SUPREME COURT OF THE STATE OF NEW YORK
COUNTY OF QUEENS: HON. ALLAN B. WEISS, PART 2

MAN CHOI CHIU and 42-52 NORTHERN BLVD., LLC, *Plaintiffs,* *-against-* WINSTON CHIU *Defendant.*
WINSTON CHIU, *Counterclaim Plaintiff/* *Third-Party Plaintiff* *-against-* MAN CHOI CHIU, *Counterclaim Defendant/* *Third-Party Defendant* *-and-* HELEN CHIU AND TERESA CHIU, *Nominal Counterclaim Defendants,* *-and-* 42-52 NORTHERN BOULEVARD, LLC, *Nominal Counterclaim Defendant.*
WINSTON CHIU, *Plaintiff,* *-against-* MAN CHOI CHIU and 42-52 NORTHERN BLVD., LLC, *Defendants.*

Index Nos. 21905/07 and 25275/07

WINSTON CHIU'S POST-TRIAL MEMORANDUM OF LAW

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TABLE OF CONTENTS

TABLE OF AUTHORITIES

RULES, CODES, STATUTES AND OTHER AUTHORITIES

PRELIMINARY STATEMENT

It is undisputed that Winston was a member of 42-52 Northern Blvd. LLC (the "LLC"), and this Court need decide only the percentage of his membership and its value as of the date of his withdrawal. According to all the LLC's records, upon which the Second Department directed this Court to rely, Winston was a 25% owner of the LLC, a single asset holding company.[1] This Court has previously ruled that Winston withdrew as a member as of February 9, 2008 ("the Valuation Date"), and both sides had two experts each opine, as of that date, on the value of the LLC and the building that it owns, which Man Choi has occupied rent free since 1999. The net asset value of the LLC is just over $10.4 million. Winston was frozen out of the LLC although he put in hundreds of thousands of dollars, the LLC's own records list him as 25% member, and he personally guaranteed the entire $3.5 million mortgage. Man Choi and his daughters (the "MCC Parties") lamely pretend that Winston has nothing to do with the LLC and that, although never an owner, he was allowed to guarantee the mortgage as a favor based on Chinese tradition.[2]

This Court should rule that Winston was a 25% member as of the Valuation Date and grant judgment to Winston for the fair value of his 25% interest in the LLC, in the amount of $2,606,750, with pre-judgment interest since at least the Valuation Date at the statutory rate.

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[1] The Second Department expressly held in *Chiu v. Chiu*, 38 A.D.3d 619, 629, 832 N.Y.S.2d 89, 92 (2d Dep't 2007) (the "2007 Appellate Order") that:

> [T]he court's determination as to the membership of the LLC **should have been based primarily on the LLC's own records, which, by law must include 'a current list of the full name set forth in alphabetical order and last known mailing address of each member together with the contribution and the share of profits and losses of each member or information from which such share can be readily derived.' The only documentary evidence that arguably satisfies this requirement consisted of the LLC's tax returns for the years 1999 and 2000, both of which listed the defendant Winston Chiu as a member having as 25% ownership of capital, profit sharing, and loss sharing** and the plaintiff Man Choi Chiu as the other member having a 75% ownership of capital, profit sharing, and loss sharing.

(2007 Appellate Order at 2-3) (citation omitted) (emphasis supplied). The evidence admitted in this case includes not only the tax returns, but the very list called for in the 2007 Appellate Division Order. This list, Def's Ex. B, which was not before the Court in the previous action, was prepared by Helen Chiu and provided to the LLC's accountant, who, unlike Helen Chiu, produced it during discovery, as discussed below.

[2] Oct. 25, 2011, Tr. at 105:3-14. The pagination for the trial transcript is not continuous. On February 2, 2012, the transcript begins anew at page 1. All citations to the transcript therefore contain both the date of the transcript and the page and line citation.

STATEMENT OF FACTS

A. Both Mr. Mercer And Mr. Nelson Agree The LLC's Net Asset Value Is $10.4 Million

Mr. Mercer concluded that the LLC's net asset value, on the Valuation Date, was $10,427,000.[3] Mr. Nelson similarly concluded that the LLC's net asset value was $10,449,739.[4]

In arriving at his value, Mr. Mercer began with the LLC's balance sheet as of December 31, 2002, and determined what the figures would be as of the Valuation Date. (Apr. 3, 2012, Tr. at 780:21-781:4). Mr. Mercer also calculated what he termed "foregone cash."[5] (*Id.* at 781:5-9). Mr. Mercer used Mr. Salmon's $13.5 million appraisal[6] of the Property.[7] He estimated cash at $450,000 based on historical levels. He then carried forward the 2002 liabilities, including the amounts due to Man Choi and an entity owned by Man Choi, 1-9 Bondst Realty, Inc. ("1-9 Bondst"), with proper adjustments. (*Id.* at 781:18-783:14). Thus, Mr. Mercer subtracted from the assets ($13,950,000) the liabilities ($5,150,000), added in the foregone cash ($1,626,000), and concluded that the net asset value of the LLC was $10,427,000, and that the fair value of a 25% interest was worth 25% of that figure, $2,606,750.[8] (*Id.* at 780:11-20; 783:15-19).

Mr. Mercer determined the amount of the foregone cash by using the rents derived by Mr. Salmon for 2006-2008, and then decreased the rents approximately 5% for each of the preceding years. From the estimated market rent owed, he offset various expenses, including renovation expenses, real estate taxes, interest expenses for the mortgage, general repairs and maintenance. He also took into account principal payments on the mortgage. He did not include foregone cash

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[3] Apr. 3, 2012, Tr. at 779:19-780:7.
[4] Pls' Ex. 35.
[5] Mr. Mercer defines foregone cash as "the cash that would have flowed through the LLC had rent been paid at market rates from the time full [sic] occupancy, which I understand to be around 2002 to the present, or to the [V]aluation [D]ate." (Apr. 3, 2012, Tr. at 784:19-23).
[6] The appraisals by Mr. Salmon and Mr. Haims will be discussed further below.
[7] The "Property" refers to the LLC's property, at 42-52 Northern Blvd., Long Island City, Queens, New York.
[8] The fair value of Winston's interest is calculated by multiplying the LLC's net asset value by his percentage interest. Any marketability discount is taken off the net asset value before multiplying the net asset value by his percentage interest. The $2,606,750 figure is arrived at by taking 25% of Mr. Mercer's net asset value of $10,427,000 with a 0% marketability discount, discussed below.

for 1999-2001.[9] In this way, and by carrying forward the LLC's debt from the 2002 balance sheet, Mr. Mercer's valuation gave Man Choi complete credit for all payments Man Choi or his entities made on behalf of the LLC.

Mr. Mercer further testified that any discount for lack of marketability should be zero percent.[10] He noted that transaction costs for selling the LLC would be between 3% and 6%.[11]

Mr. Nelson opined that, before arriving at the net asset value of the LLC as of February 9, 2008, he had to redo the books and records of the LLC, (Feb. 6, 2012, Tr. at 163:17-164:1; Mar. 14, 2012, Tr. 383:5-14),[12] because the LLC's original books and records were not in accordance with Generally Accepted Accounting Principles ("GAAP") Statement of Position 78-9 ("SOP 78-9"), Accounting for Investments in Real Estate Ventures, and a single tax court case, *Roth Steel Tube Co. v. Comm'r of Internal Revenue*, 800 F.2d 625 (6th Cir. 1986).[13] Mr. Nelson reclassified as capital contributions both payments that were related to the purchase of the Property, which had originally been booked as loans on the LLC's financial statements and reported as loans on the LLC's tax returns, as well as payments for improvements to the Property, with the effect of unilaterally diluting Winston's membership interest.[14] Mr. Nelson opined that Winston's membership interest at the outset of the LLC was 9% rather than the 25% reflected in the LLC's records and its tax returns, (Feb. 6, 2012, Tr. at 206:11-16), and that as of February 9, 2008, it had been diluted, per his remade books and records, to 5.74%, worth $450,000. (Ex. 35, p. 2).

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[9] Apr. 3, 2012, Tr. at 785:15-786:1, 786:10-789:19.
[10] Apr. 3, 2012, Tr. at 760:11-764:3, 770:13-19, 818:23-820:5.
[11] Apr. 3, 2012, Tr. at 812:3-4, 16-18.
[12] Although the Court refused to permit Winston to enter into evidence the report of Mr. Mercer, the Court overruled Winston's objection to allowing the MCC Parties to admit as evidence five binders plus some smaller exhibits (Pls' Exs. 25-37) through Mr. Nelson. These exhibits contained documents that had not been produced during discovery and documents that Mr. Nelson and his firm had created, which were his expert report. (*See, e.g.*, Feb. 6, 2012, Tr. at 170:7-172:22, 173:10-15, 173:20-190:1, 191:4-191:23, 193:2-193:13; 203:21-204:20). The Court also noted Defendant's proper objection based on an inability to determine who created the documents admitted as these exhibits. (*See, e.g.*, Feb. 6, 2012, Tr. at 182:20-25).
[13] Mar. 14, 2012, Tr. at 353:4-23; *see also* Feb. 6, 2012, Tr. at 222:5-223:4, Feb. 7, 2012, Tr. at 282:20-24.
[14] Feb. 6, 2012, Tr. at 164:14-165:11; 206:11-16.

Winston, frozen out of the LLC,[15] was never offered the chance to make capital contributions in proportion to the amounts Man Choi spent to alter the Property so Man Choi could operate an unrelated retail restaurant supply business there. Mr. Nelson determined that the LLC's fair value on the Valuation Date was $7,837,304 ($10,449,739 less a 25% marketability discount).[16]

But Mr. Nelson testified that, in his view, Winston withdrew his membership capital as of May 21, 2001, and that at the time just prior to his withdrawal, Winston had a membership interest of 7.84%, worth $14,000.[17] Mr. Nelson opined that, if Winston had withdrawn as of May 21, 2001, he would be owed only $4,400. (*See* Pls' Ex. 36). Realizing, of course, that this figure was likely to reduce his credibility to zero, Mr. Nelson came up with an unsupported methodology he called "a sort of practical approach" that raised his figure to $184,000.[18]

B. The MCC Parties Admit That Winston Is A 25% Member Of The LLC

Contrary to Mr. Nelson's testimony, numerous LLC records record Winston's membership as 25%. Def's Ex. A[19] gives a summary of contributions and loans that specifically notes that the capital contributed by Man Choi and Winston resulted in a 75%/25% split. (*Id.* at 2).[20]

The LLC's balance sheet as of December 31, 1999, (Def's Ex. C), states under the Equity Interests of Members that Man Choi's was $581,562.93 and that Winston's was $193,854.50.

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[15] Helen, Teresa, and Man Choi all testified that they do not view Winston as a member and never provided him with any information concerning the LLC. (*See, e.g.*, Oct. 31, 2011, Tr. at 223:14-19; Def's Ex. T ; Def's Ex. PP (Helen Chiu tab 23, Man Choi tab 29, Teresa Chiu tabs 2, 3); *see also* Dec. 2, 2011, Tr. at 657:19-25; Feb. 3, 2012, Tr. at 110:16-114:14). The MCC Parties changed Winston's password so he could no longer log in to view the LLC's records. (Feb. 3, 2012, Tr. at 113:4-114:14). To file his 1999 tax returns, Winston had to go to Eastbank to get the necessary information concerning the LLC, which is when he discovered that his signature had been forged by the MCC Parties to obtain control over LLC accounts. (Feb. 3, 2012, Tr. at 106:9-24; Def's Exs. HH-1 and HH-2; *see also* Feb. 2, 2012, Tr. at 82:17-85:19; 88:1-90:12).

[16] Included in this figure is an amount of $988,347, which Mr. Nelson determined that Man Choi and his entities owed as rent to the LLC as of February 9, 2008, akin to Mr. Mercer's "foregone cash." (Feb. 7, 2012, Tr. at 313:25-314:9; Ex. 35, p. 2). It is less than Mr. Mercer's figure because Mr. Nelson calculated rent for only 2006-2008. (*Id.*)

[17] Feb. 6, 2012, Tr. at 166:12-24; Mar. 20, 2012, Tr. at 418:6-9.

[18] Feb. 6, 2012, Tr. at 167:7-23; Mar. 20, 2012, Tr. at 418:16-419:20.

[19] At his deposition, Man Choi testified he prepared this document personally. (Def's Ex. PP (Man Choi tab 12)).

[20] Def's Ex. A, at 2, also shows that the only cash from Man Choi and Winston used in the purchase of the Property was Winston's $193,854.51 and Man Choi's $581,562.93 (some of which should actually have been attributed to Winston or to the 1-9 Bondst loan), and most of which represented the contract deposit. The remainder was funded by the mortgage or the loan from 1-9 Bondst St.

These figures are in a 3:1 (75%/25%) ratio. The balance sheets for 2000 through 2002 also reflect figures that are in a 3:1 ratio. (Def's Ex. C).

The tax returns for the LLC, for the years 1999 and 2000, sworn to by Man Choi on behalf of the LLC, contain a Schedule K-1 for Winston, indicating that he has a 25% interest as a member in the LLC. (Pls' Exs. 2A and 2B). Helen Chiu, the LLC's Vice-President in charge of finances and recordkeeping, (Oct. 25, 2011, Tr. at 69:15-21), testified that she provided the information used in these returns to the LLC's accountants. (Oct. 25, 2011, Tr. at 74:10-13; Def's Ex. PP[21] (Helen Chiu tabs 7, 8, 11, 15, 18)). She further prepared and provided the accountants with the 25% figure used in the K-1's. (Def's Ex. B; Ex. PP (Helen Chiu tab 14)).[22] Having received draft tax returns containing the same 75% and 25% figures, she did not request any changes, and explained them to Man Choi, who signed them.[23]

The record is replete with evidence as to why Winston was a 25% member of the LLC. **First**, unlike Man Choi, on September 8, 1999, at the closing for the Property, Winston **personally** guaranteed the entire amount of the $3.5 million mortgage.[24] **Second,** Winston made financial contributions of $60,000 and $193,854.51. (Def's Exs. D, tab 14, at 650, H and FF; Oct.

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[21] The MCC Parties' objections to Winston's designation of prior testimony in Def's Ex. PP go, at best, to weight, and do not render the designations inadmissible. To the extent the MCC Parties object to designations based on CPLR § 4519, such objections are not well-founded, because: 1) CPLR § 4519 would apply, if at all, only to Winston, not testimony by the MCC Parties; 2) CPLR § 4519 is inapplicable to documentary evidence and thus does not apply to the agreements and the signatures on which Man Choi authenticated. *Acevedo v. Audubon Mgmnt, Inc.*, 280 A.D.2d 91, 95, 721 N.Y.S.2d 332, 335 (1st Dep't 2001); and 3) Man Choi testified that Henry was not intended to be a member of the LLC and signed documents only because Man Choi did not speak English well, (Oct. 27, 2011, Tr. at 171:25-172:5, 181:13-25, 182:23-183:2), waiving any objection and opening the door for Winston's testimony. CPLR § 4519 (Practice Commentary) ("[CPLR 4519] may be used only as a shield, not a sword.")

[22] The MCC Parties fought vehemently to keep Def's Ex. B out of the record in this action, but cannot escape that it was in the files of the LLC's accountant, Mr. Miller, (*see* Nov. 28, 2011, Tr. at 427:3-14), and that Helen Chiu testified at her deposition that she had written and submitted it to the accountant, (Def's Ex. PP (Helen Chiu tab 14)), although she could predictably no longer recall having submitted the page with the list at trial. (Oct. 25, 2011, Tr. at 87:16-20) Finally, contrary to any argument by the MCC Parties, the third page contains the very information Helen states she is sending to the accountants on the first page, namely the address, name, and social security numbers of Winston and Man Choi, as well as their percentage membership interest in the LLC, and are plainly connected. (Def's Ex. B).

[23] Def's Exs. V and W; Oct. 25, 2011, Tr. at 77:2-13; Def's Ex. PP (Helen Chiu tabs 11, 13, 16, 18).

[24] Def's Ex. D, tab 8 at 515-516; *see also* Def's Exs. J, LL, OO; Pls' Ex. 21.

27, 2011, Tr. at 181:3-6; Nov. 30, 2011, Tr. at 588:22-589:22; Dec. 2, 2011 Tr. at 651:20-25;[25] Feb. 3, 2012, Tr. at 71:23-72:4).[26] **Third**, the parties agreed to a structure whereby Winston would be a 25% member of the LLC. (Def's Ex. D, tab 13).[27] The agreements[28] set up the structure whereby an entity owned by Man Choi, 1-9 Bondst, specifically referred to as "Lender", (Def's Ex. D, tab 13, at 631), would loan the LLC $1.8 million to pay the contract deposit and the down payment at the closing for the Property, the LLC would rent the Property to an entity owned by Man Choi and Henry, and Winston and Henry would be members of the LLC. (Def's Ex. D, tab 13.)[29]

C. Both Appraisers Came To Nearly Identical Values For the Property

Mr. Haims, the MCC Parties' appraiser, determined that the "as is" value of the Property as of February 9, 2008, was $13.7 million. (Nov. 2, 2011, Tr. at 331:17-20).[30]

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[25] Man Choi may argue that Winston lacks credibility. This case turns on the MCC Parties' admissions, including the business records of the LLC. Thus, Winston's credibility is irrelevant. Man Choi will likely also spend a great deal of time arguing that Winston took 100% of the deductions for the LLC's expenses on his tax returns, once he got the required information from Eastbank, since 1999. This argument simply indicates that Winston believed himself to be a member of the LLC and is not inconsistent with his position that he is at least a 25% member. Notably, Man Choi never took any deductions for LLC expenses on his tax returns compared to Winston who did so consistently. (Def's Ex. N; Pls' 17(a)-(k)).

[26] Contrary to his deposition testimony, with which he was impeached at trial, (Nov. 3, 2011, Tr. at 383:4-16), Man Choi testified that this $60,000 was not related to the purchase of the Property. (*Id.* at 384:14-21).

[27] Winston, Man Choi, and Henry signed these agreements together at Man Choi's house, and Man Choi has verified the signatures. (Nov. 3, 2011, Tr. at 386:20-21, 388:14-389:8; Def's PP (Man Choi tabs 1, 2, 5, 6, 17, 23); *see also* Feb. 2, 2012, Tr. at 47:4-13; *id.* at 47:17-48:25, 52:17-22). Henry drafted these agreements and they were edited by an attorney, who had previously worked with him and his father, Fred Samuel, Esq. (Nov. 30, 2011, Tr. at 595:10-22, *id.* at 599:1-19, 600:8-11). Henry later requested that the LLC's attorney at the closing, Ronald Fishman, Esq., include these documents in the file regarding the purchase of the Property and they subsequently were included in the Closing Statement, Def's Ex. D. (Feb. 7, 2012, Tr. at 249:4-21).

[28] Winston testified that the pages are in the correct order, (Feb. 2, 2012, Tr. at 63:22-64:15), and the signatures match up with the parties to the respective agreements, all of which Man Choi has verified.

[29] From October 1999 through December 2000, the LLC received a $50,000 monthly deposit that appears to be rent from Win Depot, in accordance with the agreements at tab 13 of the Closing Statement. (Def's Ex. KK; Ex. G (Profit and Loss Statements reflecting rental income); *see also* unsigned lease submitted to Eastbank in connection with mortgage included in Def's Ex. OO).

[30] Mr. Haims also appraised the Property in a hypothetically unrenovated state as of February 9, 2008 and June 2002, as well as value in "as is" condition for May 21, 2001, and June 2002. There are many reasons to doubt Mr. Haims' conclusions, not the least of which is the wide disparity between the values he arrived at using the Income Capitalization Approach and the Sales Comparison Approach. (*See, e.g.*, Nov. 29, 2011, Tr. at 491:20-492:6; 493:21-23; 526:4-9; *id.* at 333:14-24; Mar. 28, 2012, Tr. at 622:13-624:8; *see also* Nov. 2, 2011, Tr. at 328:18-22). However, Mr. Nelson used Mr. Haims' $13.7 million value in arriving at his value of the LLC as of the Valuation Date, and Mr. Nelson testified that using the hypothetical unrenovated figure would "wrongfully diminish[]" the

Mr. Salmon, Winston's appraiser, determined that the value of the property as of February 9, 2008, in its present condition, was $13.5 million. (Mar. 28, 2012, Tr. at 596:11-19). He further determined that properties like the LLC were in high demand as of the Valuation Date, since there were not many similar properties on the market, a conclusion also supported by the substance of Mr. Haims' testimony.[31]

Mr. Salmon estimated rental values of $11.50, $10.75, and $10.00 per square foot for, respectively, 2008-2006. (Mar. 28, 2012, Tr. at 618:25-619:4). Mr. Haims testified that the Property's arms'-length, triple net lease rental value was $11.00, $8.50, and $7.50 per square foot for 2008-2006. (Nov. 2, 2011, Tr. at 341:5-16, 342:18-25).[32] Mr. Salmon's figures are more reasonable than Mr. Haims', since rents did not increase as dramatically from 2007 to 2008 as Mr. Haims' figures would suggest.[33]

ARGUMENT

This Court must conclude that Winston was, based on the LLC's own admissions and records, a 25% member of the LLC and require the MCC Parties to pay out to Winston the fair value of his interest as of the Valuation Date, and to return his $60,000 which should be treated as

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value of Winston's interest, thereby conceding the relevant figure is the value of the Property in its "as is" condition, not a hypothetically unrenovated condition. (Mar. 20, 2012, Tr. at 467:2-6).

[31] Mar. 28, 2012, Tr. at 615:21-617:19; Nov. 29, 2012, Tr. at 454:25-455:4; *id.* at 455:8-17.

[32] Mr. Haims derived estimated rental values for modified gross leases, and then incorrectly converted the modified gross lease figures to a triple net figure. (Nov. 2, 2011, Tr. at 340:12-18). As Mr. Salmon testified, triple net leases are more common for this sort of property. (Mar. 28, 2012 Tr. at 619:10-18). Mr. Haims stated the large difference between his estimated rental for 2008 and 2007 was due to increases real estate taxes. (*Id.* at 341:17-24). This explanation failed to equalize taxes, and should not be credited. (Mar. 28, 2012, Tr. at 619:19-622:1).

[33] Although the Court did not permit Winston to ask Mr. Haims about *In re YL West 87th Street Holdings I LLC*, 423 B.R. 421 (Bkr. S.D.N.Y. 2010), in which the Bankruptcy Court found Mr. Haims used only one comparable to reach a desired value, selected an inappropriate yield rate, and chose a capitalization rate outside the industry standard, (Nov. 29, 2011, Tr. at 467:2-473:14), the Court did permit the MCC Parties to inquire during Mr. Salmon's testimony about a case, *In re City of New York*, 25 Misc. 3d 1240(A), 906 N.Y.S.2d 771 (Sup. Ct. Kings Co. 2009), they argued related to Mr. Salmon's credibility. (Mar. 30, 2012, Tr. at 631:24-632:4). With respect to the *City of New York* case, Mr. Salmon explained that he did not change his conclusion of value based on anything he was told by the City's corporation counsel, and that what he received from corporation counsel was merely a clearer way of presenting the same data. (Mar. 30, 2012, Tr. at 633:5-7; 727:11-25). Moreover, in *Island Realty Assoc., LLC v. Motta*, 21 Misc.3d 554, 559, 863 N.Y.S.2d 866 (Sup. Ct. Richmond. Co. 2008), the Court described Mr. Salmon as "a renowned certified real estate appraiser..."

a loan to the LLC. That part of Man Choi's First Cause of Action seeking an accounting should be dismissed, or at the very least deemed satisfied by the award to Winston.

I. WINSTON IS A 25% MEMBER OF THE LLC

In looking at the LLC's own records, on which the Second Department directed the determination as to the membership of the LLC be made, *see* footnote 1, *supra*, the MCC Parties have admitted repeatedly that Winston is a 25% member of the LLC.

First, the MCC Parties make this admission in the LLC's tax returns for 1999 and 2000 (the only years for which the LLC filed tax returns), sworn to by Man Choi himself. (Pls' Exs. 2A and 2B). It is black letter law that "[a] party to litigation may not take a position contrary to a position taken in an income tax return ... We cannot, as a matter of policy, permit parties to assert positions in legal proceedings that are contrary to declarations made under the penalty of perjury on income tax returns." *Mahoney-Buntzman v. Buntzman*, 12 N.Y.3d 415, 422, 881 N.Y.S.2d 369, 373 (2009) (citations omitted).[34]

Second, another record of the LLC, **the very list that the 2007 Appellate Order called**

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[34] In *Romano v. Romano*, 139 A.D.2d 979, 980, 30 N.Y.S.2d 155, 156 (2d Dep't 1987), which the Second Department relied upon in the 2007 Appellate Order, the Court cited solely the corporation's tax returns in determining that the husband owned 51% of the corporation. Indeed, the court wrote "the determination of the husband's percentage ownership of the business was not solely a matter of the parties' credibility, because the corporation's tax returns for the five-year period preceding the trial consistently indicated that the husband was only a 51% shareholder." *Id. See also Capizola v. Vantage Int'l., Ltd.*, 2 A.D.3d 843, 844, 770 N.Y.S.2d 395, 396 (2d Dep't 2003) ("respondents were estopped from claiming that the petitioner was not a shareholder", notwithstanding that his consideration for stock was not monetary, where, *inter alia*, "[t]he 1999 Subchapter S corporate tax return provided a Schedule K-1 reporting the petitioner as a 20% shareholder, and the 1999 New York State S Corporation Franchise Tax Return listed the petitioner, among all the shareholders, as holding a 20% interest in the corporation"); *Czernicki v. Lawniczak*, 74 A.D.3d 1121, 1125, 904 N.Y.S.2d 127, 131 (2d Dep't 2010) ("the parties are bound by the representations made in the partnership tax returns" and concluding that the parties were equal 50% partners, as demonstrated by their tax returns); *Naghavi v. N.Y. Life Ins. Co.*, 260 A.D.2d 252, 252, 688 N.Y.S.2d 530, 530-31 (1st Dep't 1999) (in affirming the trial court's dismissal of the plaintiff's claim, the court held that the plaintiff was precluded from asserting that his income was more than that which he had declared on his tax returns); *Friedman v. Ocean Dreams, LLC*, 15 Misc.3d 1146(A), 841 N.Y.S.2d 819 (table), at *10 (Sup. Ct. Kings Co. 2007) (New York's general rule is that "a party is estopped from taking a position which is contrary to a position taken on his or her tax returns" and noting neither plaintiff's own tax returns nor those of the company, which plaintiff prepared, reflected his ownership interest); *Zemel v. Horowitz*, 11 Misc.3d 1058(A), 815 N.Y.S.2d 496 (Table), at *6 (Sup. Ct. N.Y. Co. 2006) ("Plaintiffs are estopped from claiming to this Court that they sold the CDK Shares and loaned the proceedings [sic] to Horowitz when they, under penalty of perjury, asserted to the IRS that the transaction was something entirely different.")

for, also denominates Winston as a 25% member. (Def's Ex. B). Helen Chiu admitted she provided the list that is Def's Ex. B to the LLC's accountants to assist in their preparation of the LLC's tax returns, which Man Choi authorized her to do. (Def's Ex. PP (Helen Chiu tabs 14, 18); Nov. 1, 2011, Tr. at 313:14-18).

Third, numerous other business records of the LLC, including financial statements for the LLC prepared at Helen's direction, demonstrate that Winston's capital account was in a 3:1 ratio with that of Man Choi, demonstrating a 25% interest, as set forth above.

Fourth, Man Choi submitted two affidavits in the prior action where he admitted he was only the majority member of the LLC, which contradicted his sworn testimony in this action and demonstrates his lack of credibility. (Def's Exs. X, at ¶ 1, and Y, at ¶ 1). Other witnesses called by the MCC Parties, including the LLC's attorney, Mr. Fishman, and its accountant, Mr. Miller, admitted to their understanding that Winston was a member of the LLC. (Feb. 7, 2012, Tr. at 272:8-274:1; Def's Ex. MM; Nov. 1, 2011, Tr. at 314:3-6; *see also* Def's Ex. F).

Even if the MCC Parties are not estopped from arguing that Winston is less than a 25% member, their admissions, the documentary evidence, and reasons Winston was made such a member cannot be overcome by after the fact, self-serving explanations.[35]

A. The MCC Parties' 1031 Exchange Rationale Is Irrelevant

The MCC Parties assert that Winston was listed as a member on the LLC's tax returns, as well as other various documents, merely to help him effectuate a 1031 like-kind exchange to defer

[35] Man Choi's change of position from signing documents under oath and creating records showing Winston was a 25% owner to his current stance that Winston never owned any part of the LLC underscores his lack of credibility and can be traced to Man Choi's apparent anger over his perception of Winston's behavior shortly after Henry's death. (Nov. 3, 2011, Tr. at 359:7-25; 362:20-363:9; Oct. 27, 2011, Tr. at 194:14-195:6). Winston explained that he did not attend Henry's funeral because he was afraid of losing control and, in Chinese tradition, older people do not attend funerals of the younger generation. (Dec. 2, 2011, Tr. at 660:16-24; Feb. 3, 2012 Tr. at 107:5-12). He also testified that he did not want Man Choi's daughters and wife involved in the LLC because of their improperly avoiding taxes by paying employees in cash. (Feb. 3, 2012, Tr. at 109:16-110:1). Prior to these perceived slights, Man Choi was grateful to Winston for, *inter alia*, sponsoring Man Choi's immigration and lending him money to set him up in business. (Nov. 27, 2011, Tr. at 358:22-359:6).

the payment of certain capital gains taxes. Even if true, it is unrelated to the percentage of the LLC that Winston owns. In *Blank v. Blank*, 256 A.D.2d 688, 681 N.Y.S.2d 377 (3d Dep't 1998), the court found that where the plaintiff's interest was established by corporate tax returns, financial statements, and bank applications, as here, the defendant's contention that the paper trail showing ownership by plaintiff was simply a misunderstanding was unavailing. *See also In re Heino*, 73 A.D.3d 1062, 1064, 901 N.Y.S.2d 671, 673 (2d Dep't 2010) (where petitioner's own tax returns disputed his contention, the Court did not deem the petitioner's "explanation" for the inclusion of property on the tax returns as negating the information contained therein).[36]

B. The MCC Parties' Unilateral Attempts To Re-Characterize Loans And Contributions After The Fact To Dilute Winston Must Be Rejected

The MCC Parties' attempt to recharacterize, to Man Choi's advantage, as capital contributions payments from Man Choi or his entities that were booked as loans, must be rejected.

First, as noted above, Mr. Nelson relied on *Roth Steel*, a case never cited in any New York state court, to support the wholesale revision of the LLC's books and records. In *Roth Steel*, the Internal Revenue Service objected to the taxpayer's classification as a loss advances it made. The case concerned only the tax liability of the taxpayer, *id.* at 628, 632, and nowhere discussed how the percentage ownership of a company should be determined and the appropriateness in a context such as the case at bar to recharacterize loans as capital contributions to change ownership reported on, *inter alia*, sworn tax returns.[37]

Nor can, as the Court recognized, the MCC Parties unilaterally dilute Winston. (Mar. 14,

[36] The total gain that Winston had deferred was $20,000. (Feb. 2, 2012, Tr. at 65:8-25; Dec. 2, 2011, Tr. at 652:18-23). Even assuming a 20% tax rate for capital gains in 1999, the deferred tax would have been at most $4,000. Saving $4,000 cannot explain why Winston would apply for and personally guarantee a $3.5 million mortgage. It fails to explain why Winston was a 25% member, as opposed to say a 1% member. The reason supported by the documents from both before and after the closing was that the parties intended Winston to be a 25% member.

[37] Even assuming the *Roth Steel* factors apply, some would strongly indicate that the payments from Man Choi and his entities to the LLC, which the LLC recorded as loans, were also loans for tax purposes under *Roth Steel*. The circumstances and the parties' conduct further demonstrate that the payments were loans.

2012, Tr. at 373:18-375:17) ("THE COURT: My problem is the unilateral nature of the contribution" and also stating one member cannot change capital contribution without permission of another and that it is possible equipment purchased or alterations to building would not increase value of the LLC).[38]

The MCC Parties may argue, pursuant to their accounting claim, Winston must put in additional funds to the LLC to prevent from being diluted. This argument fails for three reasons. **First**, as shown above, Man Choi has received credit for all payments (including for customizing the Property for his companies' use, *infra*) he made on behalf of the LLC in both valuations of the LLC.[39] **Second**, Man Choi agreed that the funds from 1-9 Bondst used at the closing and for the contract deposit would be loans. (Def's Ex. D, tab 13, at 631-32). **Third**, when the reconciliation was prepared in 2001, the LLC had significant debt and the value of the Property had dropped by over $1 million according to Man Choi's appraiser.[40] Thus, Man Choi presumably had additional incentive to book his payments as loans so as to be before Winston in any dissolution as a creditor rather than an equity stake holder. *See* LLCL § 704(a). Man Choi cannot now recharacterize such loans as equity because it is advantageous to him.

Mr. Nelson stated that the value of Winston's membership interest could go up based on purported contributions made by Man Choi due to an overall increase in the value of the LLC

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[38] *See also Collins v. Telcoa Intl. Corp.*, 283 A.D.2d 128, 133–34, 726 N.Y.S.2d 679, 683-84(2d Dep't 2001) (alleged additional issuance of shares for the purpose of diluting plaintiff's percentage of ownership states a claim against majority shareholders); *Goldberg v. Goldberg*, 139 A.D.2d 695, 696, 527 N.Y.S.2d 451, 452 (2d Dep't 1988) (denying majority shareholders' motion for summary judgment that majority shareholders breached fiduciary duty when they "issued stock options and bonuses to themselves without at the same time granting him the opportunity to purchase shares on the same terms in proportion to his shares").

[39] To the extent Mr. Nelson attributed some payments to capital in arriving at his value of the LLC, the simple fact is this does not change Winston's interest, as shown in this memorandum.

[40] The LLC financial status in 2001 was precarious. Although the building was purchased for $5.45 million in September of 1999, (Def's D, at 364), it was worth only $4.2 million in March 2001. (Nov. 2, 2011, Tr. at 343:15-23) (Winston accepts Mr. Haims' appraisal as of May 2001 only for the purpose of illustrating the financial predicament of the LLC at that time and for no other purpose). The LLC's balance sheet as of December 31, 2001, showed its assets as $6.683 million and its liabilities as $6.061 million, (Def's Ex. C), and Mr. Nelson believed as of May 2001, assets exceeded liabilities by only $232,000. (Pls' Ex. 35, at p. 1).

even if the percentage of Winston's membership decreased through unilateral dilution. (Mar. 14, 2012, Tr. at 375:5-17). But, as the Court pointed out at the time, performing renovations, whatever the intention, might not increase the value of the Property and thus the value of a diluted interest might be worth less. (*Id.* at 373:18-374:6). Mr. Nelson conceded this point and that, under his theory, Man Choi's membership percentage would increase based on his purported contributions regardless of whether they increased the LLC's value. (*Id.* at 368:8-21).

Second, keeping records in accordance with GAAP is not required for the LLC, as Mr. Mercer testified without contradiction. (Apr. 3, 2012, Tr. at 815:5-22). Furthermore, SOP 78-9, upon which Mr. Nelson relied, relates to how an investor should account for investments in real estate ventures on its own books. There is no guidance at all regarding whether an investment is capital or a loan from the investee's perspective or regarding the allocation of entity ownership.[41]

Third, the clear inference from the evidence is that all the parties agreed that Winston would be a 25% member of the LLC for his contributions, including his applying for and personally guaranteeing the mortgage.[42] Mr. Nelson admitted on cross-examination that it would be erroneous to base membership interests solely on cash contributed if there were such an agreement.[43] Mr. Nelson also testified that, in preparing the Reconciliation, Mr. Miller "backed into" the 75%/25% split.[44] The only plausible reason for Mr. Miller, an accountant practicing since 1987, (Nov. 1, 2011, Tr. at 236:6-7), or his firm to have made what Mr. Nelson otherwise sees as a significant error would be because the MCC Parties instructed Mr. Miller or his firm to

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[41] SOP 78-9 does note, however, that an investment in a real estate venture "is the equivalent of a sale of an interest in the underlying real estate." Mr. Nelson agreed with this, stating "...cash is cash," and conceded that a marketability discount is not applicable to cash. (Mar. 20, 2012, Tr. at 446:7-12). Given that the appraisals of Mr. Salmon and Mr. Haims assume a hypothetical transaction took place as of the Valuation Date, meaning that the Property has been converted to cash as of the Valuation Date, this is an additional reason why there should be a 0% marketability discount, as shown in depth below.

[42] Def's Ex. D, tab 13; *id.* Tab 8, at 515-16.

[43] Mar. 14, 2012, Tr. at 375:24-376:17.

[44] Mar. 14, 2012, Tr. at 402:20-403:2; *see also* Feb. 6, 2012, Tr. at 214:1-13.

complete the Reconciliation,[45] and other financials as well as the tax returns for the LLC, to indicate that Winston was a 25% member. (*See, e.g.*, Def's Ex. B).

Fourth, Mr. Nelson's and the MCC Parties' rationale deliberately ignores the fact that entities owned by Man Choi had occupancy of the Property since September 8, 1999, (Oct. 25, 2011, Tr. at 35:17-24), at below-market rents, (Oct. 26, 2011, Tr. at 120:9-127:9; Def's Ex. G), and thus received a significant benefit for making the mortgage payments and payments on other operating and renovation expenses, which combined, were less than the market rent found by both appraisers. Furthermore, the renovations were done to customize the Property to the needs of the Man Choi owned entities occupying it which were conducting a retail and light manufacturing operation there.[46] The rationale also ignores that, under triple net leases, the tenant is responsible for all renovation expenses and thus would not get credit as contributions for renovation costs.[47]

The MCC Parties may also argue that, pursuant to LLCL §§ 504 and 509, in the absence of an operating agreement, as is the case here, Winston is entitled to receive the fair value of his membership interest in the LLC as of the date of withdrawal based upon his right to share in distributions from the LLC, and that his right to share in distributions is based on the value of the contributions of each member. Because Mr. Nelson's wholesale remaking of the books and records of the LLC must be rejected, the cash value of Man Choi's and Winston's capital would result in the 75%/25% split found in all the LLC's records. Moreover, even if this Court determines that certain payments by Man Choi were contributions, rather than loans, the value of Winston's contribution should not decrease. Guaranteeing a mortgage is a contribution under the

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[45] It also cannot be forgotten that Man Choi testified in the first action that he personally prepared the Reconciliation. (Def's Ex. PP (Man Choi tab 12)). If he did, then he plainly must have backed into the 75%/25% split to conform to the agreement with Winston.

[46] *See, e.g.*, Oct. 25, 2011, Tr. at 49:19-23; 53:7-10. The testimony and documents indicate that approximately $1.3 million was spent on the renovations only about $3,000 of which came from the LLC and the remainder from Man Choi owned entities. (Pls' Ex. 5).

[47] *See* Mar. 28, 2012, Tr. at 588:16-18; 619:10-18.

LLC law, one which the parties can value as they see fit.[48]

No actual record of the LLC has ever shown Winston to be other than a 25% member of the LLC. The MCC Parties cannot avoid their sworn tax returns and numerous other admissions through a convenient and self-serving reworking of the LLC's records under the guise of expert testimony. Accordingly, this Court must find that Winston is a 25% member.

II. LLCL § 509 REQUIRES THIS COURT TO DETERMINE THE FAIR VALUE OF WINSTON'S INTEREST AS OF FEBRUARY 9, 2008

LLCL § 509 provides, in relevant part:

> upon withdrawal as a member of the limited liability company, any withdrawing member...is entitled to receive, within a reasonable time after withdrawal, the **fair value of his or her membership interest in the limited liability company as of the date of withdrawal** based upon his or her right to share in distributions from the limited liability company. (emphasis added).[49]

The date of Winston's withdrawal was February 9, 2008. As Justice Flaherty found, Winston provided the notice to withdraw required by the relevant version of LLCL § 606, which became effective as of February 9, 2008. (Justice Flaherty Decision and Order, Index No. 25275/07, dated Mar. 31, 2008). Indeed, based on Justice Flaherty's Decision and Order, the MCC Parties sought an order that "the value of Winston's membership interest...must be valued as of...February 9, 2008." (*See* MCC Parties' Mem. of Law, dated Oct. 5, 2010, at 34). Justice Strauss granted this relief, holding that the buyout date should "be limited to February 9, 2008..." (Justice Strauss Short Form Order, dated January 26, 2011, at 3). Justice Strauss deemed Winston bound by Justice Flaherty's determination. So too are the MCC Parties.

The MCC Parties had Mr. Nelson opine that Winston withdrew his capital on May 21,

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[48] *Sachs v. Adeli*, 26 A.D.3d 52, 804 N.Y.S.2d 731 (1st Dep't 2005) (noting Plaintiff's interest in LLC increased based on guarantees he issued on two occasions); *see also* LLCL § 501 ("The contribution of a member to the capital of a limited liability company may be in cash, property or services rendered or a promissory note or other obligation to contribute cash or property or to render services, or any combination of the foregoing").

[49] Both experts used the fair value standard, (Feb. 6, 2012, Tr. at 162:1-11; Apr. 3, 2012, Tr. at 754:9-14), and, as shown above, arrived at nearly identical values for the LLC.

2001, and should be deemed to have withdrawn as of that date. Even if true that Winston took back his capital, which it is not, Winston could not have withdrawn from the LLC under New York law merely by doing so. NY LLCL § 606 (effective May 1999, when the LLC was formed),[50] which sets forth how a member may withdraw from an LLC, makes no provision that it can be done simply by withdrawing capital. Thus, even if Winston had wanted to withdraw from the LLC by taking back his initial capital contribution, he could not have done so. The Second Department's decision in the 2007 Appellate Order unequivocally demonstrates that the MCC Parties misguided effort to argue Winston took back his original contributions is a red herring. Much was made in the earlier trial before Justice Blackburne and on appeal of Winston's purported withdrawal of his original $193,854.51 and $60,000. Justice Blackburne relied on the purported withdrawal of these funds from an account at Eastbank in her decision. *Chiu v. Chiu*, 2005 WL 6578251 (Sup. Ct. Queens. Co., Nov. 18, 2005). Nevertheless, the Second Department concluded that her determination that Winston "'was never a member of the...LLC' was against the weight of the documentary and testimonial evidence." (2007 Appellate Order at 2).

Finally, the records are clear that Winston never withdrew his capital. The only money he ever had returned to him was the $290,622.77 deposited into a CD account at Eastbank, and which, when Winston withdrew it in March 2001, had grown to $302,855.70, with interest.[51] The MCC Parties have sworn that neither Henry nor Winston had authority to open the CD account, (*see* Def's Ex. PP (Man Choi tab 31)), and, at all times, treated the funds from the CD account as a loan paid back to Winston. (Def's Ex. A at 851; Def's Ex. C; Pls' Exs. 2A and 2B, at "Other

[50] The version of the law in effect at the time the LLC was formed governs. LLCL § 606(b). The relevant version of LLCL § 606 requires either a vote of the members, or, as occurred here, written notice six months before withdrawal becomes effective.

[51] There are no documents in the record that would demonstrate that the MCC Parties or the LLC repaid Winston's original contributions and it is contrary to the testimony of their own expert, Mr. Nelson, who confirmed the only funds ever returned to Winston came from the $302,855.70, which he treated as a loan to the LLC that was repaid. (Oct. 26, 2011, Tr. at 155:12-23; *see also* Def's Ex. PP (Helen Chiu tabs 21 and 22); Mar. 20, 2012, Tr. at 486:24-488:2; Pls' Ex. 33).

Current Liabilities" schedule). Thus, the $302,855.70 was Winston's to do with as he wished. It is irrelevant that he wrote checks to himself from a Charles Schwab account[52] in amounts nearly identical to his original contributions for his own accounting purposes.[53]

III. THE MARKETABILITY DISCOUNT MUST BE ZERO PERCENT

Mr. Nelson argued that a 25% percent marketability discount should be applied to the net asset value of the LLC, a single asset holding company. Mr. Nelson's qualifications as a valuation expert and particularly with respect to marketability discounts were weak with no writings or speeches on the subject.[54] The sources that he relied upon—restricted stock studies which he was unable to identify and a single chart in the so-called Pepperdine study which summarized survey results[55]—provided no persuasive evidence or reasoning to support a discount of this magnitude or any magnitude. Mr. Nelson grudgingly conceded that the purpose of a marketability discount is to account for the illiquidity of the shares of the LLC, that the LLC's assets did not include any goodwill and that the appraisal of the real property owned by the LLC involved calculation of a capitalization rate and assumed exposure time prior to the valuation date.[56] Mr. Nelson nonetheless clung to his arbitrary conclusion that the LLC's net asset value should be reduced by 25% before valuing Winston's 25% interest, with the result that Man Choi would retain the Property which could then be sold for the full appraised value with no marketability discount.

By contrast, Mr. Mercer is a leading expert on valuation, particularly marketability

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[52] Winston deposited the $302,855.70 in an account at Charles Schwab, in the name of the LLC. The name on the account is irrelevant. If Winston had opened an account in the name of IBM and made payments from that account without the knowledge or permission of IBM, no one would claim that such payments were IBM's.

[53] Feb. 2, 2012, Tr. at 27:3-12.

[54] Mr. Nelson lists only two articles on his résumé, neither of which relates to valuation, and has only one speaking engagement on an unspecified topic relating to business valuation on an unspecified date, before a Texas Bar Association. (Mar. 21, 2012, Tr. at 507:17-508:5).

[55] Mar. 20, 2012, Tr. at 427:7-22, 435:14-436:10; Mar. 21, 2012, Tr. at 508:6-15; Feb. 7, 2012, Tr. at 322:14-21.

[56] Mar. 20, 2012, Tr. at 438:10-19; 450:23-451:1; 453:6-9; 462:10-15; 464:8-12; 468:25-469:6; 471:7-15.

discounts, having written and spoken frequently on the subject.[57] Mr. Mercer explained why a marketability discount here above 0% would have the effect of denying Winston his proportionate share of the value of the LLC as a going concern, as required by *Beway*, and provide the majority owner—Man Choi—with a windfall in the same amount as the discount.[58] He also explained in detail why the sources upon which Mr. Nelson relied provided no market evidence justifying a marketability discount above 0%.[59]

The leading case on marketability discounts in New York is *Friedman v. Beway*, 87 N.Y.2d 161, 638 N.Y.S.2d 399 (1995). The court there prohibited imposition of a discount for the minority status of the dissenting shares and explicitly required that the dissenting shareholder "be paid for his or her *proportionate* interest in a going concern, that is, the intrinsic value of the shareholder's economic interest in the corporate enterprise." 87 N.Y.2d at 167, 638 N.Y.S.2d at 403 (emphasis in the original). The Court's apparent permission to impose a marketability discount under appropriate circumstances[60] has been a source of confusion in the Appellate Division and trial courts ever since. 87 N.Y.2d at 168 -169, 638 N.Y.S.2d at 403-04 (citing *Matter of Seagroatt Floral Co.*, 78 N.Y.2d 439, 442, 576 N.Y.S.2d 831 (1991)).

The nature of the confusion that *Beway* has given rise to was highlighted by Judge Warshawsky in *Murphy v. U.S. Dredging Corporation*, 2008 WL 2401230 (Sup. Ct. Nassau Co., May 19, 2008), *aff'd in part & rev'd in* part, 74 A.D.3d 815, 903 N.Y.S.2d 434 (2d Dep't 2010),

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[57] Apr. 3, 2012, Tr. at 745:14-751:20. One of Mr. Mercer's books is "Quantifying Marketability Discounts: Developing and Supporting Marketability Discounts in the Appraisal of Closely Held Business Interests" (Peabody Publishing, L.P., 1997) and the Revised Reprint (2001) and a second is "Business Valuation: An Integrated Theory, Second Edition" (John Wiley and Sons, Inc., 2007).

[58] Apr. 3, 2012, Tr. at 760:11-764:3, 770:13-19, 818:23-820:5. As an exmaple, using Mr. Mercer's valuation of the LLC, Winston's 25% interest is valued at $2,606,750 and Man Choi's remaining 75% would be worth $7,820,250. If Mr. Nelson's 25% marketability discount is applied, then Winston's 25% interest would be worth $1,955,063, but the overall value of the LLC has not decreased, meaning Man Choi's 75% interest has an implied value of $8,471,937.

[59] Apr. 3, 2012, Tr. at 802:23 -803:3; 803:11-805:21; 807:18 – 809:13.

[60] The *Beway* court wrote: "we have approved a methodology for fixing the fair value of minority shares in a close corporation under which the investment value of the entire enterprise was ascertained through a capitalization of earnings (taking into account the unmarketablity of the corporate stock) and then fair value was calculated on the basis of the petitioners' proportionate share of all outstanding corporate stock."

lv. denied, 18 N.Y.3d 953 (2012), a case involving dissolution of an enterprise that owned a portfolio of residential and commercial properties in various parts of the country many of which were subject to long term leases and various financing arrangements: "in most cases such as ours, the lack of marketability discount serves to cloak what is really a minority discount." Justice Warshawsky imposed the 15% marketability discount used by one expert who testified at the trial which the other expert "would also use but for the fact that he has concluded that no discount of this nature is appropriate under [these] facts." *Id.* On appeal the Second Department affirmed the 15% discount and noted that in order to reduce tax liability the "[c]orporation's intention was to hold its real property for a lengthy period of time." 74 A.D.3d at 817, 903 N.Y.S.2d at 437. Of course, the need to hold the underlying property to avoid gains taxes reduced the liquidity of the shares. Although a number of previous Second Department cases appeared to limit application of a marketability discount to the goodwill of a corporation, the court clarified that "the law does not limit the application of lack of marketability discount to the goodwill of a corporation *in all instances*." 74 A.D.3d at 818, 903 N.Y.S.2d at 437 (emphasis supplied).[61]

While the rulings on marketability discounts both before and after *Beway* have been uneven in the discounts that have been approved and the reasons given, the decisions are in harmony on the point pertinent to this case, that a single asset holding company presents the weakest possible case for imposition of a marketability discount. This is particularly true where, as is the case here, the asset held is a single building for which there is a tight market with high demand, no restrictions on its sale and which has been appraised as of a particular valuation date assuming exposure to market prior to the valuation date.

[61] When Mr. Nelson was asked at trial about why this case was an instance which justified not only departure from the long line of Second Department cases limiting the application of the discount to goodwill but a discount nearly 70% higher than that approved in *Murphy Dredging* his answers were vague and lacking in substance (e.g. "I mean. I didn't write the opinion. It says 'in all instances.' I think the words speak for themselves") and expressed the inaccurate view (which *Seagroatt* rejected "as a matter of law") that "New York statute says that marketability discounts are to be taken." (Mar. 20, 2012, Tr. at 450:23-453:22).

In *Matter of Seagroatt Floral Co. (Riccardi)*, 78 N.Y.2d 439, 576 N.Y.S.2d 831 (1991), a case that was cited and relied upon by both the *Beway* court and the *Murphy Dredging* court (at the Second Department), the Court of Appeals found that a 0% marketability discount was appropriate and rejected the idea that such a discount must be taken against the value of the enterprise rather than at some earlier stage. The court explained that while:

> the corporations argue that an identifiable discount must in all cases be applied against the value found – that the factor of illiquidity cannot be 'buried' in the capitalization rate . . . there is no single method for calculating that factor . . . Certainly, this Court has never mandated one. Thus, to the extent that respondent corporation suggest that illiquidity can only be taken into account by the application of a percentage discount against value—such as the Referee applied—the argument fails as a matter of law.

78 N.Y.2d at 446-47, 576 N.Y.S.2d 831. Here both real estate appraisers used the Income Capitalization Approach and developed a capitalization rate for that purpose.[62] Mr. Mercer explained that (as in *Seagroatt*) the capitalization rates accounted for any lack of marketability.[63]

In *Vick v. Albert*, 47 A.D.3d 482, 849 N.Y.S.2d 250 (1st Dep't 2008), the First Department applied *Beway* to value a partnership holding a single property and gave a 0% marketability discount holding that "application of the discounts sought by defendants would deprive plaintiffs of the decedent's proportionate interest in a going concern, since they would not receive what they would have received had the entire entity been sold on the open market unaffected by a diminution in value as a result of a forced sale." 47 A.D.3d at 484, 849 N.Y.S.2d at 252.[64] Significantly, the First Department then cited two Second Department cases both of which remain

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[62] Nov. 2, 2011, Tr. at 327:6-10; Nov. 29, 2011, Tr. 450:19-24; Mar. 28, 2012, Tr. at 580:17-20, 591:12-14.

[63] Apr. 3, 2012, Tr. at 762:22-763:4 ("In reality in the valuation of real estate or in the valuation of business enterprises when the earnings of a company or the net operating income of real estate are capitalized, they are capitalized assuming that exposure to market appropriate for the asset being sold already occurred. So that those discount rates, capitalization rates, to take into account the unmarketability of the corporate stock in valuing the net asset value for an asset holding company.")

[64] This Court should follow *Vick*, since it is not contrary to any Second Department precedent. *Stewart v. Volkswagen of Am., Inc.*, 181 A.D.2d 4, 7, 584 N.Y.S.2d 886, 889 (2d Dep't. 1992); *Mountain View Coach Lines, Inc. v. Storms*, 102 A.D.2d 663, 664, 476 N.Y.S.2d 918, 920 (2d Dep't 1984).

good law, *Cohen v. Cohen*, 279 A.D.2d 599, 719 N.Y.S.2d 700 (2d Dep't 2001) and *Matter of Cinque v. Largo Enterprises of Suffolk County*, 212 A.D.2d 608; 622 N.Y.S.2d 735 (2d Dep't 1995), for the proposition which is directly on point here: "*The unavailability of the discounts is particularly apt here, where the business consists of nothing more than ownership of real estate.*" 47 A.D.3d at 484, 849 N.Y.S.2d at 252 (emphasis supplied). In *Cole v. Macklowe*, 2010 WL 7561613 (Sup. Ct. N.Y. Co. Sept. 27, 2010), the court went one step further and precluded any testimony with respect to marketability discounts in valuing "an equity interest in various properties, each of which is owned by a Macklowe-controlled limited liability company or limited partnership." As in the instant case, there were no restrictions on the sale of the underlying property or the holding entity that owned it, and the Court continued, "in cases involving the involuntary sale of the interests of a minority owner who has essentially been forced out of a company, the minority owner is entitled to receive the 'fair value' of these interests . . . the Court in [*Beway*] implicitly recognized that a marketability discount may not be [be] applied where, as here, it is essentially based on the minority's lack of control."

Giaimo v. Vitale, 31 Misc.3d 1217(A), 930 N.Y.S.2d 174 (Sup. Ct. N.Y. Co. 2011), involved the valuation of two holding companies which owned 19 residential buildings. There the court once again gave a 0% marketability discount but based on a different rationale than in the cases above but which also applies to the instant case. *Giaimo* stated the proposition that determination of fair value is "a question of fact which will depend upon the circumstances of each case; there is no single formula or mechanical application." *Id.* at *4 (citing *Seagroatt* (which it quoted) and *Matter of DeAngles v. AVC Services Inc.*, 57 A.D.3d 989, 851 N.Y.S.2d 290 (2d Dep't 2008)). Because "the availability of similar properties on the open market is limited and . . . a buyer would accordingly buy the properties. . .through the corporations" the court affirmed the Referee's decision that the discount for lack of marketability did not apply. This

rationale for finding a 0% marketability discount would apply here with equal force since the expert appraisal testimony demonstrated that both experts believed that the availability of similar properties was "limited"[65] and Mr. Mercer testified without contradiction that there would be no impediment to a purchaser who was interested in the building from buying the LLC itself.[66]

In *Matter of Adelstein*, 2011 WL 6738941 (Sup. Ct. Queens Co., Nov. 3, 2011) (Kitzes, J.), in a fair value case involving a supermarket distribution company, and thus presumably significant goodwill, the court used a different approach and gave a discount for lack of marketability of 5% based on "transaction costs [that] are typically incurred" in the sale of a small business which the expert estimated to be between 5% and 10%. Here Mr. Mercer testified without contradiction that "[g]enerally speaking, transaction costs run from three to five to six percent..."[67] If this method is followed here, a marketability discount of 3% should be applied.[68]

By contrast, Mr. Nelson relied on restricted stock studies none of which he was able to identify but which Mr. Mercer explained has no value whatsoever to the determination of a marketability discount (if one were proper).[69] The single chart of the Pepperdine Study was also unhelpful because it was a summary of a survey of marketability discounts given by an unidentified number of appraisers under undisclosed circumstances. (*Id.* at 807:18-809:3).

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[65] Mar. 28, 2012, Tr. at 615:21-617:19; Nov. 29, 2012, Tr. at 454:25-455:4; *id.* at 455:8-17.

[66] Apr. 3, 2012, Tr. at 797:1-799:22. Mr. Mercer was the expert in *Giaimo* and he testified there as he did here that application of a marketability discount was a disguised minority discount and thus inconsistent with *Beway's* prohibition of minority discounts and its requirement that the dissenting shareholder be given a proportionate share of the value of the enterprise as a going concern. The Referee accepted Mr. Mercer's rationale and the Court found the Referee's decision consistent with both *Vick* as well as a "long line of Second Department cases" limiting application of marketability discounts to the "portion of the value of the corporation that is attributable to goodwill." *Giaimo*, 31 Misc.3d 1217(A), at *3. Although it reached the same 0% discount, the Court avoided ruling directly on whether it was proper to follow *Vick*, ruling that *Vick* may not be followed "to the extent that it is inconsistent with *Beway*." *Id.*

[67] Apr. 3, 2012, Tr. at 812:16-18.

[68] The better argument would still be to apply a 0% marketability discount because the transaction costs do not go to the value of the company itself but the amount of net proceeds that would be received if it were sold. But the transaction cost method is at least derived from current market evidence of transactions involving similar businesses, unlike the restricted stock studies.

[69] Apr. 3, 2012, Tr. at 802:23-803:3 ("My opinion is the averages of restricted stock studies bear no resemblance either in time, the studies date back to the 1960's and the nature of the business itself, all of these studies were, company, virtually all of these companies are young public companies that are thinly capitalized that have public markets."); *see also id.* at 803:11-805:21

It appears that Man Choi intends to place heavy reliance on two other cases that discuss marketability discounts, namely *Matter of Jamaica Acquisition, Inc.*, 2009 N.Y. Slip. Op. 52046(U), 2009 WL 3270091 (Sup. Ct. Nassau Co, 2009) and the equitable distribution case *Cooper v. Cooper*, 84 A.D.3d 854, 923 N.Y.S2d 596 (2d Dep't 2011). Neither of these cases provides any support for Mr. Nelson's imposition of a marketability discount of 25% in this case. The facts in *Jamaica Acquisition* are readily distinguishable because in that case, unlike here, there were restrictions on the sale of the assets owned by the enterprise—a varied portfolio of leased properties—because of the REIT structure in which the properties were to be held "for at least 10 years." Furthermore, because the enterprise there owned a portfolio of numerous properties just as in *Giaimo* and *Murphy Dredging,* the appraisal of any one property might not account for the illiquidity of the portfolio as a whole and an additional discount might be required. *Cooper v. Cooper* is unhelpful for at least two reasons: (1) it was a matrimonial equitable distribution case in which in the court was free to depart from the rules which apply to statutory fair value cases between unmarried business people;[70] and (2) it included no facts regarding the underlying business or what how the valuation was done except to describe it as a company which "distributes electronic components" rather than a holding company.

The marketability discount applied to this single asset holding company whose only asset is a highly sought after commercial building should be 0%. That the Property is owned through an LLC rather than directly by Winston and Man Choi does not justify any marketability discount

[70] *Michaelessi v. Michaelessi,* 59 A.D.3d 688, 689, 874 N.Y.S.2d 207, 208 (2d Dep't 2009) (trial court is vested with broad discretion in making an equitable distribution of marital property, and unless it can be shown that the court improvidently exercised that discretion, its determination should not be disturbed); *see also Davis v. O'Brien*, 79 A.D.3d 695, 696, 912 N.Y.S.2d 644, 646 (2d Dep't 2010) ("[t]he distribution of marital assets depends not only on the financial contribution of the parties 'but also on a wide range of nonremunerated services to the joint enterprise...'"); *Iwanow v. Iwanow*, 39 A.D.3d 471, 473-74, 834 N.Y.S.2d 247, 249 (2d Dep't 2007) ("trial court has broad discretion in selecting the dates for the valuation of marital assets..."); *McMahon v. McMahon*, 187 Misc. 2d 364, 368, 722 N.Y.S.2d 723, 726 (Sup. Ct. N.Y. Co. 2001) ("court's right to exercise discretion in marital distribution cases, does not lie in the statutory definitions which control classification of marital assets...[but] in the court's power to determine a percentage of distribution that it considers equitable, depending upon the factors of each...case.")

greater than 0%, much less a 25% discount, the only effect of which would be a windfall for Man Choi, who could then sell the building or the LLC free of any discount.

IV. WINSTON IS ENTITLED TO ADDITIONAL RELIEF

First, the MCC Parties fail to credit Winston the additional $60,000, which were used for LLC purposes, that Winston contributed to the LLC through the 1-9 Bondst account. (Def's Ex. FF).[71] The funds should be treated as an unrepaid loan to the LLC, and this Court should award Winston $60,000 and interest from May 13, 1999, in addition to the fair value of his interest.

Second, Winston brought both a direct and derivative breach of fiduciary duty claim, premised on the MCC Parties' failure to rent the Property at market value. Both experts, in arriving at the LLC's net asset value, included what they believed to be the difference between the rent paid and what the LLC could have earned in an arms' length transaction, the "foregone cash." If, and only if, this Court does not include the "foregone cash" in determining the LLC's net asset value,[72] then the "foregone cash" has to be awarded to the LLC under Winston's derivative claim,[73] and Winston is entitled to 25% of that amount. This Court should schedule a hearing concerning the amount of attorneys' fees to award for the derivative claim.

V. WINSTON SHOULD BE AWARDED PRE-JUDGMENT INTEREST

Winston should be awarded interest at 9% per year on the fair value of his interest from at least the Valuation Date. *In re Superior Vending,* LLC, 71 A.D.3d 1153, 1154, 898 N.Y.S.2d 191, 192 (2d Dep't 2010) (purchasing member to pay 9% interest since November 2002, when business relationship terminated); *Blake v. Blake Agency, Inc.,* 107 A.D.2d 139, 150-51, 486

[71] There was no evidence that 1-9 Bondst treated these funds as a loan because the deposit was to establish a banking relationship with Eastbank for the mortgage for the Property and 1-9 Bondst was used as a convenience since the LLC was not yet formed. (Feb. 2, 2012, Tr. at 27:13-28:3; 71:23-72:8).

[72] In which case, Mr. Mercer testified the LLC would be worth $8,799,926. (Apr. 3, 2012, Tr. at 780:3-7), and Winston's 25% share would be worth $2.2 million.

[73] The claim was made for the period prior to the withdrawal date. Moreover, as the MCC Parties have not yet paid out the value of Winston's interest, he still has standing to pursue such a derivative claim. *See Arfa v. Zamir*, 63 A.D.3d 484, 485, 880 N.Y.S.2d 635, 636 (1st Dep't 2009) (LLC member does not lose membership status by exercising a put until put transaction is consummated).

N.Y.S.2d 341, 350 (2d Dep't 1985) (reversing trial court and awarding interest from date of petition at 9%, stating, "justice requires that...interest be paid"); *Murphy,* 74 A.D.3d at 820 (2d Dep't 2010) (accepting that trial court applied 9% interest rate from date of valuation until entry of judgment except for a period while decision was pending, where it used 5%, and remanding 5% rate for further consideration); *Jamaica Acquisition*, 2009 N.Y. Slip. Op. 52046(U), 2009 WL 3270091, at *28 (awarding interest at the rate of 6.5% on the amount owed from the valuation date to the decision of the court; the Court appears to have chosen this 6.5% rate based on the rate payable on a line of credit at the time of the merger); *see also Beway*, 87 N.Y.2d at 170, 638 N.Y.S.2d at 404 (affirming the award of pre-judgment interest); BCL § 623(h)(6); CPLR §§ 5001; 5004.[74] Furthermore, under *In re Superior Vending and Blake,* and the BCL (see BCL § 1118(b)), it is clear that interest should run from the date of Winston's complaint, October 10, 2007, or earlier; but to make Winston whole,[75] it must at least run from the Valuation Date.

VI. JUDGMENT SHOULD BE ENTERED FOR WINSTON ON THE PORTION OF MAN CHOI'S FIRST CAUSE OF ACTION SEEKING AN ACCOUNTING

As set forth above, Man Choi has received credit for all payments he or his companies have made on behalf of the LLC. Moreover, Winston cannot be called to account for any portion of such payment.[76] Furthermore, accounting claims are generally brought against a fiduciary entrusted with property to render an account of his or her actions and for the recovery of any

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[74] Although *Blake* counsels such an award is required, even assuming it is discretionary the cases cited in this section demonstrate interest is routinely granted and the Second Department has overruled the failure to include such interest in an award in analogous BCL contexts. This is a case that screams out for an award of prejudgment interest: Winston has been forced to litigate for nearly a decade because he was completely frozen out of the LLC and, despite the clear holding of in the 2007 Appellate Order that Winston was a member, the MCC Parties continued to exclude Winston, forcing him to withdraw, while reaping the benefits of the Property and its increase in value.

[75] *Prager v. N.J. Fid. & Plate Glass Ins. Co.*, 245 N.Y. 1, 5-6, 156 N.E. 76, 80 (1927) (Cardozo, J.) ("While the dispute as to value was going on, the defendant had the benefit of the money, and the plaintiff was without it. Interest *must* be added if we are to make the plaintiff whole") (emphasis supplied).

[76] LLCL § 609 (requiring articles of organization to create such an obligation); *see also Ctr. for Rehab. & Nursing at Birchwood, LLC v. S & L Birchwood, LLC*, 92 A.D.3d 711, 714, 939 N.Y.S.2d 78, 80 (2d Dep't 2012) (member cannot be held liable for LLC's obligations simply by virtue of his status as a member thereof). There is no such provision in the LLC's articles of organization. (Def's Ex. E).

balance found to be due.[77] In this case, Winston has not been entrusted with any LLC property and has actually been excluded for over a decade. Moreover, the MCC Parties unfounded claims that Winston's pursuing of litigation may have cost the LLC money are not sufficient for an accounting, as this Court recognized.[78] Thus, this Court should dismiss or deem satisfied by the award to Winston, that part of Man Choi's First Cause of Action seeking an accounting.

CONCLUSION

On Winston's and Man Choi's First Causes of Action, the Court should declare Winston was a 25% member of the LLC on the Valuation Date, and should dismiss or deem satisfied by the award to Winston, that part of Man Choi's First Cause of Action seeking an accounting.

On Winston's Second Cause of Action for withdrawal, the Court should require, pursuant to LLCL § 509, the MCC Parties to pay Winston the fair value of his 25% interest in the LLC as of February 9, 2008, which is $2,606,750, plus pre-judgment interest from at least February 9, 2008, and return to him his $60,000, plus pre-judgment interest from May 13, 1999.[79]

On Winston's Eighth Cause of Action and Derivative Counterclaim and Third Party Claim, this Court should enter judgment in favor of Winston and the LLC, in the amount of $1,626,000, and award Winston his proportionate share of these funds, only if the Court does not include this amount in the net asset value from which it derives the fair value of Winston's 25% interest, in which case the Court must also schedule an attorneys fees hearing.[80]

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[77] *See Gottlieb v. Northriver Trading Co. LLC*, 58 A.D.3d 550, 551, 872 N.Y.S.2d 46, 46 (1st Dep't 2009); *see also* N.Y. P'ship Law § 44(1) (wrongfully excluded partner has right to accounting); BCL § 720 (permitting shareholder derivative action against officers or directors for an accounting).

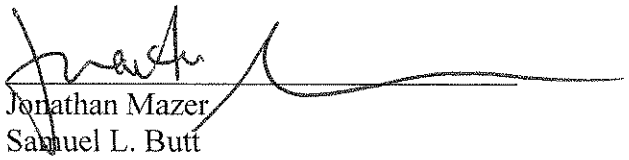
[78] Oct. 25, 2011, Tr. at 61:20-62:2 ("THE COURT: "[T]he mere fact that he brought this litigation, this litigation is taking so long, is not sufficient enough for offsetting the accounting...You need more direct documentation or information to make that connection.")

[79] Given Winston's withdrawal as of February 9, 2008, Winston does not currently seek an order requiring dissolution of the LLC pursuant to his Third Cause of Action so long as he paid the fair value of his 25% interest, $2,606,750.

[80] The Parties' other causes of actions, including that part of Man Choi's First Cause of Action that sought a declaration Winston was merely a nominal member and his Second Cause of Action that sought to expel Winston, were dismissed. *Chiu v. Chiu*, 71 A.D.3d 646 (2d Dep't 2010); *Chiu v. Chiu*, 71 A.D.3d 621 (2d Dep't 2010).

Dated: New York, New York
June 5, 2012

SCHLAM STONE & DOLAN LLP

By: 

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