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

KENNETH ROSENBLUM, Plaintiff, - v. - CRAIG TREITLER and STEVEN ROSENBLUM, Preliminary Executors of the Estate of BERNICE ROSENBLUM, Defendants.	Index No.: 654177/2015 (Crane, J.)

PLAINTIFF'S POST-HEARING MEMORANDUM OF LAW

SCHLAM STONE & DOLAN LLP

Richard H. Dolan
Vitali S. Rosenfeld
26 Broadway, 19th floor
New York, New York 10004
Telephone: (212) 344-5400
Facsimile: (212) 3447677
Email: rdolan@schlamstone.com
Email: vrosenfeld@schlamstone.com

Attorneys for Plaintiff

TABLE OF CONTENTS

PRELIMINARY STATEMENT 1

ARGUMENT 4

I. NEITHER PARTY BEARS THE BURDEN OF PROOF ON THE ISSUE OF DETERMINING "FAIR VALUE" 4

II. THE COURT SHOULD CREDIT MR. FEENEY'S REAL ESTATE APPRAISALS 6

A. Mr. Feeney's Appraisals Are Reasonably Based on His Expert Analysis of the Applicable Real Estate Market 6

B. Mr. Farrell's Projected Residential Rental Income Is Artificially Low 9

C. Mr. Farrell Applies Artificially Inflated Capitalization Rates 11

D. Mr. Farrell's Appraisals Are Inconsistent with Defendant's Earlier Appraisals 13

III. THE COURT SHOULD CREDIT MR. MERCER'S BUSINESS VALUATION 15

A. Mr. Mercer's Valuation Accurately Reflects the LLC Entities' Accounting Records and Complies with the Applicable New York Law 15

B. All Intercompany Loans Must Be Treated the Same Way 17

C. The Cash Withdrawn After the Valuation Date Pursuant to This Court's Summary Judgment Order Should Have No Effect on the Valuation 19

D. There Is No Basis for Any Marketability Discount in This Case 21

IV. KENNETH IS ENTITLED TO STATUTORY PREJUDGMENT INTEREST SINCE THE DATE OF HIS WITHDRAWAL FROM THE LLC ENTITIES 28

CONCLUSION 32

TABLE OF AUTHORITIES

Cases **Page(s)**

Aurnou v. Greenspan,
161 A.D.2d 438 (1st Dep't 1990) 31

Blake v. Blake Agency, Inc.,
107 A.D.2d 139 (2d Dep't 1985) 29

Cavalier Oil Corp. v. Harnett,
1988 WL 15816 (Del. Ch. 1988) 4

Chiu v. Chiu,
2011 WL 9154233 (Sup. Ct. Queens County Jan. 7, 2011) 22

Cinque v. Largo Enterprises of Suffolk County, Inc.,
212 A.D.2d 608 (2d Dep't 1995) 26

Cohen v. Cohen,
279 A.D.2d 599 (2d Dep't 2001) 26

Matter of Digeser v. Flach,
54 Misc. 3d 1217[A], 2017 N.Y. Slip Op. 50220[U], *7 (Sup. Ct. Albany Co. 2017) 31

Ferolito v. Arizona Beverages USA LLC,
2014 N.Y. Slip Op. 32830[U] (Sup. Ct. Nassau Co. 2014) 31

Ferolito v. Arizona Beverages USA LLC,
2014 WL 5834862 (Sup. Ct. Nassau Co. Oct. 14, 2014) 22

Friedman v. Beway Realty Corp.,
87 N.Y.2d 161 (1995) 21, 25

Giaimo v. Vitale,
101 A.D.3d 523 (1st Dep't 2012) 25, 29

In re Dissolution of Penepent Corp.,
96 N.Y.2d 186 (2001) 21

In re Orchard Enters., Inc.,
2012 WL 2923305 (Del. Ch. 2012) 5

In re Superior Vending, LLC,
71 A.D.3d 1153 (2d Dep't 2010) 29, 30

Kassab v. Kasab, 56 Misc. 3d 1213(A) (Sup. Ct. Queens Co. 2017),
aff'd as modified, 195 A.D.3d 832 (2d Dep't 2021) 26

Levine v. Seven Pines Assocs. Ltd. P'ship,
156 A.D.3d 524 (1st Dep't 2017) 25

Loengard v. Santa Fe Indus., Inc.,
70 N.Y.2d 262 (1987) 30

Man Choi Chiu v. Chiu,
125 A.D.3d 824 (2d Dep't 2015) 26, 28, 29, 30

Mandelbaum v. Commissioner,
69 TCM (CCH) 2852 (Tax Ct. 1995) 22

Matter of Cohen,
168 Misc. 2d 91 (Sup. Ct. N.Y. Co. 1995) 4

PFT Tech., LLC v. Wieser,
181 A.D.3d 836 (2d Dep't 2020) 6, 28, 29, 30

Rosenblum v. Rosenblum,
214 A.D.3d 440 (1st Dep't 2023) 28

Vick v. Albert,
47 A.D.3d 482 (1st Dep't 2008) 26

Zelouf Intern. Corp. v. Zelouf,
47 Misc. 3d 346 (Sup. Ct. N.Y. Co. 2014) 22

Zelouf Int'l Corp. v. Zelouf,
45 Misc. 3d 1205(A) (Sup. Ct. N.Y. Co. 2014) 5, 26, 27

Statutes

Business Corporation Law §623 5

Business Corporation Law §1118 .... 4, 5, 6, 30

Business Corporation Law §1118(b) 30

Limited Liability Company Law §509 .... passim

Limited Liability Company Law § 606 30

Limited Liability Company Law § 606(b) 22

Limited Liability Company Law §702 30

Limited Liability Company Law §701(c) 22

Rules

CPLR § 5001 .... 3, 31

CPLR § 5001(a) 28, 30, 31

CPLR § 5004 32

Pursuant to the Court's Orders dated April 27, 2023 and May 23, 2023 (Docket ## 639 and 646), and the parties' subsequent scheduling stipulations, Plaintiff Kenneth Rosenblum ("Kenneth") respectfully submits this Post-Hearing Memorandum of Law.[1]

PRELIMINARY STATEMENT

The issue for decision by the Court is determining the "fair value" of Kenneth's 50% ownership interest in 132 Realty LLC ("132 Realty") and Village Realty LLC ("Village Realty" and, together with 132 Realty, the "LLC Entities"), from which Kenneth withdrew, as this Court had previously determined and the First Department affirmed, as of September 20, 2019 (the "Valuation Date"). For the reasons discussed below, the Court should determine that, as of the Valuation Date, (i) the value of the building at 132 Thompson Street ("132 Thompson") owned by 132 Realty was $33,000,000, and the value of the two buildings at 35-39 Christopher Street ("Christopher St.") owned by Village Realty was $29,000,000, as explained by Mr. Feeney; (ii) no marketability discount was appropriate; and (iii) the fair value of Kenneth's interest in 132 Realty is $17,542,000, and the fair value of his interest in Village Realty is $16,368,000, as explained by Mr. Mercer. The Court should therefore award Kenneth a judgment in the amount of $33,910,000 as the fair value for his 50% interest in the two LLC Entities, plus interest on that amount at the statutory rate of 9% per annum since the Valuation Date.

As the evidence adduced at the hearing demonstrated, the dramatic differences in the parties' real estate appraisals are mostly attributable to two critical errors by Defendant's expert, John Farrell of Colliers. First, Mr. Farrell ignored that the residential rents generated by the subject properties at the Valuation Date were significantly below market and failed to make appropriate

[1] The hearing exhibits are cited in the same alphanumeric form in which they were introduced at the hearing. Citations in the form "Tr. at ___" refer to the hearing transcripts.

adjustments to the projected rental income based on the contemporaneous rental market in the area. Second, Mr. Farrell compounded his error by applying an inflated capitalization rate, based on his selection of inappropriate comparable transactions involving properties from different neighborhoods and otherwise dissimilar to the subject properties. Indeed, according to Mr. Farrell, the location and characteristics of individual properties were irrelevant for purposes of analyzing "comparable transactions" – he treated all properties as if they were financial assets for which the only salient characteristic was return on investment rather than real estate properties for which "location, location, location" is a key determinant of present and future value.

The two errors together compounded the main flaw: disregarding the specific rental market to which the subject properties belong (largely intended for the NYU student population), including the respective per-building share of rent-regulated and free-market apartment units.

As a result of these errors, Mr. Farrell's appraisals are not only almost twice as low as those produced by Plaintiff's expert, but also 21% to 34% lower than Defendant's own appraisals of the same properties as of the 2016 valuation date, which were previously presented to the Court at trial. When the Court questioned that drop in value at the hearing, Defendant could offer nothing to explain or justify such a dramatic decline in value in that three-year period. The real explanation is that Defendant selectively manipulated the comparables and the rental data for the precise purpose of producing lower-value appraisals.

As to the business valuations, Defendant's expert Hubert Klein likewise uses several manipulation techniques to further lower the value of Kenneth's share of the companies. First, Mr. Klein applies a double standard with regard to corporate loans, acknowledging loans payable as they appear in the company records (thus decreasing the value of the LLC) but discounting loans receivable from the entities owned by the same two owners in the same proportion (which would

increase the value of the LLC). Second, he discounts the amount of cash the LLC Entities had at their disposal as of the Valuation Date, improperly deducting funds withdrawn after the Valuation Date pursuant to this Court's orders to equalize the parties' capital accounts. Not only does that tactic lack any justification whatever but it also gives Defendant double the value of that cash – first, by reducing the amount that Defendant owed Kenneth to equalize the capital accounts (the reason it was withdrawn); and now again, to reduce the amount Defendant owes Kenneth for his interest in the LLC Entities. Finally, Mr. Klein applies a 15% marketability discount, without any evidentiary support for that number and without any authority supporting any such discount in the circumstances of this case, where Kenneth's interest in the LLC Entities is effectively liquid and the companies' assets consist entirely of easily marketable real estate and cash.

In contrast to Mr. Klein's manipulations, Kenneth's expert, Mr. Mercer, explained that no marketability discount is required here, given that (i) the LLC Entities own only easily marketable real estate, (ii) imposing a marketability discount in these circumstances would effectively give Defendant more than its 50% share of the Entities' values; and (iii) doing so would be contrary to the requirements of law.

Finally, once the Court determines the "fair value" of Kenneth's 50% share in each of the LLC Entities as of the Valuation Date, it should also award him interest on those amounts at the statutory rate of 9%, pursuant to CPLR 5001 and the numerous authorities that consistently award such interest in LLC dissolution, withdrawal, and buyout cases. As both parties recognized at the hearing, the Appellate Division left that issue entirely to this Court's discretion. Under LLC §509, Kenneth was entitled to receive the "fair value" of his interest "within a reasonable time" after his withdrawal from the LLC Entities – but is still waiting to receive it, some seven years after his declared withdrawal, four years after the withdrawal date determined by the Court, and where

Defendant has also claimed loudly and often that Kenneth is not entitled to receive distributions from the profits earned by the LLC Entities during that seven-year period using his 50% share of their capital.[2] Under any reasonable notion of fairness and equity, Kenneth must be compensated for Defendant's use of his capital during this time.

ARGUMENT

I. NEITHER PARTY BEARS THE BURDEN OF PROOF ON THE ISSUE OF DETERMINING "FAIR VALUE"

During the hearing, the Court asked the parties to address the question of which party bears the burden of proof in a valuation proceeding such as this one. (Tr. at 83-84).

The issue was first explored at length by Justice Stephen Crane in *Matter of Cohen*, 168 Misc. 2d 91, 93–95 (Sup. Ct. N.Y. Co. 1995), *aff'd sub nom. Application of Cohen*, 240 A.D.2d 225 (1st Dep't 1997), in the context of a "fair value" appraisal under BCL §1118. Noting the absence of controlling case law on the subject and the variety of approaches applied in other jurisdictions, the Court found the "most persuasive explanation" in *Cavalier Oil Corp. v. Harnett,* 1988 WL 15816, at *20 (Del. Ch. 1988), *aff'd* 564 A.2d 1137 (Del. 1989). The Delaware court pointed out that applying the "traditional burden of proof rules" is "not permissible in a [statutory] appraisal" proceeding, where the governing "statute directs that the Court 'shall appraise' the fair value of the dissenting shareholders' shares." Justice Crane concluded that likewise "in the New York scheme, it is the court that has the obligation to establish fair value in an appraisal," which means that "there is no occasion to approach the problem by analyzing who has the burden of proof and finding against that party if she or it fails to carry this burden":

[2] As the Court will also recall, every time that issue has come up, Kenneth has been forthright in acknowledging that Defendant will be entitled to a credit for all such distributions received by him during the relevant period, to be applied against the amount Defendant owes him for the fair value of his interest in the LLC Entities as of the Valuation Date. But for years now, Defendant has been the only party controlling the LLC Entities and receiving distributions therefrom.

> However analyzed, the court at bar has a responsibility to "determine the fair value of petitioner's shares as of the day prior to the date on which such petition was filed." BCL §1118. This formulation defies application of a burden-of-proof approach. That each party presented their views of the value of petitioner's shares through expert testimony does not require or even invite the court to measure value using or rejecting either or both opinions of value. Neither does it exonerate the court from formulating a value . . . [even] after rejecting both experts' opinions.

Matter of Cohen, *supra*. When the issue came up again 19 years later, this time in the context of a "fair value" appraisal under BCL §623, Justice Kornreich noted that "the Court of Appeals [still] ha[d] not decided the question of who bears the burden of proof in a BCL appraisal proceeding" but referred to "this court's tradition of applying the 'no-burden' approach," under which "the court will consider the parties' expert testimony as persuasive evidence of fair value, but, at the end of day, and even if the court finds neither expert to be persuasive, it is the court's burden to make a fair value determination." *Zelouf Int'l Corp. v. Zelouf*, 45 Misc. 3d 1205(A), at *5 (Sup. Ct. N.Y. Co. 2014) (citing *Matter of Cohen*).[3]

The statute applicable here, LLC §509, provides that a "withdrawing member is entitled to receive . . . the fair value of his or her membership interest in the limited liability company as of the date of withdrawal." While LLC §509 does not expressly mention, as does BCL §1118, that it is the court's function to "determine the fair value," its language implies as much: if "fair value" is to be determined in a judicial proceeding, where the only possible decision-maker tasked with making that determination is the court. Notably, New York courts have often applied reasoning by analogy in valuation cases, applying guidance from the BCL where the LLCL lacks precisely

[3] Justice Kornreich also mentioned the Delaware origin of this approach, and noted: "[W]hile recent Delaware opinions frame the burden as a double, rather than a no-burden approach ['both parties bear the burden of proving their respective valuations by a preponderance of the evidence'], since 'the court may not adopt an either-or' approach to valuation and must use its own independent judgment to determine the fair value of the shares,' it appears that Delaware effectively continues to employ a no-burden approach." *Zelouf, supra*, at *5, note 5 (quoting *In re Orchard Enters., Inc.*, 2012 WL 2923305, at *5 (Del. Ch. 2012)).

the same language but the case nevertheless presents the same issue. *See*, *e.g.*, *PFT Tech., LLC v. Wieser*, 181 A.D.3d 836, 838 (2d Dep't 2020) (holding that "the equities" of the LLC membership buyout case pointed to the same valuation date – "the day before the action was commenced" – as the one specified in BCL §1118). Indeed, although no cases appear to have expressly analyzed the burden of proof issue under LLC §509, secondary sources refer to the "no-burden" approach established in *Matter of Cohen* and reiterated in *Zelouf* as applying to *any* business valuation proceeding, without distinguishing the type of entity involved:

> In assessing trial strategy, it is important to note that **neither party appears to bear the burden of proof in business valuation proceedings**. The few instances in which the issue has arisen resulted in a "no-burden" approach that put the onus on the court. [citing *Zelouf* and *Matter of Cohen*]. Under this approach, the court will consider the parties' expert testimony as persuasive evidence of fair value, but, at the end of day, and even if the court finds neither expert to be persuasive, it is the court's burden to make a fair value determination.

4E N.Y. Prac., Comm. Litig. in New York State Courts (5th ed.), § 111:30: *Neither party bears the burden* (emphasis added).

Accordingly, neither party bears the burden of proof in determining the "fair value" of Kenneth's interest in the LLC Entities. Rather, the Court determines that "fair value" with reference to the evidence it finds persuasive.

II. THE COURT SHOULD CREDIT MR. FEENEY'S REAL ESTATE APPRAISALS

A. Mr. Feeney's Appraisals Are Reasonably Based on His Expert Analysis of the Applicable Real Estate Market

As of the Valuation Date of September 20, 2019, Plaintiff's expert, Mr. Feeney of Cushman & Wakefield, appraised the value of the 132 Thompson building at $33,000,000 (Ex. 1 at 89), and the value of the two buildings at 35-39 Christopher Street at $29,000,000 (Ex. 2 at 86).

These appraisals primarily result from Mr. Feeney's application of the direct capitalization approach – a generally accepted "methodology used by appraisers and market participants to

estimate . . . a stabilized net operating income stream" from the subject properties. (Tr. at 25:16-19). This methodology involves: (a) calculating the Potential Gross Revenue, *i.e.* the amount of rent income the property is estimated to produce on an annual basis; (b) deducting estimated vacancy and collection losses, thus calculating the Effective Gross Revenue; (c) further deducting Operating Expenses, thereby arriving at the Net Operating Income ("NOI"); and (d) dividing the NOI by the appropriate capitalization rate, which results in the appraised Value of the property. (Ex. 1 at 66-79; Ex. 2 at 63-76). Applying this methodology, Mr. Feeney determined the NOI for 132 Thompson to be $1,130,701 (Ex. 1 at 79), and the NOI for Christopher St. to be $1,008,560 (Ex. 2 at 76). Dividing each of those numbers by the appropriate capitalization rate, which Mr. Feeney determined to be in the range between 3.25% and 3.50%, he calculated the value of 132 Thompson to be $33,000,000 (Ex. 1 at 87), and the value of Christopher St. to be $29,000,000 (Ex. 2 at 84).

As a "secondary method of valuation" for the buildings, Mr. Feeney applied the sales comparison approach, which considers actual sales of comparable properties in the applicable time period, with appropriate adjustments for any differences between the comparables and the subject properties. (Tr. at 29-30; Ex. 1 at 59-65; Ex. 2 at 56-62). Application of the sales comparison approach resulted in the appraised value of $31,000,000 for 132 Thompson and $27,000,000 for Christopher St. respectively. (Ex. 1 at 65; Ex. 2 at 62). Those results were sufficiently close to serve as a confirmation of Mr. Feeney's conclusions under the direct capitalization approach, which he ultimately accepted as final and presented to the Court, as the most accurate and reliable for these income-producing properties. (Ex. 1 at 88-89, Ex. 2 at 85-86; Tr. at 29:23-25).

Critically, Mr. Feeney's appraisals are based on his analysis of the rental income generated by the subject properties around the time of the Valuation Date in the context of the contemporary

market for similar properties in the West Village. Mr. Feeney's analysis "indicated that the subject properties [were] operating below market levels." (Tr. at 26:10-12; *see also id*. at 132:3-5, explaining that, "[i]n comparison to other area buildings . . . the subject property was commanding rents that were below market."). Because the vacant units or unregulated units generating below-market "preferential" rents "would have the opportunity to command a full market level of rent for the future," he concluded that, for "fair valuation" analysis, it was not appropriate to use the existing rent for capitalization purposes. (Tr. at 132:20-22). Instead, Mr. Feeney used an "estimate" that "mirror[ed] what market participants would do" in estimating the value of the buildings (Tr. at 27:1-3) – in other words, projected the income that a reasonable investor could generate by renting all the apartments at the maximum legal rent that the market would bear. (Ex. 1 at 67-79; Ex. 2 at 64-76).

Likewise, Mr. Feeney determined the applicable capitalization rate range of 3.25% to 3.50% by "consider[ing] sales in the marketplace with known cap rates from area buildings in the West Village and some in the East Village" (Tr. at 27:19-21) – in other words, by analyzing contemporaneous transactions involving similar properties in the same and similar neighborhoods. (Ex. 1 at 85-87; Ex. 2 at 82-84). As a result, Mr. Feeney's report is well grounded in the reality of the subject properties' location and size.

While Defendant's expert, Mr. Farrell of Colliers, claimed to use the same valuation methods, *i.e.* the direct capitalization approach supplemented by the sales comparison approach, he achieved dramatically lower valuation results, due primarily to two critical errors. The first is Mr. Farrell's failure to analyze the local residential rental market and incorporate any such analysis into his estimates of the subject properties' projected income. Part of the conceptual error in Mr. Farrell's approach was his selection of "comparable transactions" – he treated all properties as if

they were financial assets for which the only salient characteristic was return on investment, rather than real estate properties for which "location, location, location" is a key determinant of present and future value.

The second flaw stems in part from the same conceptual error: Mr. Farrell's application of a severely inflated capitalization rate arose from his use of inappropriate comparables derived from properties fundamentally dissimilar to the 132 Thompson and Christopher Street properties at issue here – *i.e.,* not-very comparable properties all intentionally selected to generate a high capitalization rate.

B. Mr. Farrell's Projected Residential Rental Income Is Artificially Low

Mr. Farrell contended in his testimony that "the rent roll [in the subject properties as of the Valuation Date] is essentially at market." (Tr. at 172:3-4). Yet, he could point to nothing in his reports demonstrating any analysis leading to that conclusion. (Tr. at 174). Indeed, Mr. Farrell admitted that nothing in his reports reflected any analysis of the residential rent market rates in the neighborhood where the subject properties are located. (Tr. at 182). Even though Mr. Farrell's reports contain a "Rent Roll Analysis" heading (Ex. 3 at 61; Ex. 4 at 66), those reports contain no actual analysis of what the **market rents** would be for any of the apartments listed in the rent roll. As Mr. Feeney pointed out, nowhere does Mr. Farrell's reports analyze whether the subject properties' rent levels were "at market, above market or below market" (Tr. at 32:20-23) – and "the lack of comparable analysis for residential rents" would render Mr. Farrell's reports "deficient by bank regulations" and would prevent a bank lender from making a commitment on such reports. (Tr. at 37:1-7).

Both of Mr. Farrell's reports contain the following statement concerning the properties he used as comparables in his application of the sales comparison approach: "Sales 1, 2, 3, and 4 are considered superior to the subject property and have been adjusted downward. These adjustments

were primarily based on the existing income levels of each property." (Ex. 3 at 92; Ex. 4 at 97). In other words, Mr. Farrell admits that four out of the five properties that he himself chose as comparables for his sales comparison analysis have higher income levels than either 132 Thompson or Christopher Street. It follows logically, if these properties are truly "comparable," that the rent income the subject properties generate is **below market**, which plainly contradicts Mr. Farrell's conclusory statement in his testimony that the rents in the subject properties are "at market." (Tr. at 172:3-4). Moreover, Mr. Farrell admitted that "if a market analysis showed that the rents in these buildings were below market . . . you would look at the rents as a new owner would, bring them up to market, assuming that that was legally possible to do, and use the rents that the new owner could achieve to determine valuation." (Tr. at 184:8-13). Yet, Mr. Farrell never did anything like that, because he simply assumed the problem away.

In particular, as Mr. Farrell's report for 132 Thompson Street shows, the occupancy rate in that building as of the Valuation Date was 84.6%, with the corresponding vacancy rate of almost 16% (Ex. 3 at 61, 174-75), while the contemporaneous average vacancy rate in the Lower West Side of Manhattan was 2.6%. (*Id*. at 37). In other words, the **actual** vacancy rate shown in the rent roll of 132 Thompson Street was over 5 times higher than the **market** vacancy rate in the same area at the same time. On cross-examination, Mr. Farrell admitted that an investor buying the building in 2019 would have likely renovated the vacant apartments and establish a new market rent for them going forward – which means that the valuation should factor in "the projected income" that one could then get for such apartments "at market rate." (Tr. at 163:22-164:9). Yet, Mr. Farrell's reports never made that adjustment to the rental income, and by failing to do so, came up with an artificially low estimate of income (which, of course, was his desired result). Although Mr. Farrell claimed on cross-examination that his appraisals had assigned some income to the

vacant apartments, he had to admit that "it isn't very clearly stated" in his reports and could not point to any place in his reports setting forth any such calculations. (Tr. at 169-170).

Likewise, the rent rolls of the subject properties show a large number of units with so-called "rent preferences" or rent adjustments, *i.e.* rents lower than those that could legally be charged. (Ex. 3 at 62-63; Ex. 4 at 67-68). By definition, such preferential rents are below market. Yet, Mr. Farrell made no attempt to adjust them upwards, in order to make his projected income closer to the market level of rents. Instead, his "Potential Gross Income" appears to be a simple sum of existing annualized rents. (Ex. 3 at 82; Ex. 4 at 87).

As a result, Mr. Farrell's numbers for "Effective Gross Income" of the subject properties are substantially lower than they should be. For 132 Thompson, it is $1,524,213 (Ex. 3 at 82), compared to $1,763,155 in Mr. Feeney's appraisal. (Ex. 1 at 79). For Christopher Street, it is $1,538,511 (Ex. 4 at 87), compared to $1,829,408 in Mr. Feeney's appraisal. (Ex. 2 at 76).

C. <u>Mr. Farrell Applies Artificially Inflated Capitalization Rates</u>

Mr. Farrell's error of failing to analyze the market rental rates and failing to adjust the projected rental income of the subject properties to the market level is compounded by his use of an unreasonably high capitalization rate of 4.75% for all subject properties. This rate is derived from Mr. Farrell's survey of "comparable" capitalization rates in "relevant property sales." (Ex. 3 at 80-81; Ex. 4 at 85-86). The problem is that Mr. Farrell chooses very dissimilar properties as his comparables.

As the Court noted at the hearing, "the Village [is] the most expensive neighborhood in the city" – probably because it is "the most desirable." (Tr. at 198:2-6). Strikingly, Mr. Farrell made no effort to select as his comparables other properties in the West Village, where 132 Thomspon and Christopher Street are located. Indeed, most of Mr. Farrell's comparables are from completely

different parts of the City, and two out of the six are much differently sized buildings far uptown – as the Court noted, in a "completely different neighborhood." (Tr. at 198:2).

Nor did Mr. Farrell make any attempt to compare the subject properties only to buildings of similar size or a similar number of apartments free from rent regulation. For instance, Mr. Farrell's reports note that 132 Thompson has 26 market-rate units versus 11 rent-stabilized and 2 rent-controlled units, while the Christopher Street buildings have 39 market rate units and only 4 rent-stabilized and 1 rent-controlled units. (Ex. 3 at 61; Ex. 4 at 66). But his reports do not mention any similar information about any of the comparables. Given Mr. Farrell's lengthy discussion of the new rent regulation laws enacted in New York in 2019 (Ex. 3 at 65-69; Ex. 4 at 70-74), his failure to address the percentages of market rent units in the buildings actually impacted by those regulations is telling. For present purposes it is enough to note that he never engages in an analysis comparing that impact on the properties he selected as his comparables with either 132 Thompson or Christopher Street. Again, the decision not to do so – and it was clearly not a mere oversight – reflects the underlying objective of manipulating the data to generate a low valuation.

These and other mistakes in Mr. Farrell's analysis of comparables make that analysis essentially worthless. (Ex. 3 at 80-81; Ex. 4 at 85-86). In particular:

- 124 W 73rd St.: the building is uptown; it is under 17 feet wide and has only 8 residential units, *i.e.* is much smaller than the subject properties (Ex. 6 at 5; Ex. 7 at 2). In any event, Mr. Farrell could not explain the origin of the allegedly "reported" 5% capitalization rate for this building, nor of his alleged Net Operating Income for it. (Tr. at 204-206).

- 11 Carmine Street: the building had no known renovations since 1891, as compared to 132 Thompson renovated in 2014 (Ex. 3 at 84 and Tr. 211-212), and 11 Carmine had a much higher percentage of commercial rent income than the subject properties. (Ex. 9 at 3).

- 22 St. Marks: the building is in the East Village (rather than the West Village where the subject properties are), was last renovated in 1984, and has over 50% of rent-regulated units. (Ex. 5 at 2; Tr. at 234:3-12).

- 202 Ninth Avenue: the building is in a different neighborhood (at 23rd Street, Tr. at 237) and has only 5 total units (Ex. 10 at 2; Tr. at 240).

Notably, Mr. Farrell further compounded the error of using these inapt comparables by using many of them again in his sales comparison approach analysis. (Ex. 3 at 84; Ex. 4 at 89). The additional comparables he uses in the sales comparison approach suffer from similar flaws: many are in neighborhoods inferior to the subject properties; many have not been renovated as recently as 132 Thompson; some are significantly smaller than the subject properties, such as 418 East 9th Street with only 13 units (Ex. 3 at 87); and there is no analysis of the comparative share of free market apartments in any of these buildings versus such share in the subject properties. As a result, Mr. Farrell's sales comparison appraisals are as skewed as his direct capitalization appraisals. As Mr. Feeney bluntly put it, Defendant's appraisals "are not reasonable [or] supportable." (Tr. at 36:23-25).

D. Mr. Farrell's Appraisals Are Inconsistent with Defendant's Earlier Appraisals

One indisputable fact best illustrates the unreasonably low level of value proffered in Mr. Farrell's reports: they are dramatically different not only from Plaintiff's expert's appraisals, but also from Defendant's own appraisals previously presented to the Court at the 2020 trial. For the Christopher Street properties, Defendant's prior appraisal as of the 2016 valuation date was $24.1 million; Mr. Farrell's appraisal as of 2019 is $16 million, thus alleging an about 34% decrease in value.[4] Mr. Farrell could not point to anything in the marketplace that would explain such a sharp decline in value within the three years in question. (Tr. at 319:20-320:25). Similarly, Defendant's prior appraisal of 132 Thompson as of 2016 amounted to $23.4 million; Mr. Farrell's

[4] Looking at the same numbers from the 2019 perspective makes the difference even more stark: it would mean that, in 2016, the property was worth over 150% of its 2019 value.

appraisal as of 2019 went down to $18.5 million, which is a 21% decline in value.[5] As the Court stated at the hearing: "And I also would like an explanation. . . why the values went down so much between 2016 and 2019. That's weird, right?" (Tr. at 337:22-25). Neither Mr. Farrell nor the Estate ever offered any coherent explanation.

To the contrary, Mr. Farrell admitted that the West Village, between 2016 and 2019, was "an excellent environment for real estate values in that the interest rates were low, supply was limited, demand was high" – which would "lead to higher values going up over time", so that one "could expect real estate prices in the West Village [to] have been increasing over that period." (Tr. at 245). But Mr. Farrell's own appraisals, when compared to Defendant's prior appraisals, are so inconsistent with these statements that the most plausible explanation jumps out: Mr. Farrell's errors and manipulations were designed to generate a lower value, and his appraisals artificially lowered the value of the subject properties.

In contrast, the valuations and capitalization rates used by Mr. Feeney were in line with those derived by Kenneth's expert at the 2020 trial, Mr. Salmon, who applied a capitalization rate of 3.5% and concluded that the value of the properties were $34.5 million for Christopher St. and $32 million for 132 Thompson. Accepting the statement of Defendant's expert that, between 2016 and 2019, conditions in the real estate market for the West Village would have "le[]d to higher values going up over time," Mr. Feeney's valuations and capitalization rates make much more sense on this record.

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[5] At the same time, the capitalization rates of 3.75% to 4% that Defendant's trial expert used in his appraisals as of 2016, dramatically increased to the 4.75% now used by Mr. Farrell, whose reports and testimony contain no explanation for such an increase. Notably, Mr. Mercer found it inexplicable how capitalization rates could go up so "significantly" between 2016 and 2019, *i.e.* "in a period of time when interest rates were flattish" and the environment was "generally favorable for real estate value." (Tr. at 337:3-12).

In short, the Court should accept Mr. Feeney's analysis as supported by the totality of the evidence, and reject the artificially low valuations of Mr. Farrell.

III. THE COURT SHOULD CREDIT MR. MERCER'S BUSINESS VALUATION

A. Mr. Mercer's Valuation Accurately Reflects the LLC Entities' Accounting Records and Complies with the Applicable New York Law

Mr. Mercer is a nationally renowned business valuation expert, who has written extensively on the subject of "fair value" and whose valuation testimony has been credited by numerous courts, including in New York. (Ex. 11 at 149-159, 82). In his valuation of 132 Realty and Village Realty, Mr. Mercer applied the asset-based approach, which is commonly used for valuation of real-estate holding companies, and which essentially consists of calculating the net balance of each entity's assets and liabilities as of the Valuation Date. (Ex. 11 at 99-100).

In this case, the major assets of both LLC Entities are the respective buildings they own. With regard to these properties, Mr. Mercer relied on Mr. Feeney's real estate appraisals, which he subjected to an independent review and which he found credible and reliable. (Ex. 11 at 17-19; Tr. at 333-35). As to the LLC Entities' other assets, Mr. Mercer examined the companies' general ledgers, discussed them with the companies' CPA, and thus determined "the amount of cash that [each] company had on" the Valuation Date. (Tr. at 332:1-14; Ex. 11 at 105, 108). Mr. Mercer likewise "took account of both loans receivable and loans payable just as they existed on the valuation date." (Tr. at 333:4-7; Ex. 11 at 105, 108). Adding the assets of each LLC Entity and deducting its liabilities, Mr. Mercer determined the net asset value of each company: $35,084,000 for 132 Realty, and $32,735,000 for Village Realty. (Ex. 11 at 106, 109).

Next, Mr. Mercer determined the "fair value" of Kenneth's 50% interest in each company. The central inquiry in such an analysis is whether any marketability discount would be applied. Based on his consideration of the nature of the specific companies at issue and his extensive

analysis of the applicable New York authorities from his perspective as a business valuator (Ex. 11 at 45-88), Mr. Mercer, a leading expert on marketability discounts,[6] concluded that no such discount should be applied here. (Ex. 11 at 87).

In particular, where, as here, the companies are essentially corporate "wrappers" for the real estate they hold, exposure to the market is already embedded in the underlying real estate appraisals, and applying a marketability discount on top of those appraisals would constitute double-dipping on behalf of the buying co-owner. As Mr. Mercer explained in his testimony and as the Court aptly summarized at the hearing, "the marketability discount is really . . . baked in at the property level," so that "when you start evaluating an LLC that's holding the real estate, you don't have to worry about a marketability [discount] because it's already baked in." (Tr. at 364:16-22). For this reason and others, as Mr. Mercer's statistical analysis demonstrates, in the **vast majority** of cases concerning valuation of a real estate holding company, New York courts have applied a **zero** marketability discount. (Ex. 11 at 84, 141-42).

Having likewise applied a zero marketability discount, Mr. Mercer concluded his analysis by calculating the "fair value" of Kenneth's interest in each of the companies as 50% of the company's net value. As a result, he concluded that the fair value of Kenneth's interest in 132 Realty as of the Valuation Date is $17,542,000, and the fair value of his interest in Village Realty is $16,368,000. (Ex. 11 at 107, 110). The Court should credit this valuation as correct, because it is fully supported by the evidence and by the applicable authorities.

Mr. Klein's alternative valuations, while ostensibly applying the same methodology, represent Defendant's manipulative attempts to artificially lower the value of Kenneth's interest.

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[6] Mr. Mercer has written and spoken frequently on the subject for many years; and one of his books is "Quantifying Marketability Discounts." (Ex. 11 at 155; Tr. at 423:15-16).

B. All Intercompany Loans Must Be Treated the Same Way

As apparent from both Mr. Mercer's and Mr. Klein's business valuations, the books and records of the LLC Entities reflect several loans payable and loans receivable between the LLC Entities and the other companies jointly and equally owned by Kenneth and Bernice (the "Intercompany Loans"). In particular, as of the Valuation Date, 132 Realty had loans receivable from Standard Realty Associates ("Standard" or the "Partnership") totaling $2,072,336, as well as loans payable to Standard Realty Associates Inc. ("Standard Inc.") totaling $865,005 and loans payable to Restoration Realty Development Corp. ("Restoration") totaling $6,585. (Ex. 12 Ex. 3; E. 11 at 105). Likewise, Village Realty had loans receivable from Standard totaling $2,696,588, as well as loans payable to Restoration totaling $151,924. (Ex. 13 Ex. 3; Ex. 11 at 108). As noted above, Mr. Mercer's valuation took account of all these Intercompany Loans at their face value, as they are found on the companies' books. Mr. Klein, however, eliminated the loans receivable while preserving the loans payable, thereby artificially depressing the companies' net value. Such disparate treatment of the Intercompany Loans has no legal basis and is unfairly prejudicial to Kenneth.

As Mr. Klein stated in his reports, he eliminated the loans receivable from Standard as "uncollectible." (Ex. 12 at 21; Ex. 13 at 21). As Mr. Klein explained in his testimony, one reason that he found these loans "uncollectible" was the absence of any notes or instruments for these loans (Tr. at 447:17-20) – even though Kenneth and Bernice never signed any notes or instruments for **any** of the numerous intercompany loans or personal loans from the entities they co-owned, and none of such loans has ever been eliminated as uncollectible. Indeed, as Mr. Klein admitted, none of the loans payable by the LLC Entities to Standard Inc. or Restoration had any notes or instruments either (Tr. at 454:11-12) – which did not lead Mr. Klein to consider them uncollectible. Needless to say, as a matter of law, a loan does not become "uncollectible" merely because it is

not documented by a note or another instrument, and the Estate never previously took a position that the loans receivable by the LLC Entities were uncollectible (to say nothing of the loans taken by Kenneth and resolved by the parties' 2013 Settlement).[7] To the contrary, in numerous written submissions to the Court, the Estate vigorously argued that these particular loans receivable by the LLC Entities were valid, valuable, and payable on demand. (NYSCEF #566 at 10; #579 at 5-6).

Another reason why Mr. Klein chose to disregard the loans receivable as "uncollectible" was his assumption that "the Partnership is insolvent." (Ex. 12 at 21; Ex. 13 at 21). However, as Mr. Klein did not and could not deny, under Partnership Law, partners are personally liable for the debts of the Partnership, which means that any loan the Partnership was unable to pay would be collectible 50% from Kenneth and 50% from the Estate. As Mr. Klein admitted, he had no reason to believe that either Kenneth or the Estate was insolvent (Tr. at 449).[8] The inexorable conclusion is that there was no good reason to consider the loans "uncollectible."

Mr. Klein cited the Estate's prior demand to Kenneth, and Kenneth's alleged refusal to pay, as a further reason for his conclusion that the loans were uncollectible. (Tr. at 449-50). This faulty reasoning completely ignores that (a) no demand was never made to Kenneth based on the premise that the Partnership is insolvent or unable to pay the loans; and (b) the Estate never paid its own 50% share of the loans receivable by the LLC Entities. Even more critically, it ignores the fact that the Court previously considered the loans receivable issue in the context of the parties'

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[7] The 2013 settlement referred to similar loans, and the parties agreed to a $14 million payment in satisfaction of them and other matters, even though none of the loans was ever documented except, as here, by a notation on the entities' books.

[8] Indeed, Mr. Klein affirmatively knew that neither Kenneth nor the Estate were insolvent – at the very least because the Estate is the only remaining member of the LLC Entities, which Mr. Klein himself valued at over $29 million, and Kenneth, as a result of this very proceeding, would be entitled to a judgment of over $14 million even under Mr. Klein's biased valuations.

accounting, including the Estate's demands to Kenneth in connection with these loans, but never found the loans to be uncollectible, and "tabled" the issue of the loans to be decided in the context of the LLC Entities. (NYSCEF #587 at 2; #586 at 29-30).

In any event, while eliminating the loans receivable worth millions of dollars in favor of the LLC Entities, Mr. Klein did not eliminate any of the loans payable – even though he admitted that he did not know when they had accrued and did not consider whether they would be barred by the applicable statutes of limitations. (Tr. at 457:21-458:2). As Mr. Klein further admitted, he knew that both Standard Inc. and Restoration, as of the Valuation Date, were owned by Kenneth and Bernice on a 50-50 basis, just like the Partnership – in other words, that all the companies involved with the Intercompany Loans were owned by the same two people in the same proportion. (Tr. at 455). Yet, he eliminated the very substantial loans receivable to the LLCs while maintaining loans payable by the LLCs. Nothing in Mr. Klein's report or testimony offers any good faith basis for such disparate treatment, which has only one apparent purpose – to depress the value of the LLCs at Kenneth's expense.

Instead, the fair and straightforward way to treat the Intercompany Loans is to do what Mr. Mercer did: to consider "both loans receivable and loans payable just as they existed on the valuation date." (Tr. at 333:4-7). The LLC Entities' loans payable and loans receivable should be treated **the same way**, as a matter of both law and equity. Mr. Klein's approach is inequitable on its face, and again, reflects an intention to generate artificially low values.

C. <u>The Cash Withdrawn After the Valuation Date Pursuant to This Court's Summary Judgment Order Should Have No Effect on the Valuation</u>

As Mr. Mercer determined based on the general ledger of 132 Realty and discussions with the company's CPA, that ledger records $503,690 as "the amount of cash that the company had on" the Valuation Date. (Tr. at 332:1-14; Ex. 11 at 105). Mr. Klein admitted that that Mr. Mercer

was correct because that cash "was in the company's books." (Tr. at 459:3). The same is true for Village Realty: the books of that entity recorded $874,018 as the amount of cash Village Realty had on the Valuation Date. (Ex. 11 at 108).

Yet, Mr. Klein made downward adjustments for cash of $329,736 for 132 Realty (Ex. 12 Ex. 3, item "a"; Tr. at 458:13-15) and $840,097 for Village Realty (Ex. 13 Ex. 3, item "a"; Tr. at 458:16-18). Mr. Klein said he relied on the companies' bank statements for these numbers but, when asked whether the bank statements reflected that balance as of the last day of September 2019 rather than of the Valuation Date (September 20, 2019), confessed: "As I sit here I don't recall. . . . I don't know." (Tr. at 460:1-6). Indeed, both in his reports and in his testimony, Mr. Klein spoke of having "adjusted the cash balance" downward. (Ex. 12 at 20; Ex. 13 at 20; Tr. at 458:13-18).

Mr. Klein's reports give the game away as to the source of his downward "adjustment": "On September 20, 2019, the trial court issued a ruling that stated that the parties could withdraw money to equalize the capital accounts," which made it, as of the valuation date, "known, or knowable and reasonable to believe, that money would be withdrawn" (Ex. 12 at 21; Ex. 13 at 21) – not only from the Partnership account, but also from accounts of the LLC Entities. More specifically, as the Court well knows and as Mr. Klein could not deny, the Court's September 20, 2019 Summary Judgment Order specifically allowed Kenneth to withdraw funds from the joint companies to equalize the capital accounts. Kenneth in fact withdrew funds a few days after the Summary Judgment Order, including some funds from the accounts of the LLC Entities, for that purpose. (Tr. at 460-61). Mr. Klein made a downward adjustment for the funds Kenneth withdrew – because, in his opinion, "the assets in the balance sheet for valuation would have been lower by the amount of funds he was able to take out," as "[t]hat was a balance that went to one side

unilaterally." (Tr. at 462:6-9). What Mr. Klein did not take into account is that, once Kenneth withdrew those funds for equalization purposes, the Estate got credit for those withdrawals from the capital accounts perspective – which would make it double-dipping for the Estate to deduct these same funds from the cash that clearly was on the LLC Entities' balance sheet on the Valuation Date.

In short, there was no good basis for Mr. Klein's downward "adjustment" of the LLC Entities' cash balance as of the Valuation Date, and any such adjustment should be disregarded. Rather, the Court should credit the companies' balance sheets contained in Mr. Mercer's report. (Ex. 11 at 105, 108).

D. There Is No Basis for Any Marketability Discount in This Case

Having based his valuation on Mr. Farrell's artificially low real estate appraisals and having manipulated the LLC Entities' balance sheets as set forth above, Mr. Klein completed the job of artificially minimizing the value of Kenneth's 50% interest by applying a 15% marketability discount. But Mr. Klein's reports contain no coherent explanation as to how that number was reached, and his testimony effectively admits that there is no basis for it.

Both of Mr. Klein's reports state in identical language: "The term 'fair value' is defined herein, in accordance with New York law. As such, fair value herein is interpreted to mean fair market value to the holder as a going concern without consideration for a discount for lack of control." (Ex. 12 at 4; Ex. 13 at 4). New York law does not permit a minority discount in the valuation of an ownership interest for buyout purposes. *See Friedman v. Beway Realty Corp.*, 87 N.Y.2d 161 (1995).[9] While nominally acknowledging that rule, Mr. Klein nonetheless applied a

[9] *See also In re Dissolution of Penepent Corp.*, 96 N.Y.2d 186, 194 (2001) (explaining that a minority discount "would violate two central equitable principles of corporate governance" because it "would deprive minority shareholders of their proportionate interest in the corporation as a going concern" and "would result in shares of the same class being treated unequally)."

minority discount through the guise of a "lack of marketability" discount. While Mr. Klein goes through the motions of citing various irrelevant factors, in its essence his valuation boils down to his assumption that someone would be unlikely to purchase Kenneth's interest in the LLCs because of his lack of control. As Justice Kornreich once put it, "applying a DLOM [discount for lack of marketability] here would be the economic equivalent of imposing a minority discount." *Zelouf Intern. Corp. v. Zelouf*, 47 Misc. 3d 346, 351 (Sup. Ct. N.Y. Co. 2014).

Mr. Klein's consideration of the marketability discount is focused on the so-called *Mandelbaum* factors. (Ex. 12 at 23; Ex. 13 at 23-24). Those factors originate from *Estate of Mandelbaum v. Commissioner*, 69 TCM (CCH) 2852, at *39-40 (Tax Ct. 1995), a tax court case in which the court identified a series of criteria to determine a valuation for the sale of restricted stock in an operating company. As Mr. Klein admitted on cross-examination, *Mandelbaum* had nothing to do with a real estate holding company or with withdrawal from an LLC. (Tr. at 468:5-14). It is thus no surprise that, as Mr. Klein also admitted, no New York case dealing with valuation of a real estate holding company in the context of determining fair value under New York law has ever applied the *Mandelbaum* factors. (Tr. 467:13-16).[10]

It makes no sense to apply the *Mandelbaum* factors for another fundamental reason: because the LLC Entities were formed before 1999, they are governed by the pre-1999 LLC law, and thus anyone buying Kenneth's interest would have the absolute right to withdraw from the LLCs (just as the Court has already found Kenneth did). *See* LLC §701(c); former LLC § 606(b); *Chiu v. Chiu*, 2011 WL 9154233 (Sup. Ct. Queens County Jan. 7, 2011), *aff'd sub nom. Chiu v.*

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[10] While, as the Court noted at the hearing, Justice Driscoll *referred* to the Mandelbaum factors in *Ferolito v. Arizona Beverages USA LLC*, 2014 WL 5834862, at *19 (Sup. Ct. Nassau Co. Oct. 14, 2014), he did not *apply* them or base any analysis on them. In any event, *Ferolito* was not valuing a real estate holding company. Nor, as the Court also noted during the hearing, have Delaware courts been applying the *Mandelbaum* factors in "fair value" cases. (Tr. at 474:17-22).

Man Choi Chiu, 92 A.D.3d 914 (2d Dep't 2012). Indeed, that was the basis of this Court's summary judgment determination granting Kenneth's withdrawal claim. (NYSCEF #423 at 3). Thus, any sophisticated purchaser would know that the ownership interest here – in marked contrast to *Mandelbaum* and similar cases – is the opposite of illiquid: a member holding a 50% ownership interest in the two pre-1999 LLCs has a statutory right to withdraw and receive "fair value" for his interest – *i.e.*, the interest can be liquidated at will by the holder for fair value, which is all that "liquid" means in the context of an interest in a real estate holding company. And, if the LLCs were dissolved and the properties distributed pro rata to the members, each member would have an absolute right to partition the underlying real property, receiving fair value by that route as well.

In short, the illiquidity concerns about restricted stock that gave rise to the *Mandelbaum* factors in that case are completely irrelevant here. Yet, they were the governing premise for the Klein valuation. But even taken at face value, Mr. Klein's application of the *Mandelbaum* factors makes no sense. As Mr. Klein admitted on cross-examination, he did "not calculate how much each factor increases or decreases the discount" and did not assign any "numerical value" to each of those factors. (Tr. at 472:12-17). Moreover, Mr. Klein's specific application of many of these factors (Ex. 12 at 23; Ex. 13 at 23-24) defies logic and common sense. In particular:

- "Private versus public sales of the ownership interest": because this sale is private, Mr. Klein increases the discount. But this is not a typical private sale to a hypothetical third-party buyer. Instead, this is a compulsory sale to Bernice's Estate, given that the Court has already directed Bernice to buy out Kenneth's interest. So this is in fact the opposite of the restricted market situation of a typical private sale: Kenneth's interest is entirely liquid because the sale is mandatory.

- "Company's dividend policy": because there is "none," Mr. Klein increases the discount. But the lack of a dividend policy does not make Kenneth's interest in the LLCs any less liquid, nor does it in any way restrict the terms of the Court-ordered sale of that interest. Moreover, as Mr. Klein admitted, despite the absence of a "dividend

policy," the LLC Entities made a constant stream of distributions akin to dividends here, because the LLCs own profitable real estate generating rent income. (Tr. at 479:6-16).

- "Nature of the Company, its history, its position in the industry, and its economic outlook": Mr. Klein calls it "moderate" and says it has no impact on the discount. But the companies here are pre-1999 LLCs with real estate holdings. Under the LLCL, there were only two alternatives once Kenneth withdrew from these LLCs: either Bernice paid him "fair value" for his 50% interest as of his withdrawal date, or the LLCs had to be dissolved and the underlying properties sold. There is **no marketing** involved in either alternative, and Mr. Klein's mental exercise of analogizing to a hypothetical buyer of illiquid securities again has no relevance here.

- Mr. Klein says that the "[c]ompany's management" is "poor" and increases the discount on that basis – even though he admits having relied on the Colliers' real estate appraisal, including its assumption of competent and reasonable management. (Tr. at 481:23-8). The Estate cannot have it both ways. In any event, the alleged "poor" management does not alter the terms of the Court-ordered sale.

- "Restrictions on transferability of ownership interest": Mr. Klein states "none," thus recognizing that there are no restrictions on transferability of Kenneth's interest in the LLCs, and that his interest is entirely liquid. Yet, in the next factor, he states that the "[h]olding period for ownership interest" is "long" and counts it to increase the discount. But if there are no restrictions on transfer, it follows that there can be no "holding period" for Kenneth's interest in the LLCs.

- Likewise, Mr. Klein increases the discount based on the next factor, "[c]ompany's redemption policy," stating that there is "none." But the Court has already allowed Kenneth to withdraw from the LLCs, and no "redemption policy" is needed to implement the redemption of his interest in the companies.

- "Costs associated with making a public offering": Mr. Klein states "costly" and counts it to increase the discount. But on cross-examination, he admitted that no "public offering" and no associated "costs" would be required here. (Tr. at 482:18-25).

Given Mr. Klein's admission that there are no "[r]estrictions on transferability of ownership interest" here (Ex. 12 at 23), all his citations to restricted stock studies (*id*. at 24-25) are as irrelevant as his discussion of the *Mandelbaum* factors. What is lacking in Mr. Klein's reports is any analysis of the applicable New York law. Indeed, the only New York authorities he cites in

his reports, without analysis, are *Friedman v. Beway Realty Corp.,* 87 N.Y.2d 161 (1995),[11] *Giaimo v. Vitale*, 101 A.D.3d 523 (1st Dep't 2012),[12] and *Levine v. Seven Pines Assocs. Ltd. P'ship*, 156 A.D.3d 524 (1st Dep't 2017). It is obvious why Mr. Klein cherry-picked these three cases: in all of them, a marketability discount was applied. But all three are clearly distinguishable. *Beway* involved stock in a corporation (87 N.Y.2d at 167), not interest in a pre-1999 LLC as here; thus, there was no option for a shareholder in *Beway* to withdraw from the company as Kenneth has done here. In *Giaimo*, the entity was also a corporation, not a pre-1999 LLC – and the *Giaimo* court expressly stated: "There are **increased costs and risks associated with corporate ownership of the real estate** in this case that would not be present if the real estate was owned outright. These costs and risks have a negative impact on how quickly and with what degree of certainty the corporations can be liquidated, which should be accounted for by way of a discount." 101 A.D.3d at 524 (emphasis added). Here, by contrast, there is no "corporate ownership," and the real estate can be liquidated as if it were "owned outright" – which means that there are no "costs and risks" calling for a discount. Finally, *Levine* was a proceeding to determine the value of a dissenting limited partner's interest in a partnership – which is, again, very different from the instant situation featuring withdrawal from a pre-1999 LLC.

What Mr. Klein apparently did not consider are the many New York cases involving much more comparable facts where no marketability discount was applied. Indeed, in the **vast majority** of cases concerning valuation of a real estate holding company, New York courts in each of the Appellate Departments have applied a **zero** marketability discount. (Ex. 11 at 84, 141-42; Tr. at

[11] *Beway* and its principles are discussed at length in Mr. Mercer's report. (Ex. 11 at 62-72).

[12] *Giaimo* is also discussed in detail in Mr. Mercer's report. (Ex. 11 at 77-78).

342:19-343:24).[13] As the First Department succinctly explained: "The unavailability of the discounts is particularly apt here, **where the business consists of nothing more than ownership of real estate**." *Vick*, 47 A.D.3d at 484 (emphasis added). In *Vick*, the real estate holding company was a general partnership, from which any partner can withdraw at will, forcing a dissolution and sale; that situation of liquidity for a partner is much closer to the situation here, in which a member of the LLC has an absolute right to withdraw and be paid "fair value" than the situation of a corporate "wrapper" in *Giaimo* or any other less liquid arrangements on which Mr. Klein cited.

Indeed, as Justice Kornreich pointed out in *Zelouf Int'l Corp. v. Zelouf*, 45 Misc. 3d 1205(A), at *8 (Sup. Ct. N.Y. Co. 2014), the purpose of a DLOM (*i.e.* discount for lack of marketability) is to account for any "risk associated with the illiquidity of the shares" – which means that the discount has no place in the absence of a genuine liquidity risk:

> [T]he rationale for a applying a DLOM breaks down when one considers that **any liquidity risk** associated with Old ZIC **is more theoretical than real**. No sale of the company has occurred since its 1984 founding. Nor is there any reason to think that Danny will walk away from a company providing him with millions of dollars in income, a similar, low interest loan facility, personal and family perks and control unless he eventually turns it over to other family members, years down the road. The company, without Nahal and her family, will always remain under the

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[13] *See, e.g., Vick v. Albert*, 47 A.D.3d 482, 484 (1st Dep't 2008) (finding 0% marketability discount appropriate in determining fair value of interest in partnership holding a single property); *Man Choi Chiu v. Chiu*, 125 A.D.3d 824, 825 (2d Dep't 2015) (affirming trial court's refusal to apply any "discount for lack of marketability" in a dissolution case concerning a real estate holding LLC); *Cohen v. Cohen*, 279 A.D.2d 599, 600 (2d Dep't 2001) (where "the subject real estate holdings consist solely of real property . . . the Supreme Court properly determined not to apply a discount for lack of marketability"); *Cinque v. Largo Enterprises of Suffolk County, Inc.*, 212 A.D.2d 608, 609-10 (2d Dep't 1995) (affirming refusal "to discount the value of the petitioner's shares of the corporation due to their lack of marketability" where "the value of the corporation is attributable solely to real property and cash"); *Kassab v. Kasab*, 56 Misc. 3d 1213(A), at *8-9 (Sup. Ct. Queens Co. 2017) (recognizing Mr. Mercer as "an expert on marketability discounts" and crediting his valuation which "did not apply any marketability discount, since the companies were real-estate holding companies, whose valuation already relies upon market exposure."), *aff'd as modified*, 195 A.D.3d 832 (2d Dep't 2021).

> control of the Zelouf family. This makes the company's **illiquidity irrelevant**, **mooting the concern for which a DLOM accounts**.

Id. (emphasis added). The same reasoning applies here to rule out any discount.

In summarizing his findings, Mr. Klein listed "the lack of an operating agreement for the Company" as one of the considerations in favor of a marketability discount. (Ex. 12 at 25; Ex. 13 at 26). However, the lack of an operating agreement has no effect on the liquidity of Kenneth's interest, just as it has no effect on the liquidity of the underlying real estate owned by the LLCs. Mr. Klein admitted that "the Company owns real property, and one could directly buy the underlying assets without the additional layer of ownership." (*Id.*). For that reason, as Mr. Mercer put it, "[t]he absence of an operating agreement has really no bearing if we're selling the entire company . . . because the buyer couldn't care less about what operating agreement exists at a point in time" – which makes it "improper to use the lack of an operating agreement effectively as a restriction on transfer." (Tr. at 361:4-10).

Mr. Klein is similarly misguided in counting "the ongoing litigation between the owners" as a factor calling for a marketability discount. (Ex. 12 at 25; Ex. 13 at 26). Lowering the fair value of Kenneth's 50% membership interest because of his litigation with his mother's Estate would have the effect of a corresponding increase in the value of the Estate's 50% interest – which means that Mr. Klein's valuation plainly favors one member of the LLCs over the other in the ongoing litigation, and effectively rewards delay for its own sake. As Mr. Mercer put it in his testimony, it would be "from a valuation perspective improper to take a discount for the litigation. Because this trial is to resolve that litigation. And to discount for the litigation would be effectively to transfer value from Mr. Rosenblum to Bernice Rosenblum." (Tr. at 341:10-15); *see also* Ex. 11 at 71 (illustrating the unfair consequences of applying a marketability discount). The fundamental unfairness of rewarding one party to the litigation at the expense of the other would be compounded

here, because the litigation was caused by Bernice's failure to pay Kenneth "within a reasonable time" after withdrawal, as she was required to do under LLC §509, and otherwise holding up the division of the parties' joint business. Discounting the value of Kenneth's share in the LLC Entities in favor of Bernice's Estate would reward this bad faith conduct.

In short, there is no factual or legal basis for applying any marketability discount to the fair value of Kenneth's interest in the LLCs, and none should be applied. Accordingly, Kenneth is entitled to 50% of the established value of the LLC Entities as of the Valuation Date. Specifically, as per Mr. Mercer's valuations, the fair value of Kenneth's interest in 132 Realty is $17,542,000, and the fair value of his interest in Village Realty is $16,368,000. (Ex. 11 at 107, 110).

IV. KENNETH IS ENTITLED TO STATUTORY PREJUDGMENT INTEREST SINCE THE DATE OF HIS WITHDRAWAL FROM THE LLC ENTITIES

In its decision, the Appellate Division stated: "The trial court also did not improvidently exercise its discretion in declining to award prejudgment interest on plaintiff's withdrawal distribution." *Rosenblum v. Rosenblum*, 214 A.D.3d 440, 440-41 (1st Dep't 2023). In support of this statement, the Appellate Division cited CPLR 5001(a), which provides for judicial discretion to award prejudgment interest "in an action of an equitable nature," as well as two Second Department cases, both of which did award such interest: *PFT Tech., LLC v. Wieser*, 181 A.D.3d 836, 839 (2d Dep't 2020), and *Man Choi Chiu v. Chiu*, 125 A.D.3d 824, 826 (2d Dep't 2015).

In fact, in its prior decisions, this Court did not "exercise its discretion" in either awarding or "declining to award" prejudgment interest on Kenneth's withdrawal value, given that that value itself has not yet been determined. This Court simply never addressed the issue. Indeed, as Defendants' counsel recognized on the record at the outset of the valuation hearing, this Court had "never" previously "heard" or decided the issue of "prejudgment interest on the LLC fair value claim." (Tr. at 5:11-18). Accordingly, the only guidance that the Appellate Division's holding

provides on this issue is that this Court has discretion to "award prejudgment interest on plaintiff's withdrawal distribution."

Following the two authorities the Appellate Division cited, and countless others, this Court should award prejudgment interest to Kenneth. Given that, under LLC §509, Kenneth is entitled to receive his "fair value" "within a reasonable time after withdrawal," but has yet to be paid many years later, he is entitled to interest on that value from the date of withdrawal. *See Man Choi Chiu v. Chiu*, 125 A.D.3d 824, 826 (2d Dep't 2015) ("The Supreme Court providently exercised its discretion in awarding prejudgment interest from the date of Winston Chiu's withdrawal" from the LLC "at the statutory rate of 9%") (citing authorities)); *PFT Tech., LLC v. Wieser*, 181 A.D.3d 836, 839 (2d Dep't 2020) ("The Supreme Court providently exercised its discretion in imposing prejudgment interest" on the value of LLC membership in dissolution proceeding). Indeed, there is no authority declining to award interest in an LLC withdrawal, buyout, or dissolution case. To the contrary, courts have uniformly awarded interest in LLC dissolution and buyout cases, just as they have done in corporate dissolution and buyout cases. *See*, *e.g.*, *In re Superior Vending, LLC*, 71 A.D.3d 1153, 1154 (2d Dep't 2010) (purchasing member of LLC to pay 9% interest since the date when business relationship terminated); *cf. Blake v. Blake Agency, Inc.,* 107 A.D.2d 139, 150 (2d Dep't 1985) (reversing trial court and awarding interest at 9% per annum in a corporate dissolution case); *Giaimo v. Vitale*, 101 A.D.3d 523, 526 (1st Dep't 2012) (affirming award of interest on fair value in corporate dissolution case resulting in buyout).

The Estate cannot offer a principled distinction between the equitable reasons for an award of interest here and the many corporate dissolution and buyout cases decided under the BCL. Just as in those BCL cases, interest has been award as a matter of course in the numerous LLC dissolution, withdrawal, and buyout cases decided under the LLCL. Even though, unlike

§509 or §702, BCL §1118(b), expressly mentions the court's "discretion" to "award interest," in practice the courts have concluded that such discretion is a necessary element of the Court's equitable powers in a liquidation proceeding, and have routinely awarded interest in all buyout situations regardless of the type of entity at issue or the applicable statute. The Appellate Division's decision in this case plainly supports that conclusion. This is so because "the equities" involved in LLC membership cases point in the same direction as the corporate equities addressed by the express language of BCL §1118(b), and thus require the same result. *See PFT Tech*, 181 A.D.3d at 838 (holding that "the equities" of the LLC membership buyout case pointed to the same valuation date – "the day before the action was commenced" – as the one specified in BCL §1118).

The Estate argued before the Appellate Division that there is no statutory basis for an award of interest in a case governed by the LLCL, thus implying that *Chiu*, *PFT Tech*, *In re Superior Vending*, and similar cases were all wrongly decided. The Appellate Division rejected that position by its express reference to the trial court's "discretion to award prejudgment interest" and its express reliance on *Chiu* and *PFT Tech. Rosenblum*, *supra*. The Appellate Division also cited CPLR §5001(a), which constitutes the statutory basis for an award of interest in an LLC withdrawal case (as well as an LLC dissolution or buyout case), as it provides for recovery of interest in an action based on "an act or omission depriving or otherwise interfering with title to, or possession or enjoyment of, property," as well as "in an action of an equitable nature." A claim for withdrawal from an LLC under LLC § 606 (just as a claim for dissolution of an LLC under LLC §702) is "an action of an equitable nature" and also involves "possession or enjoyment of property" – to wit, an LLC membership with all the attendant property rights. The Court of Appeals has definitively held that "a determination of the fair value of [plaintiff's] shares and an order directing defendants to pay that value for them . . . is equitable in nature," *Loengard v. Santa*

Fe Indus., Inc., 70 N.Y.2d 262, 266 (1987), thus resolving any issue of whether a court can award interest in such a case under CPLR §5001(a). For both reasons, an award of interest in LLC dissolution, withdrawal, and buyout cases is authorized by CPLR §5001(a), as the above cases confirm.

Indeed, numerous judicial holdings emphasize that an award of interest in cases involving "fair value" determinations is driven by equity. The Second Department explicitly held that, in making a "fair value" award, "the court is not precluded from making such orders as justice requires," and that, even where the applicable BCL sections "do not specifically provide for the payment of interest on the fair value of the shares, justice requires that . . . interest be paid." *Blake*, *supra*; *accord Matter of Digeser v. Flach*, 54 Misc. 3d 1217[A], 2017 N.Y. Slip Op. 50220[U], *7 (Sup. Ct. Albany Co. 2017); *accord Ferolito v. Arizona Beverages USA LLC,* 2014 N.Y. Slip Op. 32830[U] (Sup. Ct. Nassau Co. 2014) ("The principle that prejudgment interest is to be awarded absent some showing of bad faith has since [*Blake*] been repeated numerous times, without exception, in cases at both the trial and appellate level") (quoting *Giaimo*, *supra*, noting that interest is "a cost imposed for having the use of another party's money over a period of time."). "While [CPLR 5001] makes an award of interest a matter of discretion in equity cases . . . such an award [i]s virtually mandated [where, as here,] defendants were fiduciaries and failed to properly account to plaintiff for [many] years, during which time they enjoyed the benefit of plaintiff's money. . ." *Aurnou v. Greenspan*, 161 A.D.2d 438, 439-440 (1st Dep't 1990) (holding that failure to award prejudgment interest in a partner withdrawal case "constituted an abuse of discretion under CPLR 5001").

The equities in this case point distinctly in favor of Kenneth. It is undisputed that the properties were income-producing and debt-free at all times following Kenneth's withdrawal. In

this situation, mortgaging the properties would have been the obvious way to finance Kenneth's buyout, but the Estate in fact used its control over the LLCs—in flagrant disregard of its fiduciary responsibilities to Kenneth as a withdrawing member—to *prevent* the LLCs from mortgaging their properties or otherwise raising the funds to pay him the statutorily required "fair value" within a "reasonable" period.

In summary, an award of interest from the date of withdrawal must be added to the principal amount of the "fair value" of Kenneth's interest in the LLCs that he should have received years ago, as a matter of statutory law, judicial precedent, and equity. As in most of the above cases, such interest should be at the statutory rate of 9% per annum prescribed in CPLR § 5004.[14]

CONCLUSION

For the reasons set forth above, the Court should credit Mr. Feeney's real estate appraisals and Mr. Mercer's business valuations, and grant judgment in Kenneth's favor for the fair value of his interest in 132 Realty in the principal amount of $17,542,000, and for the fair value of his interest in Village Realty LLC in the principal amount of $16,368,000, both with interest from September 20, 2019 until the date of payment at the statutory rate of 9% per annum; together with such other and further relief to Kenneth, including an award of interest and costs, as the Court may deem just and equitable.

[14] As Kenneth has always made clear, the amount to which he is entitled will be partially offset by the distributions he received from the LLC Entities since September 20, 2019 (also with interest at the statutory rate).

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SCHLAM STONE & DOLAN LLP

By: */s/ Richard H. Dolan*________
Richard H. Dolan
Vitali S. Rosenfeld
26 Broadway
New York, New York 10004
Telephone: (212) 344-5400
Facsimile: (212) 344-7677
E-Mail: rdolan@schlamstone.com
E-Mail: vrosenfeld@schlamstone.com

Attorneys for Plaintiff Kenneth Rosenblum