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STATUTES

QUESTIONS PRESENTED

Question #1 When valuing a corporation pursuant to New York Business Corporation Law § 1118 should the Court apply a discount for the lack of marketability of the shares of a closely held corporation?

The Court Below Answered "No".

Question #2 When valuing an operating corporation pursuant to New York Business Corporation Law § 1118 should the Court value the corporation as an on-going concern?

The Court Below Answered "No".

PRELIMINARY STATEMENT

This matter involves the filing of a Petition for Judicial Dissolution by the Petitioners pursuant to New York Business Corporation Law § 1104-a. Subsequent to the filing, the Appellant DAPA Communications, Inc. elected to buy out the shares of the Petitioners, pursuant to New York Business Corporation Law § 1118. The Petitioners and Appellant were subsequently unable to agree on a value for the Petitioners' shares and this matter came on for trial before the Hon. Larry M. Himelein J.S.C in the Supreme Court in Cattaraugus County, Little Valley, New York.

In its original decision, the Court used a liquidation value to determine the value of the shares of the Petitioners and applied a discount for lack of marketability to the interest of the Petitioners. [Record, Volume I, pp. 13 & 14].

The Petitioners subsequently filed a motion pursuant to New York CPLR R 4404 requesting the Court to modify its decision and make new conclusions of law and findings of fact. After oral argument on the motion, the Court changed its original decision and removed the

30% discount which it had applied to the Petitioners' shares based on lack of marketability. Judgment was subsequently entered by the Petitioners and the Appellant filed this Appeal from that judgment. [Record, Volume I, pp. 17 & 18].

Pursuant to an Order of Justice Himelein, execution on the judgment by the Petitioners was stayed on February 1, 2008 by the Appellant posting a bond in the amount of $58,850.18 with the Cattaraugus County Treasurer. [Record, Volume III, pp. 705-707.]

FACTS

Nathalie Rateau, Mireille Rateau, and Michel Rateau (collectively known as "the Petitioners") on or about the 13th day of July 2005 filed a Petition for the Judicial Dissolution of DAPA Communications, Inc. pursuant to New York Business Corporation Law § 1104-a et seq. The Petitioners collectively held a thirty-four percent (34%) minority interest in DAPA Communications, Inc. (referred to herein variously as "Dapacom" or "the Appellant").

DAPA Communications, Inc. is a New York corporation which manufactures network antennas for the cell phone industry. Sixty-six percent (66%) of the shares in Dapacom were previously held by a French company, DAPA Technology S.A.S ("Dapatech"). That company had formerly been controlled by the Rateau family, members of which are the Petitioners in this special proceeding. However, Dapatech, which held the majority interest in Dapacom, was sold in bankruptcy by the French Courts to the Carbou family who thereby obtained the controlling interest in Dapacom. Some months prior to July 2005, the new owners of Dapatech, who were now the majority shareholders in Dapacom, attempted to examine the books and records of Dapacom but were thwarted by the actions of Nathalie Rateau, one of the Petitioners who, at that time, was president of Dapacom. The majority shareholders then called a shareholders' meeting

and elected a new Board of Directors, which did not include any of the minority shareholders. The new Board of Directors, believing that Nathalie Rateau and her life partner Michelle Cranston were converting the assets of Dapacom to their own uses, dismissed both Nathalie Rateau and Michelle Cranston and placed new management in control of the company. The company is continuing to operate under that new management. Separate litigation is ongoing regarding the dissipation of corporate assets by Nathalie Rateau and Michelle Cranston.

Less than two weeks after Nathalie Rateau was dismissed as president of Dapacom, on July 13, 2005, the Petitioners filed this Petition seeking dissolution of Dapacom. [Record, Volume I, pp. 19-30]. As part of its Petition, the Petitioners made baseless allegations alleging oppression and dishonest acts on the part of the Appellant and its new management. The Petitioners originally filed the Petition in Erie County, New York. The Appellant moved to change venue since no party to this action resided in Erie County, and the action was subsequently transferred by order of the Hon. Eugene M. Fahey J.S.C. to Cattaraugus County Supreme Court, the place where venue was proper. [Record Volume I, pp. 45 & 46]. The matter was assigned to the Hon. Larry M. Himelein, J.S.C.

The Appellant timely answered the Petition on or about the 15th day of August 2005. [Record, Volume I, pp. 31-35.] The tax department of the State of New York also submitted an Answer on or about the 9th day of August 2005. [Record, Volume I, pp. 36-40]. Subsequently, on the 11th day of October 2005, Dapacom by means of a letter delivered to the Petitioners' attorneys Blair & Roach LLP, elected to buy out the shares of the Petitioners pursuant to New York Business Corporation Law § 1118. [Record, Volume I, pp. 47 & 48]. For some period of time subsequent to that election, the parties attempted to negotiate a price for the Petitioners' minority shares. However, the parties were unable to agree upon a value for the shares. The

issue of valuation therefore came on for trial before the Hon. Larry M. Himelein in Cattaraugus County, Little Valley, New York on May 3 and 8, 2007. Pursuant to statute, the day relevant for valuation purposes was July 12, 2005, the day prior to the filing of the Petition.

At trial, the Petitioners' expert witness, upon cross examination, admitted that he did not attempt to value Dapacom as an on-going concern because such valuation would be "inappropriate". [Record, Volume I, pp. 120-123]. The Petitioners' expert used a liquidation basis to value the entire company but his report did not provide a separate valuation for the shares of the Petitioners which represented 34% of the outstanding shares of the company. [Record, Volume I, p. 118]. In sharp contrast, the Appellant's expert did multiple valuations on numerous bases. Notably, the Appellant's expert, Darren Graff, performed a valuation of Dapacom on an on-going, operating concern basis, the standard mandated by the New York State Court of Appeals for a concern that is operating and not in liquidation. Mr. Graff gave his expert opinion that using an on-going concern basis valuation, the value of the 34% minority interest held by the Petitioners was zero. [Record, Volume I, pp. 219]. The Court should note that the lower Court found that Dapacom had lost $1.9 million over the four years prior to the relevant date for valuation purposes, July 12, 2005 [Record, Volume I, pp. 16 & 17]. The Appellant's expert, Mr. Graff, also performed evaluations based on a liquidation value, and he attempted to apply discounts for both the minority interest of the Petitioners and for the lack of marketability of the shares. New York Courts have held that a lack of marketability discount is generally appropriate when a company's stock is not easily sold. Dapacom is a closely held company, and there is generally no market for such shares as the 34% interest of the Petitioners. The Appellant's expert applied a 30% discount for the lack of marketability. [Record, Volume I, pp.

222-226]. The Petitioners' expert did not employ any discounts for lack of marketability or lack of control of the company. [Record, Volume I, p. 120].

On August 16, 2007 the Court issued a five-page reasoned decision using a liquidation or asset value in determining the value of the company. The Court declined to apply a lack of control or minority discount but did apply a discount for the lack of marketability. However, the Court became conceptually confused and did not apply the lack of marketability discount to the shares, but rather, the assets themselves. The Court states that there would be costs involved in selling the assets and that this was the reason for the discount. The Court found that the value of the Petitioners' shares was $42,840.00. [Record, Volume I, p. 14].

The Petitioners were not pleased with the results after the trial, but instead of filing an appeal, they filed a post-trial motion for judgment and new trial pursuant to CPLR R 4404. The hearing on that motion was delayed while the Petitioners obtained a copy of a portion of the trial transcript. At oral argument, Petitioners' attorney argued that there was no evidence before the Court as to the costs involved in selling the assets of the company in liquidation. The Court, agreeing that no such evidence had been presented, then decided to modify its previous decision.

On December 4, 2007 the Court modified its original decision and declined to apply a discount for lack of marketability to the assets, [Record, Volume I, pp. 17 & 18]; thereby increasing the value of Petitioners' shares to the total amount of $61,200.00. [Record, Volume I, p. 18]. Once again, the Court misunderstood that what was being valued was not the assets of the company, because the Petitioners do not directly own the assets; what was to be valued by the Court was the **shares** representing the 34% interest in the corporation. It was proper for the Court to apply a lack of marketability discount to the shares because they are shares in a closely

held corporation for which there is no market. The discount is not for the lack of marketability of the assets.

On or about the 18th day of December 2007, the later decision of Justice Himelein was reduced to judgment and the Petitioners were granted judgment in the amount of $76,247.24 which included interest and costs. [Record, Volume I, pp. 7-9]. Notice of Entry of the judgment was served upon the Appellant's attorneys on or about December 31, 2007. [Record, Volume I, p. 6]. On or about January 4, 2008 the Apellant timely filed a Notice of Appeal from the Petitioners' judgment. [Record, Volume I, pp. 3 & 4]. The Appellant served the Notice of Appeal on the attorneys for the Petitioners on January 5, 2008 and filed the Affidavit of Service with the Cattaraugus County Clerk on January 8, 2008. [Record, Volume I, p. 5]. On or about the 9th day of January 2008 the Appellant brought on a motion by means of Order to Show Cause before the Hon. Larry M. Himelein J.S.C. requesting that he stay execution upon the judgment pending the outcome of the appeal for a number of reasons including the fact that he had incorrectly increased the amount of the valuation in his second decision by failing to apply a lack of marketability discount. After oral argument, the judge agreed to stay execution on the judgment and required the Appellant to post a bond in the amount of $58,850.68 with the Cattaraugus County Treasurer pending the outcome of this appeal. That Order was granted on February 1, 2008 and Notice of Entry was served upon opposing counsel on February 4, 2008. [Record, Volume III, pp. 704-707].

On or about March 13, 2008 counsel for the Petitioners filed a Motion to Dismiss the Appeal of the Appellant. The Appellant timely served an Answering Affidavit on or about March 21, 2008 stating that the reason for the delay in perfecting the appeal was that there had been a delay in the delivery of the transcript which was ordered shortly after the appeal was filed.

On or about 2nd day of April 2008, the Supreme Court, Appellate Division, Fourth Department directed that the appeal would be dismissed if not perfected by May 30, 2008. [Record, Volume III, pp. 708 & 709].

ARGUMENT

A. THE COURT BELOW ERRED IN NOT APPLYING A DISCOUNT TO THE PETITIONERS' SHARES FOR THEIR LACK OF MARKETABILITY.

In the instant case, the minority shares of the Petitioners are those of a closely held corporation for which there is no public market. A lack of marketability discount is generally appropriate when a company's stock is not easily sold. Matter of Seagrott Floral Co., Inc., 78 N.Y.2d 439, 576 N.Y.S.2d 831 (1991); In re Brooklyn Home Dialysis Training Center, Inc., 293 A.D.2d 747, 741 N.Y.S.2d 280 (2nd Dept. 2002); In re Vetco, Inc., 292 A.D.2d 391, 738 N.Y.S.2d 599 (2nd Dept. 2002); Hall v. King, 265 A.D.2d 244, 697 N.Y.S.2d 19 (1st Dept. 1999); Dissolution of Funplex, Inc., 252 A.D.2d 923, 676 N.Y.S.2d 321 (3rd Dept. 1998); Lehman v. Piontowski, 203 A.D.2d 257, 609 N.Y.S.2d 339 (2nd Dept. 1994).

The 1979 amendments to the Business Corporation Law were motivated, in part, by recognition of the fact that shareholders in closely held corporations, as contrasted with shareholders in public companies, are unlikely to find prospective buyers for their shares *(see,* Sweet and Mallis, *Standing to Petition for the Judicial Dissolution Under the New York Business Corporation Law: A Needed Change,* contained in Bill Jacket, L 1979, ch 217). It follows that, whatever the method of valuing an interest in such an enterprise, it should include consideration of any risk associated with illiquidity of the shares *(see generally,* Haynsworth, *Valuation of Business Interests,* 33 Mercer L Rev 457 [1982]; 2 O'Neal and Thompson, O'Neal's Close Corporations § 9.34, at 162-163 [3d ed]). Seagrott, *supra.*

In its original decision, the Court applied a 30% discount for a lack of marketability of the Petitioners' minority interest. The amount was taken from the Appellant's expert witnesses testimony and written report [Record, Volume I, pp. 222-226 and written report Volume III pp. 542-544] which stated that 30% discount was a proper amount to apply for the lack of marketability. The lower Court accepted that amount (30%) as appropriate. [Record, Volume I, p. 13].However, the Court then conceptually confused the fact that there should be a discount for the lack of marketability of the shares, with the idea that there would be costs involved in selling off the assets of the company. Himelein J. stated in his original decision, "On the other hand, there would be significant costs involved in selling off the equipment, i.e., advertising, auctioneers and the like. Therefore, whether deemed a lack of marketability discount or a cost of sale discount the court will apply a discount of thirty percent." [Record, Volume I, pp. 13 & 14]. The authorities are clear that the lack of marketability discount is to be applied in regards to the shares of a closely held corporation because there is no marketplace in which one can normally sell such shares. The discount has nothing to do with the sale of the assets of the corporation. Dapacom was an operating concern and not being liquidated

The Petitioners, subsequent to the decision of Himelein J., and pursuant to CPLR R 4404, filed a post-trial motion for judgment and new trial requesting that the Court make new conclusions of law and finding of facts. At the oral argument on that motion, Petitioners' attorneys argued that the Court was incorrect in taking judicial notice of the fact that there would be substantial costs involved in selling off the assets of the corporation, and in finding that a discount should be applied for that fact. The Court, already confusing the marketability of the shares with the marketability of the assets of the corporation, accepted the argument, ruled that there was no evidence as to what the costs of sale of the assets would be, and issued a second