At a Trial Term of the Supreme Court of the the State of New York held in and for the Sixth Judicial District at the Broome County Courthouse in the City of Binghamton, New York commencing on the 11th day of September, 2000.

PRESENT: HON. PATRICK D. MONSERRATE,
Justice Presiding.

STATE OF NEW YORK
SUPREME COURT :: BROOME COUNTY

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**D E C I S I O N**

JOHN L. O'BRIEN, JR., JAMES E. O'BRIEN, SR., JOHN J. O'BRIEN, AND JAMES E. O'BRIEN,

Petitioners,

For the Judicial Dissolution of ACADEME PAVING, INC., and JOB, LLC.

Index No. 99-2594
RJI No. 99-1794-M

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APPEARANCES: HODGSON, RUSS, ANDREWS, WOODS & GOODYEAR, LLP
By: RICHARD L. WEISZ, ESQ., OF COUNSEL
Attorneys for Minority Shareholders
Three City Square
Albany, New York 12207-2856

STANTON M. DRAZEN, ESQ.
Attorney for Majority Shareholders
96-98 State Street, Suite 500
P.O. Box 358
Binghamton, New York 13902-0358

HINMAN, HOWARD & KATTELL, LLP
By: DARWIN R. WALES, ESQ., OF COUNSEL
Attorneys for the Corporations
80 Exchange Street
P.O. Box 5250
Binghamton, New York 13902-5250

**PATRICK D. MONSERRATE, JSC**

The warring factions of what was once the O'Brien family have left it to the Court to determine the combined fair value of the shares of two closely held corporations: Academe Paving, Inc. (an entity engaged in paving/crack-sealing roads/highways and selling stone and blacktop) and its land-holding affiliate, JOB, LLC. This came to pass with the November 10, 1999 filing by the minority shareholders (45.46%) -- Petitioners James E., Sr., John L., Jr., James E. and John J. O'Brien -- of a petition for the judicial dissolution of the companies [*BCL §1104-a*]. Within 90 days thereafter, on or about November 24th, the majority (54.54%), in the persons of Respondents Jack and Jerry O'Brien and Joann (O'Brien) Juliessen, filed an election to purchase the shares of the minority, thus effectively staying the dissolution proceedings [*BCL §1118(a)*]. A December 13th offer of $1,818,400 (based on 45.46% of $4 million) was rejected by the minority as inadequate. Subsequent negotiations have reached an impasse and the Court has been asked to resolve the valuation issue.

An evidentiary hearing was held on September 19-20, 2000 to determine the combined fair value of the subject shares as of November 9, 1999 (the day prior to the filing of the dissolution petition) [*BCL §1118(b)*].

The point of beginning for the valuation exercise is a report prepared and issued (under date of May 18, 1999) by Empire Valuation Consultants.

That valuation report [*Exhibit C-1*[1]] was commissioned by Academe at a time when all of the parties were still involved in the business operation,[2] and there was at least one offer to purchase Academe/JOB being negotiated. Emil Gelasso of Cobleskill Stone Products was a serious suitor; his May inquiries to the O'Briens about possible price brought back range estimates of "$9 to $10 million." Eventually, his July offer to management (by then, the Respondents) to buy both entities for $5 million was rejected as too low. Gelasso's interest then waned, for a time [*See Exhibits R-1, R-2, R-3*].

In any event, the May 1999 Empire valuation seems to have been done at a time when the common object of all concerned was to know what fair value the principals might reasonably expect to receive from a sale of the business. Empire's answer, "on a 100% enterprise basis," was "$7.6 million, rounded" [*Ibid., pp. 32, 44*].

The author of the report and its hearing proponent, Terence L. Griswold, ASA, and an Empire principal, performed a fairly straightforward analysis of the Academe operation using as his methodology a capitalization of earnings (or, as he termed it, "a segregated capitalization of debt-free earnings" [*p. 32*]). The resulting computations [*see p.7, infra.*] showed a value of $6,205,617 [*Exhibit F*].

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[1] There were three species of hearing exhibits: those designated as Court exhibits ("**C**"), those offered by Petitioners ("**P**"), and those by Respondents ("**R**").

[2] The final split would come in June 1999 when the majority would vote the minority "out-of-office" and assume total control of business operations.

To Griswold's view, the valuation of JOB required a different approach, given its function as a real estate holding company which owns the land on which Academe's buildings are located as well as quarries from which Academe mines sand, gravel, and slate. The several properties are on Broad Street in the City of Binghamton (#16 - 18 1/2, #20 - 22, #30, and the main office and Broad Street Mine), another in Broome County, a sand pit known as "Yary's Quarry on Route 369 in the Town of Fenton, and a gravel quarry, "The Brisben Pit", located on Route 32 in the Town of Greene (Chenango County).

Since he was not provided with market values for any of JOB's assets, he ruled out using an Adjusted Book Value methodology [*p. 30*], but with "key assumptions regarding JOB's annual mine output" [*p. 29*] he felt confident in using a Discounted Cash Flow methodology. He thereby arrived at a preliminary value of $1,848,834, from which he subtracted debt of $475,000 ("Note Payable to Academe") to arrive at his final value for JOB of $1,373,834 [*Exhibit R-I*].

When added to his previously determined Academe value ($6,205,617) the result was his "$7.6 million rounded" [*p. 44*] "on a 100% enterprise basis,

for purposes of a prospective sale" [*p. 45*]. Such was the fair value of the subject companies as of April 30, 1999.[3]

During the autumn of 1999 two events of note occurred. Mr Gelasso renewed his efforts to purchase Academe/JOB and increased his offering price to $7.6 million (although without specifics as to "time and terms")[4] . The offer was not accepted or refused before the second event: the November 10th filing of the petition by the minority shareholders for the judicial dissolution of the companies Gelasso was offering to purchase.

In the O'Brien divorce of June 1999, the Respondents/majority shareholders seem to have been awarded the custody of Mr. Griswold. When, during the summer of 2000, he was again contacted about updating his April 30th (1999) valuation to the November 9th date central to this proceeding, the atmosphere at Academe had changed dramatically.

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[3] Both prior to and during the hearing Respondents' counsel has persistently been exhorting the Court to note well that "fair market value", the mantra of all manner of appraisers and valuators is **not** the "fair value" which is the Court's holy grail in an "1118" proceeding. Why not? Because the phrase is not so defined (or otherwise) in the Business Corporation Law, a truism that even the Court of Appeals, with its occasional flair for the obvious, seems to grasp [*cf Mtr. of Seagroatt Floral (Riccardi), 78 NY2d 439, 445 (1991)*]. However, the Chief Judge uses the terms so interchangeably [*Ibid.*] that one is left to conclude that no one can seriously question that a finding of fair market value of a business/enterprise would not equate with the "fair value" of its ownership interest.

[4] The hearing testimony was not clear on whether the "financial information" provided to Gelasso during the earlier negotiations included the Empire valuation of the same figure.

Gone were the minority shareholders and "team majority" was on litigation alert". Griswold's handlers during his new assignment would be virtually exclusively members or allies of the majority (and their counsel), and if they could do anything to influence the outcome of his work in their favor, they would do it. Not so much with the valuation of Academe, but strongly so with regard to JOB, and certainly so as to the "August surprise."

His August 2, 2000 report [*Exhibit C-2*] reflects that his Academe methodology did not change and therefore many of his numbers did not either. The only new information was what income and expenses had to be plugged in to update his valuation from April to November. The result ($6,128,984) was within 1% ($77,000±) of the earlier value. To be sure, there was some interim tinkering with Academe by the majority which he was not told about and didn't detect,[5] but all in all the integrity of his earlier valuation was not seriously diminished.[6]

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[5] During the fall (before November 9th) the Respondents (Jerry, Jack, and Joann) formed JJJ Leasing, Ltd. which, as "duly authorized" by the Boards of Directors of Academe (same three people) [*Exhibit P-6*], would lease vehicles (for themselves) and equipment (for Academe) that would not show on the books as Academe assets [*Exhibit P-7,8*].

[6] Counsel for Petitioners complained of Griswold's having raised his value-lowering Cap Rate (from 9.3 to 9.6%) by attributing a negative impact on Academe's value to the July-November emergence of Bothar (a corporate creation of the ousted Academe minority, who promptly jumped back into the paving pool as competitors). Petitioners' point was that, even with Bothar on the scene, the numbers reflect that Academe was making more money and operating at a profit. True, but as Jerry O'Brien testified, Academe was forced to shave its profit *margin* substantially in order to avoid losing bids to the equally shrewd bidders from Bothar. Taught at the same knee, after all.

## ACADEME VALUATION

| | (4-30-99) | (11-9-99) |
|---|---|---|
| Average adjusted debt-free pretax income | $ 885,359 | $ 966,197 |
| State and Federal taxes (@ 40%) | - 354,144 | - 386,479 |
| Net income after taxes | $ 531,215 | $ 579,718 |
| Capitalization rate | x 9.30% | x 9.60% |
| Value of Total Invested Capital | $5,711,989 | $6,038,729 |
| Interest-bearing debt | - 538,837 | - 636,932 |
| Marketable controlling equity value of operations | $5,173,152 | $5,401,797 |
| Non-operating assets | + 1,332,465 | + 1,027,187 |
| Total | $6,505,617 | $6,428,984 |
| Cash for operating expenses | - 300,000 | - 300,000 |
| Value | $6,205,617 | $6,128,984 |

However, the same cannot be said about his valuation of JOB. First of all, Griswold was persuaded that he had been seriously wrong in the choice of his earlier methodology; he was talked out of his Discounted Cash Flow analysis. If not that method, than what? Certainly not Adjusted Book Value, since he had previously been provided with no market values for JOB's assets, an essential component of ABV valuations. "But wait", said the Respondents (figuratively, if not literally), "if it's market values you need, just ask us." Ask he did, and that's about all he did.

Understatedly prefaced "with the guidance of management", Griswold proceeded to list [*@ pp. 44-45*] the several properties and to plug in numbers given to him "per management" for original cost (intra-family transfers, all) and subsequent improvements. Only the tax-assessed valuation of each property was a verified entry, or a verifiable one. He summarized his various values [*Exhibit I*] and arrived at a preliminary value of $1,593,100 (compared with $1,848,834 in April). "And don't forget the debt," added Joann. "What debt?" queried Griswold. "The $1,100,610 mortgage." "Oh, *that* debt." Without seeing -- or looking for -- mortgage, note, or other documentation[7] Griswold dutifully entered her number and reduced his final JOB valuation to $492,490. When compared with his earlier $1,373,834 figure, the difference is a noticeable 64%.

Fortunately for the cause of fairness, there was more hearing evidence on the JOB valuation. Under further questioning Griswold conceded that there

[7] Griswold said that Joann did show him an Income Tax Return whereon she had also told the IRS that such a debt existed.

were better methods than his "taking dictation" for obtaining the market values of assets for an ABV analysis. He acknowledged that where, as here, real estate is involved, he would yield in his valuation to an appraiser qualified in that field. Such a witness was produced.

John S. Miller, MAI, of the Central New York Appraisal Group, testified as to appraisals he had done of two of the JOB properties: The Brisben Pit [*Exhibit P-4*] and "Yary's Quarry" [*Exhibit P-5*]. In each instance he used a Market Data/Comparable Sales methodology to arrive at November 1999 appraised valuations of $770,000 for the former (compared with Griswold's "estimated" $137,333) and $350,000 for the latter (compared with $149,300). Whatever cross-examination nitpicking Mr. Miller may have faced as to how "comparable" were his comparables, his testimony credibly established that the two properties (at least) had been dramatically undervalued by Mr. Griswold ("per management").

The JOB "$1 million debt" issue was addressed in two ways. First, documentary evidence was produced [*Exhibits P-1 and P-2*] to show that no real property mortgages existed of record as of November 1999 in either Broome or Chenango Counties against properties titled either to Academe or JOB. Next, Joann Juliessen was called as a witness and was asked to confirm that she had told Griswold about the debt. She had. On what had she based her statement? A (promissory) note. When asked to produce it, she could not.

The only evidence remaining in the record (after Mr. Griswold was persuaded to disavow his DCF analysis) concerning the proper methodology to

value JOB is that of Adjusted Book Value. The Court must, therefore, recompute Mr. Griswold's figures [*Exhibit I*] to increase the value of two of the assets in accordance with Mr. Miller's appraisals (which the Court found to be credible), and to eliminate any provision for debt against the real estate (because the Court found any testimonial reference thereto to have been incredible).

**JOB VALUATION (11-9-99)**

**Real Estate**:

| | |
|---|---|
| 16-18 1/2 Broad Street @ 1995 Cost | $ 31,395 |
| 20-22 Broad Street @ 1995 Cost | 128,100 |
| 30 Broad Street @ 1995 Cost | 51,019 |
| Brisben Mine (CNYAG Appraisal) | 770,000 |
| Yary's Quarry (CNYAG Appraisal) | 350,000 |
| Main Office & Broad Street Mine @ 1997 Cost | 1,065,173 |
| Marketable Adjusted Book Value | $2,395,687 |

The "August surprise" refers to events which occurred after Mr. Griswold had issued his "update" report, but before it was seen by either Petitioner's counsel or the Court.[8] He described receiving a call from Respondents'

[8] At an August 10th Chambers conference Mr. Drazen advised both the Court and his adversary that he "understood" the Empire update was nearing completion, but that in his talks with Griswold, he was informed that no "numbers" had been finalized. The "August 2nd" issuance date of the report belies the accuracy of those representations.

counsel requesting that he develop a separate marketability discount to be applied to the minority interest (but only to the minority interest) as he had valued it. His testimony on the point:

DIRECT EXAMINATION BY MR. WEISZ:

"Q. Mr. Griswold, I see that for the April 30, 1999 appraisal there was no separate marketability discount analysis, but there is one for the November 9th appraisal. Could you explain the basis of that?

A. After the issuance of both reports, the assignment, we were asked to come up with a value on a fully enterprise, the value of both entities. After the second report, Mr. Drazen asked me to address it because the case had become a 1118 vase, and in that case the definition of value is fair value, and under that definition of value for the minority interest, what other considerations would one take into consideration, and I said, well, you would address the marketability discount of that specific block of stock under that statute. And he asked me then could I quantify what the marketability discount would be applicable to the stock.

Q. Applicable to the minority interest?

A. To the block of stock, the 45 percent interest.

Q. The free enterprise value for the company?

A. Yes.

Q. Would be the value that you had without applying the marketability discount?

A. Yes.

Mr. Griswold wrote in a letter under date of August 25th [*Exhibit C-3*], and so testified at the hearing, that he would reduce the value of Petitioners' 45+% interest by 30-35% (he preferred the higher end of the range) for the lack or marketability/"illiquidity" of their minority interest in closely held corporations. On each of the five pages of his letter Griswold emphasized that the "discount" was not applicable to the value of the corporations as a whole, but only "to derive the fair value of a minority common stock interest" [*p. 1*]. "A lack of marketability discount is selected below for a minority interest in Academe common stock" [*p. 2*]. "In this case, we are valuing a minority interest ... which generically supports a lack of marketability discount ..." [*p. 3*]. "A minority equityholder of Academe and JOB owns an equity interest for which no market exists" [*p. 4*]. " ... [I]t is our opinion that no less than a 30% -to-35% discount for lack of marketability is appropriate for the equity interest in Academe and JOB to derive the fair value of the specific fractional interest in each company as of November 9, 1999" [*p. 5*].

The Court will make no such reduction, because the law of New York says that it may not be done. In an August 24th Decision the Court shared with respective counsel its views on the law:

> A minority discount on the value of Petitioners' shares will not be applied in determining value pursuant to BCL 1118. In fixing fair value a Court must determine the minority shareholders' proportionate interest in the going concern value of the corporation as a whole, that is, what a willing purchaser, in an arm's length transaction, would offer for the corporation as an operating business [*Friedman v Beway Realty Corp., 87 NY2d 161 (1995), Mtr of Pace Photographers (Rosen), 71 NY2d 737 (1988), Mtr of Walt's Submarine Sandwiches, Inc., 173 AD2d 890 (Third Dept., 1991)*]. In *Friedman, supra,* noting [*@ 168*] that "there is no

> difference in analysis between stock fair value determination under Business Corporation Law section 623, and fair value determination under section 1118", the Court of Appeals held that in either situation application of a minority discount would deprive minority shareholders of their proportionate interest in a going concern and would result in minority shares being valued below that of majority shares, in derogation of the mandate of equal treatment of all shares in the same class in minority buy-outs. The court [*@ 169-170*] rejected the minority discount on the additional ground that such a policy would encourage oppressive conduct in order deliberately to drive down the compensation necessary to buy out the minorities' shares.

The Court continued, in that same Decision, and repeats here, that marketability discounts for close corporations (such as those here) are entirely proper **if** it is a factor used in valuing the corporation as a whole, not just the minority interest. For example, the expert referred to in *Seagroatt, supra* had taken the close corporation's illiquidity into account in constructing his "Cap Rate" for valuing the entire enterprise.

That was not done here by Griswold, or even claimed to have been done. He knew that he was doing valuations of two closely held family corporations and yet in neither instance of his "market value" valuation did he feel it was necessary, or even proper, to include illiquidity as a valuation factor. His post-report letter is simply an attempt to placate the Respondents'-majority's wish to impose an impermissible "minority interest" penalty, and thus to reduce their buyout obligation to Petitioners. The Court will not be a party to such a ploy.

Moreover, the situation at hand is the empirical exception to the theoretical mental gyrations of the caselaw [*e.g. Matter of Seagroatt, supra; Amodio v Amodio, 70 NY2d 5 (1987)*]. In cases such as those the reduction of

value of close corporations is thought to be necessary to reflect the (theoretical) circumstance that no "market" buyer would want to buy into such a corporation, even if shareholders were willing to sell their interests (which, under most circumstances, they are not).

By contrast, the April 1999 Empire valuation for Academe/JOB was done for the express purpose of assisting with sale negotiations with a willing and able buyer,[9] and the $7.6 initial value for 100% of the shares in the two entities was precisely the amount to which Gelasso increased his offer for those same shares during the fall of 1999 (the very timeframe under review). Where is the need for -- or even a place for -- a "lack of marketability" discount under such circumstances? Had the sale to Gelasso been consummated, would Petitioners' 45% interest in the proceeds have been subject to a 35% "minority discount"? As Mr. Gelasso attested, yet again during his hearing testimony, Academe/JOB was/is a very desirable/marketable commodity within the local paving industry. To quote the Chief Judge: "In that the [BCL 1118] valuation proceeding avoids dissolution and allows the continuation of an operating business, the value to be ascertained is that of an interest in a going concern rather than a share of a business in the throes of liquidation" [*Seagroatt, supra, @ p. 445*].

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[9] Mr. Gelasso's bank furnished him with a Letter of Credit for up to $15 million as a sign of his "bona fides". And, in the opening paragraph of his May 18th cover letter to the April valuation report, Griswold stated: "It is our understanding that the purpose of this valuation is for a prospective sale" [*Exhibit C-1*].

As Mr. Griswold saw no need to factor an illiquidity discount into his analysis of the "enterprise value" of Academe/JOB for either April or November 1999, so the Court sees no need to do so now.

As a final matter, inasmuch as the statute gives the Court discretion in the matter of awarding interest on Respondents' payment to Petitioners [*BCL §1118(b)*], an explanation seems appropriate as to why it intends to do so. The resolution of this matter, and the Petitioners' receipt of their money, has been delayed for almost a year, more than any other reason, because of the conduct of Respondents and their counsel. Their December buyout offer, based on a "valuation" of $4 million was so low as to signal the offerors' bad faith and to assure its rejection. At the time it was made, all parties knew that Empire/ Griswold had valued the companies at $7.6 million and that Mr. Gelasso had offered to buy them at that same figure.

Next, in order to afford the minority some protection for their ownership interest during what was shaping up as a protracted process, the Court directed that the majority post a bond [*BCL 1118(c)(2)*] of $3 million by January 7th (later extended to the 14th). That was never done. Counsel for the majority pleaded poverty on behalf of his clients and persuaded the Court that such a bond *would* not be posted, not that it *could* not have been. However, the Court was talked out of holding the majority shareholders in contempt by a pledge from their counsel that the cash and other assets which would have been necessary to secure a bond could/would be put to better use by funding a realistic, fair buyout offer to Petitioners, thus bringing to an

end a matter which had even by then dragged on too long. In hindsight, the Court is not persuaded that that was done either. Interest will be awarded.

## CONCLUSION

By reason of the foregoing, the Court finds that, as of November 9, 1999, the 100% enterprise value of Academe, Inc. (and the fair value of its shares) was $6.1 million and that the like value of JOB, LLC as of the same date to have been $2.3 million. Of the combined total of $8.4 million Respondents are obligated, by their election to do so, to pay Petitioners their 45.46% share, or $3,818,640, with interest thereon at 9% per annum from November 10, 1999 to the date of payment.

Submit judgment on notice pursuant to Section 202.48 of the Uniform Rules for the Trial Courts.

Dated: September 25, 2000
Binghamton, New York

Supreme Court Justice

TRIAL EXHIBITS HAVE BEEN RETURNED TO THE COURT CLERK AND SHOULD BE RETRIEVED FROM HER BY RESPECTIVE COUNSEL. THE ORIGINAL DECISION HAS BEEN FILED WITH THE BROOME COUNTY CLERK.