STATE OF NORTH CAROLINA COUNTY OF BUNCOMBE	IN THE GENERAL COURT OF JUSTICE SUPERIOR COURT DIVISION 08 CV 06575
W. GREG GREEN and DR. KENNETH ELLINGTON, individually and derivatively on behalf of MedOasis, Inc., Plaintiffs, v. KEN CONDRA, DANIEL PREVOST, MARC MILLER, and PETER FONTAINE, individually and as current or former directors of MEDOASIS, INC., and TIM LONGBINE and DAVID PHILLIPS in their capacities as current of former directors of MEDOASIS, INC., Defendants, and MEDOASIS, INC., a North Carolina Corporation, Nominal Defendant.	**PLAINTIFFS' MEMORANDUM OF LAW IN OPPOSITION TO DEFENDANTS' MOTION TO DISMISS**

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PLAINTIFFS' MEMORANDUM OF LAW
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TO DISMISS

Plaintiffs seek to remedy Defendants' violations of state law, including breaches of fiduciary duty, aiding and abetting breach of fiduciary duty, abuse of control, constructive fraud, corporate waste, unjust enrichment, and gross mismanagement as the result of Defendants' wrongful issuance of stock to themselves and their cronies and manipulative conduct calculated to secure their own personal interests including squeezing out shareholders who threatened their continued control and positions; termination of lucrative contracts; failure to provide appropriate disclosures to shareholders; and failure to comply with appropriate corporate governance measures.

I. STATEMENT OF FACTS

Defendants' Motion to Dismiss, not a motion for summary judgment, is before the Court. Accordingly, at the risk of stating the obvious, the objective at this stage is to take the facts in the light most favorable to the plaintiff; not to weigh the Defendants' competing view of the facts. Defendants do *not* focus on the Complaint. Rather, the bulk of their brief is devoted to presenting, without citation or support, Defendants' alternate version of facts. *See, e.g.,* Defs.' Memo., pp. 2-5.[1] Plaintiffs respectfully encourage the Court to resist Defendants' invitation to consider matters outside the Complaint and instead, to take the allegations in the light most favorable to the Plaintiffs and determine, as a matter of law, whether *the Plaintiffs' version of the*

[1] Plaintiffs filed a *Verified* Complaint in this matter, whereas Defendants' Motion to Dismiss is not supported by affidavit on any other sworn statement. It goes without saying that Defendants' *unverified* allegations do not constitute evidence. Defendants chose to move for dismissal under Rule 12(b)(6), and Plaintiffs object to the introduction of any evidence at this stage not explicitly set forth in their Verified Complaint.

facts (not the Defendants' alternate version) states a claim upon which relief could be granted. In the interest of turning this matter, at this stage, back to the four corners of the Complaint, Plaintiffs set forth -- for the Court's convenience -- a narrative version of their allegations.[2]

In 2000, Asheville Anesthesia Associates ("AAA") asked Plaintiff Green to become AAA's CEO. Then in 2001, in cooperation with the AAA physicians including Ellington, Green created MedOasis (formerly known as "Medical Specialty Services, Inc.") to manage AAA as well as other anesthesiology practices. Compl. ¶ 13. The business model included shareholder participation by partners in the anesthesia groups serviced by MedOasis. Compl. ¶ 17. Since MedOasis was Greg Green's brainchild and he was to serve as the CEO, Green also was to be a shareholder. Compl. ¶¶ 12 & 16.

The Articles of Incorporation for the Company (the "Articles") stated that the Company had the authority to issue 1 million shares of common stock. The Articles did not contain a provision to address redemption of shares.[3] Green and Ellington were on the initial Board, composed of seven individuals, until November of 2005 when they were removed as directors. Green was also relieved of his CEO position. Compl. ¶¶ 14, 20.[4]

In February 2006, the Board offered to purchase all of Green's 200,000 shares for $0.898 per share. Shortly before this offer, however, Defendant Miller[5] had valued the shares at $0.99

[2] The Complaint, of course, contains significantly more detail than Plaintiffs include here.

[3] Any provision for redemption of shares had to be contained in the Articles of Incorporation to be in compliance with North Carolina law. Compl. ¶32.

[4] Defendants' Memorandum of Law seeks to explain to why Green was removed from the Board. *See* Defs.' Memo., p. 3. Needless to say, Plaintiffs deny Defendants' allegations as to why Green was removed, but the reasons are irrelevant to the matters before the Court and inappropriately raised at this Rule 12(b)(6) stage.

[5] Miller was CEO after Green.

per share. Green turned down the offer. Compl. ¶ 22.[6] The Company's minutes reflect the Board's angst over the voting power of Green and the AAA shareholders and their desire to eliminate the perceived voting block.[7] *See* Compl. ¶ 25.

Contrary to North Carolina law, MedOasis has not provided basic financial information to its shareholders. Likewise, in violation of its own Bylaws and N.C. STAT. § 55-7-01, MedOasis failed to call *any* shareholders' meetings between October 20, 2006 and August 18, 2008. Compl. ¶ 24. Because there have been no annual shareholder meetings, there have been no elections for directors as provided for in the Bylaws. The Bylaws provided that all Directors (other than the Chairman, who is selected by the other Directors) "shall be elected at the annual meeting of shareholders." Compl. Ex. C -- Bylaws, Art. V, § 3. In case of vacancies, the Board was authorized to appoint new Directors, but such newly-appointed Directors' respective terms "shall expire at the next shareholders' meeting at which directors are elected." *Id.* at § 5. As a result, only one current MedOasis Board member (Daniel Prevost) was elected at an annual meeting of the shareholders. Compl. ¶ 24.

On or about March 31, 2008, MedOasis made Ken Condra CEO and he was awarded 60,000 shares.[8] Compl. ¶ 29.

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[6] Although the Company's minutes are replete with references to redeeming or purchasing Green's shares, it is undisputed that his shares were not subject to redemption unless he voluntarily agreed to sell them back to the Company.

[7] Defendants argue that the reference to the minutes in paragraph 25 of the Complaint automatically makes such minutes part of the record which can be considered on a Rule 12(b)(6) motion. Defendants then proceed to selectively attach minutes as exhibits to their Motion to Dismiss. However, as the Court is considering a Rule 12(b)(6) motion, to the degree that there is any ambiguity as to what particular minutes mean, improperly introduced by Defendants or implicitly relied upon in the Complaint, this is a matter for discovery which cannot be resolved at the motion to dismiss stage.

[8] Condra replaced Marc Miller as CEO.

On May 31, 2008, MedOasis terminated the Management Services Agreement of its longest-standing, highest revenue, and most important client, AAA. Compl. ¶30. On June 23, 2008, relying on a provision in the Bylaws that it claimed required redemption of Ellington's shares, MedOasis sent Ellington (and apparently others) a letter in an attempt to "redeem" their shares. Compl. ¶¶ 28, 31-32 and Ex. "C". MedOasis unilaterally and arbitrarily set the share price at $0.17 per share. This amount was in stark contrast to the valuation of $0.898 per share which had been provided by MedOasis to Green in 2006. The letter stated that Ellington would receive a check in the amount of $4,420.00, but only if he complied with certain conditions including signing an agreement to indemnify the Company and to release MedOasis and its officers and directors from all claims. In short there was no unconditional offer to pay a sum sufficient to redeem the shares and no evidence that any sum had been deposited with any financial institution under an irrevocable obligation to pay Ellington the unilaterally-determined $0.17 per share redemption price on surrender of the shares, as required by N.C. STAT. § 55-7-21. Ellington never agreed to a price or to redemption. Compl. ¶¶ 34- 35.

On August 4, 2008, Green sent MedOasis a demand in accordance with the Bylaws for a special meeting of the shareholders, the purposes of which were stated as follows: (a) deletion from the amended Bylaws of the last two sentences of Article V, Section 2, first paragraph; (b) removal of one or more members of the Board; and (c) election of a new Board. Compl. ¶ 37.

Upon receipt of Green's demand, the Board hastily called an emergency meeting the very next day on August 5, 2008, to address Green's demand for a special shareholder meeting. At the time, the Board consisted of: Ken Condra (also CEO), Daniel Prevost (also SVP), Ron Evans, Peter Fontaine, and David Phillips. Present at the meeting were Condra, Prevost, Phillips, Evans, Fontaine, and Tim Longbine.[9] Compl. ¶ 39. *All* of these members, with the exception of Daniel Prevost, had joined the Board *after* the prior shareholder vote held on October 20, 2006. Compl. ¶ 24. Thus, except for Prevost, *none* of the Board members at the August 5th meeting had ever received shareholder approval.

In the August 5th meeting, the directors discussed Green and Ellington's voting power. Some twenty shareholders had granted Ellington irrevocable proxies coupled with an interest totalling 481,000 shares. Compl. ¶ 38. Thus, Ellington controlled 507,000 total shares of MedOasis and together with Green, 707,000 shares. As of that date, the Board only controlled 440,109 shares of the 1,147,109 shares issued and outstanding. Therefore, combined, Green's shares, Ellington's shares, and the shares for which Ellington held proxies would have represented a clear majority of the issued and outstanding shares. Compl. ¶ 40. The Board then erroneously decided that (i) it would not recognize Ellington's voting rights; (ii) it would not recognize voting rights of shares held by AAA members; and (iii) it would not give notice to Ellington or any of the 20 shareholders for whom Ellington held proxies. Compl. ¶ 42.

The Board did not stop there, but instead voted to issue 140,000 shares to Condra in addition to what had been *awarded* to him in March of that year and to issue 140,000 shares to Prevost. Based on these 280,000 shares, even with Ellington's 507,000 votes, the existing Board ensured would control 720,109 shares as compared to the 707,000 controlled by Ellington and Green. Compl. ¶ 42.

The Board allowed Condra and Prevost to execute promissory notes as the sole consideration for the newly issued shares. The minutes reflect that this action "was unanimously

[9] Despite the fact that it was a specially called meeting for a specific purpose, the Board considered and took other action such as accepting Ron Evans' resignation and appointing Tim Longbine as his replacement on the Board. Nevertheless, apparently both men took part in the discussion, and both were apparently allowed to vote.

approved" and do not reflect that Condra and Prevost abstained. In addition, the Board agreed that "if the purchase of shares is determined by the Company *to be invalid, then the shares and note are voidable by either Party.*" Compl. ¶ 43 (emphasis in Complaint).

The stock issued to Condra and Prevost was part of the additional 500,000 shares that the Company's shareholders had authorized to be issued by the corporation in October of 2006. However, the stated plan by the Board for issuance of stock was that only 200,000 shares would be issued to management -- 100,000 for awards and 100,000 for purchase by management.[10] The Board had awarded 60,000 shares to Condra in March of 2008. By issuing an additional 280,000 shares at the August 5th meeting, the Board thereby exceeded the allotment for shares available for purchase by management by more than 180,000 shares.

At the special shareholders' meeting on August 18, 2008, Ellington tendered the original proxies to the Board, but the Board refused to allow Ellington to vote his shares or any of the proxies he held. Compl. ¶ 49. Over the objections of Green and Ellington, the Board allowed Condra and Prevost to vote the 280,000 shares that they had issued to themselves at the August 5th meeting and Condra to vote his 60,000 shares that he admitted were not fully vested at that time. Compl. ¶ 50. The Board contended that the first two motions -- to delete the last two sentences from the Bylaws and to remove the Board -- failed. The Board refused to allow a vote on Green's motion to elect a new Board. Compl. ¶ 51.

[10] The planned allocation of the stock set forth to shareholders is reflected in the minutes. Again, to the degree that there is any ambiguity as to what particular minutes mean, this is a matter for discovery. Plaintiffs raise it to meet the outside matters raised by Defendants with regard to their assertion that the determination was protected by the Business Judgment Rule. Minutes for the Shareholders' Meeting of October 9, 2006 and the Board of Directors Meeting of that same date are attached hereto as Exhibits 1 and 2, respectively.

II. ARGUMENT

Defendants' chief tactic is to argue disputed assertions of their choosing, generally without support in the Complaint. While Defendants may disagree with the Complaint's allegations, the Motion is a *motion to dismiss*, not a motion for summary judgment, thus, the Court is to take the facts in the light most favorable to the plaintiff, not weigh Defendants' competing version of facts. And, even if the Court does elect to look beyond the Complaint to minutes or other documents upon which Plaintiffs' allegations arguably rely, it should only consider those few of Defendants' contentions that are *supported* by *citations to documents* which have been made part of the record, and which the Court could properly consider on a motion to dismiss.

Defendants attempt to recast Plaintiffs' allegations to revolve entirely upon the August 18, 2008 shareholders' meeting. This attempt to diminish Plaintiffs' claims is not unlike Defendants' actions in diluting the Plaintiffs' interests in the Company and their actions in thwarting Plaintiffs' rights to vote their shares to oust a board and management that had completely hijacked the company, running it secretively and without disclosures or input from the shareholders who were not serving on the board. Green's call for the special shareholders' meeting was in response to the gross mismanagement of the Company and the Board's brazen exclusion of shareholders from the corporate governance process. Thus, the August 18th meeting (and the events leading up to it) were merely the straw that broke the camel's back -- the culmination of the effects of ever-diminishing shareholder value and of the Board's two-plus-year departure from legitimate corporate governance. Thus, notwithstanding the fact that the actions of the Board in attempting to control the outcome of the shareholders' meeting is rank with self-dealing and improper purpose, it is without merit for Defendants to claim that the entirety of the Complaint is focused on this one shareholder meeting.

Defendants miss the point of this lawsuit. They attempt to hide behind the business judgment rule and suggest that there's some kind of wrongdoing by the Plaintiffs in their quest to replace the incumbent board of MedOasis -- a Board which, contrary to the Bylaws, had never been elected by shareholders and with whose actions Plaintiffs and other shareholders disagree. The very essence of this Complaint lies in the rights afforded shareholders under our corporate system: the right of shareholders to vote and the right of shareholders to control their stock ownership rights.

A. Injury To MedOasis

Plaintiffs' claims concern Defendants' plans to usurp control of the Company from its shareholders for the benefit of Defendants and not for the benefit of the Company or its shareholders. Remarkably, Defendants, in moving to dismiss the Complaint, argue: "Plaintiffs do not allege any facts, which . . . would show that... Defendants' alleged conduct caused injury to MedOasis." Defs.' Memo., p. 7.

It is axiomatic that a corporation is run for the benefit of its shareholders, not its board, and thus, if Defendants did what is alleged of them in the Complaint (which must be assumed for purposes of a Rule 12(b)(6) motion), then the Company as a whole necessarily will have been injured. S*ee generally*, *First Union Corp. v. SunTrust Banks, Inc.*, No. 01-CVS-10075, et al., 2001 NCBC 9, 2001 WL 1885686, at ¶¶ 4-13 (N.C. Super. Aug. 10, 2001).

To give just one example, the clear financial injury to the Company caused by Defendants' actions can be shown through Defendants' own valuation of the Company's shares. In 2006, the Defendants valued the Company at either \$0.99 or \$0.898 a share. Compl. ¶ 22. Two years later, after Defendants had terminated the contract of the highest-revenue client, the Defendants claimed the value was \$0.17 a share. Compl. ¶¶ 30 and 33. Even using Defendants' own figures, it appears that Defendants caused at least an 180% decline in share value in their efforts to protect their control of the Company. And this does not include the decline in share value caused by the issuance of the additional 280,000 *undervalued* shares.

Plaintiffs have alleged that Defendants failed to keep Plaintiffs (and other shareholders) informed of the financial condition of the Company. The specific relief sought in the Complaint includes *an accounting*. Defendants never once explain why the shareholders are not and should not be entitled to the accounting sought in the Complaint. A board cannot keep its shareholders in the dark about the financial condition of a corporation and then defeat a shareholder derivative suit (seeking among other remedies, an accounting) by faulting plaintiffs -- at the Rule 12(b)(6) stage and before any discovery -- for lack of proof as to the extent of the injury to the Company's financial condition.

Defendants also seek to insert a false dichotomy between wrongs affecting Plaintiffs' "personal rights" and wrongs affecting the rights of the Company generally. When Plaintiffs' rights as shareholders are harmed in the same manner as all of the other shareholders are harmed by Defendants' improper actions, that is a classic derivative action. However, there are situations in which plaintiffs are able to pursue direct claims. As noted in the case law cited by Defendants: "[T]he same wrongful conduct can give rise to both derivative and direct [individual] claims, for which courts have sometimes allowed shareholders to maintain derivative and direct actions simultaneously." *Norman v. Nash Johnson & Sons' Farms*, 140 N.C.App. 390, 395, 537 S.E.2d 248, 253 (2000) (quoting ROBINSON ON NORTH CAROLINA CORPORATIONS, § 17-2(a)). In *Norman*, the North Carolina Court of Appeals held that the plaintiffs in that case could pursue individual claims and that the trial court had erred in granting a dismissal of the derivative claims. *See id.* at 412. And earlier, in adopting exceptions to the general rule that a shareholder cannot sue for injuries to the corporation, the North Carolina Supreme Court specifically stated:

"We adopt these exceptions to the general rule and hold that a shareholder may maintain an individual action against a third party for an injury that directly affects the shareholder, *even if the corporation also has a cause of action arising from the same wrong. . ..*" *Barger v. McCoy Hillard & Parks*, 346 N.C. 650, 658-59, 488 S.E.2d 215, 219-20 (1997). Additionally, the court in *Gilbert v. Bagley*, 492 F. Supp. 714, 734 (M.D.N.C. 1980), found that alleged market manipulation could be "a breach of the duty owed to both the corporation and the stockholders."[11] There the court stated: "The same conduct may . . . create both derivative and individual claims." *Id.* Likewise, one of the Delaware cases cited by Defendants affirms that claims can have a "dual character," giving rise to both derivative and direct (individual) claims. *Gentile v. Rossette*, 906 A.2d 91, 99-100 (Del. 2006).[12]

B. The Business Judgment Rule

Under North Carolina law, a director is required to discharge his duties:

> (1) In good faith;
>
> (2) With the care that an ordinarily prudent person in a like position would exercise under similar circumstances; and
>
> (3) In a manner he reasonably believes to be in the best interest of the corporation.

N.C. STAT. § 55-8-30(a). A corporation's officers have the same obligations. *See id.* at § 55-8-42.

[11] The court's consideration involved an issue of whether it was appropriate for the plaintiffs to bring their claims directly without demand on the board.

[12] As in *Gentile*, Plaintiffs allege that Defendants issued "excessive" shares of stock in exchange for something of lesser value -- namely for a "voidable" promissory note by which the Defendants agreed (assuming a "voidable" note reflects any binding agreement) to pay a per-share price well below market value. Compl. ¶¶ 42-43.

Generally "directors owe three basic duties to the corporations they serve: obedience, diligence and loyalty." WILLIAM E. KNEPPER & DAN A. BAILEY, 2 LIABILITY OF CORPORATE OFFICERS & DIRECTORS, §1.05 (7th ed. 2005). The duty of obedience requires that directors operate within the powers conferred upon them by their charters, by-laws, and applicable laws and regulations. *Id.* Diligence is the standard of care required of a director to discharge his duties in good faith as an ordinarily prudent person would do under similar circumstances and in a manner reasonably believed to be in the best interests of the corporation. *Id.* The duty of loyalty "contemplates that a director must refrain from engaging in his personal activities in such a manner as to injure or take advantage of his corporation." *Id.* "The duty of loyalty, in essence, 'mandates that the best interest of the corporation and its shareholders take[ ] precedence over any interest possessed by a director, officer or controlling shareholder and not shared by the stockholders generally.'" *See In re The Walt Disney Co. Derivative Litig.*, 907 A.2d 693, 751 (Del. Ch. 2005).

North Carolina recognizes the "business judgment rule." *See* ROBINSON ON NORTH CAROLINA CORPORATION LAW, § 14.06. The business judgment rule is foremost an evidentiary rule that creates "an initial evidentiary presumption" that when a board makes a decision, it is made with due care or an informed basis and "in good faith in the honest belief that the action was in the best interest of the corporation." *Id.* The initial presumption can be rebutted, but if not, it becomes a substantive presumption. *Id.* "In brief summary, the business judgment rule holds that a court will not invalidate or hold directors liable for: (1) an advertent business decision (2) made by disinterested directors (3) within the scope of their authority (4) in good faith (5) with reasonable care and (6) not for their own self-interests." *Id.*

The business judgment rule is not the sweeping panacea Defendants portray it to be. For instance, it does not apply where "directors have made an 'unintelligent or unadvised judgment." *Disney*, 907 A.2d at 748 (citations omitted). It does not apply at all to situations in which the board does not make a decision or where there is sustained inattention and neglect that rises to the level of gross negligence. E. Norman Veasey, *What Happened In Delaware Corporate Law and Governance From 1992-2004? A Retrospective on Some Key Elements*, 153 U. PA. L. REV. 1399, 1437 (2005). The business judgment rule is overcome by a showing of gross abuse of discretion. *See Warshaw v. Calhoun.*, 221 A.2d 487, 492-93 (Del. Ch. 1966) (cited with approval in *In re J.P. Stevens & Co. Shareholders Litig.*, 542 A.2d 770, 781 (Del. Ch. 1988)); *In re Tyson Foods, Inc. Consol. Shareholder Litig.*, 919 A.2d 563, 595 (Del. Ch. 2007) (stating that the business judgment presumption is rebutted if the decision of the directors was "absolutely careless"). It can also be overcome where directors acted with a primary objective to accomplish an impermissible purpose. KNEPPER, *supra.*, at §1.06.

The business judgment rule is not implicated by Plaintiffs' claims in part, because Plaintiffs have alleged: "The conduct of the Defendants complained of herein involves a knowing and culpable violation of their obligations as directors and/or officers of MedOasis, the absence of good faith on their part, and a reckless disregard for their duties to the Company and its shareholders." Compl. ¶ 16. Also, Plaintiffs have alleged that Defendants' actions were self-interested and served no legitimate business purpose.

A board's efforts to protect itself from being removed by shareholders is *not* the type of action covered by the business judgment rule. Indeed, "the ordinary considerations to which the business judgment rule originally corresponded are simply not present in the shareholder voting context." *Blasius Indus., Inc. v. Atlas Corp.*, 564 A.2d 651, 659 (1988); *see generally First*

Union, 2001 NCBC at ¶¶ 12, 47, 152 ("The simple application of the business judgment rule without further review does not serve the needs of the system in ownership issue cases."). Citing *Blasius* with approval, Judge Tennille addressed the inherent rights afforded shareholders in his opinion in *First Union.* He explained: "'U.S. corporation law affords to stockholders three principal sources of protection of their interests: the stockholder's right to vote his or her stock, to sell stock, and the fiduciary duty of corporate officers and directors, all of which are principally enforced judicially through shareholder-initiated lawsuits.'" *Id.* at ¶ 12 (citation omitted). These protections guard against "perceived inadequate business performance." *Id.* at ¶ 12, 47. As such, where a board seeks to interfere with a shareholder vote, the rationales behind the business judgment rule are not implicated. *Id.* "If a board acts for the 'sole purpose of thwarting a shareholder vote,' the business judgment rule does not apply, and the board must prove it had a 'compelling justification for such action.'" *Id.* at ¶ 47 (quoting *Blasius*).

Defendants manipulated the August 18, 2008 shareholder vote and interfered with the shareholders' right to vote. Given the restrictions on the sale of stock contained in the Bylaws (Art. V, § 2), Plaintiffs do not have the right to sell. Hence, the *only* protection (short of suing) Plaintiffs had against mismanagement by the Board is the right to vote to replace the Board. Having manipulated a shareholder vote, Defendants now claim that Plaintiffs' claims are barred by the business judgment rule and seek to deprive Plaintiff shareholders of their only remaining right, the right to sue.

A director cannot use the business judgment rule to shield herself from claims of self-dealing in the change-in-control situation. "Where fiduciary duties arising from management control are implicated, judicial scrutiny may extend to the purpose for which an otherwise lawful course was undertaken and the result achieved." *Farndale Co. v. Gibellini*, 176 N.C. App. 60, 68, 628 S.E.2d 15, 20 (2006) (quoting *Farahpour v. DCX, Inc.*, 635 A.2d 894, 901 (Del. 1994)).

Plaintiffs are asking the Court to scrutinize the *purpose* behind Defendants' actions. Plaintiffs have pled that there was "no legitimate business purpose for Defendants' actions" and in many instances, that the actions were contrary to the Articles, the Bylaws and law. Compl. ¶ 25. Plaintiffs allege that Defendants did ***not*** discharge their duties in good faith or in a manner believed to be in the best interest of the corporation; rather, Defendants acted with purpose of *seizing control of the Company* from the shareholders and *entrenching* their position. Voting to issue 280,000 shares to existing directors the day after a shareholder had called for a special shareholder meeting and with the sole aim of diluting the voting power of the existing shareholders suggests that Defendants did *not* exercise the care that an ordinarily prudent person in a like position would exercise, especially where Defendants issued the shares in return for a voidable promissory note and priced the shares at below-market value. *See* Compl. ¶ 43.

Defensive measures adopted by a board to protect itself are subject to "enhanced scrutiny," and where the board's decision appears to have been affected by self-interest, the board's decision is judged by the "entire fairness" standard. *See generally* ROBINSON, *supra.*, § 9.08. Delaware courts have long held that where a board of directors acts with the primary or sole purpose of "entrenching" itself, the board's decision is not entitled to deference under the business judgment rule. *See Schnell v. Chris-Craft Indus., Inc.*, 285 A.2d 437, 439 (Del. 1971); *Aprahamian v. HBO & Co.*, 531 A.2d 1204, 1206-07 (Del. Ch. 1987). Courts look askance at the issuance of stock where one of the purposes of the issuance is for the existing board to maintain control. *See Condec Corp. v. Lukenheimer Co.*, 230 A.2d 769, 776 (Del. Ch. 19670; *Canada S. Oils v. Manabi Exploration Co.*, 96 A.2d 810, 813 (Del. Ch. 1953). As noted in

Judge Tennille's discussion in *First Union*, 2001 WL 1885686, at ¶ 47, where action is taken with the primary purpose of interfering with or impeding the exercise of the shareholder franchise and the shareholders are deprived of a full and fair opportunity to vote, the burden shifts to the directors to establish a "compelling justification" for their action. *See also* ROBINSON, § 9.08; *Aprahamian*, 531 A.2d at 1207 ("When the election machinery appears, at least facially, to have been manipulated, those in charge of the election have the burden of persuasion to justify their actions.").

Defendants cite *no case law* to support their arguments that the business judgment rule can extend to protect Defendants' actions to seize control of the Company and entrench themselves on the Board. Defendants cite only two cases to support their argument that the business judgment rule should apply to the facts alleged in the present Complaint (*see* Defs.' Memo., p. 10), and neither of these cases applied the business judgment rule to bar the plaintiffs' claims in those cases. In *State ex rel. Long v. ILA Corp.*, 132 N.C. App. 587, 602, 513 S.E.2d 812, 822 (1999), the court explained:

> The evidence in the record reveals that defendant's actions were more than mere errors in judgment. Instead, he was a leading participant in a plan to benefit himself and his interests at the expense of ILA. The findings of the trial court, which we have held are based on substantial evidence, support its conclusion that defendant is not protected by the business judgment rule.

In *HAJMM Co. v. House of Raeford Farms, Inc.*, 94 N.C. App. 1, 10, 379 S.E.2d 868, 873 (1989), the court, after citing the 'business judgment" rule, found that plaintiff had presented sufficient evidence to create a jury issue on the question of whether defendants had "unreasonably exercised its discretion."

As was the case in *ILA*, the Plaintiffs' Complaint does not involve actions of a board that are *merely errors in judgment*. Rather the Board's actions were *intentionally designed* to defeat the right of the minority shareholders to vote their shares collectively to replace a board they believed was mismanaging the Company. In arguing that the business judgment rule applies to the present case, Defendants contend that the issuance of 280,000 shares to existing directors on the eve of a shareholder vote was for the "rational business purpose" of providing "key executives" with "an incentive to further grow the company." Defs.' Memo., p. 12. The facts alleged in the Verified Complaint contradict Defendants' arguments.

Additionally, "[l]ike any other interested transaction, directorial self-compensation decisions lie outside of the business judgment rule's presumptive protection, so that, where properly challenged, the receipt of self-determined benefits is subject to an affirmative showing that the compensation arrangements are fair to the corporation." *Telxon Corp. v. Meyerson*, 802 A.2d 257, 265 (Del. 2002). Condra and Prevost are not entitled to business judgment rule protection in connection with their action in regard to self-interested transactions.

Again, the August 5, 2008 board meeting and the August 18, 2008 special shareholders' meeting are just part of the story. Shareholders -- not just Ellington and Green -- were dissatisfied with the leadership, management and direction of the Company. This is evidenced by the fact that twenty shareholders including Frank Moretz, Rodney Pugh and Steven Roos -- all of whom served on the Board that ousted Ellington and Green in the first instance -- gave Ellington their proxies to vote at the shareholders' meeting. Plaintiffs will be able to show that shareholders were unhappy with the complete abrogation by the Board and management of their duties to provide financial information and corporate disclosures, the failure to hold shareholder meetings or elections, the fact that only one board member was elected or ratified by the shareholders, the coercive efforts of the Board and management to reacquire the stock of certain shareholders, the sharp decline in value of the stock and perceived mismanagement of the Company. Those shareholders acted to exercise their right to vote their shares and the Board and management conspired together to squelch that right so that they could remain in their positions of control. Plaintiffs have provided ample detail in the Complaint to adequately state claims and put the Board on notice of the charges against them.

Additionally, the business judgment rule should not apply at all to actions of management. *See* Lyman P.Q. Johnson, *Corporate Officers and the Business Judgment Rule*, 60 BUS. LAW. 439, 458-66 (2005). Thus, Condra and Prevost, officers, should not receive protection of the business judgment rule.[13] Officers, unlike directors, are agents of the corporations that employ them. *Restatement (Third) Agency* § 1.01, cmt. c; *Rafool v. The Goldfarb Corp.* (*In re Fleming Packaging Corp.*), 351 B.R. 626, 635 (Bankr. S.D. Ill. 2006). Officers such as chief executive officers, chief financial officers and others are agents of the corporation. Lyman P.Q. Johnson & David Millon, *Recalling Why Corporate Officers are Fiduciaries*, 46 WM. & MARY L. REV. 1597, 1605-06 (2005). In contrast, "neither the board of directors as a body, nor individual directors, are agents of either the shareholders or of the corporation. . . ." *Id.*; *see also* RESTATEMENT (THIRD) AGENCY, Introduction, at 5. Fiduciary duties of corporate officers, properly understood, arise from their status as agents of the corporation. Johnson & Millon, *supra.*, at 1601-02; RESTATEMENT (THIRD) AGENCY §§ 8.01 (duty of loyalty) & 8.08 (duties of care, competence, diligence). For duty of care, the standard is ordinary care, and gross negligence need not be proven to impose liability. *See also* Johnson & Millon, *supra.*, at 1630, 1637 ("agency law imposes an ordinary negligence standard of care that is tougher [on the officer defendant] than the 'gross negligence' standard applicable to corporate directors.").

[13] Whether the business judgment rule can be applied to officers is an open question in Delaware.

The dichotomy between the standard of care and duties of directors versus officers on this point is further supported by N.C. STAT. §55-2-02(b)(3) which allows a corporation to include an exculpatory provision for directors on personal liability for the duty of care, but not for officers. The rationale that officers are agents of the corporation and therefore held to the standard of care applicable to agents has the salutory effect of delineating responsibilities between officers and the board of directors concerning internal controls over financial reporting and compliance with applicable laws, regulations and rules. Johnson & Millon, *supra.*, at 1637 ("As agents of the corporation, officers bear primary responsibility for stewardship of the corporation's business activities and financial reporting. The board of directors' role then is to monitor senior officers' discharge of those duties."). Generally speaking, the policies underlying the business judgment rule do not support absolving an officer of the agency obligation to exercise due care in the performance of his duties. *See* Johnson, *Corporate Officers, supra.*, at 458-66 (2005); Johnson & Millon, *supra.*, at 1642.

Whether the failure to supply financial information or other corporate disclosures to the shareholders during the period in question was a result of bad faith and improper purpose or simply the failure to implement and maintain effective internal controls over financial accounting and reporting is a question that should be examined. The bright light of discovery should reveal the answer to this question as well as the question of how and why shareholder value declined. Either way the officer defendants should not be shielded from personal liability on these issues and should not be entitled to any business judgment rule presumption.

C. Liability of Condra, Prevost, Fontaine, And Miller In Their Individual Capacities

Defendants attempt to wiggle out of personal liability for their actions by citing N.C. STAT. §55-2-02(b)(3) which permits the adoption of provisions in the articles of incorporation exculpating directors from liability for breach of the duty of care (with certain exceptions). *See* Dennis R. Honsbach, *Smith v. Van Gorkom: Managerial Liability and Exculpation Clauses - A Proposal to Fill the Gap of the Missing Officer Protection*, 45 WASHBURN L.J. 307, 312 (2006)(hereafter "Honsbach"). The MedOasis Articles contain such an exculpation provision. Compl. Ex. A. The statute provides:

> No such provision shall be effective with respect to (i) acts or omissions that the director at the time of such breach ***knew or believed were clearly in conflict with the best interests of the corporation***, . . . (iii) any transaction from which the director ***derived an improper personal benefit*** . . . .

(emphasis added).

Neither the terms of the statute nor the Articles provide for exculpation for officers. ROBINSON ON NORTH CAROLINA CORPORATION LAW, § 18.12; *see, e.g., In re LTV Steel Co.*, 333 B.R. 397, 413 (Bankr. N.D. Ohio 2005); *Pereira v. Cogan*, 294 B.R. 449, 534 (S.D.N.Y. 2003), *vacated and remanded on other grounds sub nom., Pereira v. Farace*, 413 F.3d 330 (2d Cir. 2005). Moreover, the majority interpretation is that an "exculpatory clause does not shield officers who are also directors from breach of fiduciary duty claims arising from their acts taken as officers. . . ." *See Lincoln v. DePetrillo*, 345 B.R. 33, 36-37 (Bankr. D. Mass. 2006).

The practical effect of the exculpation provision is only to allow corporations "to limit or eliminate breach of the *duty of care* as a basis for a claim for money damages." ROBINSON, *supra.*, § 18.12. Thus, an exculpation clause cannot save a director from personal liability arising out of allegations that the director engaged in self-interested transactions or self-dealing or participated in a transaction from which he derived an improper personal benefit or where he conspired with other directors to violate fiduciary duties of care, loyalty, candor and independence, all of which is alleged in the Complaint. Additionally, Plaintiffs seek equitable relief as well as monetary damages. An exculpation clause will not eliminate a claim for injunctive type relief against the directors. ROBINSON, § 18.12.

Plaintiffs have pleaded these claims with great particularity and it is disingenuous of Defendants to feign inability to connect the dots so as to be on notice of the illegality of their actions. For example, two out of the five board members who voted to award 280,000 shares in a transparent attempt to defeat shareholder activism that would have resulted in the loss of their board seats and possibly their positions as officers, had a direct conflict. Plaintiffs also allege that the directors aided and abetted breach of fiduciary duties, a cause recognized under North Carolina law. *See Blow v. Shaughnessy*, 99 N.C. App. 484, 490-91, 364 S.E.2d 44, 447-487 (1998). Sufficient allegations are pled to allow Plaintiffs to go forward with discovery and establish their legal theories of both individual and corporate liability of Defendants.

D. "Abuse Of Control," "Gross Mismanagement," "Corporate Waste," And "Unjust Enrichment"

Defendants argue that North Carolina does not recognize causes of action for abuse of control, gross mismanagement, and corporate waste. *See* Defs'. Memo., p. 13. They do not cite a single case in support of the proposition. Even assuming, *arguendo*, that these separate causes of action are not often pled, they are all varieties of breach of fiduciary duty. The effort Plaintiffs made to state the most specific causes of action possible underscores that Plaintiffs have tried to be as particular as possible in pleading their case.[14]

Moreover North Carolina courts have recognized the viability of these causes of action. *See, e.g., Lowder v. All Star Mills, Inc.*, 82 N.C. App. 470, 477, 346 S.E.2d 695, 699 (1986)

[14] If the Court agrees with Defendants and would prefer for Plaintiffs to restate these claims as a general breach of fiduciary duty claim, Plaintiffs respectfully request leave to do so. However, the more particular causes of action that Plaintiffs offer here do more to support a specific, detailed set of allegations, and Defendants' implicit request for less, rather than more, pleading detail is unusual, counterproductive, and should be rejected.

("Many justifiable and successful actions will benefit a corporation over a long period of time – such as actions to enjoin gross mismanagement – and the benefit to the corporation may be difficult or impossible to quantify."); *Corporation Comm. of N.C. v. Merchants' Bank & Trust Co.*, 193 N.C. 113, 115 (1927) (noting that bank directors can be held liable for gross mismanagement); *Anthony v. Jeffress*, 172 N.C. 378, 380, 90 S.E. 414, 415 (1916) ("While the directors are not liable for losses resulting from mistakes of judgment such as are excused in law, they are liable for losses resulting from gross mismanagement and neglect of the affairs of a corporation."). As another example, the court entered a default judgment against plaintiff, a Nevada corporation, on defendants' counterclaim for gross mismanagement by the board of directors in *Newgen Techs., Inc. v. Corcoran*, No. 3:07-cv-314, 2008 U.S. Dist. LEXIS 43924 (W.D.N.C. June 3, 2008). Indeed, in *Garlock v. Hilliard*, 2000 NCBC 11, ¶ 13 (N.C. Super. Aug. 22, 2000), although the court dismissed plaintiffs' claim for waste of corporate assets for failure to make a proper demand, the court notably did *not* state that North Carolina would not consider such a cause of action. *See also Greene v. Shoemaker*, 1998 NCBC 4 (N.C. Super. Ct. Sep. 24, 1998).

Defendants maintain that David Phillips is not an "officer" of the Company, when in fact Phillips was elected corporate secretary at the rushed August 5, 2008 Board meeting.[15] Likewise, although neither Phillips or Fontaine are paid a salary, they are eligible for compensation, including an award of stock, for their service as directors.

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[15] Additionally, Phillips signed the Amended Bylaws dated July 3, 2007 as "secretary" although he was not appointed secretary until August 5, 2008. *See* Compl., Ex. "C". Interestingly, those Bylaws indicated that they had been read and approved by both the board of directors and the shareholders, although no shareholder meeting had been held in 2007. This is just one more example of the fast and loose way in which the Board was attempting to whitewash its actions in August of 2008 to avoid being ousted from office.

E. <u>Constructive Fraud And Rescission</u>

The elements of a claim for constructive fraud, were succinctly summarized in *Terry v. Terry*, 302 N.C. 77, 85, 273 S.E.2d 674, 679 (1981), as follows: "Put simply, a plaintiff must show (1) the existence of a fiduciary duty, and (2) a breach of that duty." *Governors' Club, Inc. v. Governors' Club Limited Partnership*, 152 N.C. App. 240, 249-50, 567 S.E.2d 781, 788 (2002); *Keener Lumber Co. v. Perry*, 149 N.C. App. 19, 28, 560 S.E.2d 817, 823 (2002). Moreover, "[f]raud exists when there is a breach of a fiduciary duty." *Stone v. Martin*, 85 N.C. App. 410, 418, 355 S.E.2d 255, 259 (1987). Thus, having stated a claim for breach of fiduciary duty, Plaintiffs have also stated a claim for constructive fraud. Also, as alleged in the Complaint Defendants benefited from their breaches of fiduciary duty -- Defendants engaged in self-dealing and thwarted shareholders' rights to vote. Indeed, Defendants Prevost and Condra received a benefit when they voted to issue themselves 280,000 shares at below-market value in return for a *voidable* promissory note. *See Schmidt v. Wachovia Bank*, No. 3:08-cv-185, 2008 WL 5396684, at *2 (W.D.N.C. Dec. 23, 2008). The damage to the Company and Plaintiffs from Defendants' actions is clear. For example, Defendants decided to terminate the management services agreement with the Company's highest-revenue customer in what Plaintiffs allege was an attempt to trigger the Bylaw's redemption provisions allegedly governing the customer's members' shares and thereby attempt to prevent these shares from voting.

Defendants' argument that constructive fraud claims are subject to the heightened pleading requirements of Rule 9(b) is unavailing for two reasons. First, the North Carolina Supreme Court has noted: "The very nature of constructive fraud defies specific and concise allegations . . . ." *Terry*, 302 N.C. at 85, 273 S.E.2d at 679. As such, as noted above, all that's required to plead constructive fraud are allegations of a fiduciary duty and a breach of that duty. *Governors' Club*, 152 N.C. App. at 249-50, 567 S.E.2d at 788; *Keener Lumber*, 149 N.C. App. at

28, 560 S.E.2d at 823. Second, Plaintiffs have pleaded the claims with sufficient particularity to pass even Rule 9 standards.

Defendants challenge the rescission claims on the same basis. However, where a defendant has breached a fiduciary duty owed to a plaintiff, there is also fraud. *Stone*, 85 N.C. App. at 418, 355 S.E.2d at 259. Defendants are conflating the pleading requirements for actual fraud with those constructive fraud. Defendants did not dispute that Plaintiffs have pled that Defendants breached their fiduciary duties. Moreover, cancellation of the shares is the appropriate remedy if shares were improperly issued. *Stone*, 85 N.C. App. at 420, 355 S.E.2d at 261.

As recently stated: "It is clear enough that a director's failure to see to it that the corporation is operated according to law is a breach of fiduciary duty." *Ehrenhaus v. Baker*, No. 08 CV 22632, 2008 NCBC 20, 2008 WL 512899, at ¶ 106 (N.C. Super. Ct. Dec. 5, 2008). Here, under the North Carolina statute, the Company was required to hold a shareholders' meeting every year, *see* N.C. STAT. § 55-7-01, and the Bylaws required that the directors be elected at the annual meeting. (Bylaws, Art. V, § 3). The Board failed to call an annual meeting at any time during 2007, and by the time a shareholders' meeting was called in August of 2008 -- at Green's request -- only one Board member had been on the Board the last time a shareholder meeting was held back in 2006. By failing to call an annual meeting and see to it that they themselves were elected by the shareholders, and the failure to provide financials, the Board failed to ensure that the Company was operated according to law and thus breached their fiduciary duty. The same is equally true, if not more so, of the officer defendants.

F. <u>Fiduciary Duty of Majority Shareholders</u>

As noted in the case law cited by Defendants, "minority shareholders in a closely held corporation who allege wrongful conduct and corruption against the majority shareholders in the corporation may bring an individual action against those shareholders, in addition to maintaining a derivative action on behalf of the corporation." *Norman v. Nash Johnson & Sons' Farms*, 140 N.C.App. 390, 405, 537 S.E.2d 248, 259 (2000). North Carolina allows minority shareholders to bring such claims because "the illiquidity of a minority shareholder's interest in a close corporation render him vulnerable to exploitation by the majority shareholders." *Id.* at 404 (quoting *Meisleman v. Meisleman*, 309 N.C. 279, 291, 307 S.E.2d 551, 559 (1983)).

All the policy reasons for allowing minority shareholders to bring direct, as well as derivative, claims are present here where MedOasis' shareholders are prohibited from selling or otherwise transferring their shares without "prior written approval" from the Board, which enjoys "complete discretion" on whether to grant or deny such approval. Bylaws, Art. X, § 2. The only way for a shareholder who wants to sell to be able to recoup his investment in the Company is for him to sell his shares back to the Company, and here, Defendants' behavior in undervaluing the shares forms part of Plaintiffs' claims. For example, Green was offered $0.898 per share for his shares back in 2006, even though this amount was less than valuation provided by Miller (then CEO) shortly before the offer to Green. Compl. ¶ 22. The Board sought to redeem the shares held by Ellington for a mere $0.17 a share, even though the Board's own CPA consultants had valued the shares as high as $0.40. *Id.* at ¶ 33. The reason for such undervaluation is simple self-interest on the part of Defendant members of the Board -- Board members who availed themselves of the opportunity to buy into the Company at this artificially low price of $0.17 per share themselves, thereby diluting the value of the shares already held by Plaintiffs as well as their voting power. *See* Defs.' Memo., p. 9.

Moreover, under North Carolina law, majority shareholders owe a fiduciary duty to minority shareholders. *See Farndale Co. v. Gibellini*, 176 N.C. App. 60, 67, 628 S.E.2d 15, 19

(2006); *Freese v. Smith*, 110 N.C. App. 28, 37, 428 S.E.2d 841, 847 (1993); *Loy v. Lorm Corp.*, 52 N.C. App. 428, 433, 278 S.E.2d 897, 901 (1981). Indeed, when it is alleged that a majority shareholder's actions were unfair to minority shareholders, the burden shifts to the majority shareholder to show that its actions were "eminently fair to the minority and undertaken in good faith." *Farndale*, 176 N.C. App. at 70, 628 S.E.2d at 21; *Loy*, 52 N.C. App. at 433, 278 S.E.2d at 901; *see also Freese*, 110 N.C. App. at 37, 428 S.E.2d at 847.

G. Accounting and Declaratory Judgment

Defendants do not explain why Plaintiffs' claims for an accounting and declaratory judgment should be dismissed. When an accounting is ordered, the full extent of Defendants' self-dealing will become apparent, as will the clear injury to the Company and its shareholders. Having failed to explain why Plaintiffs' accounting and declaratory judgment claims should be dismissed, Defendants cannot explain why the other nine counts of Plaintiffs' Complaint -- which seek damages based on the same wrongful conduct giving rise to the accounting and declaratory judgment claims -- should be dismissed.

CERTIFICATE OF SERVICE

I hereby certify that on the 27th day of March, 2009, the foregoing PLAINTIFF'S MEMORANDUM OF LAW IN OPPOSITION TO DEFENDANTS' MOTION TO DISMISS was served on the following persons via the North Carolina Business Court's electronic filing system, email, and first class mail addressed to the following counsel of record:

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NC Bar # 26238 / VA #36369
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Counsel for Defendants

/s/ John O'Shea Sullivan

John O'Shea Sullivan
John O'Shea Sullivan
(with permission)

CERTIFICATE OF COMPLIANCE

The undersigned hereby certifies that the foregoing Memorandum in Opposition to Defendants' Motion to Dismiss is compliant with the seven thousand five hundred (7,500) word limit specified in Rule 15.8 of the General Rules of Practice and Procedure for the North Carolina Business Court.

/s/ John O'Shea Sullivan
John O'Shea Sullivan

CONFIDENTIAL

MedOasis
... Medical Specialty Services Management

Frank H. Moretz, MD
Chairman of the Board

Internal Memo

framo49@charter.net

76 Peachtree Road, Suite 300, Asheville, NC 28803, (828)771-5206, fax (828)254-9611

Date: October 18, 2006

To: MedOasis Shareholders

From: Frank Moretz, MD, Chairman of the Board
Marc Miller, MBA, FACMPE, CEO
Mike Crawford, Partner, Dixon Hughes, LLC

Subject: MedOasis Shareholder's Meeting, October 9, 2006.

Dear Shareholders,

The following is a summary of the Shareholder's Meeting held on October 9, 2006 at the Rock Barn Golf and Country Club in Conover (Hickory), NC.

The meeting was called to order at 5:50pm by Dr. Frank Moretz, Chairman of the Board.

Opening comments from the Chairman

Dr. Moretz thanked everyone for coming to the meeting. We had a quorum, so he called the meeting to order. He mentioned that there were 779,000 shares represented either in person or by proxy.

As we reported in the 2005 MedOasis Stockholder's Report, MedOasis had another good year in 2005.

In addition, the Company continues to thrive in 2006 and is healthy and growing.

The next regular annual shareholders meeting will be the first quarter of 2008.

Election of the Board of Directors

A motion was made to re-elect the Board of Directors including Daniel Prevost, the Senior Vice President of MedOasis. The motion was seconded and a vote was taken.

PLAINTIFF'S EXHIBIT
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The vote passed and the following people were elected to the Board of Directors of MedOasis until the next shareholder's meeting 1st qtr 2008.

Brett Cleveland, MD
Ron Evans, MD
Marc J. Miller, CEO
Frank Moretz, Chairman
Daniel Prevost, Sr. V.P.
Rodney Pugh, MD
Steve Roos, MD

2005-2006 Strategic and Financial Highlights - Marc J. Miller, CEO

MedOasis 2005 Financial Performance – Net Income: $157,000
MedOasis 2006 Financial Forecast – Net Income: $200,000
MedOasis 2007 Forecast – We expect to have a successful year.

Profitability will be invested in cash on the balance sheet for working capital, and investing in personnel and resources.

2006 was highest client acquisition year: $10 million in new client revenues.

We will lose Cumberland Anesthesia as a client as of November 2006. MedOasis collected an average of $50,000 per month more than their previous billing company (Medac).

We successfully transitioned through the "MedApproach Situation" this past year. (Owensboro and Crescent Anesthesia)

Healthcare Trends in the United States

US Healthcare Expenditures were over 16% of Gross Domestic Product in 2004
Most other countries average only 7% to 10%.
55% of healthcare dollars are spent on Physician Services and Hospital Care

MedOasis will be concentrating on services to Physicians and Hospitals in 2007.

Mission of MedOasis: To Create Shareholder value by offering high quality business and management consulting services to physician practices and hospitals while providing a rewarding career and a quality work environment to our employees.

Mr. Miller reminded the Shareholders that the first words of the Mission Statement are "To Create Shareholder Value". MedOasis will be pursuing this mission first and foremost.

Marc Miller the MedOasis CEO will be handing down more of the operations of the company to the Executive Team that includes Daniel Prevost, Senior Vice President, Tammy Colwell, Vice President, David Perry ,Corporate Controller, Nancy Robinson, Human Resources, Nancy Lawson, AAA Executive Manager, and Anne Humphrey, GAA Executive Manager.

MedOasis Growth Strategy – Daniel Prevost, Senior Vice President.

Primary Clients will be Physician Groups and Hospitals in 2007.

We will be using direct Marketing to clients.

We will also be pushing opportunities to the MedOasis billing department through Hospital and Physician practice Consulting. We will seek assistance from our MD consulting partners in these consulting assignments.

MedOasis will continue to position itself in the marketplace as a "value-added" provider of services, instead of a "low-cost" provider. Clients will experience a higher net income with MedOasis in spite of a slightly higher fee. The additional collections from MedOasis will more that offset the slightly higher fee.

There are 182 client groups within a 400 mile radius of Asheville. MedOasis has established some form of a relationship with 93 out of the 182 groups.

Consulting for Practices and Hospitals develops credibility and helps us to get to know the leaders of the client organizations. Consulting services include:

- Revenue Cycle Management
- Hospital Stipend Negotiations
- Pay for Performance
- Regionalization into outpatient centers (surgery centers, ASC's, etc.
- OR Utilization (with MD partners)
- CRNA Employment
- Etc.

US Outpatient cases continue to migrate away from the main hospital systems and into the surgery centers. There are over 5,000 surgery centers now nationwide.

MedOasis will be assisting our existing clients and new clients with Regionalization to take advantage of the "Outpatient Cases" migration away from hospitals.

Billing and Collections, Tammy Colwell, Vice President

MedOasis has consistently increased new client revenues by 10%.

The MedOasis billing department is making enhancements to its processes

- Electronic Medical Records
- Check 21 – Scanning personal checks.
- Automated patient account debiting.
- Data Warehousing from PPM Billing software and Financial System

The billing department is also becoming more automated and efficient.

Producing more work with less resources.
Improving the performance metrics system.
Receiving electronic Payments from insurance companies.
Image Management system under development
Demographic Downloads from Hospitals

Client Service and Retention

Developing a proprietary "dashboard" reporting system.
Created an enhanced department organization through "Team Leaders".
Another Executive Client Manager has been hired.

Pay for Performance – Marc J. Miller, CEO

National Committee on Quality Healthcare, 2006 – "Pay for performance is a reimbursement system whereby purchasers are going to begin paying on quality and performance as opposed to volume."

MedOasis is developing a proprietary Pay for Performance Model involving a collaborative effort between Hospitals, Physician Practices, and MedOasis.

The differentiator of the model is the "MedOasis Consolidated Data Warehouse". The collaborative P4P Quality Initiative Program will "feed" the Data Warehouse along with the MedOasis Financial System, and the Billing System. The Consolidated Data Warehouse will then generate reports that will be delivered to the Payor community for maximum practice income.

Summary of MedOasis Services and Advantages of MSO Model

Regionalization of Clients
Pay for Performance
Help Clients Migrate with Emerging Trends
Legislation Involvement
Billing and Collections
Management Services
Hospital and Practice Consulting

Advantage of MedOasis is access to multiple payors, hospitals, states, group governance models, hospital support models, multiple state associations and legislative efforts.

Presentation by Dixon Hughes, LLC – Mike Crawford, Partner

MedOasis approached a nationally recognized consulting firm to help determine the best plan for transitioning MedOasis from a Phase I start-up company (first 5 years) to a Phase II growing service organization. MedOasis chose Dixon Hughes, LLC.

Mike Crawford is a Partner in Dixon Hughes. All his clients are medical groups and healthcare. He is the Managing Partner of the Asheville office and all offices in Western North Carolina.

Dixon Hughes is the 18th largest Healthcare Consulting firm in US. It is a $150 million company with 900 employees.

What is the purpose of the company? - MedOasis Mission statement
The Mission Statement begins with the purpose of "creating shareholder value".

MedOasis Phase I Start up Company vs Phase II Growth Company:

MedOasis now has the infrastructure and personnel in place to grow the value of the company. The Company is now positioned to go out and pick up additional anesthesia groups. ("The right people are on the bus, and the right people are in the right seats on the bus")

MedOasis can be built into a dominant player in the Southeastern US in the coming years.

What are the key issues that need to be dealt with? What changes need to be made?

MedOasis Management Team was underrepresented on the Board of Directors. The Election of Daniel Prevost has helped to balance this out.

MedOasis is not a physician group; it is a Management Services Organization. Get some outside board members who are objective third parties. MedOasis may have to pay the new board members. This would be very valuable.

Medoasis Stockholders – Why are we authorizing and issuing new shares?

- The Management team – Provide an incentives to operate and grow the Company
- Gaston Anesthesia – Solve under-representation
- Asheville Anesthesia and Gaston Anesthesia new MD's.
- A Strategic Partnership – Prepare the organization to respond quickly to strategic partnership opportunities.

According to the North Carolina General Statute 55, Shareholders need to amend the Articles of Incorporation. Everyone attending the meeting was presented with the new proposed Articles of Incorporation amendment to review.

During the Company's start up Phase I, it was in a "survival mode". Now the Company is transitioning into the Phase II "growth mode". We need new shares for incentives, and strategic partnerships.

The issuance of new shares will dilute the value of the shares if those shares are awarded. However, if the Company allows individuals to purchase the shares at fair market value, then there will be no dilution.

The Board will be issuing shares. This will result in the shareholders value per share taking a small step backwards with the long-term intention of making up that value.

500,000 is probably the right amount of new shares to authorize.

A vote took place on ratifying the board's resolution to authorize the additional 500,000 shares and amending the articles of incorporation to reflect the additional 500,000 shares of stock. A motion was made and seconded. Discussion took place to include votes from Greg Green and Ken Ellington. The vote was taken and passed by super-majority.

A vote took place to change the address of the corporation to 76 Peachtree Road, Asheville, NC 28803. A motion was made and seconded. The vote took place and passed by super-majority.

A vote took place to change the registered agent of the corporation to Marc J. Miller. A motion was made and seconded. The vote took place and passed by super-majority.

Discussion took place on good communication from the Board of Directors before each Shareholder's meeting.

The meeting was adjourned at 7:00pm..

MEDOASIS
. . . Medical Specialty Services Management

Marc J. Miller, MBA, FACMPE
President and CEO
828-242-5949
marcmiller@medoasis.com

Internal Memo

76 Peachtree Road, Suite 300, Asheville, NC 28803, (828)771-5206, fax (828)254-9611

Date: October 20, 2006

To: MedOasis Board of Directors

From: Frank Moretz, MD, Chairman of the Board
Marc Miller, MBA, FACMPE, CEO
Mike Crawford, Partner, Dixon Hughes, LLC

Subject: MedOasis Board of Directors Meeting, October 9, 2006.

Dear Board of Directors,

The following are the minutes of the Board of Directors Meeting held on October 9, 2006 at the Rock Barn Golf and Country Club in Conover (Hickory), NC.

The meeting was called to order at 7:10pm by Dr. Frank Moretz, Chairman of the Board.

Opening comments from the Chairman

Dr. Moretz welcomed Daniel Prevost to his first Board of Director's meeting.

Approval of the Minutes of the Board of Directors Meeting, June 29th, 2006

The Board discussed the resolution of the Board on June 29th to authorize the additional 500,000 shares of new stock, and tonight's Shareholder's vote by super-majority to ratify the Board's decision to authorize the additional 500,000 shares of stock, and to amend the articles of incorporation.

Dr. Pugh asked for clarification on how the shares are to be issued.

The group discussed the minutes and clarified the following:

26,000 to be purchased by Asheville Anesthesia for new MD's
26,000 to be purchased by Gaston Anesthesia for new MD's

PLAINTIFF'S EXHIBIT 2

47,663 to be awarded to Gaston Anesthesia for under-representation (.01 cents/share)
100,000 to be awarded to Mgmt. Team (.01 cents per share)
100,000 to be purchased by the Management Team
200,337 to be purchased by a Strategic Partner or other future use

Dr. Cleveland mentioned that he would like Anne Humphrey to be awarded some shares (.01 cents per share) of stock for her service and not have to purchase. Dr. Cleveland understood that some of the 200,000 shares would be awarded to the other members of the Management Team (other than Prevost and Colwell).

The Board decided to vote on approving the minutes, and then continue to address the question of the 200,000 shares for the Management Team.

The Board approved the minutes of the Board of Directors Meeting, June 29th, 2006.

After some discussion a motion was made to have Marc Miller issue the 200,000 shares to the Management Team at his discretion. The motion was seconded.

More discussion of the motion:

Dr. Roos asked if Mr. Miller should inform the Board of how he decided to issue the shares as it happens, or perhaps at a subsequent board meeting.

Dr. Pugh said if they are awarded he would like to see the same vesting program used (explained in the minutes of the June 29 meeting.).

The Board voted and the motion passed to give Mr. Miller the authority to issue the 200,000 shares for the Management Team at his discretion.

Mr. Miller said he will keep the Board informed of his decisions on this matter.

<u>CEO Compensation Program</u>

Dr. Moretz said he invited Mike Crawford (Dixon Hughes Business Consultant) to the Board meeting to discuss the CEO's compensation. The Board feels ill-equipped to determine the CEO's compensation.

Mr. Crawford said there are surveys that are available to help determine appropriate compensation for a CEO. It would certainly be difficult to make a change downward at this time. Look at the surveys and accumulate data on CEO's comparable to Mr. Miller's situation.

MedOasis now is a larger company, and the personnel are now equipped to run a company larger than what we have today. So it is difficult to justify calculating what Mr. Miller's appropriate salary should be based on the past. You have to look at the present and the future.

The Board asked what criteria is used to determine a CEO's compensation; Is it based on number of employees, income, or margin, years on the job, or years in the position? Can you afford the salary of the CEO when MedOasis plans on making $200,000 profit?

Mr. Crawford - You cannot afford to try and save money by not having "the right guy driving the bus" because of where you are headed. You cannot look at where you were, you must look at where you want to be. You have to build the infrastructure for where you want to be. So the parameters are "what are the comparable salaries paid to company CEO's, what are you asking the person to do, number of clients, revenues, etc. . Do what it takes to have the right person and keep him from "leaving the ship".

Dr. Moretz - You not only want to pay someone, but you want to incentivize him for continued success. What we have done in the past has been flawed and the Board is looking for some parameters to make decisions on.

Crawford – Figure out what a comparable base salary is and then have an incentive plan based on some measures of success, such as increasing revenue, corporate profitability, etc, and that should tie into Marc's incentive payment.

Dr. Pugh - We have some measurements in place for 2006. (The measurements stated in the minutes of the February 2 and June 29 Board meetings are: 1) Corporate health/profitability, 2) Founding Client Satisfaction, 3) Discretion of the Board)

A variety of methods and measurements were discussed, and the conclusion was the measurements should be based on what is important for MedOasis in the next 12 months. "There is no magic formula". In a growing business like MedOasis, clients will come and go, you may make a good business decision to let a client go.

Next Steps: Mike Crawford, the Board, and the CEO should all decide together on what the measurements of success should be.

Dr. Roos – "What if the best person for the job costs more? Does the company ask the CEO to take less in the short term, and reward him in the long-term? What is most important; infrastructure, growth, or financial stability? Can the Company afford a CEO at Marc's level considering all the things the Company needs to pay for to take the Company into the new growth phase ?

Mr. Crawford – It would be remiss to decrease the salary of the CEO. You would be saying he has your confidence, but you want to lower his salary. It's the "no good deed goes unpunished" scenario. For example a Company may lower its benefits, but then wonders why they have an exit of good employees. Dr. Cleveland -The Board is not talking about decreasing the salary of the CEO.

Mr. Crawford – Every year you need to retain a portion of the Company's earnings to grow the Company, and if Marc is providing good leadership, then some of the profits should go to him as a"kudos" and a reward. Some profits should stay to reinvest in the

Company. The Board will have to decide what the incentive will look like each year when you've had the benefit to look back at the past year.

Dr. Roos – Can MedOasis afford to share profits with the CEO, and can the company afford the CEO if the CEO is compensated the way he really should be compensated?

Mr. Crawford – Yes. And also the Company can afford the CEO.

Mr. Crawford – People in leadership positions should be adequately compensated for what they are doing. It's a tough job at the top. You first have to decide what the measurements are for the incentive. Some measurements can be objective (numbers oriented). Some measurements can be subjective (surveys and evaluation).

Marc Miller - The first thing is to establish the guaranteed salary and then an incentive. (Which is the program the CEO is on today.) There are hundreds of sources and variables to consider at the 50th and 75th percentile to pay the base salary of a CEO of a Company similar to MedOasis, so that is the easy part. The incentive portion is the more challenging part. For instance, MedOasis is 171% of budgeted profitability for the year, but an incentive of only 98% has been paid.

Dr. Pugh mentioned there are other factors that determine the CEO incentive other than profitability, such as employee retention.

Mr. Miller agreed, but reminded the Board that the quarterly incentive portion is based only on company profitability and client satisfaction.

Dr. Cleveland – The incentive program was designed for balance throughout the year, and then catching up at the end of the year. If we have a good year then Marc should be paid a good bonus at the end of the year.

The group re-established that $72,000 - $80,000 is the annual incentive payment for "meeting expectations". We can go over that or under that depending on how the Company does.

Next Steps: The 2006 Compensation Committee will work with Mike Crawford to develop a draft of the CEO salary and incentive program for 2007 considering industry benchmarks. They will then publish the draft via an e-mail to the full board and the CEO for review and discussion.

The Compensation Committee for 2007 will be determined at the next Board Meeting.

<u>2006 Budgeted Client Gain Update</u>

- New Client, Georgia +$ 4.5 mil
- New Client, South Carolina +$ 5.5 mil
- Loss of Cumberland Anesthesia ($5.5 mil)

Other Business

Greg Green's Ownership of 200,000 Shares of MedOasis stock.

The Board discussed their desire to re-purchase Mr. Green's shares. Mr. Green stated he expects to be paid "market value" for his shares, and he insists on considering the financial performance of the Company in 2006 in figuring "market value". The Company's performance is extraordinarily good this year and therefore Mr. Green will likely be asking for an offer more attractive than what he already rejected earlier in the year.

The Board discussed the possibility of MedOasis as a Company re-purchasing Mr. Green's shares. Mr. Miller reminded the Board of its fiduciary responsibility and considering some of the discussions earlier he suggested it would not be financially prudent for the Board to re-purchase Mr. Green's shares. Mr. Miller suggested that the Board seek out existing shareholders who may be interested in purchasing Mr. Green's shares.

The Board discussed the possibility of finding an equitable way to offer the shares to existing shareholders. Should the shares replace the shares offered for purchase as part of the 500,000 authorized shares?

A resolution was not reached. The Board will continue to discuss this issue informally between now and the next Board of Directors meeting.

A motion was made to adjourn the meeting. The motion was seconded. A vote was taken and passed. The meeting was adjourned at 7:00pm..