

**IN THE CIRCUIT COURT OF COOK COUNTY, ILLINOIS
COUNTY DEPARTMENT, CHANCERY DIVISION**

**THE PENNSYLVANIA AVENUE FUNDS,
On Behalf of Itself and Others Similarly
Situated,**

Plaintiff,

vs.

**CFC INTERNATIONAL, INC., ROGER F.
HRUBY, WILLIAM GARDNER BROWN,
ROBERT B. COVALT, GREGORY M.
JEHLIK, DENNIS W. LAKOMY, RICHARD
PIERCE and DAVID D. WESSELINK,**

Defendants.

Case No.

06CH12464

CLASS ACTION

**COMPLAINT FOR BREACH OF
FIDUCIARY DUTY**

INTRODUCTION

1. This is a class action on behalf of the public stockholders of CFC International, Inc. ("CFC" or the "Company") against CFC and its Board of Directors arising out of the defendants' agreement to enter into an acquisition agreement with an affiliate of Illinois Tool Works, Inc. ("Illinois Tool") whereby Illinois Tool will acquire the Company for a mere \$16.75 per share (the "Sham Acquisition Proposal") in order for defendant and majority/controlling shareholder Roger F. Hruby to advance his own interests and the interests of his own nominated directors at the expense of those of the Company and its shareholders. Indeed, as discussed below, the Sham Acquisition Proposal is worth \$3.25 per share *less than* an acquisition proposal only one year ago, for \$20.00 per share, which was ultimately terminated. Moreover, the Sham Acquisition Proposal is the product of a Board of Directors (the "Board") who are highly conflicted and did not (and cannot) represent the public shareholders of CFC with impartiality and vigor.

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CHANCERY DIVISION
DOROTHY BROWN
CLERK

2. The Sham Acquisition Proposal falls on the heels of the termination of another failed attempt to buy the Company at virtually the same unconscionable price by Quad-C Management, Inc. ("Quad")

3. Simply put, the Sham Acquisition Proposal is structured as a *fait accompli* due to the conflicted directors' majority interest in CFC. Defendants' ownership interest in the Company was not as liquid as defendants had desired. So, in spring of 2005 (if not before), the defendants, led by Hruby, were determined to sell the Company with almost total disregard for the price, just as long as Hruby could cash out of the Company obtaining the liquidity he had long desired. In fact, in May of 2005, defendants agreed to the \$20.00 per share buyout offer from Audax Group ("Audax"), which was terminated, according to defendants, following the Board's inability to recommend the transaction to its shareholders. Following the Audax acquisition termination, defendant Hruby exclaimed that the Company was well positioned for future growth. Months later, Hruby would stun investors again when, despite the Company's "future," Hruby agreed to sell the Company to a second acquirer, Quad, for even less – just \$16.50 per share.

4. Each of the defendants has directly violated and/or aided and abetted the other defendants' violations of the fiduciary duties owed to the public shareholders of CFC. Absent judicial intervention, the Company's shareholders will be stripped of their ownership interests through improper and illegal means. Defendants have a duty to maximize shareholder value – not minimize it. Defendants have accepted an offer which significantly undervalues CFC without regard to shareholders' interests or even their opinion (vote). Such harmful and absurd conduct warrants immediate judicial intervention. This action seeks to enjoin defendants' unlawful conduct. This action does not seek compensatory damages.

JURISDICTION AND VENUE

5. This Court has jurisdiction over each of the defendants because they conduct business in, reside in and/or are citizens of Illinois. Certain of the defendants are residents and citizens of Illinois, including defendants Hruby, Jehlik and Lakomy, and CFC has its principal place of business in the State of Illinois located at 500 State Street, Chicago Heights, Illinois. Moreover, the conduct at issue took place in this county. Venue is proper in this Court because defendants' wrongful acts arose in and emanated from this county.

PARTIES

6. Plaintiff The Pennsylvania Avenue Funds, at all times relevant hereto has been a stockholder of CFC.

7. Defendant CFC serves as a holographic and specialty coated film company in the United States and Europe. It engages in the design, manufacture and marketing of chemically complex, multilayer, transferable coatings and holographic technologies. The Company offers holographic, printed, security, pharmaceutical, specialty pigmented and simulated metal products. CFC's holographic products include holograms used as security markings on products, such as computer microprocessors and merchandise; transportation and event tickets and other products susceptible to counterfeiting or tampering, as well as holographic images for packaging and other visual markets; printed products that include engineered board coatings for ready to assemble and promotional furniture, picture frames, manufactured housing and window treatments; and security products, such as tamper-evident signature panels and abrasion resistant tipping foils for transaction cards, as well as specialized multi coercivity magnetic stripe products applied to both plastic transaction cards and disposable fibrous substrates, such as driver's licenses, student identification cards, airline tickets, mass-transit tickets, bank books and telephone debit cards. In addition, the Company provides pharmaceutical products that consist of functional coatings for heat transfer

printing on pharmaceutical products, such as intravenous solution bags, syringes and other uses requiring nontoxic ingredients and adhesion; and specialty pigmented and simulated metal products that include automobile batteries, cosmetics containers, industrial signage and other products. CFC offers its products to various markets, such as holographic packaging and authentication seals; furniture and building products; pharmaceutical products; and transaction cards, including credit cards, debit cards, ATM cards and access cards, and intaglio printing.

8. Defendant Roger F. Hruby ("Hruby") is Chairman of the Board of CFC and has served as a director since the Company's formation. Hruby owns or beneficially controls approximately 2,359,021 shares of CFC common stock, or 58.6%.

9. Defendant William Gardner Brown ("Brown") is a director of the Company. Brown owns or beneficially controls approximately 182,519 shares of CFC common stock, or 4.5%.

10. Defendant Robert B. Covalt ("Covalt") is a director of the Company.

11. Defendant Gregory M. Jehlik ("Jehlik") is the President and Chief Executive Officer, and a director of the Company.

12. Defendant Dennis W. Lakomy ("Lakomy") is the Executive Vice President and Chief Financial Officer, and a director of the Company. Lakomy owns or beneficially controls approximately 328,510 shares of CFC common stock, or 8.2%.

13. Defendant Richard Pierce ("Pierce") is a director of the Company.

14. Defendant David D. Wesselink ("Wesselink") is a director of the Company.

15. The defendants named in ¶¶8-14 are sometimes collectively referred to herein as the "Individual Defendants."

16. Each of the Individual Defendants is beholden to and controlled by defendant Hruby. Each was hand-picked by Hruby and appointed with the understanding that they would not frustrate Hruby's decisions relating to "his" Company, the sale of the Company included.

17. By virtue of their positions as directors and/or officers of CFC, the Individual Defendants have, and at all relevant times had, the power to control and influence, and did control and influence and cause CFC to engage in the practices complained of herein.

FIDUCIARY DUTIES OF THE INDIVIDUAL DEFENDANTS

18. By reason of the above Individual Defendants' positions with the Company as officers and/or directors, said individuals are in a fiduciary relationship with plaintiff and the other public stockholders of CFC and owe plaintiff and the other members of the Class a duty of highest good faith, fair dealing, loyalty, due care and full, candid and adequate disclosure.

19. Each of the Individual Defendants is required to act in good faith, in the best interests of the corporation's shareholders and with such care, including reasonable inquiry, as would be expected of an ordinarily prudent person. In a situation where the directors of a publicly traded company undertake a transaction that results in a change in corporate control (particularly when it involves a decision to eliminate the shareholders' equity investment in a company), the applicable state law requires the directors to take all steps reasonably required to maximize the value shareholders will receive rather than use a change of control to benefit themselves. To diligently comply with this duty, the directors of a corporation CFC not take any action that:

- (a) adversely affects the value provided to the corporation's shareholders;
- (b) contractually prohibits them from complying with or carrying out their fiduciary duties;
- (c) discourages or inhibits alternative offers to purchase control of the corporation or its assets; or

(d) will otherwise adversely affect their duty to search and secure the best value reasonably available under the circumstances for the corporation's shareholders.

20. As described herein, the Individual Defendants have breached their fiduciary duties by taking actions designed to deter higher offers from other potential acquirers so as to ensure the defendants receive hundreds of thousands of dollars in personal benefits at the expense of CFC shareholders. Defendants cannot possibly fulfill their fiduciary obligations after implementing provisions which disable them from maximizing shareholder value. The Individual Defendants have breached their fiduciary obligation to act reasonably.

CLASS ACTION ALLEGATIONS

21. Plaintiff brings this action pursuant to 735 ILCS 5/2 801 on its own behalf and as a class action on behalf of all holders of CFC common stock, who are being and will be harmed by defendants' actions described below (the "Class"). Excluded from the Class are defendants herein and any person, firm, trust, corporation or other entity related to or affiliated with any defendants.

22. This action is properly maintainable as a class action.

23. The Class is so numerous that joinder of all members is impracticable. There are over 4 million shares of CFC stock issued. The shares trade on the Nasdaq and thousands of CFC stockholders of record are located throughout the United States.

24. Questions of law and fact are common to the Class and predominate over questions affecting any individual Class members. The common questions include, *inter alia*, the following:

(a) whether the defendants breached their fiduciary duties of care, loyalty, good faith, due care and/or candor owed by them to plaintiff and the other members of the Class in connection with the proposed sale of CFC;

(b) whether the defendants have breached their fiduciary duty to secure and obtain the best price reasonable under the circumstances for the benefit of plaintiff and the other members of the Class in connection with the proposed sale of CFC;

(c) whether the defendants have, in bad faith or for improper motives, erected and/or retained barriers to discourage other offers for the Company or its assets;

(d) whether plaintiff and the other members of the Class would be irreparably harmed were the provisions and conduct detailed herein allowed to persist; and

(e) whether the compensation to be paid to plaintiff and the Class is unfair and inadequate.

25. The defendants have acted or refused to act on grounds generally applicable to the Class thereby making appropriate final injunctive relief with respect to the Class as a whole.

26. Plaintiff is committed to prosecuting this action and has retained competent counsel experienced in litigation of this nature. The claims of plaintiff are typical of the claims of the other members of the Class and plaintiff has the same interests as the other members of the Class. Accordingly, plaintiff is an adequate representative of the Class and will fairly and adequately protect the interests of the Class.

27. Plaintiff anticipates that there will be no difficulty in the management of this litigation as a class action.

28. For the reasons stated herein, a class action is superior to other available methods for the fair and efficient adjudication of this controversy.

BACKGROUND TO PROPOSED MERGER

29. CFC serves as a holographic and specialty coated film company in the United States and Europe. It engages in the design, manufacture and marketing of chemically complex, multilayer, transferable coatings and holographic technologies. The company offers holographic,

printed, security, pharmaceutical, specialty pigmented and simulated metal products. CFC's holographic products include holograms used as security markings on products, such as computer microprocessors and merchandise; transportation and event tickets and other products susceptible to counterfeiting or tampering, as well as holographic images for packaging and other visual markets; printed products that include engineered board coatings for ready to assemble and promotional furniture, picture frames, manufactured housing and window treatments; and security products, such as tamper-evident signature panels and abrasion resistant tipping foils for transaction cards, as well as specialized multi coercivity magnetic stripe products applied to both plastic transaction cards and disposable fibrous substrates, such as driver's licenses, student identification cards, airline tickets, mass-transit tickets, bank books and telephone debit cards. In addition, the company provides pharmaceutical products that consist of functional coatings for heat transfer printing on pharmaceutical products, such as intravenous solution bags, syringes and other uses requiring nontoxic ingredients and adhesion; and specialty pigmented and simulated metal products that include automobile batteries, cosmetics containers, industrial signage and other products. CFC offers its products to various markets, such as holographic packaging and authentication seals; furniture and building products; pharmaceutical products; and transaction cards, including credit cards, debit cards, ATM cards and access cards, and intaglio printing. The company is headquartered in Chicago Heights, Illinois.

30. In November 1995, the Company's board of directors retained Everen Securities to bring CFC public. There the Company sold 1.2 million shares of the Company's stock for \$9.50 per share. Months later, defendant Hruby saw his net worth, *vis-à-vis* the Initial Public Offering ("IPO"), explode. With the Company public, Hruby believed that the public markets would provide the necessary liquidity for him to diversify his personal net worth should he so desire.

31. While the Company continued to grow, the Company's share volume remained rather stagnant. Hruba planned to enhance the attractiveness of the Company and thereby increase the volume of shares traded by attending and sponsoring various expositions. However, his plans for liquidating his interests in CFC remained a distant dream.

32. After consulting with bankers, among others, Lincoln Partners, Hruba realized that diversifying or otherwise divesting himself and his family of the shares, creating the much desired liquidity he sought, would be much more difficult than he ever imagined. Hruba and his co-directors realized that in order to divest themselves of their CFC shares and do so without disrupting the market (i.e., the price), it would take years. For Hruba, the idea of spending the next few years trying to obtain liquidity by dribbling his shares into the market on a daily basis was not attractive. No longer concerned for the Company or the shareholders, Hruba decided he would agree to liquidate his interests and that of the entire Company and shareholders, if necessary, as long as he could liquidate his own shares and do so quickly.

33. On March 1, 2005, the Company issued a press release entitled "CFC International, Inc. Reports Restated Fourth Quarter and Year End 2004 Results." The press release stated in part:

- *Record annual sales of \$82.6 million, up 32% over \$62.8 million in 2003.*
- *Fully diluted earnings per share increased to \$0.19 for the fourth quarter of 2004, versus (\$0.02) for the fourth quarter in 2003, as restated. This included a foreign currency exchange gain of \$0.07 in the fourth quarter of 2004, and \$0.03 in the fourth quarter of 2003, on a fully diluted basis, related to the restatement.*
- *Fully diluted earnings per share for the year end 2004 exceeded the Company's previous guidance of \$0.72 to \$0.76, increasing to \$0.90, versus \$0.06 for the year end in 2003, as restated. This includes a foreign currency exchange gain for the year ended 2004 of \$0.11, and for the year ended 2003 of \$0.10, on a fully diluted basis, related to the restatement.*
- *Net income in the fourth quarter of 2004 of \$858,000, up from a loss of \$72,000 for the fourth-quarter 2003, and \$4.0 million, up 1439% for the year end of 2004. This includes a foreign currency exchange gain related*

to the restatement in the fourth quarter 2004 of \$295,000 (after tax) and in the fourth quarter of 2003 of \$130,000 (after tax); and for the calendar year 2004 of \$500,000 (after tax) and for the calendar year 2003 of \$423,000 (after tax).

* * *

"Once again I would like to reiterate our pleasure in reporting a very solid performance in 2004," said Greg Jehlik, CFC's President and Chief Executive Officer. "Through our focused and coordinated efforts around the world, CFC was able to deliver favorable results to its shareholders. Our goal in 2005 is to effectively execute our Annual Operating Plan and continue to grow in a profitable manner."

Sales for the year of 2004 totaled \$82.6 million, an increase of 32 percent from \$62.8 million for the same period last year. The 2004 sales increase was a result of higher sales volume in all of the Company's product groups. In particular, the Company had strong sales in its printed patterned products, security products and holographics, in packaging, security and authenticity. The Company also benefited from a strong Euro which positively affected sales by \$2.0 million for the full year of 2004. Net income for the year increased to \$4.0 million, or \$0.90 per share on a fully diluted basis in 2004, from a net income of \$261,000 or \$0.06 per share on a fully diluted basis for the same period last year, as restated. Net income for the year was favorably affected by higher sales, and the Company leveraged its manufacturing infrastructure. Net income was also affected by foreign currency exchange gains in 2004 and 2003 totaling \$500,000 and \$423,000, respectively, as a result of the restatement.

"Our 2004 performance was the best ever for CFC," said Roger Hruby, CFC's Chairman. "We are now reaping the benefits of our investments in people, processes and equipment. We are pleased to report that we exceeded our previous guidance of \$0.72 - \$0.76, coming in at \$0.90 per share on a fully diluted basis for 2004, including \$0.11 related to the foreign currency exchange gain. Hruby further added, "Based upon the Company's 2004 results and the economic outlook for 2005, CFC anticipates earning net income of \$1.10 - \$1.15 per share on a fully diluted basis, utilizing a 35.4% tax rate."

34. On May 3, 2005, the Company issued a press release entitled "CFC International, Inc. Announces that It Has Signed a Letter of Intent to Be Acquired and Reports 2005 First Quarter Results." The press release stated in part:

Worldwide holographic and specialty coated film manufacturer, CFC International, Inc. announced today that it has entered into a letter of intent to merge the Company with an affiliate of Audax Group, a private equity firm, for an enterprise value of \$109.4 million, which equates to an expected share price range for this transaction

between \$19.50 and \$20.00 per share. The proposed transaction is subject to a number of conditions, including completion of due diligence and the negotiation and execution of a definitive agreement, and there can be no assurance that a transaction will be completed. The Company expects the transaction, if completed, to close during the third quarter of 2005.

35. On August 15, 2005, the Company issued a press release entitled "CFC International, Inc. Reports 2005 Second Quarter Results." The press release stated in part:

- *Net sales increased to \$22.2 million for the second quarter of 2005, up 14.8% from \$19.4 million for the second quarter in 2004. Net sales for the first half of 2005 were up 12.5% to \$45.2 million, up from \$40.1 million for the same period last year.*
- *Fully diluted earnings per share increased to \$0.43 per share for the six months ended June 30, 2005, up from \$0.39 per share for the six months ended June 30, 2004*

... Worldwide holographic and specialty coated film manufacturer, CFC International, Inc., today reported results for the second quarter of 2005. Net sales for the second quarter 2005 increased 14.8% to \$22.2 million, compared to \$19.4 million in the second quarter of 2004. This increase in sales is due to growth on a worldwide basis of the Company's printed pattern products and pharmaceutical products, and strong domestic holographic sales, resulting from the introduction of a new holographic security product used on transaction cards.

* * *

"In the second quarter of 2005, CFC once again delivered solid sales growth," said Greg Jehlik, CFC's Chief Executive Officer and President. "Our second quarter results reflect increased sales in our long-standing markets, that we are focused on our strategic initiatives and that we are well-positioned to leverage future opportunities with new products such as our recently launched HoloLam Plus™ for the transaction card industry."

* * *

"We are very pleased with the positive results that we have delivered for the first half of 2005," said Roger Hruby, CFC's Chairman. "We achieved increases in both total net income and net sales for the first half of 2005, as compared to the same period a year ago, and we are well positioned to continue to deliver profit growth and strong sales as we move into the second half of 2005."

The Company also announced today that the letter of intent with Audax Group of the proposed acquisition of CFC has been terminated. Roger F. Hruby, CFC's Chairman, said, "As our negotiations with Audax progressed, it became

