SUPREME COURT OF THE STATE OF NEW YORK
COUNTY OF NEW YORK

ROBERT M. LEVINE, AS TRUSTEE OF THE MARION LEVINE REVOCABLE TRUST, Petitioner, -against- SEVEN PINES ASSOCIATES LIMITED PARTNERSHIP, Respondent.	INDEX NO.151958/2014

MEMORANDUM OF LAW IN SUPPORT OF APPLICATION FOR PRETRIAL DISCLOSURE PURSUANT TO NEW YORK BUSINESS CORPORATIONS LAW § 623(H)(4) AND NEW YORK CIVIL PRACTICE LAW AND RULES § 408

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INTRODUCTION

Robert M. Levine, as Trustee for the Marine Levine Revocable Trust (the "Levine Trust" or "Petitioner") brought a dissenter's rights claim pursuant to the New York Limited Liability Partnership Act (the "Partnership Act") §§ 1102 and 1105 and New York Business Corporations Law ("Corporations Law") § 623 to fix the fair value of the Levine Trust's interest in Seven Pines Associates Limited Liability Partnership (the "Partnership"). (*See* NYCSEF Doc. No. 1; Petition.) Specifically, the Levine Trust seeks to protect itself from actions taken by Seven Pines Associates Limited Partnership (the "General Partner" or "Respondent") that changed the character of its investment (*see* 12B Fletcher Cyc. Corp. § 5906.10). The transaction at issue is a restructuring of the Partnership by the General Partner and other interested partners in the form of a merger which closed on January 8, 2014. (*See* NYSCEF Doc. No. 36; Levine Aff. Ex. 1.) In connection with that transaction, the Partnership offered the Levine Trust only $325,000 for its 4.165% partnership interest. For a number of reasons, the Levine Trust did not accept the Partnership's offer and exercised its right to dissent. This Court is now charged with determining the fair value of the Levine Trust's interest (*see* Corporations Law § 623[h] [4].)

In order to determine the fair value of the Levine Trust's interest, the Court will need to determine the value of the Partnership's sole asset, which is a 304 unit apartment building located in Yonkers, New York (the "Partnership Property"). Currently, the Levine Trust knows of three different "valuations" of the Partnership Property, ranging from $16 million to $33 million; all of which were created by, or relied upon by, the Partnership at one time or another in the last two years. The Partnership – not the Levine Trust – has possession, custody and control over each of these valuations and all background documents, communications, and other information related to them. The Levine Trust and the Court cannot properly evaluate these valuations (or the

Partnership's assertions about the valuations) without additional information. Accordingly, the Levine Trust respectfully requests, pursuant to § 623 of the Corporations Law and § 408 of the CPLR, that the Court allow pretrial disclosure on issues related to these valuations.

FACTUAL AND PROCEDURAL BACKGROUND

Petitioner's dissenter's rights claim derives from an interested party transaction that occurred in January 2014 wherein the Partnership was restructured to "merge" with and into its General Partner and other affiliated entities. (*See* NYSCEF Doc. Nos. 1, 6, 36; Petition, Notice of Petition, Levine Aff. Ex. 1). In connection with the restructuring, the Partnership offered the Levine Trust $325,000 for its 4.165% interest. (*See* NYSCEF Doc. No. 36.) The price offered to the Levine Trust – and the other disinterested limited partners – was determined using a formula that the Partnership created (the "Merger Calculation") for valuing the Partnership Property. In the formula, the Partnership used a Net Operating Income of $825,000 and a capitalization rate of 4.9% for a value of the Partnership Property of $16 million. That value was significantly less than the value reached by an appraisal performed on the Partnership property by an independent third party appraiser just one year earlier (the "2012 Appraisal"). Specifically, the 2012 Appraisal valued the Partnership Property at $33 million.

As it is statutorily permitted to do, the Levine Trust dissented from the Partnership's offer of $325,000. (*See* NYSCEF Doc. Nos. 44 and 45; Levine Aff. Exhs. 9 and 10.) When the Partnership failed to comply with its obligations under § 623 of Corporations Law, the Levine Trust had no other option but to bring this action and request that the Court to "fix" the fair value of its partnership interest.

The Partnership filed its Answer on April 18, 2014. According to the CPLR, an Answer was all that was required and anticipated in response to the Petition (CPLR § 402). Yet, at the same time that the Partnership filed its Answer, it filed a lengthy and unnecessary opposition brief.

With that brief, the Partnership asked the Court to ignore both the 2012 Appraisal for $33 million and the Merger Calculation at $16 million. Instead, the Partnership submitted yet a new appraisal from BCS Valuations, Inc. (the "BCS Appraisal"). The BCS Appraisal valued the Partnership Property at $21 million – a number inconsistent with both the 2012 Appraisal and the value reached with the formula for the Merger Calculation.

The Levine Trust submitted its "reply" to the Partnership's Opposition on April 28. (*See* NYSCEF Doc. No. 49.) The parties disagree about the procedure for dissenter's rights proceedings like this one under the Corporations Law § 623 and CPLR § 409. The Partnership apparently contends that the proceeding should be dealt with summarily, without discovery and without a hearing. The Levine Trust maintains that in a dissenter's rights petition, Section 623 of the Corporations Law controls and the Court should consider a variety of factors, including expert testimony, before rendering its decision (*see* Corporations Law § 623[h] [4] [discussing a trial, pretrial discovery and expert testimony]; *see also Friedman v. Beway Realty Corp.*, 87 NY2d 161, 163 [1995] [discussing valuation proceeding under Corporations Law § 623, which involved a bifurcated trial and expert testimony]; *In re Carolina Gardens Inc. v. Menowitz*, 1996 WL 34573714 [N.Y. Sup. Ct., Jan. 26, 1996, No.112637/93] [trial order in valuation proceeding under Corporations Law § 623 describing testimony of numerous witnesses including experts, architect and management witnesses]). Where there are issues of fact such as competing valuations of the Partnership Property, a summary disposition is inappropriate and not anticipated by the statutes (*see* Corporations Law § 623; CPLR § 410). The parties are scheduled to appear before the Court on June 12, 2014 to discuss the proper procedure for this dispute.

ARGUMENT

Section 121-1105 of the Partnership Act, provides that "[i]f a former limited partner and the surviving or resulting limited partnership fail to agree on the price to be paid for the former

limited partner's partnership interest . . . the procedure provided for in paragraphs (h)-(k) of section six hundred twenty-three of the business corporation law shall apply . . . ." (Partnership Law § 121-1105 [b]). Section 623 of the Corporations Law, in turn, states that:

> [T]he court may, in its discretion, permit pretrial disclosure, including, but not limited to, disclosure of any expert's reports relating to the fair value of the shares whether or not intended for use at the trial in the proceeding and notwithstanding subdivision (d) of section 3101 of the civil practice law and rules.
>
> (Corporations Law § 623[h] [4]).

Because the Levine Trust properly dissented, this Court is charged with determining the fair value of the Levine Trust's interest in the Partnership. In making its determination of fair value the Court is to consider "all . . . relevant factors" that may bear on the fair value of the Levine Trust's interest (*id.*). So that the Court may do so, that same section provides that a party may apply to the Court for pretrial disclosure, including the disclosure of expert testimony, regardless of whether that testimony will be offered at trial (*id.*).

Pretrial disclosure is generally governed by CPLR § 3101, which requires "full disclosure of all matter material and necessary in the prosecution or defense of an action, regardless of the burden of proof, by . . . a party, or the officer, director, member, agent or employee of a party . . . ." (CPLR § 3101[a] [1]). "This provision [i.e., CPLR § 3101] has been liberally construed to require disclosure where the matter sought will assist preparation for trial by sharpening the issues and reducing delay and prolixity. Thus, restricted only by a test for materiality of usefulness and reason, pretrial discovery is to be encouraged." (*Sinosky v. Sinosky*, 26 AD3d 874, 875 [4th Dept 2006] [internal quotation marks omitted]; *see also Melworm v. Encompass Indem. Co.*, 112 AD3d 794, 795 [2d Dept 2013] [CPLR 3101 "is liberally interpreted in favor of disclosure"]). "Liberal discovery is favored and pretrial disclosure extends not only to proof that is admissible but also to matters that may lead to the disclosure of admissible proof." (*Twenty Four Hour Fuel Oil Corp.*

v. Hunter Ambulance Inc., 226 AD2d 175, 176 [1st Dept 1996]; s*ee also Mann ex rel. Akst v. Cooper Tire Co.*, 33 AD3d 24, 29 [1st Dept 2006] ["The scope of disclosure provided by CPLR §3101 is generous, broad, and is to be construed liberally"]; *Yoshida v. Hsueh-Chih Chin*, 111 AD3d 704, 705-06 [2d Dept 2013] ["The Court of Appeals' interpretation of 'material and necessary' . . . has been understood to mean nothing more or less than 'relevant'"]).

In order to determine the value of the Levine Trust's interest, the Court will be required to determine the value of the Partnership Property. There are currently three competing valuations of the Partnership Property, all of which were commissioned, created, or relied upon by the Partnership at some point in the past two years. Each of those valuations is relevant and information about them is essential to a fair determination of the value of the Levine Trust's partnership interest. Accordingly, the Levine Trust makes this application for pretrial disclosure pursuant to Corporations Law § 623 and CPLR § 408.

I. The Levine Trust Is Entitled To Information About The $33 Million Appraisal Performed In 2012 – A Value Almost Double What The Partnership Offered In The Merger.

In 2012, a disinterested third party appraiser valued the Partnership Property at $33 million and supported that value with both an income capitalization approach and a sales comparison approach. (*See* NYSCEF Doc. No. 38; Levine Aff. Ex. 3.) For its income capitalization approach, the third party appraiser used a 7.5% capitalization rate ("cap rate"). (*Id.* at 40.)

The Partnership accepted this valuation and used it to obtain financing in the fall of 2012. But in the fall of 2013, it ignored the 2012 Appraisal value and created its own valuation at almost 50% less. Now, without producing any information related to the 2012 Appraisal, the Partnership tells the Court that the 2012 Appraisal is irrelevant and riddled with errors. The Levine Trust and the Court are not required to take the Partnership at its word. The 2012 Appraisal is the only pre-suit valuation performed by a third party appraiser. It is not only relevant, it is extremely

persuasive as to the true value of the Levine Trust's interest. The Levine Trust should be permitted to test the validity of the 2012 Appraisal and the veracity of the Partnership's assertions of irrelevance and error through pretrial disclosure.

II. The Levine Trust Is Entitled To Information About The Merger Calculation Because The Insufficiency Of That Calculation Formed The Basis For The Levine Trust's Claim.

When the Partnership elected to determine a value for the merger consideration offered to the disinterested limited partners, it chose not to use the $33 million dollar value in the 2012 Appraisal. Instead, the Partnership developed a formula using a Net Operating Income of $825,000 and a cap rate of 4.9% ("Merger Calculation"). The aforementioned formula determined a value for the Partnership Property of approximately $16 million – a value significantly lower than in the 2012 Appraisal. (NYSCEF Doc. No. 2; Petition Ex. B.) Based on that formula, the Partnership supported its offer of $325,000 to the Levine Trust. Now, the Partnership seeks to abandon this valuation, claiming that the $16 million value is too low but the formula using a 4.9% cap rate was too generous.[1] (*See* NYSCEF Doc. No. 34 at 6).

It is important not to forget that the merger at issue was not an arms-length third party transaction. It was an interested party transaction wherein the General Partner and affiliates of Equity Resources, Inc. bought the interests of six disinterested limited partners. When the Partnership (in particular, the General Partner) determined the formula for the merger calculation, it did so as a fiduciary for the disinterested limited partners, including the Levine

[1] It is not surprising that the Partnership now seeks to abandon its formula. When you apply the actual 2013 financial statements to the formula used by the Partnership, the value of the Partnership Property is not $16 million, but $27 million. If you apply the projected Net Operating Income for 2014, the value of the Partnership Property would be as high as $46 million, depending on what vacancy factor is applied.

Trust. There are a number of questions around why the Partnership valued the Partnership Property the way it did. For example, why did the Partnership use an artificially depressed Net Operating Income of $825,000? Why did the Partnership use a 4.9% capitalization rate? Did the Partnership pay the capital accounts in addition to the merger consideration or was that included in the value?[2] The answers to each of these questions affect the determination of fair value for the Levine Trust's interest. As mentioned above, the Partnership now seeks to abandon its own formula on which it boasts to the Court that every single limited partner (other than the Levine Trust) was convinced not to dissent. (*See* NYSCEF Doc. No. 34.) The Levine Trust and the Court are entitled to know how the Partnership reached that formula, why, and why now it seeks to abandon it.

III. The Levine Trust Is Entitled To Information About The BCS Appraisal Procured By The Partnership In Response To The Dissent Because That Appraisal Suffers From A Number of Deficiencies.

The third – and most recent – valuation of the Partnership Property was commissioned in response to the Levine Trust's dissenter's rights claim. The new "BCS Appraisal" valued the Partnership Property on two different dates, November 11, 2013 and January 8, 2014, for a relevant value of approximately $21 million. (NYSCEF Doc. No. 34 at 7; Opposition at 7.) The Partnership asks this Court to accept the BCS Appraisal to the exclusion of any other valuations. And consequently, the BCS Appraisal is the only appraisal about which the Partnership has provided substantive information.

It begs the question: why? The BCS Appraisal is inconsistent with what the Partnership previously provided the disinterested limited partners in the Merger Calculation. Why did the

[2] If the capital accounts were included in the merger consideration, the "value" paid for each interest in the merger was significantly less than what the Partnership has represented. The Levine Trust's capital account is currently worth approximately $121,559.

Partnership elect to abandon all previous Appraisals? How did BCS Valuations reach its value? What documents did it consider? What was the scope of BCS's assignment?

Though the Partnership touts the BCS Appraisal as the only one of any relevance, in reality, the BCS Appraisal suffers from a number of errors. First, the income capitalization approach used by BCS used an entirely new cap rate of 6.75% without any explanation for why the cap rate has changed from the Partnership's previous selection of 4.9%. (*See* NYSCEF Doc. No. 33 at 62.) Second, BCS's calculations of Net Operating Income are inaccurate and lower than those reflected in the actual 2013 financial statements for the Partnership. (*Compare* NYSCEF Doc. No. 33 (Schwartz Aff. Ex. 1); *to* NYSCEF Doc. No. 46 Levine Aff. Ex. 11.) Third, the BCS Appraisal uses a sales comparison approach which fails to account for any of the properties considered in the 2012 Appraisal and instead compares dissimilar (and several smaller) properties. (*Compare* Levine Aff. Ex. 3 *with* NYSCEF Doc. No. 33; Schwartz Aff. Ex. 1.) Finally, the BCS Appraisal uses a 10% vacancy rate which is not accurate, does not reflect the actual vacancy rate of the Partnership Property which is currently at 5% and falling, and does not take into account the likely increases in rent that will result from the removal of HUD status.

The Partnership has not presented a single argument or piece of evidence to explain the deficiencies in the BCS Appraisal. The Levine Trust is entitled to pretrial disclosure so that it can determine why these errors exist and how they impact the overall value of the Partnership Property and accordingly, the Levine Trust's own partnership interest. At a minimum, the Levine Trust is entitled to its own appraisal of the Partnership Property which it cannot obtain without access to the relevant information.

CONCLUSION

For all the foregoing reasons, the Levine Trust respectfully requests that the Court grant its Application for Pretrial Disclosure in the form of written discovery and limited factual depositions and expert depositions on the issues relevant to its claim for fair value, in particular the 2012 Appraisal, the Partnership's formula for value determined in 2013 in connection with the merger, and the BCS Appraisal.

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