HONORABLE JOHN P. ERLICK

IN THE SUPERIOR COURT OF THE STATE OF WASHINGTON FOR KING COUNTY

ROBERT M. ARNOLD, derivatively on behalf of MOD SYSTEMS, INC. and BANANA CORPORATION, Plaintiffs, v. MARK PHILLIPS, KENNETH GORDON, JANDE DOE GORDON, and the marital community composed thereof; ANTHONY BAY, JANE DOE BAY, and the marital community composed thereof; MOD SYSTEMS, INC. and BANANA CORPORATION, Defendants.	NO. 09-2-07963-3 SEA SUPPLEMENTAL DECLARATION OF DENNIS M. MANDELL RE: MOD SYSTEMS DEMAND REVIEW COMMITTEE REPORT

Dennis Mandell declares under penalty of perjury of the laws of the State of Washington that:

1. My education, training, experience and qualifications are set out in my previous declaration "Declaration of Dennis M. Mandell" being filed in conjunction with this declaration and will not be repeated here.

2. I have been asked by Mark Johnson, Mr. Phillips' attorney, to review the final report of the MOD Systems Demand Review Committee (DRC) issued June 15, 2009 (Report), attached hereto as Exhibit 1. I have reviewed, and participated in preparing

ORIGINAL

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Special Litigation Committee (SLC) reports on several occasions concerning both public and private companies.

3. I can state unequivocally that it is the worst example of an SLC report I have ever seen. SLCs are to be independent and impartial in their investigations and this Report lacks any independent credibility. One of the members of the DRC, Anthony Bay, is a defendant in the case and was directly involved in MOD's accounting and business practices. The only other DRC member, Kyleen Cane has a long term, extensive professional relationship with the woman who instigated the case, Jan Wallace, including being the attorney for several companies in which Kyleen Cane was or is an officer. Kyleen Cane cannot be expected to assess, impartially and independently, the credibility of Jan Wallace. David Douglass, DRC's investigator and MOD's former interim Chief Financial Officer was directly involved MOD's accounting and business practices. Last, it's troubling that MOD's counsel Lane Powell, which participated in all of MOD's major business activities, also participated in this process and failed to identify a responsible attorney.

4. The accounting firm that the DRC "consulted" with, I assume to offset the glaring independence conflicts, did not even provide a written report nor a responsible individual from the firm (Deloitte). This is highly unusual and the conclusion, which is attributed to Deloitte, is suspect. All we have is the DRC paraphrasing what Deloitte allegedly said, ending with the ludicrous conclusion that Deloitte had no basis to conclude "that the transactions indentified in the DRC's Preliminary Report did not occur." The issue isn't whether the transactions occurred, it is whether there was evidence of fraud and embezzlement.

5. In addition to lacking any independent credibility, the Report fails to provide any creditable evidence of the alleged "pervasive, systematic scheme". To respond to the Report: we would need to have the same access as Deloitte had to the "data and other evidence available to David Douglass and the DRC"; access to the Deloitte professionals

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for interviews; copies of the MOD Board of Directors meeting concerning Deloitte's alleged presentation; and an inspection of MOD books and records including a copy of MOD's QuickBooks file as of the date of this declaration.

I state under penalty of perjury under the laws of the State of Washington that the foregoing is true and correct.

Executed this 21 day of September, 2009.

Dennis M. Mandell

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Exhibit 1

JUNE 15, 2009

TO: MOD Systems Incorporated Board of Directors and Board Observers

FROM: Lane Powell PC

RE: Demand Review Committee Report

This Report is being prepared by the Demand Review Committee pursuant to the Transition Agreement between Mark Phillips and MOD Systems Incorporated ("MOD").

Background of Demand Review Committee Investigation.

In mid-December 2008, MOD shareholder Robert Arnold made a written demand on MOD and its Board of Directors in the form of a draft, unfiled Complaint. Among other things, the Arnold Complaint asserted derivative claims on MOD's behalf against Mr. Phillips, a MOD Director and its CEO, Kenneth Gordon, a MOD Director, and others, including alleged misappropriation of MOD funds and breach of fiduciary duty by Mr. Phillips and Mr. Gordon. In response, on January 22, 2009, MOD's Board of Directors created a Demand Review Committee ("DRC") comprised of Directors Anthony Bay and Kyleen Cane to investigate the allegations in the Arnold Complaint and additional allegations made by his counsel in early January 2009. MOD's corporate counsel, Lane Powell PC, was asked to assist the DRC in conducting its investigation.

Lane Powell retained David Douglass of Tatum LLC, MOD's former interim CFO, to review MOD's accounting records and transactions from its inception in light of the allegations in the Arnold Complaint, and to recommend enhanced internal financial and accounting controls for MOD. Mr. Douglass began reviewing the QuickBooks accounting records of MOD and ADot Corporation ("ADot"), another company owned by Mr. Phillips, in late January 2009 pursuant to an Action Plan approved by the DRC. In addition, Mr. Douglass informally interviewed Jan Wallace, a financial and business consultant retained by Mr. Phillips on behalf of MOD, ADot and another of his companies, Banana Corporation ("Banana"), and with whom Mr. Phillips had an intimate relationship. Mr. Douglass also informally interviewed various MOD Directors, officers and employees, including Mr. Phillips, Mr. Gordon, Doug Lower, Rich Barber, and Derek de Bakker, regarding various transactions reflected in MOD and ADot's accounting records, enhancing MOD's financial and accounting controls, and other matters. Mr. Douglass reported periodically to Lane Powell and the DRC in February and March 2009 on the progress of his review and investigation.

On March 17, 2009, the DRC and Lane Powell interviewed Ms. Wallace in Seattle, and reviewed documents she obtained from one of Mr. Phillips' laptop computers, regarding: (a) financial, consulting and other services she provided MOD, ADot, Banana and Mr. Phillips pursuant to an alleged oral agreement with him and later pursuant to a written consulting agreement between MOD and Meteor International Group Corp. ("Meteor"), (b) Mr. Phillips' misappropriation of MOD funds for his personal use; and (c) alleged misconduct by Mr. Phillips and other MOD employees, including Mr. Phillips' alleged deletion of emails, substance abuse, and assault and battery against her.

On March 17, the DRC and Lane Powell also interviewed Mr. Gordon and MOD employee Michael Streicher, and they interviewed MOD employee Doug Lower on March 18. Following the regularly scheduled meeting of MOD's Board of Directors in Seattle on March 18, the DRC and Lane Powell interviewed Mr. Phillips. The next day, Lane Powell met with Mr. Phillips' counsel, Tony Gewald and Ron Braley, and provided them with copies of the documents Ms. Wallace had given the DRC.

Mr. Gordon resigned as a Director of MOD on March 26, 2009. Mr. Phillips resigned as a Director and as MOD's CEO, and he and MOD entered into a Transition Agreement and related agreements, effective as of March 27. On April 3, Lane Powell prepared the DRC Investigation Preliminary Report for MOD's Board of Directors and Board Observers, and MOD placed Mr. Phillips and Mr. Gordon on paid administrative leave.

The DRC requested another interview of Mr. Gordon, but he declined to participate. Mr. Gordon was subsequently terminated by MOD for cause on May 8.

On May 6, 2009, the DRC's Preliminary Report was forwarded to Messrs. Gewald and Braley. Lane Powell and MOD subsequently provided certain spreadsheets and supporting documents prepared by Mr. Douglass and other documents and information requested by Mr. Phillips, Mr. Gordon and Mr. Phillips' counsel.

On May 18, Mr. Gewald forwarded a letter with summaries and other documents concerning (i) the DRC's preliminary finding that Mr. Phillips had misappropriated $100,000 of MOD funds that had been wire transferred to his personal counsel at the Holman Cahill law firm; and (ii) certain expenses paid by MOD that Mr. Douglass and the DRC found preliminarily were or may have been personal expenses of Mr. Phillips and not business expenses.

On April 24, 2009, Lane Powell and MOD retained Deloitte Financial Advisory Services LLP ("Deloitte") to review the DRC's Preliminary Report, including the analyses, methodology and investigative procedures utilized by Mr. Douglass and the DRC, and the data and other evidence available to Mr. Douglass and the DRC, and to provide a quantitative assessment of the preliminary findings of Mr. Douglass and the DRC's accounting investigation.

On June 8, Deloitte presented its findings orally to MOD's Board of Directors and Board Observers, and to Mr. Arnold's counsel and accountant. In sum, Deloitte reported that no material financial data or information came to its attention that would lead Deloitte to conclude that the transactions identified in the DRC's Preliminary Report did not occur.

The DRC's investigation is continuing. However, neither the DRC, Lane Powell nor Mr. Douglass has reviewed documents other than MOD and ADot's accounting records and information and the documents provided by Ms. Wallace and Mr. Phillips' counsel. In particular, the data, including emails, collected by Lane Powell's e-discovery vendor, Applied Discovery, from computers and servers at MOD and the personal laptop and other computers used by Mr. Phillips, Mr. Gordon, Ms. Wallace and others, has not been searched for relevant documents due to the prohibitive cost of doing so. Neither has the DRC nor Mr. Douglass conducted any additional interviews, excepting Mr. Douglass' interview of Mr. Bay regarding the expenses identified in Mr. Gewald's May 18 letter.

Findings of Investigation.

The DRC has concluded that Mr. Phillips and Mr. Gordon engaged in a pervasive, systematic scheme to exploit their positions as MOD's CEO and former *de facto* CFO, respectively, for their own personal benefit. Among other things, they misappropriated MOD funds, misused its employees, assets and resources, in bad faith and contrary to the best interests of MOD and its other shareholders. Mr. Phillips and Mr. Gordon did not disclose their conduct and activities to MOD's Board of Directors and the Series A investors.

Based on (i) Mr. Douglass' interviews, and his investigation and review to date of MOD and ADot's accounting records and the May 18 letter and exhibits from Mr. Phillips' counsel, (ii) the DRC and Lane Powell's limited interviews and review of documents provided by Ms. Wallace and Mr. Phillips' counsel, and (iii) Deloitte's report following its review and evaluation of the DRC's Preliminary Report, the DRC has reached the following findings:

1. **MOD Payments to Holman Cahill Law Firm—$100,000.** There is evidence that Mr. Phillips misappropriated $100,000 of MOD funds by funneling them through his personal counsel, Larry Garret at the Seattle law firm of Holman Cahill Garret Ives Oliver & Andersen, to Ms. Wallace, who in turn paid it to Mr. Phillips or as he directed.

2. **Inter-company Payments by MOD to ADot.** There is evidence that Mr. Phillips and Mr. Gordon misappropriated as much as $446,000 in MOD funds that were invoiced by ADot to MOD and paid by MOD to ADot.

3. **MOD Payment of Phillips' Personal Expenses.** There is evidence that Mr. Phillips has incurred as much as $524,000 in personal or non-business-related expenses that have been paid by MOD. Based on Mr. Douglass' review of MOD's accounting records and the May 18 letter and exhibits from Mr. Phillips' counsel, and his interviews, Mr. Douglass has compiled the following categories of personal expenses of Mr. Phillips that were paid by MOD for which it has not been reimbursed:

a. **Probable Personal Expenses—$268,252.** This amount includes $30,000 of ADot legal fees, $40,000 for travel and entertainment with no supporting documentation, $8,000 in Salvador Dali lithographs, $13,159 in purchases at Hermes and Louis Vuitton, $13,780 in personal airfare, $9,469 in furniture and other items purchased at a Tokyo department store, $9,200 in purchases at the Limn furniture store, $8,130 in clothing, $6,150 in dental and DNA testing expenses, and charitable contributions exceeding $28,600.

b. **Potential Personal Expenses—$90,810.** These are expenses that may have been a personal or a business expense, including almost $53,600 in electronics items purchased from Sony and at Magnolia Audio.

c. **Questionable Business Expenses—$108,650.** These are expenses ostensibly incurred for MOD's benefit that were likely unnecessary or inappropriate given MOD's financial condition, and if so, they were an abuse of Mr. Phillips' discretion.

d. **Expenses with No Supporting Documentation—$42,708.** These include $5,474 in expenses incurred prior to June 4, 2008, and another $37,234 incurred thereafter.

e. **Jan Wallace-Related Expenses—$14,279.** This amount includes expenses related to Mr. Phillips' non-business travel and entertainment with Ms. Wallace.

4. **Jan Wallace/Meteor Settlement—$126,000.** Mr. Phillips promised or entered into alleged oral or written agreements with Ms. Wallace and the company he formed for her, Meteor, that created significant potential unrecorded liability exposure to MOD without the approval of MOD's Board of Directors or despite its disapproval. As a result, MOD recently paid Ms. Wallace $126,000 to settle her claims against MOD arising out of its contract with Meteor and her alleged oral agreement with Mr. Phillips to provide consulting services to MOD.

5. **Pending Request for Reimbursement—$220,173.** In December 2008, Mr. Phillips requested that MOD reimburse him for $220,173 in expenses. These expenses include $106,439 for ADot legal expenses, and $113,734 in travel, entertainment and other expenses incurred prior to October 2008, when MOD's books were closed prior to the Series A investment transactions.

Mr. Douglass found that Mr. Phillips had already been reimbursed for more than $6,000 of these expenses. MOD determined that Mr. Phillips' reimbursement request fell within the scope of the DRC investigation, and the DRC has determined that Mr. Phillips' reimbursement request should be denied.

6. **Misuse of MOD Employees.** There is evidence that Mr. Phillips asked MOD employees to perform services for him while they were being paid by MOD. Josette Jenkins, Lauren Kronmiller, Rachel Huffman and Eric Lundvall received approximately $99,864 in compensation from MOD while performing work for Mr. Phillips' personal benefit.

Mr. Phillips' Response to DRC Report.

Paragraph 4 of the Transition Agreement between Mr. Phillips and MOD provides in pertinent part as follows:

> 4. Repayment of Expenses. Upon completion of the investigation by the Demand Review Committee, the Company will present Phillips with a report itemizing those expenses and transactions for which the Company believes it is entitled to reimbursement and which informs Phillips of the total amount of reimbursement to which the Company deems itself entitled (the "Report"). Within 30 calendar days of receiving the Report, Phillips agrees to review the report and, within such time, to provide backup documentation and a rationale for any and all expenses and transactions brought into question as well as a request for credit for unreimbursed bona fide business expenses and to deliver this to the Company. . . .

Accordingly, this Report will be provided to Mr. Phillips and his counsel pursuant to paragraph 4 of the Transition Agreement, and Mr. Phillips will be afforded thirty (30) days from the date he receives this Report "to provide backup documentation and a rationale for any and all expenses and transactions brought into question" in this Report "as well as a request for credit for unreimbursed bona fide business expenses and to deliver this to" MOD.

MOD Reservation of Rights.

MOD reserves all of its rights and remedies to recover damages or seek reimbursement of other expenses from Mr. Phillips that are attributable to him or his misconduct and that are not set forth in this Report.

HONORABLE JOHN P. ERLICK

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ROBERT M. ARNOLD, derivatively on behalf of MOD SYSTEMS, INC. and BANANA CORPORATION, Plaintiffs, v. MARK PHILLIPS, KENNETH GORDON, JANDE DOE GORDON, and the marital community composed thereof; ANTHONY BAY, JANE DOE BAY, and the marital community composed thereof; MOD SYSTEMS, INC. and BANANA CORPORATION, Defendants.	NO. 09-2-07963-3 SEA AFFIDAVIT OF MARK JOHNSON RE: FACSIMILE TRANSMISSION PURSUANT TO GR 17(a)(2)

STATE OF WASHINGTON)
) ss.
COUNTY OF KING)

MARK JOHNSON, being first duly sworn upon oath, deposes and states as follows:

I have examined the facsimile transmission of the Supplemental Declaration of Dennis M. Mandell Re: Mod Systems Demand Review Committee Report and have determined that it consists of three pages (nine pages with attached exhibit and this affidavit), and that it is complete and legible.

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The document was faxed to me at the law firm of Johnson Flora, PLLC, to the address, phone and fax number listed in the lower right hand corner of this document.

Further your affiant sayeth naught.

Mark Johnson, WSBA #8463

SUBSCRIBED AND SWORN TO BEFORE ME this 21st day of September 2009.

SHERYL R. BRADY
NOTARY PUBLIC
COMMISSION EXPIRES 4-19-12
STATE OF WASHINGTON

Sheryl R. Brady
Notary Public in and for the State of Washington, residing at Seattle.
My commission expires: April 19, 2012

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