

2007

# William Borghetti v. System & Computer Technology, Inc. : Brief of Appellant

Utah Court of Appeals

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IN THE UTAH SUPREME COURT

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WILLIAM BORGHETTI, et al

Plaintiffs/Appellants,

v.

SYSTEM & COMPUTER  
TECHNOLOGY, INC., et al

Defendants/Appellee.

Court of Appeals No. 20070513-SC

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BRIEF OF APPELLANT

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**APPEAL FROM A FINAL JUDGMENT OF THE THIRD DISTRICT COURT  
THE HONORABLE JOHN PAUL KENNEDY**

---

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OCT 05 2007

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LIST OF PARTIES

WILLIAM BORGHETTI,  
MICHELLE BORGHETTI,  
LA DOZZINA SPORCA, LLC.,  
LA FAMIGLIA BORGHETTI, LLC.,

Plaintiffs,

SYSTEM & COMPUTER TECHNOLOGY, INC.  
THOMAS LEWIS, JR.,  
DARIN GILSON,  
CHAD MUIR,  
FRED HARMON,  
DAVID PETERSCHMIDT,  
DAVID GARDNER,  
ALLEN FRIEDMAN,  
ERIC HASKELL,  
MICHAEL CHAMBERLAIN,  
DAVID MURRAY,  
ANDY COOLEY,  
SCOTT DOUGHMAN,  
JOHN DUNN,  
TYLER THATCHER,  
THOMAS WEISEL, & PARTNERS,  
SUNGARD/SCT, INC.,  
CAMPUS PIPELINE, INC.,  
FRED HARMAN,  
OAK INVESTMENT PARTNERS,  
BENDINGER, CROCKETT, PETERSON AND  
CASEY,  
JEFFERY S. WILLIAMS

Defendants

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## TABLE OF CONTENTS

TABLE OF AUTHORITIES .....	-ii-
STATEMENT OF JURISDICTION .....	-1-
STATEMENT OF ISSUES PRESENTED .....	-1-
STANDARD OF REVIEW .....	-1-
STATEMENT OF THE CASE .....	-1-
SUMMARY OF ARGUMENT .....	-6-
ARGUMENT AND AUTHORITY .....	-7-
<b>KALAY’S AFFIDAVIT CLEARLY STATED THAT THE FAIR VALUE OF     PLAINTIFFS’ SHARES IN CPI WAS BETWEEN \$4.2 MILLION     AND \$6.706 MILLION. THAT FACT, WHILE DISPUTED BY THE     DEFENDANTS’ EXPERTS, REQUIRED THAT THE SUMMARY     JUDGMENT MOTIONS BE DENIED. ....</b>	<b>-7-</b>
<b>THE DISTRICT COURT INCORRECTLY CONCLUDED THAT THE     MARKET VALUE OF THE COMPANY ON THE DATE OF THE     MERGER WAS THE ONLY PROPER CALCULATION OF     DAMAGES.     .....</b>	<b>-8-</b>
CONCLUSION .....	-13-
STATEMENT REGARDING ADDENDUM .....	-13-

## TABLE OF AUTHORITIES

<u>Bill Brown Realty, Inc. v. Abbott</u> , 562 P.2d 238 (Utah 1977) .....	-7-
<u>Bingham Consolidation Co. v. Groesbeck</u> , 2004 UT App 434, 105 P.3d 365 (Utah Ct. App. 2004) .....	-10-
<u>Cede &amp; Co. v. Technicolor Inc.</u> , 684 A.2d 289, 296-297 (Del. 1996) .....	-8-, -9-
<u>Holbrook Co. v. Adams</u> , 542 P.2d 191 (Utah 1975) .....	-7-
<u>Mountain Estate Landscape and Snow Removal Specialists, Inc. v. Mountain States Tel. &amp; Tel. Co.</u> , 844 P.2d 322 (Utah 1992) .....	-1-
<u>Neiderhauser Bldrs. &amp; Dev. Corp. v. Campbell</u> , 824 P.2d 1193 (Utah Ct. App. 1992) .....	-7-
<u>Oakridge Energy Inc. v. Clifton</u> , 937 P.2d 130, 132 (Utah 1997) .....	-10-
<u>Paskill Corp. v. Alcoma Corp.</u> , 747 A.2d 549, 556 (Del. 2000) .....	-10-
<u>Schurtz v. BMW of N. Am., Inc.</u> , 814 P.2d 1108 (Utah 1991) .....	-7-
<u>Weinberger v. UOP, Inc.</u> , 457 A.2d 701 (Del. 1983) .....	-8-, -9-

## STATUTES AND RULES

8 <i>Del. C.</i> §262 .....	-3-, -8-
<i>Utah Code Ann.</i> §78-2-2(3)(j)(Rep. Vol. 9 2007) .....	-1-

### STATEMENT OF JURISDICTION

This Court has jurisdiction over this appeal pursuant to the provisions of *Utah Code Ann.* §78-2-2(3)(j)(Rep. Vol. 9 2007)

### STATEMENT OF ISSUES PRESENTED

Did the Court below err when it granted summary judgment by concluding that Plaintiffs failed to come forward with evidence of damages?

### STANDARD OF REVIEW

A district court's granting of a motion for summary judgment is reviewed for correctness; viewing the facts in the light most favorable to the nonmoving party.

Mountain Estate Landscape and Snow Removal Specialists, Inc. v. Mountain States Tel. & Tel. Co., 844 P.2d 322 (Utah 1992).

### STATEMENT OF THE CASE

This is an appeal from two separate summary judgments entered in the underlying case.

The Court below granted summary judgment for both defendants on one issue, damages, holding that Plaintiffs had not come forward with any evidence of damages. (R. 5368, R. 5358).

Plaintiffs, however, had presented an affidavit of Avner Kalay, a world renowned economist, which gave a range of damages for Plaintiffs of between \$4.2 million and

\$6.706 million. (R. 4645, ¶14).

### Summary of the Claims

In 1998, William Borghetti formed Campus Pipeline, Inc. (A Delaware Corporation f/k/a Campus Communications; hereafter “CPI”). (R. 1982, p. vii). Mr. Borghetti and the other Plaintiffs were all shareholders of common stock in CPI. (R. 1855, p. 2). System and Computer Technology (hereinafter “SCT”) made capital contributions to the company in exchange for common stock giving it 60% control over Campus Communications. (R. 1982, p. vii).

In 1999 and 2000 CPI sold preferred shares in its company which gave the preferred shareholders the first \$80.9 million in the event of a liquidation. (R. 1855, p.6-7).

In 2002, SCT, the largest and controlling shareholder made an offer to purchase CPI in a “cash out” merger. (R. 1855, p. 15). Defendant Thomas Weisel Partners, LLC (“TWP”) was retained by CPI to perform an appraisal/fairness opinion for CPI. (R. 1855, p. 15). TWP was only to be paid (a minimum of \$800,000.00) if the company was in fact liquidated. (R. 1855, p. 15 and 16).

On September 5, 2002, the CPI board of directors voted to approve a merger with SCT. (R. 1855, p. 21). The merger took effect on October 23, 2002 for a price of \$42,000,000. (R. 5368, p.2).

Plaintiffs stock was cancelled as a result of the acquisition, and they received nothing



(zero consideration) for their shares. (R. 5368, p.2).

Despite the clear interests of the Campus Pipeline common stockholders to reject the acquisition, Campus Pipeline's directors and officers approved a transaction with SCT that gave significant value to insiders (money), including the directors and officers who approved the transaction, and to SCT (the company and its assets), but nothing at all to Campus Pipeline's common stock. (R. 3957, Ex. NN, ¶¶5-14).

Because Borghetti opposed the acquisition, he was entitled under section 262 of the Delaware General Corporation Law (DGCL) to file an appraisal action in Delaware to seek a determination of the "fair value" of his shares in CPI as of the effective date of the acquisition. (R. 5368, p. 7). Section 262 of the DGCL requires that an appraisal action be filed within 120 days from the effective date of the acquisition. (R. 5368, p. 7).

To address his remedies, Borghetti alleged that he entered into an attorney client relationship with the Bendinger defendants based upon numerous in person meetings, phone calls, retention of valuation professionals, and Bendinger's taking of the only copy of Mr. Borghetti's file. (R. 3957, ¶¶ 1-35). The Bendinger defendants continued working with Mr. Borghetti on his case for over six months, during which time the statute of limitations for an appraisal action passed. (Id.). The Bendinger Defendants failed to file an appraisal action within 120 days and failed to advise Borghetti that they were not going to file such an appraisal action. (R. 3957, ¶¶ 1-35).

Plaintiffs brought this action against System and Computer Technology, Inc. and

Campus Pipeline's officers and directors for breach of fiduciary duty, unjust enrichment, misrepresentation and fraud. In this same litigation one of the Plaintiffs, William Borghetti, (hereinafter "Borghetti") brought a claim for legal malpractice against Bendinger, Crockett, Peterson and Casey and Jeffrey S. Williams (hereinafter "Bendinger defendants") for failing to timely file a Delaware state "appraisal action."

Despite the length of their relationship, researching of appraisals and fraud claims, the hiring of a valuation expert, and six months of in person and telephone meetings, the Bendinger defendants denied the existence of the attorney client relationship and claimed that Borghetti suffered no damages.

The SCT defendants claimed that they did their best to sell the corporation at the best price and that Plaintiffs suffered no damages. They also claimed since they sold at less than the liquidation preference that Plaintiffs could not show any damages.

Plaintiffs claimed (a) that there was no reason to sell; (b) that there were many other options available to keep CPI a going concern; (c) that there were substantial conflicts of interests for all parties that "approved" the transaction; and (d) that Plaintiffs were damaged as a result of receiving zero consideration for their shares.

Plaintiff William Borghetti ("Borghetti") claimed that CPI should not have approved the acquisition because it was unfair to the common shareholders since they received zero consideration.

The Kalay Opinions and the Opinions of the Defendants' Experts on the issue of Damages.

Plaintiffs' expert, Avner Kalay is a professor at the David Eccles School of Business at the University of Utah where he teaches courses in valuation. He received his B.A. in economics from Tel Aviv University, a Masters in Business Administration from the University of Rochester and a PhD in Business Administration from the University of Rochester. (R. 4645, ¶¶1-2). He was a Chairman of the Finance Department at Tel Aviv University, and a tenured member of NYU's business school faculty. (R. 4645, ¶¶3-4). Professor Kalay has published numerous articles in leading finance journals and formerly worked as a consultant for the SEC (R. 4645, ¶¶5-6).

In March 2006 Kalay prepared a valuation report for this matter in which he utilized an option pricing theory in order to value Campus Pipeline. (R. 3247, exh. C). Kalay determined that Campus Pipeline had a value of \$63.6 million and \$72.9 million at the end of 2002 and that the fair value of the Plaintiffs' shares at the time of the "cash out" merger was between \$4.2 million and \$6.706 million. (R. 4645, ¶¶ 13-14).

To arrive at that value, Kalay used what is known as the Black-Scholes method of valuation. (R. 4645, ¶15).

Kalay's conclusions in his report concerning use of the Black-Scholes methodology are highly supported by the available literature. Fischer Black and Myron Scholes won the Nobel Prize for Economics in 1997 for their work "The Pricing of

Options and Corporate Liabilities.” (R. 4645, ¶¶29b).

The Black-Scholes model is the seminal work in options pricing theory and it has not only been utilized in valuing options, but has been used to value equity and debt in a company. (R. 4645, ¶¶29a).

Nonetheless, the District Court granted summary judgment for both groups of Defendants on the erroneous conclusion that Plaintiffs did not have evidence of damages.

### SUMMARY OF ARGUMENT

The granting of summary judgement was incorrect because there was a disputed fact: the fair value of Plaintiffs’ shares at the time of the merger. The district court’s conclusion either disregarded the damage calculation of Avner Kalay, or it incorrectly concluded that the market value of the company on the date of the merger was the proper calculation of damages.

Delaware law clearly required that the district court determine the fair value of the Plaintiff’s shares as opposed to the market value of the company. In determining such fair value, the court was required to take into account all relevant factors, including the expert opinion of Dr. Kalay.

## ARGUMENT AND AUTHORITY

**KALAY'S AFFIDAVIT CLEARLY STATED THAT THE FAIR VALUE OF PLAINTIFFS' SHARES IN CPI WAS BETWEEN \$4.2 MILLION AND \$6.706 MILLION. THAT FACT, WHILE DISPUTED BY THE DEFENDANTS' EXPERTS, REQUIRED THAT THE SUMMARY JUDGMENT MOTIONS BE DENIED.**

In determining whether the trial court correctly found that there were no genuine issues of material fact, the appellate court views the facts and all reasonable inferences in a light most favorable to the party opposing the motion. Neiderhauser Bldrs. & Dev. Corp. v. Campbell, 824 P.2d 1193 (Utah Ct. App. 1992). The Court accords no deference to a trial court's legal conclusions given to support the grant of summary judgment, but reviews them for correctness. Schurtz v. BMW of N. Am., Inc., 814 P.2d 1108 (Utah 1991). It only takes one sworn statement to dispute averments on the other side of controversy and create an issue of fact, precluding summary judgment. Holbrook Co. v. Adams, 542 P.2d 191 (Utah 1975). The presence of a dispute as to material facts disallows the granting of a summary judgment. Bill Brown Realty, Inc. v. Abbott, 562 P.2d 238 (Utah 1977).

In its order granting summary judgment to the SCT defendants, the District Court stated:

Plaintiffs have failed to come forward with evidence creating a genuine issue of material fact on the question of whether they suffered damages. Because damages are a necessary element of each of the causes of action they bring against Defendants, Plaintiffs cannot prevail on any of their claims as a matter of law. (R. 5358, p 3-4).

That conclusion failed to recognize or account for paragraph 14 of Avner Kalay's affidavit in opposition to the motions for summary judgment. That paragraph reads:

14. In the March 2006 report later modified by my deposition testimony, I concluded that the fair value of Mr. Borghetti's shares at the time of the merger was between \$4.2 million and \$6.706 million."

Under both the legal malpractice causes of action and the breach of fiduciary duty, unjust enrichment, misrepresentation and fraud causes of action, the measure of the Plaintiffs' damages was the value of their shares of common stock in CPI at the time of the merger when they were cancelled. Dr. Kalay's opinion was that they were worth between four and six million dollars at the time they were cancelled.

Thus, there was a disputed fact: the value of the Plaintiffs' shares. Because there was a disputed fact, the granting of summary judgment was incorrect and should be overturned.

**THE DISTRICT COURT INCORRECTLY CONCLUDED THAT THE MARKET VALUE OF THE COMPANY ON THE DATE OF THE MERGER WAS THE ONLY PROPER CALCULATION OF DAMAGES.**

In Weinberger v. UOP, Inc., 457 A.2d 701 (Del. 1983), the Delaware Supreme Court explicitly broadened the interpretation of the Delaware Corporations Code, section 262 on appraisal rights, and adopted a more liberal approach to the valuation process (Id. at 704). The Court concluded that an exclusive method for valuation was outmoded and a more liberal approach to stock valuation and appraisal proceedings must include proof of value by *any* techniques or methods which are generally considered acceptable in the financial community (Id. at 712). They held that the most popularly employed techniques for valuation no longer exclusively control appraisal and valuation proceedings, and that alternative valuation techniques should be allowed. (Id. at 713; See also, Cede & Co. v. Technicolor Inc., 684 A.2d 289, 296-297 (Del. 1996)). The Court in Weinberger further concluded that when determining the value that the stockholder is entitled to be paid for that which has been taken from him, a number of relevant factors are to be included. The

Court stated:

In determining what figure represents [the] true or intrinsic value, the appraiser and the courts must take into consideration all factors and elements which reasonably might enter into the fixing of value. Thus, market value, asset value, dividends, earning prospects, the nature of the enterprise and any other facts which were known or which could be ascertained as of the date of merger and which throw any light on *future prospects* of the merged corporation are not only pertinent to an inquiry as to the value of the dissenting stockholders' interest, but ***must be considered*** by the agency fixing the value. . . This is not only in accord with the realities of present day affairs, but it is thoroughly consonant with the purpose and intent of our statutory law. It is significant that section 262 now mandates the determination of 'fair' value based upon 'all relevant factors.' Only the speculative elements of value that may arise from the 'accomplishment or expectation' of the merger are excluded. We take this to be a very narrow exception to the appraisal process.... But elements of future value, including the nature of the enterprise, which are known or susceptible of proof as of the date of the merger and not the product of speculation, may be considered. (*Id.* at 713; italics in original)

Thus, not only are acceptable valuation methods to be liberally construed by the Courts, but, according to Weinberger all the relevant factors should be included when determining value as well (See Also, Cede & Co. at 295<sup>1</sup>).

Even elements of "future value" may be considered. Weinberger and all of its progeny dictate that "market value" is simply a fact to be used in coming up with "fair

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<sup>1</sup> The Court in Cede Co. v. Technicolor, Inc. cited and followed Weinberger for the proposition that the Court must broaden the process for determining fair value, and factors that are not the product of speculation may be considered when determining value, including the nature of the enterprise (Cede Co. v. Technicolor, Inc. (1996) 684 A.2d 289, 295).

value.”<sup>2</sup> In fact the Black-Scholes method used by Kalay utilized market value as a factor. Kalay first determined the market value of the company to be between \$63.6 million and \$72.9 million. (R. 4645, ¶13). Kalay also accounted for the liquidation preference of approximately \$82 million. Kalay utilized those figures and others to come up with the “fair value” of Plaintiffs shares (the range of the “fair value” lost was between \$4.2 million and \$6.706 million).

Utah has also adopted a broad and liberal interpretation of the valuation methods that are allowed. In Bingham Consolidation Co. v. Groesbeck, 2004 UT App 434, 105 P.3d 365 (Utah Ct. App. 2004), the Utah Court of Appeals stated that the goal of appraisal is to ascertain the actual worth of that which the dissenter loses . . . there are no fixed methods for valuating the shares, and most courts permit all generally accepted techniques of valuation used in the financial community. (*Id.* at 370, citing Oakridge Energy Inc. v. Clifton, 937 P.2d 130, 132 (Utah 1997), See also, Paskill Corp. v. Alcoma Corp., 747 A.2d 549, 556 (Del. 2000)). They concluded that they are in agreement with other jurisdictions that, “a court should make use of all generally accepted techniques of valuation used in the financial community.” (Bingham at 375, See also, Paskill Corp. at 556).

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<sup>2</sup> This is precisely why defendant’s own expert stated that shares can be “out of the money” yet still have value. An “out of the money” scenario is exactly what we have here because the liquidation preference exceeds market value. Commons shareholders in these scenarios must have protection – otherwise, they can be frozen out at any time for any reason.



Defendants' own expert, Grabowski, in his expert report of May 31, 2006 points out this exact contention. He states that, "The Black-Scholes option pricing model is widely accepted in the financial community as a methodology to estimate the price of an option, or derivative instrument, and . . . may be used in certain instances to provide the value of the equity of a company under financial distress." (R. 1982, Ex. W, Grabowski Report, p. 14).

Pursuant to both Delaware and Utah law the Court should have liberally and broadly interpreted what valuation methods are to be allowed in such proceedings as this. The area of valuation is no longer controlled exclusively by certain methods, and those formulas and techniques which are generally accepted in the financial community are now clearly allowed by the Courts. (See, Weinberger at 712 and Bingham Consolidation at 370).

In stating that the Plaintiffs could not show damages, the District Court erred in two ways.

First, as shown above, market value is not solely determinative of "fair value."

Second, and more importantly, The market value of \$73.7 million to \$83.2 million cited by the Court was Professor Kalay's determination that Campus Pipeline as an entity had a market value of that amount at the time of the merger. Section 262 and the cases clearly state that the court is to determine the fair value of the shares on the date of the merger – not the company. It is a distinction that is not splitting hairs.

CPI was founded in 1998. In 2002, it was still clearly a start up venture. It is not surprising that the stock was “out of the money.” Google, Yahoo, and any other startup company experiences a period of initial capitalization where expenditures exceed earnings. The Defendants’ own expert acknowledged that “out of the money” stock still has value. For that reason, section 262 and the Delaware and Utah cases require that the value of the shares be determined – not the book, asset, or market value of the company. Each share of stock at the time of the merger was like owning a lottery ticket. If the company succeeded, they would have value. If the company ultimately failed, they would be worthless. The Plaintiffs had the right to continue to hold those shares and have the company continue in business.

Just like a losing lottery ticket has no value – a potentially winning lottery ticket clearly has a value. CPI had not failed. Its stock clearly had a value or expectation interest. Dr. Kalay’s opinion used Nobel prize winning methods to determine that value. It was the Defendants’ experts who failed to provide any legitimate value. They–like the court–used market value of the company. It is axiomatic that a share of stock that shows any possibility of success, has a value.

Instead of realizing on that value the common shareholders were given nothing. At the same time, the conflicted directors, the conflicted officers, and the controlling shareholder all walked away with either substantial cash payments or the company itself.

## CONCLUSION

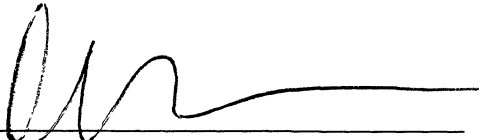
The Court below erred in simply looking at Professor Kalay's calculation of market value and holding such figures to be the "end all, be all" in this action. Instead, the Court below should have focused on the "fair value" damage calculation from Professor Kalay. That fair value damage calculation clearly and undoubtedly shows that Plaintiffs suffered damages of between \$4.2 million and \$6.706 million. Respectfully, the Appellants request that both Summary Judgment Orders and Judgments be vacated and reversed and the case remanded for trial below.

## STATEMENT REGARDING ADDENDUM

Attached as an addendum are:

1. Delaware Corporations Code, section 262
2. Affidavit of Avner Kalay
3. Affidavit of Daniel Greenwood

Dated this 16 day of October, 2007

  
\_\_\_\_\_  
Curtis L. Wenger,  
Attorney for Plaintiffs/Appellants

## **PROOF OF SERVICE**

I am a citizen of the United States and employed in Salt Lake County, Utah. I am over the age of eighteen years and not a party to the within-entitled action. My business address is City Centre I, 175 East 400 South, Suite 900, Salt Lake City, Utah 84111. I am readily familiar with this firm's practice for collection and processing of correspondence for mailing with the United States' Postal Service, Federal Express and hand delivery. On ~~August 12, 2004~~ <sup>October 5, 2007</sup>, I placed for delivery via U.S. Mail two true and correct copies of the within document, **APPELLANT'S BRIEF** in a sealed envelope, to the following:

John Pearce  
JONES WALDO HOLBROOK & McDONOUGH PC  
170 South Main Street Suite 1500  
Salt Lake City, Utah 84101


Stuart Schultz  
Strong & Hanni  
3 Triad Center Suite 500  
Salt Lake City, Utah 84180

And, one original and nine copies of **APPELLANT'S BRIEF** were served,  
[ ] via United States Mail, first-class postage prepaid, to:  
[ ] via hand delivery

to the Clerk of the Utah Supreme Court

I declare that I am employed in the office of an attorney that has been admitted to this Court at whose direction the service was made.

Executed on October 5, 2007 at Salt Lake City, Utah.

A handwritten signature in black ink, consisting of a stylized 'M' followed by a long horizontal stroke.

**CWEST'S DELAWARE CODE ANNOTATED**  
TITLE 8. CORPORATIONS  
CHAPTER 1. GENERAL CORPORATION LAW  
SUBCHAPTER IX. MERGER, CONSOLIDATION OR CONVERSION  
→§ 262. Appraisal rights

(a) Any stockholder of a corporation of this State who holds shares of stock on the date of the making of a demand pursuant to subsection (d) of this section with respect to such shares, who continuously holds such shares through the effective date of the merger or consolidation, who has otherwise complied with subsection (d) of this section and who has neither voted in favor of the merger or consolidation nor consented thereto in writing pursuant to § 228 of this title shall be entitled to an appraisal by the Court of Chancery of the fair value of the stockholder's shares of stock under the circumstances described in subsections (b) and (c) of this section. As used in this section, the word "stockholder" means a holder of record of stock in a stock corporation and also a member of record of a nonstock corporation; the words "stock" and "share" mean and include what is ordinarily meant by those words and also membership or membership interest of a member of a nonstock corporation; and the words "depository receipt" mean a receipt or other instrument issued by a depository representing an interest in one or more shares, or fractions thereof, solely of stock of a corporation, which stock is deposited with the depository.

(b) Appraisal rights shall be available for the shares of any class or series of stock of a constituent corporation in a merger or consolidation to be effected pursuant to § 251 (other than a merger effected pursuant to § 251(g) of this title), § 252, § 254, § 257, § 258, § 263 or § 264 of this title:

(1) Provided, however, that no appraisal rights under this section shall be available for the shares of any class or series of stock, which stock, or depository receipts in respect thereof, at the record date fixed to determine the stockholders entitled to receive notice of and to vote at the meeting of stockholders to act upon the agreement of merger or consolidation, were either (i) listed on a national securities exchange or (ii) held of record by more than 2,000 holders; and further provided that no appraisal rights shall be available for any shares of stock of the constituent corporation surviving a merger if the merger did not require for its approval the vote of the stockholders of the surviving corporation as provided in subsection (f) of § 251 of this title.

(2) Notwithstanding paragraph (1) of this subsection, appraisal rights under this section shall be available for the shares of any class or series of stock of a constituent corporation if the holders thereof are required by the terms of an agreement of merger or consolidation pursuant to §§ 251, 252, 254, 257, 258, 263 and 264 of this title to accept for such stock anything except:

a. Shares of stock of the corporation surviving or resulting from such merger or consolidation, or depository receipts in respect thereof;

b. Shares of stock of any other corporation, or depository receipts in respect thereof, which shares of stock (or depository receipts in respect thereof) or depository receipts at the effective date of the merger or consolidation will be either listed on a national securities exchange or held of record by more than 2,000 holders;

c. Cash in lieu of fractional shares or fractional depository receipts described in the foregoing subparagraphs a. and b. of this paragraph; or

d. Any combination of the shares of stock, depository receipts and cash in lieu of fractional shares or fractional depository receipts described in the foregoing subparagraphs a., b. and c. of this paragraph.

(3) In the event all of the stock of a subsidiary Delaware corporation party to a merger effected under § 253 of this title is not owned by the parent corporation immediately prior to the merger, appraisal rights shall be available for the shares of the subsidiary Delaware corporation.

(c) Any corporation may provide in its certificate of incorporation that appraisal rights under this section shall be available for the shares of any class or series of its stock as a result of an amendment to its certificate of incorporation, any merger or consolidation in which the corporation is a constituent corporation or the sale of all or substantially all of the assets of the corporation. If the certificate of incorporation contains such a provision, the procedures of this section, including those set forth in subsections (d) and (e) of this section, shall apply as nearly as is practicable.

(d) Appraisal rights shall be perfected as follows:

(1) If a proposed merger or consolidation for which appraisal rights are provided under this section is to be submitted for approval at a meeting of stockholders, the corporation, not less than 20 days prior to the meeting, shall notify each of its stockholders who was such on the record date for such meeting with respect to shares for which appraisal rights are available pursuant to subsection (b) or (c) hereof that appraisal rights are available for any or all of the shares of the constituent corporations, and shall include in such notice a copy of this section.

Each stockholder electing to demand the appraisal of such stockholder's shares shall deliver to the corporation, before the taking of the vote on the merger or consolidation, a written demand for appraisal of such stockholder's shares. Such demand will be sufficient if it reasonably informs the corporation of the identity of the stockholder and that the stockholder intends thereby to demand the appraisal of such stockholder's shares. A proxy or vote against the merger or consolidation shall not constitute such a demand. A stockholder electing to take such action must do so by a separate written demand as herein provided. Within 10 days after the effective date of such merger or consolidation, the surviving or resulting corporation shall notify each stockholder of each constituent corporation who has complied with this subsection and has not voted in favor of or consented to the merger or consolidation of the date that the merger or consolidation has become effective; or

(2) If the merger or consolidation was approved pursuant to § 228 or § 253 of this title, then either a constituent corporation before the effective date of the merger or consolidation or the surviving or resulting corporation within 10 days thereafter shall notify each of the holders of any class or series of stock of such constituent corporation who are entitled to appraisal rights of the approval of the merger or consolidation and that appraisal rights are available for any or all shares of such class or series of stock of such constituent corporation, and shall include in such notice a copy of this section. Such notice may, and, if given on or after the effective date of the merger or consolidation, shall, also notify such stockholders of the effective date of the merger or consolidation. Any stockholder entitled to appraisal rights may, within 20 days after the date of mailing of such notice, demand in writing from the surviving or resulting corporation the appraisal of such holder's shares. Such demand will be sufficient if it reasonably informs the corporation of the identity of the stockholder and that the stockholder intends thereby to demand the appraisal of such holder's shares. If such notice did not notify stockholders of the effective date of the merger or consolidation, either (i) each such constituent corporation shall send a second notice before the effective date of the merger or consolidation notifying each of the holders of any class or series of stock of such constituent corporation that are entitled to appraisal rights of the effective date of the merger or consolidation or (ii) the surviving or resulting corporation shall send such a second notice to all such holders on or within 10 days after such effective date; provided, however, that if such second notice is sent more than 20 days following the sending of the first notice, such second notice need only be sent to each stockholder who is entitled to appraisal rights and who has demanded appraisal of such holder's shares in accordance with this subsection. An affidavit of the secretary or assistant secretary or of the transfer agent of the corporation that is required to give either notice that such notice has been given shall, in the absence of fraud, be prima facie evidence of the facts stated therein. For purposes of determining the stockholders entitled to receive either notice, each constituent corporation may fix, in advance, a record date that shall be not more than 10 days prior to the date the notice is given, provided, that if the notice is given on or after the effective date of the merger or consolidation, the record date shall be such effective date. If no record date is fixed and the

notice is given prior to the effective date, the record date shall be the close of business on the day next preceding the day on which the notice is given.

(e) Within 120 days after the effective date of the merger or consolidation, the surviving or resulting corporation or any stockholder who has complied with subsections (a) and (d) hereof and who is otherwise entitled to appraisal rights, may commence an appraisal proceeding by filing a petition in the Court of Chancery demanding a determination of the value of the stock of all such stockholders. Notwithstanding the foregoing, at any time within 60 days after the effective date of the merger or consolidation, any stockholder who has not commenced an appraisal proceeding or joined that proceeding as a named party shall have the right to withdraw such stockholder's demand for appraisal and to accept the terms offered upon the merger or consolidation. Within 120 days after the effective date of the merger or consolidation, any stockholder who has complied with the requirements of subsections (a) and (d) hereof, upon written request, shall be entitled to receive from the corporation surviving the merger or resulting from the consolidation a statement setting forth the aggregate number of shares not voted in favor of the merger or consolidation and with respect to which demands for appraisal have been received and the aggregate number of holders of such shares. Such written statement shall be mailed to the stockholder within 10 days after such stockholder's written request for such a statement is received by the surviving or resulting corporation or within 10 days after expiration of the period for delivery of demands for appraisal under subsection (d) hereof, whichever is later. Notwithstanding subsection (a) of this section, a person who is the beneficial owner of shares of such stock held either in a voting trust or by a nominee on behalf of such person may, in such person's own name, file a petition or request from the corporation the statement described in this subsection.

(f) Upon the filing of any such petition by a stockholder, service of a copy thereof shall be made upon the surviving or resulting corporation, which shall within 20 days after such service file in the office of the Register in Chancery in which the petition was filed a duly verified list containing the names and addresses of all stockholders who have demanded payment for their shares and with whom agreements as to the value of their shares have not been reached by the surviving or resulting corporation. If the petition shall be filed by the surviving or resulting corporation, the petition shall be accompanied by such a duly verified list. The Register in Chancery, if so ordered by the Court, shall give notice of the time and place fixed for the hearing of such petition by registered or certified mail to the surviving or resulting corporation and to the stockholders shown on the list at the addresses therein stated. Such notice shall also be given by 1 or more publications at least 1 week before the day of the hearing, in a newspaper of general circulation published in the City of Wilmington, Delaware or such publication as the Court deems advisable. The forms of the notices by mail and by publication shall be approved by the Court, and the costs thereof shall be borne by the surviving or resulting corporation.



(g) At the hearing on such petition, the Court shall determine the stockholders who have complied with this section and who have become entitled to appraisal rights. The Court may require the stockholders who have demanded an appraisal for their shares and who hold stock represented by certificates to submit their certificates of stock to the Register in Chancery for notation thereon of the pendency of the appraisal proceedings; and if any stockholder fails to comply with such direction, the Court may dismiss the proceedings as to such stockholder.

(h) After the Court determines the stockholders entitled to an appraisal, the appraisal proceeding shall be conducted in accordance with the rules of the Court of Chancery, including any rules specifically governing appraisal proceedings. Through such proceeding the Court shall determine the fair value of the shares exclusive of any element of value arising from the accomplishment or expectation of the merger or consolidation, together with interest, if any, to be paid upon the amount determined to be the fair value. In determining such fair value, the Court shall take into account all relevant factors. Unless the Court in its discretion determines otherwise for good cause shown, interest from the effective date of the merger through the date of payment of the judgment shall be compounded quarterly and shall accrue at 5% over the Federal Reserve discount rate (including any surcharge) as established from time to time during the period between the effective date of the merger and the date of payment of the judgment. Upon application by the surviving or resulting corporation or by any stockholder entitled to participate in the appraisal proceeding, the Court may, in its discretion, proceed to trial upon the appraisal prior to the final determination of the stockholders entitled to an appraisal. Any stockholder whose name appears on the list filed by the surviving or resulting corporation pursuant to subsection (f) of this section and who has submitted such stockholder's certificates of stock to the Register in Chancery, if such is required, may participate fully in all proceedings until it is finally determined that such stockholder is not entitled to appraisal rights under this section.

(i) The Court shall direct the payment of the fair value of the shares, together with interest, if any, by the surviving or resulting corporation to the stockholders entitled thereto. Payment shall be so made to each such stockholder, in the case of holders of uncertificated stock forthwith, and the case of holders of shares represented by certificates upon the surrender to the corporation of the certificates representing such stock. The Court's decree may be enforced as other decrees in the Court of Chancery may be enforced, whether such surviving or resulting corporation be a corporation of this State or of any state.

(j) The costs of the proceeding may be determined by the Court and taxed upon the parties as the Court deems equitable in the circumstances. Upon application of a stockholder, the Court may order all or a portion of the expenses incurred by any stockholder in connection with the appraisal proceeding, including, without limitation, reasonable attorney's fees and the fees and expenses of experts, to be charged pro rata against the value of all the shares entitled to an appraisal.

(k) From and after the effective date of the merger or consolidation, no stockholder who has demanded appraisal rights as provided in subsection (d) of this section shall be entitled to vote such stock for any purpose or to receive payment of dividends or other distributions on the stock (except dividends or other distributions payable to stockholders of record at a date which is prior to the effective date of the merger or consolidation); provided, however, that if no petition for an appraisal shall be filed within the time provided in subsection (e) of this section, or if such stockholder shall deliver to the surviving or resulting corporation a written withdrawal of such stockholder's demand for an appraisal and an acceptance of the merger or consolidation, either within 60 days after the effective date of the merger or consolidation as provided in subsection (e) of this section or thereafter with the written approval of the corporation, then the right of such stockholder to an appraisal shall cease. Notwithstanding the foregoing, no appraisal proceeding in the Court of Chancery shall be dismissed as to any stockholder without the approval of the Court, and such approval may be conditioned upon such terms as the Court deems just; provided, however that this provision shall not affect the right of any stockholder who has not commenced an appraisal proceeding or joined that proceeding as a named party to withdraw such stockholder's demand for appraisal and to accept the terms offered upon the merger or consolidation within 60 days after the effective date of the merger or consolidation, as set forth in subsection (e) of this section.

(l) The shares of the surviving or resulting corporation to which the shares of such objecting stockholders would have been converted had they assented to the merger or consolidation shall have the status of authorized and unissued shares of the surviving or resulting corporation.

Current through 76 Laws 2007, ch. 181. Revisions to Acts made by the Delaware Code Revisors were unavailable at time of publication.

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END OF DOCUMENT

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Attorney for Plaintiffs

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IN THE THIRD JUDICIAL DISTRICT COURT FOR SALT LAKE COUNTY,  
STATE OF UTAH

---

WILLIAM BORGHETTI, MICHELLE  
BORGHETTI, LA DOZZINA SPORCA,  
LLC., LA FAMIGLIA BORGHETTI,  
LLC., CAMPUS PIPELINE, INC.,  
(DERIVATIVELY)

Plaintiffs,

vs.

SYSTEM & COMPUTER  
TECHNOLOGY, INC., a corporation;  
THOMAS LEWIS JR., DARIN GILSON,  
CHAD MUIR, FRED HARMON, DAVID  
PETERSCHMIDT, DAVID GARDNER,  
ALLEN FRIEDMAN, ERIC HASKELL,  
MICHAEL CHAMBERLAIN, DAVID  
MURRAY, ANDY COOLEY, SCOTT  
DOUGHMAN, JOHN DUNN, TYLER  
THATCHER, THOMAS WEISEL  
PARTNERS, SUNGUARD/SCT, Inc.,  
CAMPUS PIPELINE, INC., FRED  
HARMAN, OAK INVESTMENT  
PARTNERS, BENDINGER, CROCKETT,  
PETERSON AND CASE, a professional  
corporation, JEFFREY S. WILLIAMS, and  
Does 1 to 100, inclusive..

Defendants

**AFFIDAVIT OF AVNER KALAY IN  
SUPPORT OF PLAINTIFFS'  
OPPOSITION TO DEFENDANTS'  
MOTIONS FOR SUMMARY  
JUDGMENT AND IN SUPPORT OF  
PLAINTIFFS' OPPOSITION TO  
DEFENDANTS' MOTION TO  
STRIKE**

CASE NO.: 040921012

JUDGE: John Paul Kennedy

Certificate No.: 525 מספר אישור:

Authentication of signature

אימות חתימה

I the undersigned, Ilan Dovev, Adv. notary at Midot House 51 Weizmann St. Tel-Aviv, ISRAEL, hereby certify that on 22/11/2006 there appeared before me at my office Mr. Kalay Avner, whose identity was proved to me by identity booklet No. 030221006 issued by Home Office at Ramat-gan on 17/08/1984, and signed of his own free will the attached document marked A.

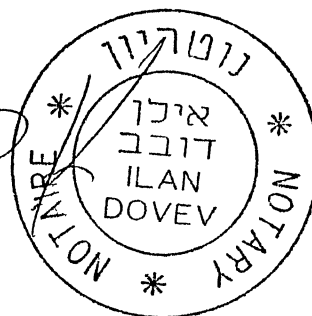
In witness whereof I hereby authenticate the signature of Mr. Kalay Avner by my own signature and notary's seal this 22/11/2006.

אני הח"מ אילן דובב, עו"ד נוטריון מבית מידות, רח' ויצמן 51 תל-אביב, מאשר כי ביום 22/11/2006 ניצב לפני במשרדי מר קלעי אבנר, שזהותו הוכחה לי על פי תעודת זהותו מספר, 030221006 שניתנה מאת משרד הפנים ברמת גן ביום 17/08/1984, וחתם מרצונו החופשי על המסמך המצורף והמסומן באות A.

ולראיה הנני מאמת את חתימתו של מר קלעי אבנר בחתימת ידי ובחותמי היום 22/11/2006.

דובב אילן עורך דין  
Advocate & Notary

Signature



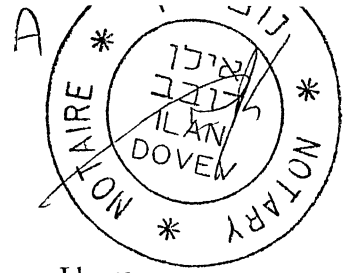
חותם הנוטריון  
Notary's seal

שכר טירחה נוטריוני  
בתוספת מע"מ כחוק. שולם.

הברמן דובב שטרן ושות' משרד עורכי דין ונוטריונים בית מידות ויצמן 51 תל אביב

Harman Dovev Stern & Co. Law Offices & Notaries

מקד זה הופק ע"י עו"ד דובב אילן



AFFIDAVIT OF AVNER KALAY

I, Avner Kalay, being first duly sworn, deposes and states as follows: I have personal knowledge of the items contained in this affidavit and would testify consistent hereto if I were called to testify.

1. I am a professor of Finance at the University of Utah David Eccles School of Business in Salt Lake City, Utah.
2. I received my B.A. in economics from Tel Aviv University in 1973, my M.S. in Business Administration from the University of Rochester in 1977 and a Ph.D in Business Administration from the University of Rochester in 1979.
3. I was a member of NYU's finance department during 1978-1987, and was tenured at NYU in 1985
4. I have previously been the Chairman of the Finance Department at Tel Aviv University, and presently am still a professor of finance there.
5. I have also worked for the Securities and Exchange Commission as a consultant in Washington, DC.
6. I have been published numerous times in journals in the finance community and co-wrote Dividend Policy: Its Impact on Value, in 1999.
7. I am co-founder and co-organizer of the Utah Winter Finance Conference held every year since 1991.
8. I have served as an expert witness in a number of cases involving business valuations, including but not limited to, MCN Energy V Crown Asphalt Corporation, Etrade V LifeWise, and SCO V. IBM.

IL  
DOV

9. I have been a consultant for numerous companies operating in different industries, including Coco Cola, American Express, Intel, Hermes Associates, among others.
10. In a recent ranking of financial economists by citation to their work in top finance journals from 1974-1998 ranked me at the top 100 in the world.
11. I have participated in over 50 professional conferences as a presenter, discussant, and session chair on a range of financial issues, and I give frequent lectures about my research at other universities.
12. On or about March 2006 I prepared a valuation report for Plaintiff's in this matter.
13. In my report I determined that Campus Pipeline at the time of acquisition had an approximate value of \$73.7 million to \$83.2 million.
14. In the March 2006 report later modified by my deposition testimony, I concluded that the fair value of Mr. Borghetti's shares at the time of the merger was between \$4.2 million and \$6.706 million.
15. In my report I employed a widely used and generally accepted valuation method called the Black-Scholes model, developed by Fischer Black and Myron Scholes in 1973 as a method used to value options.
16. In my report I point out that the Black-Scholes method is an appropriate method for valuing equity in a levered firm, because equity in a levered firm, such as Campus Pipeline, can be viewed as a call option to buy the assets of the firm (Report, 9).



17. The Black Scholes option pricing model is an appropriate valuation model for equity in a levered firm whether or not the firm is in financial distress or operational distress. It is not disputed that Campus Pipeline had "debt-like" potential obligation to its preferred stockholders. So whether or not Campus Pipeline was in financial distress or in operational distress the Black Scholes option pricing model can be used to value its equity.
18. The appraisal action statute in Delaware provides that value the court considers is the fair value of the shares. Delaware Corporations Code, section 262(h): "After determining the stockholders entitled to an appraisal, the Court shall appraise the shares, determining their fair value exclusive of any element of value arising from the accomplishment or expectation of the merger or consolidation, together with a fair rate of interest, if any, to be paid upon the amount determined to be the fair value. In determining such fair value, the Court shall take into account all relevant factors."
19. Campus Pipeline at the time of acquisition had preferred stockholders, and holders of Series A and B preferred stock were to be paid the sum of \$82.93 million in the event of liquidation, prior to any payment to the common stockholders. Because of this large liquidation preference the preferred stock shares were debt like in nature making Campus Pipeline a highly levered firm (See, Kalay Report 9-10 "Equity in a levered firm can be viewed as a call option to buy the assets of the firm . . . The analogy to the case of Campus Pipeline is straightforward. Campus Pipeline, at the time of the acquisition by SCT, had almost no long-term debt. Yet . . . holders of Series A and B



preferred stock are to be paid the sum of \$82.93 million in the event of liquidation prior to any payment to the common stockholders.”; See Grabowski Report 13-14 “Campus Pipeline is considered to be a highly levered firm because of the large liquidation preference (\$82.9 million) of the preferred shares, which are debt-like in nature.”).

20. Pursuant to the literature on the subject and the research I have encountered, along with my education, experience and training, it is clear that Black-Scholes is the seminal work in options pricing theory, is the most widely used and most recognized model for the valuation of options and has not only been employed to value options, but also to value equity and debt in a company like Campus Pipeline.
21. In reviewing Defendant’s expert report prepared by Roger Grabowski, I noticed that despite Grabowski’s deposition testimony that my use of the Black-Scholes model was inappropriate because Black-Scholes is generally used to value publicly traded companies, Grabowski himself in his report discusses the model’s use in the area of real options where the underlying asset is *not* traded.
22. Grabowski’s report on Campus Pipeline even mentions that the Black-Scholes method is utilized in the financial community and is also utilized in some circumstances, to value the equity of a company.
23. In my opinion, the discount cash flow analysis, used by Hoffman and Grabowski, can result in undervaluing of the firm because that analysis does





not capture certain complexities and nuances that the Black-Scholes option pricing theory does.

24. My report assumes that no acquisition took place, and is dependent on the assumption that CPI continued to operate for 9 to 13 years, but the methods employed by Defendant's expert, the Discounted Cash Flow Analysis, also makes these same assumptions.
25. The income approach, market approach, and cost approach are generally accepted valuation methodologies, and the Black-Scholes method is also generally accepted and has been in use since 1973. It is in fact an "income approach" method.
26. Valuation guidelines state clearly that when a good estimate of the market value is available it is best to use it. I use the price paid for Campus Pipeline as the starting point of my evaluation of the market value of its equity. That I use the price paid for Campus Pipeline to compute its full market value is my use of the market approach. Thus my analysis is consistent with the income approach as well as the market approach.
27. The "bad act" discussed in my report is relevant only to the issue as to whether Campus Pipeline should have been sold from the financial economics perspective. It is not utilized in my calculation of fair value and has no effect on the fair value issue.
28. Attached is my expert report which is true, accurate, reliable, and provides my opinion in this case other than the error in the final calculation corrected



by me in my deposition, such that Borghetti's damages range from \$4.2 million to \$6.706 million.

29. The following is some of the authoritative literature that I believe supports my conclusions on the use of the Black-Scholes methodology (along with other literature cited in my deposition):

- a. The Black-Scholes model is the seminal work in options pricing theory and it has not only been utilized in valuing options, but has been used to value equity and debt in a company. (See generally, Damodaran, Aswath. Investment Valuation: Tools and Techniques for Determining the Value of Any Asset, 2<sup>nd</sup> Ed. New York: John Wiley & Sons, Inc. 1996, page 828-829).
- b. Scholes and [Robert] Merton shared the 1997 Nobel Prize in economics for their work on the development of this formula (Brealey, Richard A., and Stuart C. Myers, and Alan J. Marcus. Fundamentals of Corporate Finance, 4<sup>th</sup> Ed. New York: McGraw Hill Companies, Inc., 2004, page 651)
- c. An options approach to valuation has been cited as a powerful tool in the financial community because it allows an analyst to capture certain complexities and nuances . . . [and] using the risk adjusted discount rate version of the discount cash flow (DCF) analysis can result in overlooking an important option that is available and substantially undervaluing the firm. (See, Boer, Peter F. The Real Options Solution:



Finding Total Value in a High-Risk World New York John Wiley & Sons, Inc , pp vii, 95, 100)

- d It has been heavily cited and discussed that equity can be viewed as a call option and therefore one would value equity as an option using the option pricing technique (See, Damodaran, Aswath (2006) The Cost of Distress Survival, Truncation Risk and Valuation Social Science Research Network [http //ssrn com/abstract=887129](http://ssrn.com/abstract=887129), pages 2, 36)
- e Equity is a kind of option on the assets (See, Callaghan, Clark and Jack Ayer (1999) Good News for the Black Scholes Sufferers No 1 Norton Bankr L Adviser 7)
- f Since 1973, the Black-Scholes-Merton methodology has been applied to a wide variety of contingent claims Financial guarantees can be analyzed as put options, and the equity of a levered firm can be analyzed as a call option on the firm's assets ” (Gray, D and Robert Merton and Zvi Bodie “A New Framework for Analyzing and Managing Macrofinancial Risks ” Prepared for the CV Starr/RED Conference on Finance and the Macroeconomy, October 11-12, 2002 New York, N Y , page 4)
- g Some analysts have found that it is possible to consider a company's equity as a call option, wherein the underlying asset is the value of the company's debt In this context, option pricing models, such as the Black-Scholes model can be used for valuing a target's equity (Feiris,



Kenneth R. and Barbara S. Pettit. Valuation: Avoiding the Winner's Curse. New Jersey: Prentice Hall, Inc. 2002, page 126).

- h. In an article entitled "IS: Valuation Methods: Insights from Capital Markets Theory and Practice," Tim Weitzel, Cornelia Gellings, Daniel Beimborn and Wolfgang Konig, explore the use of the Real Options Approach for valuing information systems (IS) and information technology (IT) businesses. They state that "IS valuation has long been a core research challenge [and] real options approaches have received attention as methodological means of overcoming some shortcomings of traditional valuation approaches like net present value . . . The real options approach employs the financial option theory based on the Black-Scholes formula. (Beimborn, Daniel and Cornelia Gellings, Wolfgang Konig, Tim Weitzel. (2003). "IS Valuation Methods: Insights from Capital Markets Theory and Practice." Presented at the 7<sup>th</sup> Pacific Asia Conference on Information Systems, July 10-13, 2003, Adelaide, South Australia, pp. 1, 10)/
- i. In the article entitled "High Stakes in High Technology: High-Tech Market Values as Options," authors Michael Darby, Qiao Liu, and Lynne Zucker explore the theory that a high tech firm can be valued using option theory. They state that "because we know that achievement of technological breakthroughs – or failure to achieve them in R&D project, affects the firm's market valuation, we expect that a certain type of discontinuity in the firm's market value will



occur whenever the firm makes frontier discoveries or announces failure . . . we take a “traditional view” of treating the firm’s equity value as a call option written on the firm’s valued assets . . . ” (Darby, Michael and Qiao Liu and Lynne Zucker. (2004) “High Stakes in High Technology: High-Tech Market Values as Options.” *Economic Inquiry*, Vol.42, No.3: 351-369 at 352).

- j. Aswath Damodaran, professor of Finance at the Stern School of Business at NYU teaches equity valuation and financing courses, and in his book, Investment Valuation: Tools and Techniques for Determining the Value of Any Asset, he utilizes the Black-Scholes model to determine the values of equity and debt in a firm. He says that equity is a call option on the value of the firm and therefore employs the option pricing technique. (Damodaran, A (2002). Investment Valuation: Tools and Techniques for Determining the Value of Any Asset, 2<sup>nd</sup> Ed. New York: John Wiley & Sons, page 828).
- k. Many in the field have deemed option pricing theory a viable alternative to other traditional valuation models. Because of limitations associated with the implementation of other traditional valuation models, the 1990’s saw the development of a number of alternative valuation frameworks . . . Discounted cash flow analysis (DCFA) assumes the capital structure of a company is stable over time. In the case of a leveraged buy-out or a debt restructuring after a



merger or an acquisition, the analyst needs an alternative approach that overcomes the assumption of stable capital structure underlying DCFA

Finally, where investments are structured as sequential rounds of financing, some analysts have found it useful to model the valuation using real options analysis (Ferris, K Petitt, B Valuation Avoiding the Winner's Curse Financial Times Prentice Hall Books, New York, NY 2002, page 108)

- l In a paper by Andreas Charitou and Lenos Trigeorgis, the authors point out that the equity of a levered firm can be viewed as a call option to acquire the value of the firm's assets, and they employ the option pricing theory or contingent claims analysis introduced by the seminal work of Black and Scholes and Merton They further discuss how the Black and Sholes and Merton work of option valuation or contingent claim analysis has been applied to the valuation of various corporate securities seen as packages of claims or options on the total value of the firm's assets (Charitou, Andreas and Lenos Trigeorgis Option-Based Bankruptcy Prediction Social Science Research Network June 2000)
- m Black-Scholes applies to contingent claims, therefore you ought to be able to analyze all kinds of assets using Black-Scholes techniques (See, Callaghan, Clark and Jack Ayer (1999) Good News for Black Scholes Sufferers No 1 Norton Bankr L Adviser 7, 10)



- n. The options pricing method takes into account factors that the other methods may ignore, such as flexibility of the firm and distress of the firm. The option pricing method captures the value of a firm's flexibility and takes into account the company's distress as well, and when dealing with a distressed firm, you have to consider that the equity of the firm takes on option characteristics. (See, Copeland, T., and Tim Koller and Jack Murrin. (1994) Valuation: Measuring and Managing the Value of Companies. New York: McKinsey & Company, Inc., page 399; See Also, Damodaran, Aswath. (2006) The Cost of Distress: Survival, Truncation Risk and Valuation Social Science Research Network: <http://ssrn.com/abstract=887129>, pages 2, 36).
- o. The more traditional valuation methods such as the risk adjusted discount rate version of the Discounted Cash Flow analysis (DCFA), tends to underestimate the value of a firm's equity. Most DCF valuation approaches only define a single scenario . . . DCF valuations [can] underestimate the value of the firm . . . because they ignore the options that these firms have to invest more in the future and take advantage of unexpected success in their businesses. These options are increasingly called "real options" because the underlying assets are real investments, and they might explain, at least in some cases why discounted cash flows understate the value of technology firms .
- (Roos, G. and Oliver Gupta. (2001) "Valuation of Private Technology



Firms: A Discussion Paper on Dealing with the Associated Problems.”

Intellectual Capital Services, pp 24-25)

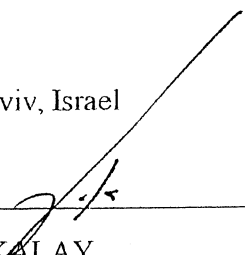
- p. The discounted cash flow models understate the value of equity in firms with high financial leverage and negative operating income, since they do not reflect the option that equity investors have to liquidate the firm's assets. Black and Scholes suggest that the equity in a levered firm can be thought of as a call option (Pengfei, H and Hua Yimin. (2002) Real Option Valuation in High-Tech Firm. Gothenburg University School of Economics and Commercial Law, pp. 41-42)
- q. The field of finance has developed a variety of option pricing models with the fundamental ones being the binomial model and the Black-Scholes model option pricing models. Over time, these models and their extensions have been used in a variety of evaluative settings (Benaroch, Michel and Robert Kauffman. (1999) “A Case for Using Real Options Pricing Analysis to Evaluate Information Technology Project Investments.” *Information Systems Research*, Vol. 10, No.1 70-86)
- r. The Black-Scholes method is currently the most recognized and widely used theoretical model for the valuation of options. (Hitchner, James R. Financial Valuations: Applications and Models. Hoboken: John Wiley & Sons, Inc., 2003, page 927)

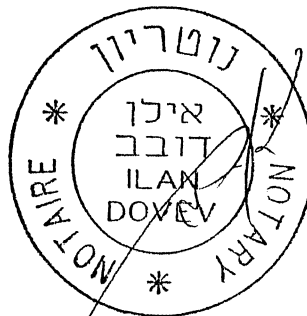




- s. The Black-Scholes model now seems to be by far the most important single breakthrough of the “golden decade,” and ranks with the Modigliani-Miller Theorem and the CAPM of Sharpe and Lintner in its overall importance for financial theory and practice. (Duffie, Darrell. (1992) Dynamic Asset Pricing Theory. Princeton: Princeton University Press, page xiii).

Executed this \_\_22\_\_ day of November, 2006, at Tel Aviv, Israel

  
AVNER KALAY



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Attorney for Plaintiffs

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IN THE THIRD JUDICIAL DISTRICT COURT FOR SALT LAKE COUNTY,  
STATE OF UTAH

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WILLIAM BORGHETTI, MICHELLE  
BORGHETTI, LA DOZZINA SPORCA,  
LLC., LA FAMIGLIA BORGHETTI,  
LLC., CAMPUS PIPELINE, INC.,  
(DERIVATIVELY)

Plaintiffs,

vs.

SYSTEM & COMPUTER  
TECHNOLOGY, INC., a corporation;  
THOMAS LEWIS JR., DARIN GILSON,  
CHAD MUIR, FRED HARMON, DAVID  
PETERSCHMIDT, DAVID GARDNER,  
ALLEN FRIEDMAN, ERIC HASKELL,  
MICHAEL CHAMBERLAIN, DAVID  
MURRAY, ANDY COOLEY, SCOTT  
DOUGHMAN, JOHN DUNN, TYLER  
THATCHER, THOMAS WEISEL  
PARTNERS, SUNGUARD/SCT, Inc.,  
CAMPUS PIPELINE, INC., FRED  
HARMAN, OAK INVESTMENT  
PARTNERS, BENDINGER, CROCKETT,  
PETERSON AND CASE, a professional  
corporation, JEFFREY S. WILLIAMS, and  
Does 1 to 100, inclusive..

Defendants

**AFFIDAVIT OF DANIEL  
GREENWOOD IN SUPPORT OF  
PLAINTIFFS' OPPOSITION TO  
DEFENDANTS' MOTIONS FOR  
SUMMARY JUDGMENT AND IN  
SUPPORT OF PLAINTIFFS'  
OPPOSITION TO DEFENDANTS'  
MOTION TO STRIKE**

CASE NO.: 040921012

JUDGE: John Paul Kennedy

I, Daniel Greenwood, being first duly sworn, deposes and state as follows: I have personal knowledge of the items contained in this Affidavit and would testify consistent hereto if I were called to testify.

1. I am a Professor of Law at the S.J. Quinney College of Law at the University of Utah, where I have been employed since 1992.
2. I am a graduate of Harvard College and Yale Law School.
3. After I graduated from law school I clerked for the Honorable Richard Owen, USDJ, in the Southern District of New York and then practiced corporate litigation as an associate attorney with Cleary, Gottlieb, Steen & Hamilton for several years.
4. My major area of academic research is the theory and practice of corporate governance, with a special emphasis on the relationships of the various parties to the corporation as governed by the law of fiduciary duty.
5. My opinions stated below are based on the evidence I have reviewed in this case, my knowledge of general principles and goals of corporate governance in general and the funding of start-up companies specifically, and the case law of Delaware, Utah and other American jurisdictions.
6. The circumstances in the Campus Pipeline, Inc. ("Campus Pipeline"), and System & Computer Technology, Inc. ("SCT"), transaction involve the important fiduciary obligations that insiders and dominant shareholders have toward minority, passive, shareholders in closely held corporations. Since minority shareholders in closely held corporations are particularly susceptible

to exploitation by over-reaching insiders, courts are especially careful to impose high fiduciary duties.

7. The directors and managers of Campus Pipeline violated their duty of loyalty by placing the interests of managers in retaining their job, of insiders including SCT, of preferred shareholders, and of continuing development of the product, above the interest of common shareholders in obtaining value for their shares. Had they not done so, they would have decided that selling the company at that time was not in the best interests of the company and its stockholders. Moreover, once they made the decision to sell the company, they failed to fulfill their *Revlon* duty to maximize the return to shareholders in a sale.
8. The directors and managers of Campus Pipeline violated their duty of care by failing to employ appropriate outside experts, by instructing their expert to limit its inquiry to such a degree as to make the expert opinion meaningless, by failing to explore possible alternative transactions that would have created more value for the common shares, and by deciding to enter into a transaction that offered the common shares no value while giving significant value to insiders.
9. SCT – the dominant shareholder – benefited at the expense of and detriment to the other shareholders, because the sale of Campus Pipeline to SCT allowed SCT to acquire the assets of Campus Pipeline with no payment to Campus Pipeline's common stock.

10. The managers, inside directors and dominant shareholder of Campus Pipeline had serious conflicts of interest, which they allowed to distort their judgment and deflect them from their clear legal duties.
11. The individual insiders received valuable compensation, retention bonuses and other payments in connection with the sale of Campus Pipeline and thus had a financial interest in consummating the sale regardless of whether it was in the interest of Campus Pipeline or its outside stockholders. SCT, the dominant shareholder, received the assets and business of Campus Pipeline without making a payment to the other common shareholders and thus had an interest in minimizing the sales price in conflict with the interest of the outside stockholders. These financial interests created a conflict of interest and precluding their acting as independent brokers of the fate of the common stock.
12. The independent directors of Campus Pipeline failed to insist on independent financial and legal advice, failed to conduct an independent investigation into the merits of the proposed transaction from the perspective of the common stock as a whole, and allowed themselves to be used for the interests of the insiders in breach of their duties of care and loyalty.
13. Thomas Weisel Partners, who were employed by the directors to evaluate the proposed transaction, was financially interested in the transaction as a holder of Campus Pipeline preferred stock, with financial interests at odds with those of the common stock.

14. The financial interests of the common stock barred this transaction, which voluntarily eliminated their interests in a going concern without any payment whatsoever. A Board of Directors acting in the interest of the company and its common stock would not have chosen to voluntarily sell Campus Pipeline for a sum less than the preference value of the preferred stock. At any sale price below the preference value, the common stock would receive nothing, which is the worst possible outcome for the common stock. Thus, any course of action that offered the common shareholders any possibility of future value would have been preferable from the perspective of the common stock.
15. Fundamental principles of corporate law require that the directors act in the interest of all the common stock, and not merely the majority shareholder.
16. In the venture capital context, it is routine for investors to negotiate the right to close down the company at various points if it is not doing well. No such agreement appears to be applicable here. Given the prevalence of such agreements, its absence should be seen as a contractual acceptance of the usual rule that when the interests of the common stock conflict with those of the preferred stock, the law requires the directors to put the interests of the common stock first. This is particularly true where, as here, the directors propose to exclude the common stock from any interest in the company's future, thus destroying the entire economic basis of the common stock.
17. Since the sale of Campus Pipeline to SCT gave no value to the common stock, it cannot have been in the interest of the common stock. Therefore, the

director's approval of this transaction violated their fiduciary duties as a matter of clear law.

18. Plaintiffs in this action have calculated their damages using the "real options" method. This is a standard method of valuing equity interests, which emphasizes the value of the equity-holders right to decide whether to continue or fold the business. I have taught corporate finance to law students for many years. The option theory method of valuing equity appears in each of the standard law school corporate finance texts as a central part of the standard understanding of how and why equity investments have value. (See, e.g., Carney, Corporate Finance, 539-540; Klein & Coffee, Business Organization and Finance, 341-342; Bratton, Corporate Finance, 136, excerpts collectively attached hereto as Exhibit R)

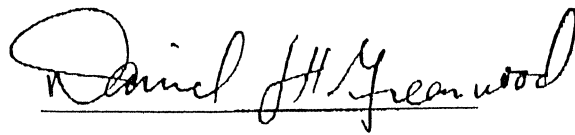
19. Attached is my expert report which is true, accurate, reliable, and provides my opinions and the basis for my opinions in this case. Set forth in detail in my report is my opinion that:

- a. The directors and officers of Campus Pipeline breached their fiduciary duty of loyalty because they had financial conflicts of interest in the transaction, they took no measures to mitigate these conflicts of interest or obtain independent advice, and they placed their own personal interests and the interests of SCT ahead of the interests of Campus Pipeline and its outside stockholders.
- b. The officers and directors of Campus Pipeline breached their fiduciary duty of care because they exercised no care in this transaction in

failing to consider alternative course of action (including operating the company or finding alternative transactions), and in instructing their outside consultant, Thomas Weisel Partners to assume the very result in needed to consider, and they were grossly negligent in terminating the interests of the common stock for a payment of zero.

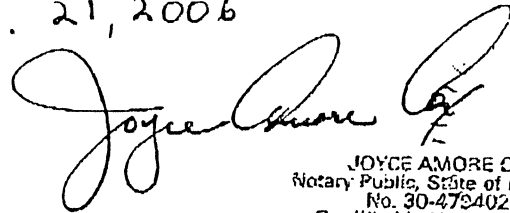
- c. The directors and officers of Campus Pipeline breached their *Revlon* duties, because when the sale of a company becomes inevitable it is their sole duty to maximize the return to the common shareholders, and Defendants approved a transaction that gave the common shareholders nothing.

I declare under penalty of perjury that the foregoing is true and correct. Executed this 21<sup>st</sup> day of November, 2006, at Hempstead, N.Y.



DANIEL JH GREENWOOD

Sworn before me on  
Nov. 21, 2006



JOYCE AMORE COX  
Notary Public, State of New York  
No. 30-4794025  
Qualified in Nassau County  
Certificate Filed in New York County  
Commission Expires March 22, 2010

June 30, 2010