

IN THE UNITED STATES DISTRICT COURT
DISTRICT OF MINNESOTA

VERITEC, INC. and VERITEC
FINANCIAL SYSTEMS, INC.,

Plaintiffs,

V.

AURORA FINANCIAL SYSTEMS, INC.,
SMART SMS CORP., SCOTT A. STAGG,
AMIR KHAN and MICHAEL R.
CIBEREY,

Defendants.

Case No. 11-cv-00376 (SRN/SER)

SECOND AMENDED COMPLAINT

Plaintiffs Veritec, Inc. and Veritec Financial Systems, Inc., for their Second Amended Complaint against Defendants Aurora Financial Systems, Inc., Smart SMS Corp., Scott A. Stagg, Amir Khan and Michael R. Ciberey, state as follows:

BACKGROUND

This suit concerns Defendants' improper and unlawful assertions of U.S. Patent No. 7,229,006 B2 ("the '006 Patent") against certain software owned by Plaintiffs which, among other things, assists in account management of debit cards ("the Banking Software"). Plaintiffs lawfully acquired such software from the software's owner and inventor before the purported assignment of any patent rights to Defendants. Defendants were aware of such lawful acquisition, yet nonetheless have made extra-judicial claims about Plaintiffs' purported patent infringement relating to Plaintiffs' use and licensing of

the Banking Software to various financial institutions with which Plaintiff has or has sought business relationships. In this suit, Plaintiffs assert claims for: (1) a declaratory judgment of non-infringement of the '006 Patent due to legal estoppel and implied license; (2) tortious interference with prospective economic advantage; (3) false advertising under Section 43(a) of the Lanham Act; and (4) violating Minnesota's Deceptive Trade Practices Act, Minn. Stat. § 325D.44.

PARTIES, JURISDICTION AND VENUE

1. Veritec, Inc. ("VT") is a Nevada corporation doing business at 2445 Winnetka Avenue N., Golden Valley, Minnesota, 55427. Veritec Financial Systems, Inc. ("VTFS") is a subsidiary of Veritec; it is a Delaware corporation also doing business at 2445 Winnetka Avenue N., Golden Valley, Minnesota, 55427. Where appropriate, both companies are collectively referenced as "Veritec".

2. Smart SMS Corp. ("Smart") is or was a public company incorporated in Florida, with a principal place of business at 29 Wilcrest, Suite 220, Houston, Texas, 77042. On information and belief, Smart previously had a principal place of business at 3 Greenwich Office Park, Greenwich, Connecticut, 06831.

3. Aurora Financial Systems, Inc. ("Aurora Financial") is a Delaware corporation with a principal place of business at 3 Greenwich Office Park, Greenwich, Connecticut, 06831. Aurora Financial also has an office at 500 West Madison Street, Suite 1730, Chicago, Illinois, 60661.

4. Scott A. Stagg ("Stagg") is an individual residing in White Plains, New York.

5. Amir Khan (“Khan”) is an individual residing in Wilton, Connecticut.

6. Michael R. Ciberey (“Ciberey”) is an individual residing in White Plains, New York.

7. Smart was principally run by three people: Stagg, Khan and Ciberey. Stagg is the former Chairman of the Board of Smart, is a lender to Smart and a substantial shareholder of the common shares of Smart. Khan is a former President and Director of Smart, a lender to Smart and a substantial shareholder of the common shares of Smart. Ciberey is a former President of Smart.

8. On or about November 3, 2009, Stagg, Khan and Ciberey formed Defendant Aurora Financial with its principal place of business at Stagg’s office, the same location which had previously served as the headquarters of Smart. Ciberey was installed as Aurora Financial’s President, and Khan was named its Chief Marketing and Strategic Officer. On information and belief, Stagg and Khan are the principal shareholders of Aurora Financial.

9. Both Smart and Aurora Financial functioned as the mere instrumentalities of Stagg, Khan and Ciberey, and injustice or fundamental unfairness would occur if the corporate veil of those purported corporations was left intact.

10. Veritec seeks declaratory relief under 28 U.S.C. § 2201.

11. This Court has subject matter jurisdiction over this action under 28 U.S.C. §§ 1331, 1338, 1367, 2201 and 2202.

12. This Court has personal jurisdiction over all Defendants inasmuch as they have conducted business in, and directed actions towards residents of, Minnesota

pertaining to the '006 Patent, including their efforts to tortiously interfere with Veritec's business relationships in Minnesota.

13. Venue is proper in this district under 28 U.S.C. §§ 1391(b) and (c).

STATEMENT OF FACTS

Veritec Owns The Banking Software At Issue

14. VTFS is a third-party processor of debit cards. Among other things, processors receive transactions from merchants and communicate with the appropriate financial institutions to facilitate the transactions. VT owns and markets the Banking Software, and VTFS is authorized to operate and manage the Banking Software as a wholly-owned subsidiary of VT. The Banking Software is critical to the business of Veritec.

15. VT acquired the Banking Software through valid and binding agreements with the prior owner of the software, RBA International, Inc. ("RBA").

16. On April 5, 2007, VT provided RBA with a loan in the amount of \$100,000. In return, RBA provided VT with a promissory note that identified the software owned by RBA as collateral to the loan. (Exhibit A). That software is the same Banking Software at issue in this case.

17. On April 27, 2007, VT lent RBA an additional \$100,000, and the promissory note was re-written to include this amount and a small amount of interest that RBA had not yet paid. (Exhibit B).

18. The April 27, 2007 promissory note provided RBA with an interest-free loan on the borrowed sum of \$200,900. In consideration of this interest-free loan, the note

expressly provided that Veritec would receive immediate availability of two software licenses of the Banking Software at no charge which could be sold by Veritec.

19. The April 27, 2007 promissory note also provided that, in the event of a default by RBA, VT could further take possession of, use, modify and sell the Banking Software:

As collateral for this Note, RBA International shall maintain a copy of the RBA Java and IVR software (used for the RBA banking system) and related documentation in escrow at Fortix for Veritec. These software escrow terms, the agent, and location are the same as for the West Coast Bank escrow terms.

Veritec shall have no right to access or use the software unless and until one or more of the following conditions occur:

- (1) Any payment due hereunder is not made on or before the due date, and RBA International does not timely cure such failure after proper notice of default by Veritec,

* * * *

Upon the occurrence of an event set forth above, and with written notice of such occurrence by Veritec to RBA International and Fortix, ***Veritec may take possession of the software and may use and modify it at any time thereafter for the sole purposes of serving its existing and future customers and selling a Veritec/RBA integrated solution. The original software released through these escrow terms may be sold to banks, financial Institutions, or credit unions without the prior written approval of both Mark Silbernagel and Rene' Babi (founders of RBA).*** Licensees will only have access to a copy of the RBA Java and IVR software (used for the RBA banking system) and documentation held in escrow at Fortix for Veritec in the event Veritec or RBA are no longer in business.

(Exhibit B; emphasis added).

20. In mid-2007, after RBA defaulted on the April 27, 2007 promissory note, Veritec took possession of the Banking Software pursuant to the express terms of that note.

21. Confirming VT's ownership of the Banking Software, on March 28, 2008, RBA and VT executed a Letter of Understanding and Mutual Release. (Exhibit C). That agreement states, among other things:

Veritec has in its possession the RBA Java and IVR software (used for the RBA banking system), the source code for the software and the supporting documentation for the software (hereinafter collectively referred to as "the Software"). The Software was delivered by RBA to Veritec in payment of the Promissory Note dated April 27, 2007 (the "Note"). RBA has represented to Veritec that the CD delivered by RBA to Veritec as payment for the Note contains a true, correct, complete and working copy of the Software. RBA elected to pay the Note through delivery of the Software, rather than pay in cash.

* * *

The Note grants Veritec the right to sell or license the Software, without restriction, to any existing or future customers. The Note also grants Veritec the right to modify the Software in any manner that it chooses prior to selling or licensing the Software.

Rene Babi signed that agreement on behalf of RBA while it owned the '006 Patent (Exhibit D); Babi is a named inventor of the '006 Patent. (Exhibit C; emphasis added).

Defendants Are Competitors Of Veritec

22. Veritec is in the business of merchant services and payments. In that industry, merchants obtain merchant accounts which enable them to accept payments from their customers by debit or credit cards. Merchant accounts are issued by merchant banks. Merchant banks may process merchant account transactions themselves, or use third-party processors such as Veritec.

23. Merchants can obtain these payment services directly through merchant banks, through processors such as Veritec that are aligned with merchant banks, or through authorized agents called Independent Sales Organizations (known as “ISOs”) who essentially resell the services of merchant banks or processor/merchant bank alliances.

24. Veritec develops and sells prepaid card programs, such as its Visa® debit cards marketed under the MTC or Mobile Toggle Card™ and blinx ON-OFF™ brands. In order to market such programs, Veritec must be sponsored by a merchant bank, who issues the accounts. Additionally, Veritec serves as a third-party processor to merchant banks for transactions of the banks’ or others’ prepaid cards. Whether Veritec is marketing and processing transactions for its own cards, or merely acting as a third-party processor to merchant banks for other cards, Veritec’s business depends on its relationships with merchant banks.

25. Smart is (or at least was) a competitor of Veritec, including through its wholly-owned subsidiary Columbia Card Systems International LLC who offered Visa® debit card programs. Smart also had business dealings with RBA, and pursuant to those dealings, purportedly acquired the ‘006 Patent and other assets from RBA through foreclosure proceedings in or around February of 2009. (Exhibit D).

26. From at least January 2009 to August 2009, Veritec exchanged correspondence with Smart, including Defendant Khan, in efforts to establish mutually beneficial business arrangements between Veritec, Smart and RBA. No agreements were reached between Veritec and Smart.

27. Smart and the principals who ran Smart (Messrs. Stagg, Khan and Ciberey) at all relevant times knew that Veritec had lawfully obtained the Banking Software through the above-identified agreements between Veritec and RBA.

28. On or about January of 2010, Defendants Stagg, Khan and Ciberey effected the transfer of certain Smart assets to Aurora Financial. Such transactions included the purported assignment of the '006 Patent and other intellectual property from Smart to Aurora Financial. (Exhibit D).

Defendants' Attempts To Drive Veritec Out Of Business

29. In 2009, Defendants Khan and Stagg informed Rene Babi of RBA that they were exploring ways to put Veritec out of business in order to eliminate competition.

30. In early 2009, Veritec sought to establish a merchant bank relationship with University National Bank ("UNB"), which is located in St. Paul, Minnesota. By mid-March of 2009, the parties were negotiating a license and software maintenance agreement, and had exchanged drafts of the same.

31. Defendants became aware of the negotiations between Veritec and UNB and immediately sought to thwart the development of that business relationship. Accordingly, Smart principals Stagg, Khan and Ciberey, and/or employees acting at their direction, contacted UNB in early 2009 and represented that (1) Veritec's Banking Software was owned by Smart, and infringes the '006 Patent, and (2) UNB would be sued if it entered into a contract with Veritec. These statements were false, misleading and made in bad faith because they relied on Defendants' objectively baseless infringement allegations.

32. Defendants' interference was successful, and UNB informed Veritec that UNB could not enter into the requested contract because it did not wish to be involved in litigation.

33. In late 2009, Stagg, Kahn and Ciberey formed Aurora Financial, and in early 2010, they arranged the transfer of the '006 Patent and other intellectual property from Smart to Aurora Financial. Also in 2010, they transferred the campaign to interfere with Veritec's business from Smart to Aurora Financial.

34. In August 2010, Aurora Financial sent a letter to Veritec purporting to inform it of the '006 Patent and its applicability to Veritec's products, and requesting that Veritec cease any activities which would read on the '006 Patent. Veritec responded in September 2010 informing Aurora Financial of its rights to use, modify and sell under its contractual arrangement with RBA.

35. Also in 2010, Veritec developed a merchant bank relationship with Palm Desert National Bank ("Palm Desert") of California. After extensive negotiation, Palm Desert agreed that it would serve as Veritec's merchant bank, subject to Veritec satisfying certain conditions, all of which Veritec was prepared to meet.

36. However, Defendants discovered the relationship between Veritec and Palm Desert, and improperly interfered with it. Specifically, in late December of 2010, Aurora Financial President Ciberey called Palm Desert and stated: (1) Veritec's Banking Software infringes the '006 Patent, and (2) Aurora Financial had a "Cease and Desist" against Veritec. These statements were false, misleading and made in bad faith because they relied on Aurora Financial's objectively baseless infringement allegations.

Defendants were successful in disrupting and delaying the proposed deal between Veritec and Palm Desert.

37. Defendants' interference has damaged Veritec. Among other things, Veritec had and has contracts with various companies under which such companies would provide Visa® debit cards to their customers and/or members, which cards would be processed through Veritec. As Defendants know, however, such contracts cannot be performed unless and until Veritec has a binding contract with a merchant bank.

COUNT I

DECLARATORY JUDGMENT OF NON-INFRINGEMENT OF THE '006 PATENT AND ANY OTHER PATENT OWNED BY DEFENDANTS ON WHICH RENE BABI IS A NAMED INVENTOR DUE TO LEGAL ESTOPPEL AND IMPLIED LICENSE

38. Veritec restates and realleges the allegations of Paragraphs 1 through 37 as if fully set forth herein.

39. Defendants have alleged in correspondence directly to Veritec, as well as in statements in the marketplace to Veritec's potential business partners, that Veritec has infringed one or more claims of the '006 Patent.

40. An actual and justiciable controversy exists between Veritec and Defendants concerning the Banking Software's infringement of the '006 Patent and any other patents owned by Defendants on which Rene Babi is a named inventor.

41. Given Veritec's lawful acquisition of the Banking Software – and the express confirmation of RBA and Babi that Veritec has the unfettered right to use, revise and sell that software – Veritec is entitled to a declaratory judgment that it does not

infringe the '006 Patent, and any other patent owned by Defendants on which Babi is a named inventor, due to legal estoppel and implied license.

42. Legal estoppel bars Defendants, the purported successors-in-interest of RBA, from derogating from the rights granted to Veritec by asserting the '006 Patent, or any other patents owned by Defendants on which Rene Babi is a named inventor, against Veritec for its Banking Software because RBA and Rene Babi assigned Veritec rights in the Banking Software and received consideration for such assignment while RBA owned the patents.

43. At a minimum, Veritec has an implied license to use, revise and sell the Banking Software under the '006 Patent, and any other patent owned by Defendants on which Babi is a named inventor, because (1) to the extent such patent rights cover the Banking Software, it is inferred that there has been a relinquishment of those rights against the Banking Software, and (2) the circumstances of Veritec's acquisition of the Banking Software from RBA plainly indicate that the grant of a license to Veritec should be inferred.

COUNT II

TORTIOUS INTERFERENCE WITH PROSPECTIVE ECONOMIC ADVANTAGE BY DEFENDANTS

44. Veritec restates and realleges the allegations of Paragraphs 1 through 43 as if fully set forth herein.

45. Veritec had ongoing business relationships or a reasonable expectancy of entering into business relationships with banking institutions which would serve as merchant banks for Veritec's products and services.

46. Defendants, knowing of these relationships and expectancies, intentionally and without justification engaged in wrongful acts and unjustified interference with those relationships and expectancies by (1) communicating to the banking institutions and others that Veritec's Banking Software infringes the '006 Patent, and (2) otherwise misrepresenting the ownership of Veritec's Banking Software. As the direct result of these wrongful acts and unjustified interferences, Defendants convinced at least two banking institutions, in Minnesota and California, not to do business with Veritec.

47. Defendants' actions were in bad faith because they relied on Defendants' objectively baseless infringement allegations.

48. Veritec has suffered damage as the result of Defendants' interference.

COUNT III

FALSE ADVERTISING—SECTION 43(A) OF THE LANHAM ACT

49. Veritec restates and realleges the allegations of Paragraphs 1 through 48 as if fully set forth herein.

50. Defendants' statements, made in the course of promoting their own products and services, that Veritec infringed the '006 Patent and did not own the Banking Software, were false, misleading and made in bad faith because they relied on Defendants' objectively baseless infringement allegations.

51. Defendants' false, misleading and bad faith statements deceived, and have a tendency to continue to deceive, a substantial segment of their intended audience including at least two merchant banks in Minnesota and California with whom Veritec has or has sought business relationships.

52. The deception of the statements was material, and has influenced, and will continue to influence, the contractual decisions of merchant banks and other business partners of Veritec, specifically companies that plan to purchase its prepaid card programs and card transaction processing services.

53. The deceptive statements were made to, at least, merchant banks in Minnesota and California, and were thereby placed into interstate commerce.

54. The deceptive statements injured, and are likely to continue to injure, Veritec.

55. The deceptive statements violate Section 43(a) of the Lanham Act, codified at 15 U.S.C. § 1125(a), which prohibits Defendants from using false, misleading or disparaging representations of fact that misrepresent the nature, characteristics or qualities of Veritec's products and services.

56. Veritec has suffered damage as the result of Defendants' interference.

COUNT IV

DECEPTIVE TRADE PRACTICES—MINN. STAT. § 325D.44

57. Veritec restates and realleges the allegations of Paragraphs 1 through 56 as if fully set forth herein.

58. Defendants' statements, made in the course of promoting their own products and services, that Veritec infringed the '006 Patent and did not own the Banking Software, were false, misleading and made in bad faith because they relied on Defendants' objectively baseless infringement allegations.

59. Defendants' false, misleading and bad faith statements deceived, and have a tendency to continue to deceive, a substantial segment of their intended audience including at least two merchant banks in Minnesota and California with whom Veritec has or has sought business relationships.

60. The deception of the statements was material, and has influenced, and will continue to influence, the contractual decisions of merchant banks and other business partners of Veritec, specifically companies that plan to purchase its prepaid card programs and card transaction processing services.

61. The deceptive statements were made to, at least, merchant banks in Minnesota and California, and were thereby placed into interstate commerce.

62. The deceptive statements injured, and are likely to continue to injure, Veritec.

63. The deceptive statements violate the Uniform Deceptive Trade Practices Act adopted by Minnesota, including at least Subsection eight (8), codified at Minn. Stat. § 325D.44(8), which prohibits Defendants, in the course of business, from disparaging the goods, services, or business of Veritec by false or misleading representation of fact.

COUNT V

DECLARATORY JUDGMENT OF NON-INFRINGEMENT OF THE '006 PATENT

64. Veritec restates and realleges the allegations of Paragraphs 1 through 63 as if fully set forth herein.

65. Defendants have alleged in correspondence directly to Veritec, as well as in statements in the marketplace to Veritec's potential business partners, that Veritec has infringed one or more claims of the '006 Patent.

66. An actual and justiciable controversy exists between Veritec and Defendants concerning the Banking Software's infringement of the '006 Patent.

67. Veritec has not infringed and does not infringe, directly or indirectly, any valid and enforceable claim of the '006 Patent, either literally or under the doctrine of equivalents, at least because its Banking Software does not implement the claims of the '006 Patent.

68. A judicial declaration of non-infringement is necessary and appropriate so that Veritec may ascertain its rights regarding the '006 Patent.

RELIEF SOUGHT

WHEREFORE, Plaintiffs Veritec, Inc. and Veritec Financial Systems, Inc. demand judgment against Defendants Aurora Financial Systems, Inc., Smart SMS Corp., Scott A. Stagg, Amir Khan and Michael R. Ciberey, and all persons in active concert or participation with them as follows:

A. A declaration that Plaintiffs do not infringe the '006 Patent, and any other patent owned by Defendants on which Babi is a named inventor, by using, revising or selling the Banking Software due to legal estoppel and implied license;

B. A declaration that Plaintiffs have not infringed and do not infringe any valid and enforceable claim of the '006 Patent because their Banking Software does not implement the claims of the '006 Patent;

C. An award of compensatory damages adequate to compensate Plaintiffs for the harm caused to them as a result of Defendants' unlawful acts;

D. An injunction, as permitted by the Lanham Act and Minnesota law, prohibiting Defendants from making false, misleading, disparaging and bad faith statements that Veritec infringes the '006 Patent or other patents owned by Defendants on which Babi is a named inventor, or that Veritec otherwise does not own or have the right to use, modify or sell the Banking Software;

E. An award of punitive damages;

F. A determination that this case is exceptional within the meaning of 35 U.S.C. § 285, and an award to Plaintiffs of the costs of this action and their reasonable attorneys' fees; and,

G. Such other relief as Plaintiffs are entitled to recover under any applicable law and as this Court and/or a jury may determine to be proper and just.

JURY DEMAND

Plaintiffs Veritec, Inc. and Veritec Financial Systems, Inc. hereby demand a trial by jury on all issues triable to a jury in this case.

Respectfully submitted,

Date: July 13, 2011

/s/ Brian E. Haan

Paul K. Vickrey (*Admitted Pro Hac Vice*)

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VERITEC, INC. and VERITEC
FINANCIAL SYSTEMS, INC.**

CERTIFICATE OF SERVICE

The undersigned hereby certifies that on July 13, 2011 the foregoing:

SECOND AMENDED COMPLAINT

was filed with the Clerk of Court pursuant to the Court's CM/ECF procedures, which will provide electronic notification to the following counsel of record:

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***Attorneys for Defendants, Aurora Financial Systems, Inc., Scott A. Stagg, Amir Khan
and Michael R. Ciberey***

I further certify that I caused a copy of the aforementioned documents to be served on the following via the following methods:

Smart SMS Corp. (*Service of Process*)
330 Roberts Street
Suite 203
East Hartford, CT 06108-3654

/s/Brian E. Haan