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UNITED STATES DISTRICT COURT
FOR THE DISTRICT OF COLUMBIA

UNITED STATES OF AMERICA, : Civil Action
 : No. 1:11-cv-00948
Plaintiff, :
 : September 12, 2011
v. : Morning Session
 :
H&R BLOCK, INC., et al., : Washington, D.C.
 :
Defendants. :
..... :

TRANSCRIPT OF PRELIMINARY INJUNCTION HEARING - DAY 5
BEFORE THE HONORABLE BERYL A. HOWELL
UNITED STATES DISTRICT COURT JUDGE

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25 Proceedings reported by machine shorthand, transcript
produced by computer-aided transcription.

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P R O C E E D I N G S

THE DEPUTY CLERK: This is Civil Case 11-948, United States of America v. H&R Block, et al.

MR. WAYLAND: Do you need appearances again?

THE COURT: I hope not.

MR. WAYLAND: Okay.

THE COURT: I think we don't have a new court reporter so she knows who everybody is.

MR. WAYLAND: Just a couple of matters, your Honor.

THE COURT: Yes.

MR. WAYLAND: The government rested at the end of the day Friday with respect to witnesses. As your Honor is aware, we have an agreement with the defendants that at the end of the trial, we will have an agreed-upon submission of documents which will identify for the Court, and that will be part of our case as well. And we have the right under the agreement that governs the conduct of the case to call rebuttal witnesses.

THE COURT: Any housekeeping matters from you?

MR. ROBERTSON: No, your Honor. Good morning. Robby Robertson for the record. And we will start our case this morning, your Honor, and Mr. Eric Stock from our firm is sitting here, now standing up here.

THE COURT: Good morning.

MR. ROBERTSON: Mr. Eric Stock will be the attorney handling the first witness. And that's all I have

1 administrative and I can step aside.

2 THE COURT: Let's just review the schedule for just a
3 little bit, if we could.

4 So do you expect to call two witnesses, I think I
5 understood from you, Mr. Robertson?

6 MR. ROBERTSON: There are two third-party witnesses
7 that we will call this morning and then when they are finished,
8 then provided we have more time, the next witness would be
9 Dr. Meyer after that. And then we'll probably then be rolling
10 into the days off at least for us anyway on Tuesday and
11 Wednesday. Be back on Thursday.

12 If Dr. Meyer is finished, that's great. If not, we'll
13 complete that testimony on Thursday. And I don't know what --
14 if your Honor has a different schedule for Thursday.

15 THE COURT: No. My sentencing commission meeting
16 schedule has been slightly revised so I just wanted to alert you
17 all to that now. I'm not going to pull the rug out from under
18 you in any way so depending on your witness availability, we
19 will keep to the schedule that I outlined at the pretrial. But
20 my sentencing commission meeting has been postponed in terms of
21 the start time until 2 o'clock tomorrow. So if we can -- if we
22 don't finish with witnesses today, if it's possible schedulewise
23 to finish at least Dr. Meyer, if she's on tomorrow morning, if
24 you can check on that availability and let me know, unless you
25 know now.

1 MR. ROBERTSON: Your Honor, we can do that. What we
2 normally can't do is remove Mr. Cobb, but he's going to bring
3 him in later in the week. We had him on Friday sitting here all
4 day, and I just don't want him to come back another time and
5 another time.

6 But that's the only other person I think we have a
7 scheduling issue with. I think Dr. Meyer is fine.

8 THE COURT: So we would have Mr. Cobb then on Thursday.

9 MR. ROBERTSON: I believe that's correct, yes.

10 THE COURT: Okay.

11 MR. ROBERTSON: Thursday or Friday, depending how it
12 works out.

13 THE COURT: I'm trying very hard to -- and I would
14 really like to finish all the testimony by Thursday of this
15 week. On Friday I have a number of other matters that are going
16 to require extensive argument, including a suppression hearing
17 and various other arguments. So if we have to hear witnesses on
18 Friday, it might not be till very late in the day.

19 MR. ROBERTSON: We'll see what we can do, your Honor,
20 Friday to avoid that if we can.

21 THE COURT: Just to alert you, I prefer to finish
22 everything if we can on Thursday.

23 MR. ROBERTSON: Once we finish with that, what's your
24 Honor's pleasure in terms of where we go from there because I
25 think that involves a lot of scheduling as well. I don't know

1 how it happened, but I have another antitrust PI, believe it or
2 not, the same month on the 28th. It's a small one, thank
3 goodness.

4 THE COURT: Business is good, Mr. Robertson.

5 MR. ROBERTSON: I have to go out to Denver for that
6 one. But sometimes it's helpful to have at least proposed
7 findings from each side.

8 THE COURT: Yes. I would like to have proposed
9 findings from each side and any briefs from each side. I know
10 that you all have reserved time for your closings, and it's
11 during that period that, you know, I'm hoping to be able to ask
12 you a number of questions as we would at an oral argument.

13 MR. WAYLAND: We had hoped, your Honor, that the
14 closings would be postponed until you had all the briefs so that
15 it would be a more useful exercise for you.

16 THE COURT: Okay. I think that's fine.

17 Have you all talked about a schedule for your briefing?

18 MR. WAYLAND: We have had very preliminary discussions
19 this morning, your Honor, which we're hoping to talk a little
20 bit more about at lunch. Maybe come back after lunch.

21 THE COURT: What I'd like to do rather than dictating a
22 schedule to you for briefing, since I want to get the best work
23 product I can from both of you, so I think in light of that, I'd
24 like you all to work out a schedule that you think will enable
25 you to produce the best work product possible to me.

1 So I'll wait to hear from you about that briefing
2 schedule.

3 MR. WAYLAND: All right, your Honor.

4 MR. ROUSH: With regard to finishing on Thursday, just
5 we actually have two business people. We've taken a couple of
6 people off our witness list or plan to at this point. We still
7 have two business people that we'd like to go on Thursday. Then
8 there would be the rebuttal case, if they are planning on
9 calling folks. Realistically, it's not likely we'll finish on
10 Thursday unless there is a change on their rebuttal case.

11 MR. WAYLAND: My guess, your Honor, is we're going to
12 go Monday. You can tell us just to come back on Monday. I
13 think the rebuttal we'll know by the end of the day Thursday.

14 THE COURT: Okay. And that's fine. What we'll do
15 is -- I mean, we'll have a better sense at the end of the day on
16 Thursday exactly what's left and how much time it will take. I
17 have to pick a jury in my next case Monday morning, and then
18 I'll just tell that jury to come back, you know, to start that
19 next case, you know, perhaps Wednesday if we think we need to go
20 through Monday and Tuesday.

21 MR. WAYLAND: Thank you, your Honor.

22 THE COURT: Okay.

23 MR. ROBERTSON: Your Honor, if I could then turn the
24 podium over to my partner, Mr. Stock.

25 THE COURT: Mr. Stock, welcome. Are you ready to call

1 your witness?

2 MR. STOCK: Yes. We call Dane Kimber.

3 MR. WAYLAND: Your Honor, Mr. Buterman from the United
4 States will be handling this.

5 MR. BUTERMAN: Your Honor, I believe that there are
6 going to have to be sealed portions with both this witness and
7 the next witness. Frankly, I believe that the government's
8 cross of these witnesses is going to be pretty -- is not going
9 to be that extensive. It might make more sense -- I believe
10 Mr. Stock is going to be doing an open session and then a closed
11 session -- if we just continue afterwards and the government
12 does its cross and close. And then after lunch we can go
13 through the transcript and unseal the relevant portions. It
14 just seems like there's not enough to open and close.

15 THE COURT: Okay. That's fine.

16 MR. STOCK: No objection. Most of our direct can be
17 open, your Honor.

18 THE COURT: Okay.

19 MR. STOCK: Mr. Kimber.

20 (WHEREUPON, the witness was sworn.)

21 DANE L. KIMBER,
22 called as a witness herein, having been first duly sworn, was
23 examined and testified as follows:

24 THE COURT: Good morning.

25 THE WITNESS: Good morning.

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DIRECT EXAMINATION

BY MR. STOCK:

Q Mr. Kimber, what is your full name?

A Dane Lee Kimber.

Q And where do you live?

A Just south of Provo, Utah.

Q What is your educational background?

A I have a bachelor's degree in information systems from Brigham Young University.

Q And is Brigham Young University located in Provo?

A It is.

Q Who are you employed by, Mr. Kimber?

A I'm employed by TaxHawk, Incorporated.

Q And what's your relationship with TaxHawk?

A I'm one of the two founding owners and currently a principal.

Q And what's your current job title at TaxHawk?

A Vice president.

Q And what are your responsibilities as vice president?

A I'm responsible for the day-to-day operations of the business areas such as payroll and HR, as well as over the engineering or software development portion of our company.

Q Do you have any responsibilities relating to the business strategy of TaxHawk?

A I do.

1 Q And what about the pricing of TaxHawk's products?

2 A Yes.

3 Q When did you start TaxHawk?

4 A We formed the company in February of 2001.

5 Q Could you please briefly give us a description of how you
6 started the company.

7 A In January of 2001, I received a phone call on a Saturday
8 afternoon from a long-time friend, and he described the idea
9 that he had of forming a company and doing taxes online. We
10 talked about it. I spent the next year designing our
11 preliminary software, and we then launched that in January of
12 2002.

13 Q And where were you employed at the time?

14 A I was working for Novell, Incorporated, in Provo, Utah.

15 Q And did there come a time when you quit your job at
16 Novell?

17 A I did. It was that following summer.

18 Q Now, how many employees does TaxHawk have now?

19 A We have roughly 20 to 25.

20 Q During peak season, does that number change?

21 A We got up last peak season to roughly 35 employees.

22 Q Could you please explain what types of products TaxHawk has.

23 A TaxHawk provides online software to allow an individual
24 income taxpayer to prepare their federal and state return and
25 E-file that if they so desire with the government.

1 Q Does TaxHawk run any Web sites?

2 A We do.

3 Q How many Web sites?

4 A We have five Web sites that we use and market differently.

5 Q Which TaxHawk Web site has the most customers?

6 A FreeTaxUSA.com.

7 Q Which TaxHawk Web site has the second most customers?

8 A That would be the Web site of our company name,

9 TaxHawk.com.

10 Q And why do you operate your Web sites separately instead of
11 just using one Web site?

12 A We decided at the beginning because of the thought we had
13 originally to offer different federal forms such as the 1040EZ,
14 the 1040A, to market them differently and on different Web
15 sites.

16 Q Do all of your Web sites use the same tax preparation
17 engine?

18 A It is. It's the same base engine behind all of them.

19 Q Now, in general, which federal tax forms can TaxHawk's tax
20 preparation engine process?

21 A We support the main tax form, the 1040 and 5054, attached
22 schedules or forms to that main form.

23 Q What percentage of federal taxpayers do you believe your
24 company can serve with its existing federal tax form
25 capabilities?

1 A Based on our calculations, we support over 95 percent of the
2 American taxpaying public.

3 Q Which states does TaxHawk's tax preparation engine cover?

4 A We cover 42 of the 44 states that have a state income tax.

5 Q And are there two states that have a state income tax that
6 you don't cover?

7 A There are.

8 Q And what are those states?

9 A Those are the states of Tennessee and New Hampshire.

10 Q And why have you chosen not to cover those two states?

11 A Basically, as we looked at the possibility of or the idea of
12 supporting those states, in our estimation, those state income
13 tax filings are not used by the majority of people in those
14 states.

15 Q Is it in your plan to cover those states in the near
16 future?

17 A It is.

18 Q In the next two to three years?

19 A Yes.

20 Q If you decided this year that you had to cover those two
21 states, do you think you could cover those two states by next
22 tax season?

23 A By working extra time, we could -- we have the expertise to
24 do it. We chose not to at this point.

25 Q Turning now to your business and pricing strategy.

1 Does your company offer tax preparation solutions through
2 the Free File Alliance Web site operated by the IRS?

3 A We do.

4 Q And do you also offer tax preparation for visitors who come
5 straight to your Web site?

6 A Yes.

7 Q Okay. Without giving out precise numbers, because we're
8 trying to keep this portion of the questioning nonconfidential,
9 can you give us a sense as to how much of your business comes
10 from the FFA Web site for Free File Alliance and what proportion
11 comes from direct visits to your Web sites?

12 A Without using numbers?

13 Q Just -- do most come from one or the other?

14 A Most come from directly to us. It is a smaller percentage
15 but still significant that come through FFA.

16 Q Okay. So focusing on the customers that come to your Web
17 sites directly, can you tell me the pricing for the products
18 offered on your Web site Free Tax USA.

19 A Yes. We offer the federal tax return, the preparation and
20 E-filing thereof, for free to all customers. We then for those
21 42 states that we support, we offer the state tax filing for
22 9.95.

23 Q And do you have a deluxe product that you offer on Free Tax
24 USA?

25 A We do. We also offer a deluxe upgrade for 5.95 that

1 includes priority support which bumps them to the top of the
2 queue if they e-mail us a support question. And it allows for
3 unlimited amending of that return if that's required through the
4 year, as well as assistance with any audit letters that they may
5 receive from the IRS.

6 Q Okay. Just so the record is clear, what proportion of
7 taxpayers do you believe can prepare their federal taxes on Free
8 Tax USA for free?

9 A 100 percent of the ones we support or the same percentage,
10 over 95 percent of the American taxpaying public.

11 Q Okay. Now, on your second most popular Web site, TaxHawk,
12 could you please tell us the pricing that you used on that Web
13 site.

14 A The pricing we chose to use there was to offer the
15 preparation and E-filing of the federal tax return along with
16 the state tax return free to all those with an AGI or adjusted
17 gross income of 20,000 or less.

18 For those that have an AGI over 20,000, the federal return
19 is still free, but the state return is 12.95.

20 Q Thank you.

21 Now, when did your company first conceive of the idea to
22 offer free federal tax returns online?

23 A It was sometime in the summer of 2002.

24 Q Do you know when your Free Tax USA Web site was
25 registered?

1 A I do. We registered that domain a little bit of time after
2 having those conversations in September of 2002.

3 Q And whose idea was it to offer free federal tax returns
4 online on Free Tax USA?

5 A It was a joint decision between Scott and I. The idea to
6 register the domain was my idea.

7 Q And had the Free File Alliance started at that time?

8 A It had not.

9 Q When the Free File Alliance started, did you use Free Tax
10 USA in the Free File Alliance Web page?

11 A Yes. We used that Web site as our entrant into the Free
12 File Alliance, yes.

13 Q Now, when did you start offering free federal filings on
14 Free Tax USA -- on the Free Tax USA Web site?

15 A We offered free to, with no AGI restrictions, in tax year
16 2003.

17 Q Okay. And the prior tax year, had you offered it with AGI
18 restrictions?

19 A We did. It was restricted to, I believe, 30,000. An AGI of
20 30,000 or less could get it for free, but anybody over 30,000
21 could not.

22 Q And that's tax year 2002?

23 A That's tax year 2002.

24 Q Tell us again what the offer was in tax year 2003.

25 A 2003, the offer was that it was free to any individual that

1 lived in one of 14 states that we had listed there. But it was
2 free for 100 percent of those people.

3 Q And whose idea was it to eliminate the AGI restrictions that
4 you had had in the prior year, tax year 2002?

5 A It was a goal, I guess you could say, that we had from since
6 registering the Web site, but it was between conversations
7 between Scott and I. We talked about doing it.

8 Q Thank you.

9 Now, turning to the products, the tax preparation engine
10 offered by TaxHawk, what is your assessment of the quality of
11 the digital tax preparation services offered by TaxHawk?

12 A We believe they're very high quality.

13 Q And how do you know it's a high-quality product?

14 A I would base that statement on the growth that we have year
15 to year and the comments and compliments that we receive via
16 e-mail and even some by phone directly to our office.

17 Q Do you believe that you have high-quality software
18 engineers?

19 A I do, absolutely.

20 Q And what do you base that view on?

21 A Based on their education and having worked with them and the
22 many opportunities we give them to maintain their skills and
23 become trained on new and innovative technologies.

24 Q Speaking of innovation, would you describe TaxHawk as an
25 innovative company?

1 A I believe we are.

2 Q In what ways? Could you give us examples of how TaxHawk has
3 been innovative.

4 A We encourage our employees, not just our engineers, but all
5 of our employees to present ideas of improving our product or
6 making our product more user friendly or usable, period. One
7 example of this was approximately three years ago we were
8 presented with the idea of a feature called a "bookmark," which
9 would allow the customer to put a bookmark, if you will, in a
10 section of the tax return where they did not have the complete
11 information to fill it in completely. They could then return
12 later to that easily by going to their bookmarks and selecting
13 that page that they had marked and going back and entering the
14 information in a future date.

15 And since adding that feature, we've received many
16 compliments that suggests people like it a lot.

17 Q Has that feature been emulated by other digital tax
18 preparation companies?

19 A We noticed that it had been added.

20 Q Is there anything innovative about TaxHawk's state
21 pricing?

22 A Innovative to the point that we offer the state return along
23 with the federal return for free. We don't -- we know that
24 there have been at least a company or two that have done that in
25 the past. But as far as we're aware of, we're the ones doing

1 that right now.

2 Q What about the name "Free Tax USA"? Is there anything
3 innovative about the name?

4 A I like the name having been the one who thought of it. But
5 we know through our experience that when you are trying to
6 market your company via search engines, that having the words or
7 the phrases that you would expect a consumer or a taxpayer to
8 type in when searching for a tax preparation company appear in
9 your URL or your domain name, as well as the title of your Web
10 site, that it lends more credibility in the search engines,
11 gives you a boost up the page, if you will.

12 Q Thank you.

13 MR. STOCK: Your Honor, there's one point I neglected
14 to make at the beginning, which is as I get into issues that may
15 involve confidentiality, I want to recognize that the witness
16 has counsel present in the front row. So his counsel may also
17 have views on confidentiality issues. I neglected to say that
18 at the beginning.

19 THE COURT: What is the name of his counsel?

20 MR. STOCK: Mr. Quinn Kofford.

21 BY MR. STOCK:

22 Q Okay. So Mr. Kimber, to follow up on that, could you
23 explain how the name "Free Tax USA" gives you an advantage for
24 specific search terms.

25 What are those terms?

1 A We make the assumption that many people looking to file
2 their taxes online are looking to do it at the lowest cost
3 possible, free. And when someone types in the words "free" and
4 "tax" in combination with other words, albeit "return" or "free
5 tax online" or various other combinations, we generally appear
6 in the top three natural hits on the resulting page.

7 Q Now, I understand that your company's sales and customer
8 information is confidential. We'll seal the courtroom and talk
9 in a little more detail about that later.

10 A Okay.

11 Q But in the public portion, I'd like to talk about your
12 growth rates, if that's okay.

13 A Uh-huh.

14 Q Could you please tell us your average growth rate for
15 taxpayers using your products over the past two years.

16 A We've seen the growth rate over the past two years be
17 roughly 30 percent.

18 Q And do you expect that growth rate to continue?

19 A We do.

20 Q And have you examined your growth rate in the postseason
21 since April 2011, since the close of tax season?

22 A We have.

23 Q And what was your growth rate since April 2011 of this
24 year?

25 A When we -- and it's roughly been a month that we looked at

1 that -- we have noticed a growth since April 20th of about
2 60 percent, as opposed to that same time period -- as compared
3 to that same time period last year.

4 Q And have you ever seen growth levels that high before?

5 A In the previous few years, we've noticed some growth, but
6 not as significant as a jump from roughly 30 to 60 percent that
7 we've seen this year.

8 Q Now, Mr. Kimber, in light of your growth rate, what efforts
9 have you undertaken to ensure that you're capable of continuing
10 to expand quickly?

11 A Ever since our first year in business, I've made it a
12 specific -- a personal goal, as well as a company goal, to
13 always evaluate the next year and the upcoming year and see what
14 percentage growth we expect and to have in place the hardware,
15 the bandwidth, and the software scalability to handle five to
16 seven times the traffic of what we expect.

17 Q So are you saying that for this coming year, you ensured
18 that TaxHawk would have enough infrastructure to support 5- to
19 700 percent of the customers that you expected?

20 A That's correct.

21 Q Okay. Mr. Kimber, turning more specifically to the
22 marketing techniques used by TaxHawk and, specifically, Free Tax
23 USA. You told us about the natural search functions and
24 innovations of Free tax USA.

25 What other types of advertising do you use?

1 A We send e-mails out to our existing customers and also allow
2 them the opportunity to refer their friends and family, if you
3 will, to our product. And we e-mail those individuals as well
4 with offers and incentives to come and use us as their tax
5 preparation site.

6 Q Okay. So in addition to natural search and e-mail
7 marketing, what other types of marketing do you engage in?

8 A We also use the idea of pay per click through Web site or
9 paid search engine traffic with several different major search
10 engines.

11 Q I'd like to get into that in a little more detail, but
12 before we do, I just want to make sure we've covered the other
13 types of marketing that your company engages in.

14 We have natural search, paid search, e-mail marketing.
15 Anything else?

16 A We have done other types of marketing in the past. We've
17 produced some radio ads in a local market in Utah. We've
18 produced several marketing videos that we've put on YouTube that
19 would present the idea that we'd like people to come and file
20 with us. Stop paying too much for taxes, come file with Free
21 Tax USA.

22 We also produced a TV ad that ran through Google TV earlier
23 this tax season.

24 Q Okay. Now, I'm going to take a little risk here. Well, let
25 me ask you a question. I'm going to ask you to explain the

1 difference between paid search and natural search.

2 In explaining that difference, would it be helpful for you
3 to actually have a screen showing a search engine?

4 A That would make it easier for me to show where on the page
5 the two different types of search appear through Google
6 specifically.

7 Q Okay. So I'm going to make an attempt here to be very
8 21st century.

9 Can you see that?

10 A Yes.

11 Q Okay. So this is Google, and I'm going to type in a search
12 "free tax return."

13 So have you seen this type of screen before?

14 A Yes. So at the top there and highlighted in tan or somewhat
15 of a yellowish-orange, are paid ads in the search engine. Those
16 are paid for positions, if you will, by bidding on those
17 keywords that were just typed in by you, the user.

18 The listings in white below that are what I would term
19 "organic listings" or "natural listings" that come based on the
20 search engine crawling many Web sites and ranking their
21 importance on various keywords.

22 Q Okay. So let's try to go in order. Let's try to finish up
23 on natural search first.

24 You told us about the use of your innovative name with
25 "free" and "tax." Does that -- well, let me take a step back.

1 It looks like your search results on "free tax return" were
2 pretty effective. Is that consistent with what you typically
3 see with searches with the terms "free" and "tax" in them?

4 A Generally. Any combination of those two with other words
5 will generally see us in the top three or at least on the first
6 page of the results, yes.

7 Q And is there anything in addition to having the words "free"
8 and "tax" in your name that you do to try to make sure that
9 you're in the top results for natural search?

10 A We both -- before the season ends, during the season, we'll
11 identify keywords that we want to target and produce pages that
12 are written towards and highlight those specific words that
13 we're looking to target.

14 And we refer to those as "organic landing pages," if you
15 will. That the search engine can crawl our Web site, find those
16 pages that may have the topic of tax deductions. And then when
17 those terms are typed in, the idea is that that page we've
18 specifically written on that topic of tax deductions will appear
19 in some of the top results.

20 Q Now, let's say -- do you pay anything to Google for these
21 natural search results?

22 A Not for the natural search ones, no.

23 Q So let's say all of a sudden a million new people found your
24 listing at Free Tax USA on natural search here at the bottom,
25 the second entry, and they all click through and purchased your

1 product.

2 Would you have to pay anything additional for those new
3 million customers?

4 A Not for the ones that would click on the link in white there
5 at the bottom of the screen, no.

6 Q So let's turn now to the portion in yellow at the top.

7 Could you tell us how -- is that the paid search section of
8 the page?

9 A That is.

10 Q Could you tell us how paid search works.

11 A So we, as a company, bid on those specific keywords, an
12 amount to be -- to appear when they're typed in -- when users
13 type them in so we can appear on the results. And that's
14 highlighted in orange.

15 And so every time a customer clicks through on that orange
16 link, we are charged a fee per click.

17 Q So on the orange section, if someone clicked on this and
18 went through to your Web site, you would pay a fee per click?

19 A Yes.

20 Q And how do you decide how much you're willing to bid for the
21 terms for paid search?

22 A We have internal discussions principally between Scott and
23 myself and a gentleman we've hired as a marketing director. And
24 those ideas or measurements or boundaries, if you will, are
25 fluctuated sometimes daily during the season where we're willing

1 to say, okay, I'll pay up to X amount on this keyword and if
2 we -- we monitor those closely, and if we see that they're
3 performing, we'll raise the amount we're willing to pay for
4 that. If they're not performing, we'll back off and focus our
5 efforts elsewhere.

6 Q Is there a concept called "return on investment"?

7 A Yes. That's what we're looking at basically is we -- as
8 someone clicks through, we're charged for that click. That
9 person may or may not end up paying us and filing their taxes
10 with us, but the idea is that a large enough percentage of them
11 will; that the return or the revenue we see from all those
12 people coming through paid search will be large enough to -- and
13 larger than the amount we're paying for those clicks.

14 Q Okay. So if I understand you correctly, you have a
15 calculation as to what revenue per click you're earning on
16 certain terms; is that right?

17 A That's correct.

18 Q And are you saying that when you bid on terms, how does that
19 compare to what your revenue per click or return on investment
20 is? How do you set that?

21 A Well, we want the return on investment to be as large as
22 possible. There isn't a set percentage. There are starting
23 points that we start out with on each different keyword. And
24 then we fluctuate those.

25 If it's growing fast enough and large enough, sometimes

1 we're willing to deal with a little bit less of a percentage of
2 return on investment than we would be if we're not throwing a
3 lot -- or throwing very little money at it.

4 Q So is it correct to say that, in general, if the amount
5 you're paying per click is below your return on investment or
6 revenue per click, then you're making money with every click?

7 A Yes.

8 Q So if you're satisfied with your pay-per-click costs, but
9 for some reason the number of clicks that you're getting has
10 increased beyond what you expected, is that a problem for you?

11 A We're prepared for the extra traffic. And it's not a
12 problem to increase our revenue, no, our return.

13 Q So just to take a hypothetical example, if you're satisfied
14 with your pay-per-click cost and your revenue-per-click earnings
15 and for some reason the market has changed and the amount of
16 clicks you get for your paid search doubles, is that going to
17 double your cost?

18 A It will double our cost.

19 Q Is that a problem for you?

20 A It's not a problem as long as the return on investment
21 continues to remain at or near what we're looking for.

22 Q So you have no problem expanding your pay-per-click expenses
23 as long as the revenue per click is still above the amount
24 you're paying on pay per click?

25 A That's correct.

1 Q Okay. Mr. Kimber, turning toward the competition, what
2 types of customers does Free Tax USA target?

3 A We consider all the American taxpayers, the American
4 taxpaying public, as our audience or our customers -- our
5 potential customers.

6 Q Do you consider people using pen and paper to do their taxes
7 potential customers of yours?

8 A I do.

9 Q Do you consider people who go to accountants potential
10 customers of yours?

11 A I do.

12 Q Are you aware of any advertisements made by Free Tax USA
13 that are seeking to draw customers currently going to a tax
14 store or an accountant?

15 A I would label a video we put on YouTube where we actually
16 shot -- used a high-powered rifle and blew a hole in an iPad and
17 filmed that with a high-speed camera. Basically, the title of
18 the ad was "Why Pay Too Much for Preparing Your Taxes" -- or
19 "Paying Too Much for Your Taxes is Like Throwing Money Away,"
20 which you'd be doing if you blew a hole in an iPad.

21 And in the marketing message that we had with that ad was
22 don't pay over a hundred dollars to file your taxes. You can
23 come and do your federal and your state for as little as \$10
24 with us.

25 Q And is it your view that the use of the term "\$100"

1 signifies something about who that ad was aimed at?

2 A It was aimed at people that would go into a storefront or to
3 an accountant and prepare their taxes -- or have their taxes
4 prepared.

5 Q Does Free Tax USA emphasize pricing in its marketing?

6 A We do.

7 Q What company do you believe has a pricing strategy that's
8 closest to yours?

9 A There are probably several that would be close to us. I
10 would label TaxSlayer, OnLine Taxes, TaxACT as some.

11 Q And why do you consider their pricing strategy to be similar
12 to TaxHawk's?

13 A I believe they fit into the same cost structure, I guess you
14 would say, where the federal return is free and you can get the
15 state for a low cost or what I view as low cost.

16 Q Do you believe that the pricing strategies that your company
17 has used have led to your company acquiring a customer base with
18 any particular preferences with respect to price?

19 A I believe our customers, as well as most of the taxpaying
20 Americans, want to get the best deal they can in preparing the
21 taxes. So free and low cost definitely attracts them.

22 Q Do you believe your customers are highly price sensitive?

23 A I believe they are price sensitive, yes.

24 Q And I think you said you saw TaxACT engage in similar
25 pricing strategies as your company?

1 A They are one of the companies I listed, yes.

2 Q Would you similarly expect that TaxACT customers are highly
3 price sensitive?

4 MR. BUTERMAN: Objection.

5 THE COURT: Sustained.

6 BY MR. SCOTT:

7 Q Do you have any reason to believe that TaxACT would have a
8 different type of customer base?

9 MR. BUTERMAN: Same objection, your Honor.

10 MR. SCOTT: I'm just asking if he has any reason to
11 believe that they're different.

12 MR. BUTERMAN: Your Honor, we have TaxACT witnesses on
13 the stand we can talk to. TaxACT customers, I don't know that
14 Mr. Kimber is the right person to be talking about that.

15 THE COURT: Yes, sustained.

16 BY MR. ROUSH:

17 Q Okay. Mr. Kimber, does everyone who uses Free Tax USA
18 choose to purchase a state return?

19 A Not everybody.

20 Q For customers that choose not to file a state return with
21 Free Tax USA, but they do file their federal forms through Free
22 Tax USA, what's your understanding in terms of how they may be
23 handling their state filing, if they have one?

24 A Yeah. For those that are required to file a state tax
25 return along with their federal and they choose not to do it

1 with us, I would assume that they're either printing out a form
2 from their state and filling it out by hand or --

3 MR. BUTERMAN: Move to strike, your Honor, as
4 speculation.

5 THE COURT: Overruled.

6 BY MR. SCOTT:

7 Q You can continue.

8 A -- or they would go to their -- that specific state's Web
9 site, many of which offer a means of filing your state return
10 directly with them for certain customers.

11 They could very well reenter all their federal information
12 in another piece of tax software as well and just to file the
13 state return, but those are some options that I would see.

14 Q If you raise your state price, would you be concerned that
15 the percentage of Free Tax USA customers paying for a state
16 filing would change?

17 A If we raised the price significantly, I would see probably
18 the significant loss in the customer base as well.

19 Q And would one of your concerns be that those customers
20 choosing not to file their state returns are doing it by hand?

21 A That would still remain one of the options I would see they
22 would have, yeah.

23 Q And would you be concerned about that?

24 A As concerned as any other option that they would have that
25 they'd be leaving us for.

1 Q Is that one reason you don't raise your state price?

2 A Yes.

3 Q Now, if your customers were to -- is the scope of your free
4 offering comparable to TaxACT's free offering, to your
5 knowledge?

6 A Yes. The free offering for the federal, yes.

7 Q Do H&R Block and Intuit also offer free products, to your
8 knowledge?

9 A They do.

10 Q And do their free products have the same capabilities as
11 yours?

12 A Not in our estimation.

13 Q And how are their free products less capable?

14 A One of the products is basically a 1040EZ. The 1040EZ is
15 free. If you need more features or different forms, than you
16 need to upgrade or choose different software.

17 The other one of those two companies allows the filing of a
18 1040 with limited types of income, but if you get into
19 investment income, stock sales, business income on a Schedule C
20 or other things of that level, you're forced to upgrade to a
21 different product in order to file that type of a return.

22 Q And what about the state prices offered by TurboTax and
23 H&R Block? Do you know how they compare to yours?

24 A Currently, they are both somewhere around \$30 -- \$30.95 or
25 29.95 -- in order to prepare and file the state return.

1 Q Could you remind us of what the Free Tax USA state price is.

2 A 9.95. About a third.

3 Q Now, Mr. Kimber, let's hypothesize that for some reason you
4 chose to raise your state price from 9.95 to 12.95.

5 Would you be concerned that your customers would switch to a
6 competitor?

7 A I honestly -- with that level of increase, we have done that
8 on another one of our Web sites, TaxACT -- or TaxHawk, as I
9 mentioned earlier, and have not seen ill effects. But that
10 would be a concern.

11 Again, it's the magnitude of the increase. I know that we
12 purposely placed our price in single digit pricing below \$10 for
13 a reason and a basic marketing reason; that people tend to buy
14 things that are less than \$10 more rapidly. And so increasing
15 it by 2- to \$3, I don't know what specific effects that would
16 have, but that is a concern that I would have is that, yeah, we
17 would lose customers by raising the price.

18 Q And if you lost customers to other digital providers, which
19 customers do you think you'd be more -- which competitors do you
20 think you'd be most likely to lose customers to?

21 A With the price sensitivity that I've felt that our users
22 have, I would -- and with my experience, I'd believe that if we
23 raised our price significantly, they would look for the next
24 cheapest and best option. Evaluating not only on price, but on
25 quality of the software, but they would go to something that was

1 at least what we were charging before.

2 Q And can you give us examples of companies who have products
3 in that range.

4 A Oh, it would be companies similar to the ones I mentioned
5 earlier; the TaxACT, TaxSlayer, OnLine Taxes, as well as several
6 others.

7 Q And would it be similar if you raised the price of your
8 deluxe product? What competitors would you be concerned about?

9 What digital competitors would you be concerned about losing
10 customers to if you raise the price of your deluxe product?

11 A Probably those same -- it would be those same companies that
12 I just mentioned.

13 Q You consider TaxACT to be more innovative than your company
14 in the current marketplace?

15 A No.

16 Q Is TaxACT's product better than yours?

17 A I don't believe it is, no.

18 Q Does TaxACT have lower prices than TaxHawk?

19 A Not in our evaluation of the prices, no.

20 Q Can you give me some specific examples where your prices are
21 lower than TaxACT's prices.

22 A We can file the federal and state tax return for 9.95. And
23 I'm going on recollection. There's a charge for adding your
24 state on to your free federal with TaxACT, as well as an
25 E-filing charge. You can print it and file that way -- file by

1 paper for free -- but then there is an additional E-filing
2 charge that we include in our price.

3 So after that charge is added on, I don't remember
4 specifically the amount but we we're still less.

5 Q What about your state tax filings? Could you tell us if
6 there's a way to -- I think you talked about this before but
7 just for clarification, is there a way to file your state taxes
8 for less on TaxHawk than is available on TaxACT's Web site?

9 A Yes. Well, if you have an AGI of 20,000 or less and you go
10 to our TaxHawk.com Web site, you can actually get the state tax
11 return along with your federal tax return both for free.

12 Q Okay. Mr. Kimber, have you heard about the proposed
13 transaction between H&R Block and TaxACT?

14 A I have.

15 Q And have you been made aware that the Department of Justice
16 in this case is concerned about the effect that the acquisition
17 could have on the competitiveness of the TaxACT product?

18 A Yes, I'm aware of that.

19 Q Post-transaction, could customers unhappy with changes in
20 the TaxACT product or pricing use your product instead?

21 A We believe they could, yes.

22 Q And if that generated a lot of business for Free Tax USA,
23 would your servers be able to handle it?

24 A Yes.

25 Q How much would your business be able to expand in the first

1 year? What would your infrastructure support?

2 A With our initial setup, we would be able to handle five to
3 seven times the traffic that we anticipate for that year. That
4 being said, we view our company as agile and able to quickly
5 react as well and could put things in place if we saw those
6 trends coming to handle even more than that.

7 Q And what about your cost-per-click advertising? What if the
8 number of clicks you got doubled or tripled? Would you be
9 willing to pay for the additional clicks as long as it stayed
10 under your return on investment?

11 A As long as the return on investment was continuing, yes.

12 Q And if disappointed -- if all of a sudden there was a change
13 in the market and your return on investment, your revenue per
14 click improved, would you be willing to increase the amount that
15 you pay per click to search engines now?

16 A Yeah. That would be part of our evaluation as we went
17 along, yes. We would evaluate that and as long as the return on
18 investment continued to be consistent or at the level that we
19 were expecting, we would increase.

20 Q And if -- let's hypothesize that the TaxACT price went up or
21 the scope of the TaxACT free offering were reduced.

22 Would you consider emphasizing that in your advertising?

23 A I would consider that, yes.

24 Q And could you show us on the Web page where you're able to
25 advertise for paid search.

1 Is there somewhere you could emphasize that in your paid
2 search advertising?

3 A Well, as you noticed in the paid ad there, the title "Free
4 Tax USA," that's the official site. "100 percent free tax
5 preparation." I can use as much of that title or the words
6 where we have stated, "Start your 2010 IRS tax return."

7 I can place verbiage in there to describe or to be more
8 detailed why they should come. We're easy to use. We're the
9 cheapest one out there. We're the only one offering a free
10 state. Whatever we choose to do, we can emphasize there.

11 Q And would you be willing -- would you consider changing the
12 emphasis in your paid search advertisings if there were a new
13 opportunity that arose as a result of this transaction?

14 A We would -- we'd evaluate any opportunity that presented
15 itself. We would -- we'd consider doing what we needed to to
16 highlight our strengths, if you will. Shine a flashlight on
17 where we believe we're strong and we have the best position and
18 go from there.

19 Q Now, do you believe that TaxACT customers dissatisfied with
20 post-merger pricing would be responsive to advertising by you
21 that emphasized your company's superior pricing?

22 MR. BUTERMAN: Objection, your Honor.

23 MR. WAYLAND: Your Honor, I'm asking him what he
24 believes and not for the truth of the matter. I'm just asking
25 as a basis for what he would do.

1 THE COURT: It's overruled. You may answer.

2 BY THE WITNESS:

3 A Could you restate the question.

4 Q Sure.

5 Do you believe that TaxACT customers dissatisfied with
6 post-merger pricing would be responsive to advertising by you
7 that emphasized your company's superior pricing?

8 A That would be our reasoning behind doing the advertising is
9 we would feel that they're going to be responsive to it, yes.

10 Q And do you think that TaxACT customers -- let me rephrase.

11 In forming your competitive response to TaxACT, would you be
12 assuming that your company had a better or worse chance of
13 acquiring dissatisfied TaxACT customers as a result of a price
14 increase than another company like H&R Block?

15 MR. BUTERMAN: Objection.

16 THE COURT: If you understand that question, you may
17 answer.

18 MR. STOCK: Let me rephrase, your Honor.

19 BY MR. STOCK:

20 Q And I'm asking you in connection with -- is your perception
21 of what TaxACT customers would do relevant to the business
22 decisions that you made -- that you make?

23 A Is my perception of what those customers would do in a
24 hypothetical case?

25 Q Is it relevant to whether you would invest in advertising?

1 A It would place a role, yeah, it would be relevant. It
2 wouldn't be the only thing, but it would be relevant.

3 Q So in making that decision, if TaxACT customers were
4 disappointed in a price increase, what would be the assumptions
5 that you would make in terms of whether those customers would be
6 likely to come to your company in response to price advertising
7 as compared to going to a company like H&R Block?

8 MR. BUTERMAN: Objection.

9 THE COURT: Overruled.

10 BY THE WITNESS:

11 A My assumptions would be the same that I basically stated
12 earlier. That the consumer would want to maintain the service
13 level for the price that they've been paying. They don't want
14 to pay more. And so they would look at us as an option because
15 we would be better priced.

16 Q Thank you.

17 MR. STOCK: Your Honor, I have a couple more questions,
18 and unfortunately they're of a confidential nature.

19 THE COURT: Can I just ask you a couple questions.

20 Have you done an analysis or an explanation for why you
21 had 60 percent growth in the last tax season?

22 THE WITNESS: We haven't done that at this time.

23 THE COURT: So you don't know why?

24 THE WITNESS: We don't have a complete answer, no.

25 We're going to do that, but we haven't at this point.

1 THE COURT: Right. So you don't know right now whether
2 it's because you've got the lowest price on the market?

3 THE WITNESS: My assumption is that that has a lot to
4 do with it, but, yeah, I don't know that for a fact.

5 THE COURT: And do you try and migrate customers from
6 one product to another, for example, from Free Tax USA to
7 TaxHawk?

8 THE WITNESS: No. As we do the marketing, we try not
9 to cannibalize or steal from our own customers -- or in those
10 words. We market Free Tax USA, for example, through pay per
11 click and organic search, and it is the Web site that's linked
12 from the IRS free file page.

13 TaxHawk.com we market with the different states because
14 it has a strength of having a free state return and so the
15 different State Departments of Revenue all link to us. And the
16 keywords we choose to target pay per clickwise have to do with
17 free states and the strengths that TaxHawk has.

18 THE COURT: And are you basically offering the same
19 product on those two sites or are there different feature
20 differences that you get for free versus what you pay for?

21 THE WITNESS: There is not any difference in the
22 features. That you have the ability and the types of data that
23 you can enter on TaxHawk.com versus Free Tax USA, is the same
24 both federally and for the state.

25 THE COURT: And in your deluxe product, do you offer

1 that through both Free Tax USA as well as TaxHawk?

2 THE WITNESS: We don't. That is one difference. We
3 offer the deluxe through Free Tax USA only.

4 THE COURT: Only. Not through TaxHawk?

5 THE WITNESS: Not through TaxHawk.

6 THE COURT: And is one of the features that you offer
7 through your deluxe product the ability to import your data from
8 the prior year? Were you able to do that --

9 THE WITNESS: You're able to do that with our basic
10 service, if you will.

11 THE COURT: And the basic service is free?

12 THE WITNESS: Yes. If you prepared with us last year
13 and you log in with your user name and password that you used
14 the previous year, your data is automatically rolled forward.
15 So as long as they've used us consistently, that data can be
16 rolled forward year after year.

17 THE COURT: And do you know how many other free
18 products are available for tax preparation that allow the free
19 import of data from one year to the next without paying for an
20 upgrade?

21 THE WITNESS: We're not aware of any.

22 THE COURT: Are you the only one that you're aware of?

23 THE WITNESS: In our investigation, yes.

24 THE COURT: Okay. Thank you.

25 MR. STOCK: Thank you, your Honor. I believe we'll

1 have to close the courtroom at this time.

2 THE COURT: Can I just stop for one second.

3 Mr. Buterman, are there any portions of your redirect
4 that you can do in open session before we go to closed session?

5 MR. BUTERMAN: I believe that I can, your Honor.

6 THE COURT: If you don't mind, Mr. Stock, could we do
7 that to keep as much in the public arena as possible?

8 MR. STOCK: That would be fine, your Honor.

9 CROSS-EXAMINATION

10 BY MR. BUTERMAN:

11 Q Good morning, Mr. Kimber.

12 A Good morning.

13 Q I just want to pick up on a question that the Judge just
14 asked you a minute ago. I want to make sure we're all clear.

15 None of your products allow for the importation of data from
16 another company, correct?

17 A That's correct. Unless you're talking about the -- yeah, it
18 would be the user importing his own data looking at a previous
19 year's tax return and entering into ours as the basic
20 information of the W-2 and the types of income he had.

21 But no, we don't allow for importing from another tax
22 software.

23 Q And you're aware that companies such as TaxACT, H&R Block,
24 and TurboTax do offer PDF imports or other types of imports that
25 allow customers who had used a different program in a prior year

1 to import their data into their softwares, correct?

2 A Yes, I'm aware of that.

3 Q And just so we're clear, none of the TaxHawk Web sites offer
4 that?

5 A That's correct.

6 Q Now, I'm hoping -- I wanted to begin today by just clearing
7 up one issue that I believe there might be some confusion on.

8 Now, I know you weren't in the Court last week, but Mr. Dunn
9 was here and he testified repeatedly that both TaxACT and Free
10 Tax USA's free edition support all federal IRS forms.

11 That is incorrect, true?

12 A All federal IRS forms that the IRS accepts to be filed.

13 Q Let me ask it differently.

14 A Okay.

15 Q It's true that TaxHawk does not support all federal forms,
16 correct?

17 A That's correct.

18 Q In fact, none of the TaxHawk Web sites support all federal
19 forms even in paid versions, correct?

20 A That's correct.

21 Q And TaxHawk has never supported all federal forms?

22 A That's correct.

23 Q Okay. And I believe you mentioned it earlier. There are
24 54 forms -- federal forms -- that TaxHawk supports?

25 A That's the number I last counted, yes.

1 Q Now, Mr. Stock also spoke with you regarding the states that
2 TaxHawk covers and does not cover. It's true that TaxHawk does
3 not provide support for all of the forms in the states for which
4 it does provide functionality, correct?

5 A We do not support every form for each of the states, that's
6 correct. We support the ones we essentially deemed as giving us
7 large enough coverage for that state.

8 Q And among the forms for which TaxHawk provides no support
9 for the majority of states, are non-year resident and part-year
10 resident income tax filers, correct?

11 A That's correct.

12 Q TaxHawk is looking into the possibility of adding support
13 for those forms, correct?

14 A We are.

15 Q Do you have an estimate of how long it would take you to add
16 support for those forms?

17 A Our current idea is the next two to three years.

18 Q And in addition to -- and in addition, TaxHawk doesn't
19 support forms for cities that have income tax requirements,
20 correct?

21 A That's correct.

22 Q And what cities are you aware of that don't -- that do have
23 income tax requirements?

24 A I believe there are some in the state of New York, the city
25 of New York. I believe there's some in Michigan. And those are

1 some basic ones I'm aware of.

2 Having not delved into that area as a company, not
3 particularly -- I don't have a lot of knowledge on that right
4 now.

5 Q And so it's your understanding that both New York City and
6 Detroit are two of the cities that have income tax -- city
7 income tax requirements?

8 A That's my understanding.

9 Q Do you have an estimate of how long it would take TaxACT to
10 support all the forms, if it wanted to?

11 A TaxACT?

12 Q Excuse me. TaxHawk.

13 A We would probably take ten years or so to put that -- to put
14 all those into place. I would qualify that by saying because
15 that's what we want to do. We're a -- I like to call us a
16 "lifestyle" company. We like the lifestyle we have as owners.
17 We want our employees to have a life, if you will.

18 I do feel we have the expertise to do that more rapidly but
19 we choose not to.

20 Q Now, moving away from the forms, TaxHawk does not currently
21 offer its digital self-preparation tax product to software that
22 an individual can download and install on a personal computer,
23 correct?

24 A That's correct.

25 Q And TaxHawk has never seriously considering -- has never

1 seriously considered offering that capability?

2 A We've spoken about it, but determined in our -- internally,
3 that it doesn't make sense for us.

4 Q And one of the reasons that you've determined that that
5 doesn't make sense is because it would require significant work
6 and expenses given the type of software code that your tax
7 engine is built on, correct?

8 A Correct. It would take more work than we deem worth it, I
9 guess you could say.

10 Q And it would also require you to redesign your method of
11 data storage, correct?

12 A That is correct, yes.

13 Q And TaxACT does not have a version of its product that
14 people can buy in a detail store such as Staples or Best Buy,
15 correct?

16 A No. It's a no-box product, no.

17 Q TaxHawk does not provide any face-to-face support,
18 correct?

19 A Walk in? You mean, walk into our company and sit down face
20 to face with somebody?

21 Q Well, what I mean is -- yes.

22 A No.

23 Q And TaxHawk does not provide any phone support, correct?

24 A No. We've talked about that idea and tabled it at this
25 point.

1 Q Okay. In fact, the only support that TaxHawk provides for
2 its customers is e-mail support, correct?

3 A That is. And along those lines, we feel we have some of the
4 best in the business so ...

5 Q And the e-mail support that we're talking about is not tax
6 advice, is it?

7 A It is not. It's technical support regarding application.

8 Q In other words, TaxHawk does not provide any tax advice or
9 support in connection with any of its products, correct?

10 A That's correct. Other than to -- somebody writes in and
11 says I have such and such a form that I need to enter into my
12 taxes, where do I do that? Not, with this information, do I
13 qualify for such and such a credit? We don't answer those types
14 of questions.

15 Q And besides offering printed and bound tax returns, TaxHawk
16 does not offer any related products or services, correct?

17 A Related to?

18 Q Any other products or services.

19 A No. We have the state return, the deluxe product, and the
20 printed and bound.

21 Q For example, TaxHawk does not offer any refund anticipation
22 checks, correct?

23 A No.

24 Q Now, we talked about TaxHawk's inability to import data from
25 a prior return that someone did using a different product.

1 What about does TaxHawk allow for importation of W-2s or
2 1099s?

3 A Importation from the physical form?

4 Q Importation of data from financial services companies or the
5 like.

6 A We do not at this time, no.

7 Q And you're aware that TaxACT, H&R Block and TurboTax all
8 offer some form of that functionality?

9 A Yes.

10 Q Now, it's your understanding that TaxHawk sales are much
11 smaller than those of H&R Block, TaxACT, and Intuit, correct?

12 A We are -- we have less of a percentage of the market, yes.

13 Q And you sometimes refer to those companies as the "big
14 three"?

15 A We have.

16 Q In setting TaxHawk's prices, TaxHawk does not take into
17 account the prices of CPAs or brick-and-mortar tax preparation
18 businesses, correct?

19 A Yeah. In setting our own prices, no, we don't care whether
20 they're increasing their prices or not.

21 Q And isn't it true that you believe that very few of
22 TaxHawk's customers compare its products to those of CPAs or
23 brick-and-mortar assisted shops?

24 A That's correct, to the point that unless somebody -- if a
25 customer going to a brick-and-mortar shop becomes disenchanted

1 with the service they're getting or the price they're paying, I
2 think that opens us up as an option to them.

3 But in someone shopping that's already at a -- with an
4 accountant, unless given a reason to look elsewhere, I don't
5 believe they're going to go looking because they're satisfied
6 where they're at.

7 Q Now, Mr. Kimber, in addition to pricing, do you believe that
8 reputation, trust, and brand recognition are among the most
9 important factors in growing the market share in the digital tax
10 preparation business?

11 A I do.

12 Q And with respect to reputation, trust, and brand
13 recognition, you believe those factors pose a significant
14 challenge for any digital do-it-yourself tax preparation
15 business seeking to expand, correct?

16 A When you're beginning the business just starting out, yes.

17 Q And you believe that in order to substantially increase
18 customers, digital do-it-yourself companies must build a strong
19 reputation through word-of-mouth referrals, correct?

20 A We have done that.

21 Q And it's very challenging for a digital do-it-yourself tax
22 preparation business to build a strong reputation through word
23 of mouth if its existing customer base is small, correct?

24 A Through word of mouth, if you start small, you've got very
25 few people to refer others do. That would be the case.

1 Q And you believe that as a result, it can be difficult for a
2 digital do-it-yourself tax business to quickly expand its market
3 share, correct?

4 A Unless they look at options such as pay per click and other
5 options of marketing out there, yes.

6 Q Mr. Kimber, TaxHawk was an original member of the FFA, was
7 it not?

8 A We are.

9 Q And TaxHawk's membership in the FFA contributed to its
10 growth over the past eight years, correct?

11 A It has been one of the contributing factors, yes.

12 Q And you believe that the effectiveness of the FFA in terms
13 of growing TaxHawk's customer base has diminished in recent
14 years, correct?

15 A It has decreased naturally over the years, yes. As we
16 received them as a customer, for example, then they become our
17 customer and we market to them and bring them back year after
18 year.

19 Q Now, Mr. Stock showed you a screenshot from Google earlier,
20 and in that screenshot you were pretty high up in both paid and
21 natural search, were you not?

22 A Yes.

23 Q And in paid, it was actually just your company and
24 TurboTax's that were listed, correct?

25 A Uh-huh, that's correct.

1 Q And I believe you said you were within the top three in
2 natural search?

3 A Yeah. We were listed -- on that particular example, we were
4 listed number two behind the IRS free file page.

5 Q And I believe you testified a few moments ago that you
6 believe that TaxHawk is just as innovative as TaxACT; is that
7 correct?

8 A I believe we are, yes.

9 Q And that TaxHawk's product is just as good as TaxACT's?

10 A I believe it is, yes.

11 Q Okay. And in terms of the number of people who use your
12 product versus TaxACT's, TaxACT is several times larger than
13 yours, correct?

14 A They are. They have more customer base, yes.

15 Q And I believe you mentioned a few moments ago that you have
16 all this excess capacity currently; is that correct?

17 A We do.

18 Q Why aren't you bigger?

19 A Again, in my opinion, since -- when TaxACT was started, it
20 was my understanding that they began their company with a
21 somewhat complete product, if you will, a support for most, if
22 not all, of the states and many of the federal forms.

23 Where when we began our company in the 2002 filing season --
24 tax year 2001 -- we started with a simple 1040EZ. The next year
25 we had a 1040EZ, a 1040A, and a full 1040 with very few attached

1 schedules. And the years since then have added states in
2 different increments up to the point that we have now where we
3 have had a full product -- in our definition of a full
4 product -- for the past two to three seasons.

5 Q And so despite starting in 2002, your overall market share
6 of the total number of E-filers has not significantly increased,
7 has it?

8 A Over the past ten years?

9 Q Yeah.

10 A Oh, it has significantly.

11 Q Where was it in, say, 2006?

12 MR. STOCK: I just want to note that TaxHawk considers
13 its numbers of customers to be confidential. So to the extent
14 that Mr. Buterman is going to go into market shares, that could
15 divulge a number of customers. We just want the witness'
16 confidentiality rights to be respected.

17 THE COURT: Is this an area we can cover in the closed
18 session?

19 MR. BUTERMAN: We can cover it, although I will note,
20 your Honor, that the document that we plan to use is a document
21 that's already been shown to the public. I'm happy to do it,
22 though, in the closed session.

23 THE COURT: Okay. Is this an appropriate time then to
24 close the courtroom?

25 MR. WAYLAND: Yes.

1 MR. STOCK: We have no objection to closing the
2 courtroom. I do have some redirect to the form coverage that I
3 can do now if you prefer.

4 THE COURT: I would so that once we get to the closed
5 session, after the closed session, this witness can be excused.

6 REDIRECT EXAMINATION

7 BY MR. SCOTT:

8 Q Mr. Kimber, do you feel that the federal and state forms
9 that your product covered are sufficient to make you a
10 significant competitor?

11 A I do.

12 Q And if any of the forms in question you felt were critical
13 to have on short notice, is there any that you think it would
14 take you more than a year or two to put in place?

15 A At one or two or three at a time, no. And I emphasize
16 maintain the lifestyle that we prefer as a company for us and
17 our employees.

18 Q And Mr. Buterman pointed out that your free offering doesn't
19 cover every single federal tax form; is that right?

20 A That's correct.

21 Q But is it correct that you testified -- well, why don't you
22 repeat for the Court.

23 For the federal tax forms that your product does cover, what
24 percentage of taxpayers do you believe that is sufficient to
25 satisfy?

1 A In our calculations, it covers over 95 percent of the
2 American taxpaying public.

3 Q And what if I asked you -- what if I changed the question
4 and said what percentage of taxpayers that are eligible to
5 E-file their taxes, what percentage of those taxpayers do you
6 think are covered by the forms that your product covers?

7 A I think that would increase it by a percentage or two.
8 Probably up near 97 percent.

9 Q And do you feel that -- do you believe that your products'
10 coverages in the states where it is present covers the vast
11 majority of taxpayers in those states?

12 A I do.

13 THE COURT: Can I just follow up on this just so I'm
14 clear.

15 Are there some forms that the IRS allows to be E-filed
16 federally that you just don't support? And if so, what is that
17 for or forms?

18 THE WITNESS: One, for example, is a form -- I hope I
19 get the number right -- I think it's 1310, which is a support
20 for deceased taxpayers. Filing the final return for a deceased
21 person. We don't support that at this moment in time. And it
22 can be E-filed.

23 So that's one example. There are others.

24 BY MR. SCOTT:

25 Q And do you have a sense as to what percentage of American

1 taxpayers use that form?

2 A Use that form in particular?

3 Q Yes.

4 A I don't have that form, but it would be with the other
5 forms, less than 5 percent.

6 Q Less than 5 percent for the forms collectively that you
7 don't cover?

8 A Right.

9 Q Right. Now, Mr. Buterman asked you -- I believe he asked
10 you if you have a small market share, if it's difficult to
11 expand. And I believe you answered that, yes, with word of
12 mouth it's difficult to expand if you have a small market share.

13 Do you believe your company has a small market share?

14 A I don't view our company as having a small market share.

15 Q Do you view your company as having a significant market
16 share?

17 A I do.

18 Q Now, Mr. Buterman asked you if you'd take into account the
19 pricing of brick-and-mortar assisted prices when you set your
20 price.

21 Do you remember that?

22 A Yes.

23 Q And I believe you said that you don't take those prices into
24 account?

25 A No.

1 Q In fact, I believe you said that if those prices are
2 increasing, that doesn't affect your price?

3 A That's correct.

4 Q Now, are you aware of the prices for the paid products of
5 H&R Block and Intuit?

6 A Roughly, yes.

7 Q And do you know if those prices have been increasing over
8 the past several years?

9 A When we've taken the time to look at that or monitor it, if
10 you will, we've noticed that they have increased.

11 Q And have those price increases had a material impact on the
12 prices that you charge?

13 A It has not. We view that as an internal decision and don't
14 really base it on what they're doing.

15 Q In fact, have your prices changed during the time period
16 that -- have the prices on Free Tax USA changed during the time
17 period that -- let's say in the past five years?

18 A No, they haven't. They've remained the same.

19 THE COURT: Is that the same for TaxHawk or have your
20 prices for TaxHawk changed?

21 THE WITNESS: TaxHawk, we -- I don't want to say the
22 year that we did, but several years ago we increased it to 12.95
23 for the state return. And that was the same time that we
24 brought in the free state/free federal combination offer for
25 those under 20,000.

1 BY MR. SCOTT:

2 Q Was that price change influenced by the prices set by Intuit
3 or H&R Block?

4 A No. It was an experiment or an idea we wanted to try.

5 MR. STOCK: We can go into closed session, your
6 Honor.

7 THE COURT: We will close the courtroom.

8 I'd ask counsel for both sides to look at everybody who
9 remains in the spectator portion of the courtroom to let me know
10 if you recognize these people and are they appropriate to
11 remain.

12 MR. ROBERTSON: Yes, your Honor. Everybody on this
13 side is okay; meaning, the left side of the courtroom as I face
14 the front.

15 THE COURT: I understand.

16 Mr. Buterman.

17 MR. BUTERMAN: Everyone on this side is fine, your
18 Honor.

19 THE COURT: Okay. The courtroom's now sealed. And
20 this portion of the record will be sealed.

21 MR. STOCK: Your Honor, I have one question that I may
22 have forgotten to ask that is unconfidential. Do you mind if I
23 just ask and we can unseal that?

24 THE COURT: Yes, it's fine.

25 BY MR. SCOTT:

1 Q Mr. Kimber, when you offered in tax year 2003 a free federal
2 product, do you remember if you had any AGI limitations in
3 2003?

4 A Tax year 2003?

5 Q Right.

6 A I believe that was the year we had an AGI of 30,000 or
7 less.

8 Q If I'm right, I think you said in 2002 you said you had
9 30,000 less.

10 A Calendar year 2003, that's correct. Tax year 2002 is where
11 we had a limit of 30,000 or less. In 2004 and 2005, we offered
12 it free to everybody based on the state of residence.

13 Q And that's tax year 2003 and tax year 2004, correct?

14 A That's correct.

15 MR. BUTERMAN: Your Honor, may I just redirect the
16 witness on that one question?

17 THE COURT: I have to make sure I understand this.

18 In tax year '04 and '05, you offered free federal to
19 only taxpayers from 14 states?

20 THE WITNESS: Yes.

21 THE COURT: And was that free federal and state or just
22 free federal?

23 THE WITNESS: Just free federal.

24 THE COURT: Okay.

25 THE WITNESS: And that was tax year 2003. And in '04,

1 that was increased to 26 states.

2 THE COURT: I see.

3 THE WITNESS: Residents of 26 states.

4 THE COURT: Okay. And then in '04, that was increased
5 to 26 states?

6 THE WITNESS: Yes.

7 THE COURT: And what about in '05? Did you also
8 increase the number of states?

9 THE WITNESS: We did increase the number of states.
10 That was a year that the Free File Alliance introduced as, for
11 lack of a better word, mandated by the IRS, an AGI limit for all
12 companies to observe. And I believe that year it was, I want to
13 say, 50,000 or close to that is when AGI was 50,000 or less, and
14 then residents of, I believe it was, up to 31 states that we
15 supported that year.

16 THE COURT: So in '05, you offered free tax preparation
17 and filing to taxpayers in 31 states but who also met the IRS
18 FFA AGI limit?

19 THE WITNESS: That's correct.

20 MR. STOCK: Could I clarify one thing about that, your
21 Honor?

22 THE COURT: Yes, please.

23 BY MR. ROUSH:

24 Q Is that on the Free Tax USA Web site?

25 A That is on the Free Tax USA Web site.

1 Q In tax year 2005, did you have a free for all, no AGI
2 limitation on any of your other Web sites?

3 A We did on several other Web sites.

4 Q And when you offered free for all with no AGI limitation in
5 tax year 2003, whose idea was that?

6 A That was mine and Scott's.

7 RE CROSS-EXAMINATION

8 BY MR. BUTERMAN:

9 Q Just one point of clarification. It wasn't until TaxACT
10 went free for all that TaxHawk went free for all on the Free Tax
11 USA site, correct? It wasn't until after?

12 A That we went --

13 Q Went free for all with no AGI limitations and no state
14 limitations.

15 A And free AGI and no state limitations would have been in
16 2000 -- that would have been the 2009 tax year, yeah. So it was
17 after --

18 Q Thank you.

19 A -- on Free Tax USA.

20 FURTHER REDIRECT EXAMINATION

21 BY MR. SCOTT:

22 Q And to be clear about the state limitations you had, you
23 offered that free for all in every state for which you had a
24 product; is that right?

25 A Yeah. And some additional ones, yeah.

1 MR. SCOTT: Okay. On to the actual confidential
2 portion. I believe that everything above what we just talked
3 about can be unsealed.

4 THE COURT: So for purposes of the record and the court
5 reporter, we are now sealing the record.

6 (The following portions, pages 62-68, were designated as
7 confidential/attorneys' eyes only and sealed under a
8 separate transcript per order of the Court.)

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1 THE COURT: Mr. Roush, are you doing the next witness
2 for the defendants?

3 MR. ROUSH: Yes, your Honor.

4 THE COURT: And who might that be?

5 MR. ROUSH: Defendants call Brian Rhodes to the stand.

6 THE COURT: Good morning, Mr. Rhodes.

7 (WHEREUPON, the witness was sworn.)

8 JAMES BRIAN RHODES,
9 called as a witness herein, having been first duly sworn, was
10 examined and testified as follow:

11 DIRECT EXAMINATION

12 BY MR. ROUSH:

13 Q Good morning, Mr. Rhodes.

14 A Good morning.

15 Q Can you please state your full name and current employer for
16 the Court.

17 A James Brian Rhodes. My current employer is TaxSlayer, a
18 subsidiary of Rhodes Financial Services.

19 Q What is Rhodes Financial Services?

20 A It is the parent company of TaxSlayer.com, of TaxSlayer Pro,
21 of Rhodes Murphy, of a couple different land development
22 companies, and also some insurance and investment companies.

23 Q And where is Rhodes Financial Services located?

24 A Out of Evans, Georgia.

25 Q And where is TaxSlayer.com located?

1 A Out of Evans.

2 Q What line of business is TaxSlayer engaged?

3 A We offer online tax preparation.

4 Q What is your current position at TaxSlayer?

5 A The product manager.

6 Q How long have you been in that position?

7 A Six years.

8 Q What, generally, are your responsibilities and duties as
9 product manager at TaxSlayer?

10 A I oversee the day-to-day operations of product development
11 along with support.

12 Q Are you involved in the strategic planning for TaxSlayer?

13 A I am.

14 Q And are you involved in marketing strategy for TaxSlayer?

15 A I am.

16 Q What previous positions, if any, have you held while at
17 TaxSlayer or Rhodes?

18 A I was a software consultant for TaxSlayer Pro, our
19 professional software. I also prepared taxes for Rhodes Murphy
20 in our retail offices.

21 Q What is TaxSlayer Pro?

22 A It is a tax professional software that we sell to
23 accountants across the country that was started in the early
24 '90s.

25 Q When you say it's a tax professional software across the

1 country, who are its customers?

2 A Accountants, CPA, anybody who would assist an individual
3 preparing their tax return.

4 Q And how, if at all, is TaxSlayer Pro related to
5 TaxSlayer.com?

6 A It is the backbone for the tax calculation engine.

7 Q And how long has TaxSlayer Pro been in business?

8 A Since '92.

9 Q And how long has TaxSlayer.com been in business?

10 A 2003.

11 Q If you want to grab a glass of water, go ahead.

12 A Please.

13 Q I think you mentioned Rhodes Murphy.

14 What is Rhodes Murphy?

15 A We have 16 retail offices across the Augusta area --
16 Augusta, Georgia area -- where we assist individuals in
17 preparing their tax returns.

18 Q And are all 16 of those tax preparation stores owned by
19 Rhodes Financial?

20 A There are ten company owned and 16 -- excuse me; six
21 franchises.

22 Q For clarity of the record, can we use the term "TaxSlayer
23 Pro" to refer to TaxSlayer Pro, but just say "TaxSlayer" when
24 referring to TaxSlayer.com?

25 A Absolutely.

1 Q What basic consumer tax prep products did TaxSlayer offer in
2 tax season 2011?

3 A We had three different offers; classic -- our classic
4 package -- our free edition, and our premium edition.

5 Q What was the range of prices for those three products?

6 A The free edition consisted of a free federal tax return if
7 you qualified for the federal 1040EZ, with a 14.90 state charge.
8 The classic package was a 9.95 charge for the federal, and a
9 4.95 charge for the state. And the premium was a 19.95 charge
10 for the federal, and a 4.95 charge for the state.

11 Q So ranging between free and 24.90?

12 A Roughly.

13 Q Did TaxSlayer experiment with any new products last year?

14 A We did. We -- towards the end of tax season around the
15 beginning of April, we released a "call a tax professional" for
16 very few users. We wanted to get an idea of what kind of calls
17 we would be receiving, how long those calls would take.

18 We also offered a different mechanism for individuals to pay
19 for their tax prep fee coming out of their refund.

20 Q And the "call a tax preparer" product, who are the tax
21 preparers that customers called?

22 A This year they were just internal accountants that we have,
23 but basically right now we're deciding whether we use our Rhodes
24 Murphy offices to facilitate that, or do we use our users of our
25 TaxSlayer Pro software.

1 THE COURT: Can I interrupt just one second.

2 Are you the Rhodes of Mr. Rhodes in the Rhodes Murphy
3 retail outlets?

4 THE WITNESS: I'm a son, yes.

5 THE COURT: The son. I just wanted clarify that.
6 Thank you. I was curious about that.

7 BY MR. ROUSH:

8 Q And that hybrid product, will you offer that next year?

9 A We will.

10 Q Now, I'll get into numbers in the closed session so I'm
11 going to ask you some general questions, and let's avoid the
12 numbers until we do go into a closed session.

13 A Okay.

14 Q Can you tell the Court generally whether TaxSlayer has grown
15 in revenue since it first started.

16 A We have.

17 Q And did TaxSlayer grow in revenue from tax season 2010 to
18 tax season 2011?

19 A We did.

20 Q Has TaxSlayer grown in overall units since it first
21 started?

22 A We have.

23 Q Did TaxSlayer grow in overall unit from tax season 2010 to
24 tax season 2011?

25 A We have.

1 Q To what, if anything, do you attribute that growth?

2 A In the beginning, we had a lot of referrals and as our
3 business has grown, we've been able to ramp up our marketing
4 expenditure. I believe our product is based on tax preparers.
5 We were the ones who developed it in order to assist an
6 individual fill out their tax return. Along with customer
7 support and just the ease and use of our package -- of our
8 software package.

9 Q So focusing on your product, what about TaxSlayer's product
10 do you feel attributed to TaxSlayer's growth?

11 A I would say the ease of use. We really tried to streamline
12 the process, give the user the ability to be assisted if they
13 would like, but also allow them to navigate as they please.

14 Q You also mentioned marketing as being something that
15 attributed to TaxSlayer's growth in your view; is that
16 correct?

17 A Correct.

18 Q What about marketing do you feel attributed to the growth?

19 A Well, along with your normal marketing ad words, banner ads,
20 that sort of stuff, we've also engaged in marketing parts of
21 NASCAR. We've been doing that for three years now. Plan on
22 doing it next year. And we've also just signed on to be the
23 premium sponsor of the Gator Bowl this year.

24 Q You mentioned ad words. Can you describe to us what that
25 marketing involves.

1 A When you -- as the previous person testified, basically when
2 you pay for search words that people are searching, as they
3 click through them, you pay based on the click-through rate.

4 Q And you mentioned your NASCAR sponsorship. Can you describe
5 that for the Court.

6 A This year we've just signed another deal with Dale
7 Earnhardt, Jr.'s racing team -- his nationwide racing team. He
8 will sponsor -- excuse me; he will race two races for us this
9 year, including Daytona and Bristol, along with ten other races
10 from another driver and his team.

11 Q And you mentioned the sponsorship of the Gator Bowl.
12 When did that occur?

13 A Just recently actually. We've been in negotiations for the
14 past several months, and I believe we just announced it publicly
15 within the last couple weeks.

16 Q And for how many years is that?

17 A A three-year deal.

18 Q Does TaxSlayer also use social media for its marketing?

19 A We do.

20 Q And can you describe that, please.

21 A We use Facebook, Twitter, YouTube. We've been very
22 successful in having YouTube campaigns where we've allowed
23 people to produce commercials that we may or may not use in our
24 marketing across the country. Along with awarding it with some
25 kind of prize, usually 25,000 or something like that.

1 That's been pretty successful for us.

2 Q Do those submitted YouTube commercials remain on YouTube
3 even if you haven't selected them?

4 A They do.

5 Q Do you also view TaxSlayer's price as being a reason for its
6 growth?

7 A I do.

8 Q Why is that?

9 A We believe it's a competitive price compared to other
10 products that are available. And that's one reason why we've
11 kind of kept that price in line. It's helping our growth.

12 Q Have you read the public version of the government's
13 preliminary injunction motion in this case?

14 A I have.

15 Q What view, if any, do you have of the government's assertion
16 in its preliminary injunction motion that TaxACT has been,
17 quote, "the driving force behind every major competitive
18 development in the digital DIY market over the past seven
19 years"?

20 A Probably a little stretch to say every innovative -- I'm not
21 sure what the word --

22 Q "Major competitive development."

23 A Yes. A little stretch.

24 Q Do you view TaxACT as having been responsible for any major
25 competitive developments?

1 A I do. As I recall, they were one of the first companies to
2 really push or engage in this free product that exists now today
3 in the marketplace.

4 Q And to your recollection, when was that?

5 A Around 2004, 2005.

6 Q Since that time, are there any other major competitive
7 developments that you would attribute to TaxACT?

8 A Not that I personally know.

9 Q Do you view TaxACT since that time as being innovative?

10 A No more than any other tax software company.

11 Q Is TaxACT as innovative as TaxSlayer?

12 A They're a good piece of software, and I believe that our
13 software is just as good and we are just as innovative.

14 Q Where do your customers come from?

15 A From anyone who is looking to file their tax return, whether
16 it be through -- excuse me; they come from anywhere looking to
17 file tax returns.

18 Q So if someone used a tax store last year, could they
19 potentially be your customer this year?

20 A Yes.

21 Q If someone used pen and paper last year, could they
22 potentially be your customer this year?

23 A They could.

24 Q If someone used TurboTax could someone potentially be your
25 customer?

1 A They could.

2 Q And if you lose customers, where are they going?

3 A I would imagine the same places that we are receiving
4 them.

5 Q Now, do you in turn focus your marketing dollars on all of
6 those companies and forms of tax preparation?

7 A We do not specifically address brick-and-mortar retail
8 offices as a company policy. We've gotten into some problems
9 when we've been so-called alienating our tax preparer
10 professional users, so as a company policy, we don't actively
11 try to advertise against accountants -- against people who go
12 into retail stores.

13 Q Because some of those people -- can you explain that policy
14 in a little more detail.

15 A Our customer -- our company started off with TaxSlayer Pro,
16 and we have over 8,000 users across the country. And as we
17 actively tried to engage in marketing to say do not go to this
18 assisted tax prep, we tended to upset that user base. So we've
19 stayed away from that.

20 But we believe that -- and just general marketing and brand
21 awareness, that you're still attracting those users, but we're
22 not specifically stating it in our advertising that we want to
23 pull them away.

24 Q And your NASCAR sponsorship, do you understand that only
25 customers of online digital tax preparation are viewers of

1 NASCAR?

2 A No.

3 Q And for the Gator Bowl similarly, do you understand that
4 viewers the Gator Bowl are only digital tax preparers?

5 A No. Anybody who would be needing to file a tax return.

6 Q What is your view of H&R Block's proposed transaction of
7 TaxACT?

8 A We are actually happy that this acquisition has been
9 proposed. We think that it's great for TaxACT to have made
10 something for themselves and to be a potential merger company.

11 We feel that if H&R Block decides to drop the brand of
12 TaxACT or raises their prices, that we'll be ready to gain some
13 more market share based on that.

14 Q And even if they don't raise price or eliminate the brand,
15 do you anticipate that TaxSlayer may be able to take some of the
16 former TaxACT customers?

17 A It would be harder, but I think that opportunity still is
18 out there.

19 Q And what do you base that on?

20 A We've noticed in the past on our professional site that when
21 companies are bought out, that the end user may not necessarily
22 have good feelings towards the buyer and would look to go
23 elsewhere. So that's been big for us on our professional
24 package when companies get bought out. I think we would see
25 some of that on this side as well.

1 Q After reading the preliminarily --

2 THE COURT: Excuse me. Could you just explain that a
3 little bit.

4 Does it have to do specifically with H&R Block
5 potentially competing with some of the tax professionals who buy
6 your TaxSlayer Pro?

7 THE WITNESS: No, ma'am. What I'm getting at is when
8 tax professional companies have been bought out, the users of
9 those software -- of those packages may not necessarily agree
10 with the new owner and have tended to shop elsewhere because of
11 that. And we feel that to some degree, that you would have some
12 of that crossover as well if H&R Block became the owner of
13 TaxACT. That people may migrate just because H&R Block is now
14 the owner. We've seen that on the professional side.

15 BY MR. ROUSH:

16 Q If they were to migrate, you think there's a potential they
17 would migrate to TaxSlayer?

18 A Absolutely.

19 Q So after reading the preliminary injunction motion, do you
20 understand that the government is asserting that this
21 transaction could lead to the elimination of TaxACT or increase
22 in its prices?

23 A I'm sorry. Could you repeat that.

24 Q Do you understand that the government is asserting that this
25 transaction could lead to the elimination of TaxACT or an

1 increase in its prices or decrease in its services?

2 MR. BUTERMAN: Objection.

3 THE COURT: Overruled.

4 BY THE WITNESS:

5 A We do.

6 Q If the government is right, how, if at all, would that
7 impact TaxSlayer?

8 A We would actually welcome that. We believe that we're
9 poised and ready to take those customers who would want to go
10 elsewhere for lower prices.

11 MR. ROUSH: Your Honor, the rest of my questions would
12 be for a closed session. Given the back and forth that we saw
13 occur before, what I'd ask is that we actually do the closed
14 session, then let them start their cross with that. I don't
15 think I'll have any redirect that I have to have in closed
16 session so we can open it right back up after that, if that's --
17 with your indulgence, if we could handle it that way.

18 I think it will save a lot of time, but that's my view.

19 MR. BUTERMAN: I'm fine whichever way your Honor wants
20 to proceed.

21 THE COURT: Okay. So we're going to -- as opposed to
22 clustering all the closed at the very tail end of the witness'
23 testimony, we're going to come back for an open
24 cross-examination of this witness so you can move right to the
25 redirect now -- so you can move right to the closed direct now.

1 That's what you're suggesting?

2 MR. ROUSH: Yes, your Honor. I think we'll have a lot
3 less of the two of us getting up and doing recross and redirect
4 because I think while I'm going to focus on numbers with him, I
5 don't think the recross or redirect will need to have much of
6 that. I've talked to Mr. Buterman, and he said he has one thing
7 that he thinks will need to be in closed session. So I think it
8 would be a compact closed session.

9 MR. BUTERMAN: The only thing I would note, your Honor,
10 is that I don't believe that the defendants are planning on
11 putting on another witness in this morning's session. And if
12 that's the case, then if we go -- if we do it in the way we did
13 it last time, we could close and come back after lunch.

14 THE COURT: Well, I hope to get this witness done
15 before lunch. Okay. So we will close the courtroom now.

16 How long do you think that your closed direct will be,
17 Mr. Roush?

18 MR. ROUSH: 20 minutes.

19 MR. BUTERMAN: Mine is going to be five minutes.

20 THE COURT: Okay. Fine. Just for a sense of how long
21 the courtroom will be closed for those who have to leave.

22 MR. ROUSH: Thank you, your Honor.

23 THE COURT: Okay. I'll excuse the spectators during
24 this portion of the examination.

25 (The following portions, pages 84-98, were designated as

1 confidential/attorneys' eyes only and sealed under a
2 separate transcript per order of the Court.)

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CROSS-EXAMINATION

BY MR. BUTERMAN:

Q So we're clear, Mr. Rhodes, TaxSlayer introduced its first online product in 2003; is that correct?

A Correct.

Q And prior to this year, TaxSlayer did not have a free federal product to offer through its Web site; is that correct?

A Correct.

Q And the free product -- federal product -- that it did roll out, only allows for E-filing of a federal return on a form 1040EZ, correct?

A Correct.

Q Now, TaxSlayer used to offer both an online and a downloadable version of its product, correct?

A Correct.

Q In 2009, TaxSlayer stopped offering its downloadable product to new customers, correct?

A That's correct.

Q And the reason that it did so is because the service costs for downloadable products were too burdensome, correct?

A And we didn't -- correct. And we didn't see a future.

Q So now only existing customers can download a version of TaxSlayer, correct?

A Correct.

1 Q TaxSlayer also does not offer its software on a CD through
2 retailers, correct?

3 A Correct.

4 Q And one of the reasons it does not do so is because of the
5 additional cost that would need to be incurred to start offering
6 the retail product, correct?

7 A Correct.

8 Q Now, H&R Block -- you understand that H&R Block, TaxACT, and
9 TurboTax all offer some ability to import data from third-party
10 networks?

11 A I am.

12 Q But TaxSlayer does not offer the ability of individuals to
13 import directly into their tax returns certain data such as W-2s
14 or 1099s?

15 A Correct.

16 Q And TaxSlayer does not allow for an importation of a prior
17 year's tax return from other companies, correct?

18 A Currently we do not.

19 Q Now, in your view, TaxSlayer competes with TurboTax, H&R
20 Block, and TaxACT on price, correct?

21 A Correct.

22 Q And when setting the prices for TaxSlayer's products, it
23 considers the prices charged by other providers of digital
24 do-it-yourself products, correct?

25 A Every year we do sit down, and we take a look at what our

1 competitors are charging, yes.

2 Q And you consider the prices of both your competitors' paid
3 and free offerings, correct?

4 A We do.

5 Q Now, TaxSlayer also competes with TurboTax, H&R Block, and
6 TaxACT on features such as usability, correct?

7 A We do.

8 Q When setting TaxSlayer's prices, it doesn't consider the
9 prices charged by CPAs or brick-and-mortar tax preparation
10 businesses, correct?

11 A We do not.

12 Q And even though TaxSlayer does obtain some sales from people
13 switching to its products from pen and paper and
14 brick-and-mortar stores, TaxSlayer does not directly compete
15 against those tax preparation methods, correct?

16 A As I mentioned before, we do not compete on an advertising
17 manner.

18 Q When we looked at Tab 3 a few moments ago and you listed
19 your competitors for TaxSlayer, you did not list any assisted
20 tax preparation products, did you?

21 A Correct. I also did not list the IRS, pen and paper.

22 Q Thank you.

23 A Yeah.

24 Q Now, if TaxSlayer were to raise its prices a material
25 amount, you do not believe that TaxSlayer's customers would

1 choose to go to tax stores or CPAs, correct?

2 A I do not.

3 Q And you do not believe that TaxSlayer's customers would
4 switch to pen and paper either, correct?

5 A I do not.

6 Q As a matter of corporate policy, TaxSlayer has decided not
7 to take on debt or give up ownership in exchange for funding,
8 correct?

9 A That's correct.

10 Q And you do not envision this transaction changing that,
11 correct?

12 A The proposed where H&R Block, I think, has publicly stated
13 that it would not change prices or get rid of the TaxACT
14 product.

15 Q Oh, I'm talking about TaxSlayer. You do not envision this
16 transaction changing TaxSlayer's corporate policy not to take on
17 debt or give up ownership in exchange for funding, correct?

18 A What I was -- in my deposition or declaration, I spoke to
19 the proposed acquisition where H&R Block has publicly stated
20 that they would not raise prices or get rid of TaxACT. So if
21 those were to change, then we may seek funding.

22 Q Now, you believe that success in the market for digital tax
23 preparation products requires not only good tax preparation
24 functionality, but also a well-known brand and a good reputation
25 for products that allows individuals to prepare tax returns

1 easily and accurately?

2 A I do.

3 Q And you believe that developing a good reputation takes
4 years of consistently good performance, correct?

5 A It does.

6 Q And that developing a well-known brand takes years of
7 significant marketing expenditures and traditional and online
8 media, correct?

9 A Correct.

10 Q And you do not know of any way that you could double the
11 size of TaxSlayer in one to two years, correct?

12 A I do not.

13 Q And do you believe that there is no silver bullet for a
14 small company to grow market share quickly, correct?

15 A Correct.

16 MR. BUTERMAN: That's all I have, your Honor.

17 THE COURT: Mr. Roush.

18 REDIRECT EXAMINATION

19 BY MR. ROUSH:

20 Q You were asked if TaxSlayer's product imported data from
21 other companies' products.

22 Do you recall that?

23 A I do.

24 Q Are you aware of any company's offering that imports data
25 from other companies' products?

1 A There are some companies who do that.

2 Q What companies?

3 A I know TaxACT imports from other competitors. I would
4 imagine TurboTax does as well, but I'm not a hundred percent on
5 that.

6 Q Are you certain that TaxACT's product does that?

7 A Yes.

8 Q You mentioned that you -- you were asked some questions
9 about downloadable products and CDs?

10 A I was.

11 Q And at this time, has TaxSlayer made decisions to offer
12 downloadable products?

13 A We only offer that product to returning -- to existing
14 customers. We do not sell it to new users.

15 Q And why don't you sell it to new users?

16 A We had many internal debate about this, whether there is a
17 future in that market, and the up-front cost that it would take
18 to go down that road. And we would have to pull money from
19 other places to do it. And right now it doesn't seem like a
20 good fit.

21 Q And similarly with regard to a CD product, have you made a
22 decision whether or not to invest in that sort of product?

23 A The same as the downloadable.

24 Q You don't think it would be a profitable investment?

25 A Maybe in the short term, but we feel that that product may

1 not be around in the future.

2 Q You mentioned that you didn't think if TaxSlayer raised its
3 prices that its customers would go -- would switch to assisted.

4 Do you recall that?

5 A I do.

6 Q And you mentioned that you didn't think they would switch to
7 pen and paper.

8 Do you recall that?

9 A I do.

10 Q And why wouldn't they, in your view?

11 A Unless the user was just dissatisfied with the process of
12 filing the tax return on their own, I couldn't imagine they
13 would go back to an accountant. I really couldn't imagine them
14 going back to pen and paper after experiencing using a Web site
15 to file their tax return. That's why I said that.

16 Q Do you view there as being other significant or good
17 products on the market to which they could turn?

18 A Oh, absolutely. There's many.

19 Q Has TaxSlayer ever changed its price in response to
20 TurboTax's prices?

21 A We have not.

22 Q Has TaxSlayer ever changed its price in response to H&R
23 Block's prices?

24 A No.

25 Q Has TaxSlayer ever changed its prices in response to

1 TaxACT's prices?

2 A No.

3 MR. ROUSH: No further questions, your Honor.

4 MR. BUTERMAN: Nothing further, your Honor.

5 THE COURT: Nothing further. You're excused.

6 Thank you very much. We can break for lunch until 1:15

7 when you'll have your next witness ready?

8 MR. ROUSH: Dr. Meyer is here, yes.

9 THE COURT: Good. Thank you. Have an enjoyable lunch.

10 (Lunch recess was taken at 12:17 p.m.)

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CERTIFICATE OF OFFICIAL COURT REPORTER

I, Lisa S. Schwam, certify that the foregoing is a correct transcript from the record of proceedings in the above-entitled matter.

SIGNATURE OF COURT REPORTER

DATE