I think you may have a claim for damages; that is, all the expenses associated with that effort should be paid to the company in recompense for the injury inflicted on the company for launching the committee, and its advisors, on a pretext. And there may be a claim for waste related to all the lavish perks. Id. at 13.

Indeed, how could the result be different? Causing the Company to engage in a sham process for the purpose of deceiving shareholders and seeking to aid the single largest stockholder in avoiding his fiduciary duties could not pass muster under any analysis. Moreover, deliberately shutting down the broadly empowered Special Committee after it sought to pursue other alternatives for the benefit of all stockholders constitutes bad faith.

**B. The Section 144 and 157 Claims are Legally Sufficient**

Defendants argue that Plaintiffs' §144 claims fail as a matter of law because Plaintiffs failed to plead noncompliance with any of the three requirements of §144. DOB 37. This argument ignores Plaintiffs' Complaint. Plaintiffs plead in ¶151 that V. Gupta's self-dealing transactions "were (i) not approved by disinterested directors; (ii) not approved by a shareholder

vote; and (iii) not fair to infoUSA and its shareholders." Defendants also argue that there are no allegations to demonstrate that the challenged transactions were unfair to IUSA. DOB 37. The Complaint, however, pleads numerous examples of wasteful misuse and abuse of the Company's assets. The Raval Report and the failure of the beholden board to take action on it are proof of such misuse and abuse.

The Defendants' straw man argument under §157 is also wrong. The issue is not whether the former official who became a "consultant" was "eligible" for an option grant under the Company's 1997 Stock Option Plan. DOB 38. Plaintiffs' claim is that V. Gupta did not have the unilateral authority to give him the option. Under the 1997 Stock Option Plan, the Plan's Administrator (i.e. the Compensation Board or a board committee) "in its discretion, selects the directors, employees and consultants to whom options may be granted, the time or times at which such options shall be granted, and the number of shares subject to each such grant." DOB Ex. 4 at p. 21. Accordingly, Plaintiffs have stated a legally sufficient claim when they allege that V. Gupta's unilateral grant of the option violated the 1997 Stock Option Plan as well as §157.

**C. The Standstill Letter Claim is Legally Sufficient and States a Direct Claim.**

As shown above, the Standstill Letter between the Company and V. Gupta is invalid under §141(a). Defendants' reliance on Unisuper Ltd. v. News Corp., 2005 WL 3529317 (Del. Ch. Dec. 20, 2005) (DOB 38) is misplaced. The contract at issue in Unisuper (an agreement to hold a shareholder vote on a poison pill) did not violate §141(a) because it did not impermissibly cede power over the poison pill to an outside group or to an individual; rather, it ceded power to the company's shareholders or to the principal for which the directors were acting as agent. Id. at \*6. Here, in contrast, the Standstill Letter does not cede authority over the Rights Plan to IUSA's stockholders. Rather, it contractually prohibits IUSA's board from including V. Gupta in the Rights Plan, even if it served the best interests of the stockholders. This contractual abdication

of the directors duties is legally impermissible. Abercrombie v. Davies, 123 A.2d 893, 899 (Del. Ch. 1956) rev'd on other grounds, 130 A.2d 338 (Del. 1975). Moreover, it states a direct claim, Grimes v. Donald, 673 A.2d 1207, 1212 (Del. 1996), as to which demand is not even required.

Plaintiffs' claim is also ripe. Unlike Bebchuk v. CA, Inc., 902 A.2d 737 (Del. Ch. 2006) (DOB 39), the issue here is not whether a proposed bylaw, which is subject to a stockholder vote, is valid. The Standstill Letter is an executed agreement which purports to bind the Company and limit the Company's board's ability to amend the Rights Plan to terminate the exemption in it for V. Gupta. Thus, the legality of this agreement is ripe for review.

Moreover, the challenge to the Standstill Letter and Rights Plan is ripe because of V. Gupta's "creeping takeover" of IUSA. The Standstill Letter allows V. Gupta to exercise his existing options or any new options that the Company may award him. V. Gupta, accordingly, is free to increase his 41% stock position incrementally to a majority position thus destroying any opportunity for the public stockholders to receive a control premium while capturing the same for himself. This presents an immediate and direct harm to the public stockholders of IUSA.

**D. The Complaint States Legally Sufficient Claims for Breach of Fiduciary Duty and Waste.**

The Defendants argue that the fiduciary duty claim in Count IV should be dismissed because "nearly all" of the allegations in it were made in Cardinal's First Amended Derivative Complaint which this Court previously dismissed. DOB 39. This disingenuous argument ignores the fact that the only claim asserted and dismissed in Cardinal's prior complaint was its claim that the Special Committee has been improperly dissolved and should be reconstituted. This Court did not previously dismiss claims for waste and breach of fiduciary duty in connection with the related party transactions between IUSA and V. Gupta nor did it dismiss any of the disclosure claims alleged in the Complaint.

Defendants also rely on the business judgment rule. *DOB 39*. The business judgment rule does not apply where, as here, directors act disloyally, without care or in bad faith. In Re Walt Disney Co. Deriv. Litig., 906 A.2d 27, 52 (Del. 2006). At a minimum, the Complaint alleges that the directors acted in bad faith by intentionally acting with a purpose other than what was in IUSA's best interests and by consciously disregarding their duties to IUSA. Such conduct is not protected by the business judgment rule. *Id.* at 67.

The Complaint also alleges viable breaches of the directors' fiduciary disclosure obligations. Defendants V. Gupta, Haddix, Raval, Kaplan and Walker and former director Andersen knowingly misled IUSA's stockholders by mischaracterizing the true nature of the Company's payments to Annapurna and Aspen Leasing in IUSA's Form 10-Ks. The Company's 2005 Proxy Statement seeking, among other things, stockholder approval of an amendment to IUSA's 1997 Stock Option Plan was also false and misleading because it under reported V. Gupta's stock ownership by 4.4%. This misrepresentation injured the stockholders in their vote to amend the Option Plan. It is a direct, not derivative, fiduciary duty claim, Dieterich v. Harrer, 857 A.2d 1017, 1029 (Del. Ch. 2004), as to which demand is not even required.

As explained above, the Complaint also pleads a claim of waste. Contrary to Defendants' argument, Plaintiffs have alleged extensive and wide ranging facts showing that the challenged travel and entertainment did not have a valid purpose. For example, Plaintiffs allege that the only record produced by Defendants to substantiate the usage of the American Princess yacht – its logbook – does not reveal any business usage at all in violation of IRS regulations and the Company's own Code of Conduct. Even Raval concluded that nearly \$300,000 in 2004 alone was for personal usage of the yacht. Likewise, he concluded that \$120,000 was paid for personal usage of a residence and \$195,000 for undefined "service charges for travel services." Compl.

¶68. These admissions completely refute Defendants' argument that Plaintiffs have not stated a claim for waste. And they are just the "tip of the iceberg" because they only cover one year, 2004. Indeed, this Court recognized that something was amiss when it determined that documents concerning the "controversial use of planes and yachts" did not merit confidential designation and allowed Dolphin to inspect an additional two years of related party transaction and compensation documents. Dolphin Ltd. P'ship I, 2006 WL 1071518.

**CONCLUSION**

The Court should deny Defendants' motion to dismiss. Demand is excused because, for the reasons set forth in the Complaint and this brief, demand on IUSA's board would be futile. In addition, Plaintiffs' claims are legally sufficient under the Rule 12(b)(6) pleading standard. This case should be allowed to proceed so that V. Gupta and the other directors can be held accountable for years of unfair self dealing and the other actions complained of in the Complaint.

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