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STATE OF MINNESOTA | DISTRICT COURT

COUNTY OF HENNEPIN | FOURTH JUDICIAL DISTRICT

Versique Inc., formerly known as Versique Acquisition, Inc.,

Petitioner,

v.

Paul Beard,

Respondent.

Court File No. 27-CV-14-20377

FINDINGS OF FACT, CONCLUSIONS OF LAW, AND ORDER

The Court conducted a bench trial in this case from September 21–25, 2015. John A. Cotter and John A. Kvinge of Larkin Hoffman represented Petitioner Versique, Inc., formerly known as Versique Acquisition, Inc. Norman J. Baer and Amelia R. Selvig of Anthony Ostlund Baer & Louwagie, P.A. represented Respondent Paul Beard.

INTRODUCTION

This is a "dissenter's rights" proceeding in which the parties seek a judicial appraisal of the shares in the petitioning corporation. The primary issue is the fair market value of the company ("enterprise value") on August 19, 2014, the date of the merger that "cashed out" (the company's preferred term) or "squeezed out" (Respondent's preference) Respondent as a shareholder.

According to the valuation experts who testified, the enterprise value is $2.498 million, $4.1 million, or $10.3 million. The shareholders themselves offered a wider range of opinions. They thought the company was worth $400,000 to $12 million. The parties do agree, however, that once the enterprise value is determined, Respondent, a

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one-third shareholder until the merger, is entitled to one-third, subject to possible minor adjustments.

During the five-day trial, the Court received numerous exhibits and testimony from 11 witnesses, including four experts. The parties submitted post-trial briefing and proposed findings and conclusions.

Upon the record in this case, the Court makes the following Findings of Fact, Conclusions of Law, and Order.

FINDINGS OF FACT

Procedural History

1. This Petition is brought pursuant to Minn. Stat. section 302A.473 for a determination of the fair value of stock in McKinley Consulting, Inc. ("MCI"), which was merged into Petitioner Versique Acquisition, Inc. on August 19, 2014. As a result of a later merger, Versique Acquisition, Inc. was renamed Versique, Inc. Because the parties agree that Versique, Inc. is the real party in interest, and is liable for any judgment, the caption is amended accordingly by this order. To minimize confusion, the entity being valued will be referred to as "MCI," as it was known before the merger that triggered this suit. Unless otherwise stated, the facts below refer to MCI before August 19, 2014, the merger date and valuation date.

2. MCI was a closely-held Minnesota corporation owned in equal shares by Respondent Paul Beard, Anthony Sorensen, and Christopher Ohlendorf.

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3. MCI was incorporated in December 2003. From its incorporation until December 20, 2012, Beard, Sorensen, and Ohlendorf were also the directors of MCI. On December 20, 2012, Beard was not re-elected as a director of MCI.

4. On August 18, 2014, MCI's shareholders voted to approve a Plan of Merger between MCI and Petitioner. The Plan of Merger had been approved by the Board of Directors through a Special Committee Action dated July 28, 2014. MCI's Board of Directors determined the "Aggregate Consideration" for each MCI shareholder to be $832,666.66. Beard dissented from the merger.

5. On August 19, 2014, Articles of Merger were filed with the Minnesota Secretary of State. MCI merged into Petitioner with Petitioner as the surviving corporation.

6. On September 16, 2014, Beard made a written demand to Petitioner under Minn. Stat. section 302A.473, subdivision 4 for payment of the fair value of his MCI shares.

7. On September 17, 2014, Petitioner tendered $834,856.69 to Beard consisting of $832,666.66 for his MCI shares and $2,109.03 in interest.

8. On October 15, 2014, Beard notified Petitioner that he believed the amount he received for his shares was less than the fair value of $4,000,000, and demanded a supplemental payment of $3,165,143.40, plus interest.

9. The parties did not agree to an alternative price to be paid for Beard's shares.

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10. On December 12, 2014, Petitioner filed its Petition for Determination of Fair Value in Hennepin County District Court.

11. On January 2, 2015, Beard filed his Answer and Counterclaim seeking a determination of fair value of his shares in MCI and other equitable relief.

The Business of MCI

12. MCI is an IT staff augmentation business located in St. Louis Park, Minnesota. The staff augmentation business is a form of matchmaking. MCI searches for IT consultants and then matches them with companies seeking consultants for temporary placement in their IT departments. The IT staff augmentation industry is at the lower end of the IT consulting industry in terms of gross profit margin and overall profitability. In contrast, IT consulting firms that perform work on a project basis ("Statement of Work") tend to have higher gross margins and profitability because the project work they perform allows them to obtain higher profit margins. In the Twin Cities, the IT staff augmentation industry is quite competitive, with many different individuals and entities, small and large, competing to serve the needs of customers desiring temporary IT consultants to work at their businesses.

13. The consultants that MCI places are paid by MCI either on a W-2 or 1099 basis. That expense is essentially the "cost of services sold." The difference between this cost and the price paid by the customer is the gross margin.

14. The three shareholders in MCI were also involved in affiliated companies such as McKinley Group, Inc. That company searched for and placed various types of professionals in permanent positions with companies. It was more of a typical

"headhunter" operation and was often labelled the "perm" (short for permanent) business, as opposed to MCI's "temporary" work.

15. By 2012, McKinley Human Resources, Inc. and McKinley Finance, Inc. also existed within the constellation of McKinley companies.

16. By agreement dated October 31, 2012, the McKinley shareholders, having different business philosophies, separated their business interests and divided up the companies. As part of that agreement, Beard exited McKinley Group and other affiliated companies. He and two other McKinley shareholders took a portion of McKinley Group and McKinley Finance and began doing business as SkyWater Search Partners. Ohlendorf and Sorenson kept the remainder of McKinley Group and McKinley Human Resources and renamed them Versique Search and Consulting and Versique HR.

17. Beard, Sorenson, and Ohlendorf could not agree on how to split MCI so they remained as equal shareholders until Beard was ousted via merger.

18. Between the 2012 separation and the cash-out merger on August 19, 2014, friction existed between Beard, on the one hand, and Sorenson and Ohlendorf, on the other hand. Before being cashed out as a shareholder, Beard lost a bid for re-election to the Board when Sorenson and Ohlendorf did not vote for him in December 2012.

19. Part of the friction involved disagreement over the allocation of expenses. All of the McKinley companies, including MCI, were housed in one space, with several employees serving multiple companies. Overhead and employee expense was allocated among the companies, first on a "headcount" (number of employees) basis and, later, after a controller was hired, on headcount and an estimation of time spent (for

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employees) in each company. Beard was particularly troubled by allocation of some entertainment and allegedly personal expenses on the part of Sorenson and Ohlendorf. He also disagreed with the compensation Sorenson and Ohlendorf received from MCI. Neither was a full-time employee of MCI.

20. Another part of the friction was due to a concerted effort by Sorenson and Ohlendorf in 2013 and 2014 to implement a program of cross-referrals of customers among the McKinley companies. MCI employees, some of whom were aligned with Beard, concluded that this cross-referral effort benefited the other McKinley companies owned by Sorenson and Ohlendorf far more than it did MCI, where Beard had an ownership interest. In addition, Sorenson and Ohlendorf encouraged the use of certain "online, inbound marketing and recruiting tools," which some of the successful employees in MCI felt were of little utility and occasionally counterproductive.

21. This friction mushroomed into a lawsuit by Beard against Sorenson and Ohlendorf alleging corporate waste and mismanagement and other breaches of fiduciary duty. That "fiduciary-duty" lawsuit was assigned to this Court. Case No. 27-CV-14-10662. MCI appointed a Special Litigation Committee ("SLC") to evaluate the derivative claims made by Beard on behalf of MCI. The SLC consisted of retired Judge John Borg, supported by retired Judge Michael O'Rourke as his counsel and Schecter Dokken Kanter as consulting accountants. The SLC concluded that claims purporting to be on behalf of the company against Sorenson and Ohlendorf should not be pursued. Those derivative claims were dismissed.

22. Beard then amended his claims in the fiduciary-duty lawsuit by issuing a Supplemental Complaint. By that time, this dissenter's case had been filed and was assigned to this Court as well. Because the same parties (or at least principals) and counsel were involved in both cases, the parties agreed that discovery could be used in both cases. All but one minor claim in the fiduciary-duty lawsuit were dismissed on summary judgment by Order dated September 17, 2015, four days before this dissenter's trial began. The dismissals were based primarily on procedural grounds, as the Court concluded that most of the claims were derivative claims that Beard could not pursue.

23. After the valuation date, certain key employees of MCI left and MCI's business did not do as well as anyone expected. The parties argue about the significance and causes of these events. MCI claims that it learned in discovery that Beard was working behind the scenes with certain of these key employees, thereby causing dissension in the ranks before the valuation date, and that this information would cause any prospective buyer to reduce its valuation of the company. Beard contends that he was not causing problems and that he was merely consoling and consulting with employees who were unhappy with Sorenson and Ohlendorf's management. He also correctly observes that after the valuation date, MCI fired employees who were important to MCI's success.

Petitioner's Valuations of MCI

24. The two remaining shareholders of MCI, Sorenson and Ohlendorf, opined at trial as to valuation. Both said that they would use a formula of four to six times EBITDA (earnings before income taxes, depreciation, and amortization), less long-term

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debt. According to Ohlendorf, EBITDA for the 12 months prior to the merger was $644,000, with long-term debt of $732,000. At four times EBITDA, the formula results in a valuation of $1,884,000, but Ohlendorf said even that was too high, particularly based on information he learned after the merger. Sorenson used a similar formula and concluded that if he had known at the valuation date information he later acquired, he believed the company was worth only $400,000 to $500,000.

25. Petitioner presented two expert witnesses, John Heidebrecht and Arthur Cobb, to testify about the value of MCI. Heidebrecht concluded that the fair market value of MCI as of May 31, 2014 was $2,498,000. His appraisal was the basis for the payment to Beard by MCI of the estimated fair value. As a result, Heidebrecht's valuation date necessarily preceded the actual merger and valuation date in this case by about eleven weeks, but the difference in the valuation dates is not significant because no substantial changes occurred in MCI or its business outlook during this interim. Cobb concluded that the fair market value of MCI as of the merger was $4,100,000.

Respondent's Valuations

26. As noted earlier, Beard originally stated that the fair value of his one-third interest was $4,000,000, implying an enterprise value of $12,000,000. At trial, Beard testified that he believed an appropriate valuation formula was "one times revenue." He considered revenue to be $15,000,000, which meant an enterprise value of $15,000,000, which he discounted to $12,000,000.

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27. Beard called Robert Strachota to testify as his expert witness about the value of MCI. Strachota concluded that the fair market value of MCI as of August 18, 2014 was $10,300,000.

Reconciliation of Valuations

28. Of the three traditional methods of valuation, the only one that all three appraisers used was the income approach. All used a discounted cash flow as their measure of value for the income approach. Even Sorenson and Ohlendorf used a multiple of EBITDA, which is a form of income approach. When Beard used revenue in his valuation formula, he was using revenue as a proxy for income.

29. While other approaches were considered and in some cases employed by the appraisers here, the income approach is the most reliable for MCI. The lack of publicly available information on comparable companies, combined with the absence of prior sales of MCI stock, precludes a reliable market approach.

30. In 2012, MCI purchased Novon Consulting Corp. for $1,054,014 and a promissory note of $750,000, with the possibility of earnout payments depending on whether earnings targets were reached. Soon after the acquisition, MCI lost much of the Novon business, including some employees. Goodwill arising from this acquisition was the single largest asset reported on the balance sheet of MCI as of the valuation date. Because of the disappointing results of the Novon acquisition, this goodwill had little or no value. On the other hand, this also reduced the likelihood of earnout payments due in the future.

31. MCI's reported assets did not include all assets. Its single largest asset had little or no value. For this service business, the asset approach is not particularly helpful. In any event, it would serve at best to set a minimum value.

32. This judicial appraisal will therefore focus on the income approach, and specifically the discounted cash flow models generated by the appraisers. In a discounted cash flow, an appraiser develops projections, generally for the next five years plus a residual value, of the cash flow that a company is expected to generate. Simulating the hypothetical buyer, the appraiser determines the fair market value of the company by discounting to present value the projected cash flow. The discount rate is dependent largely on the opportunity cost of capital and the perceived risk of that particular investment. *See Rainforest Café v. State of Wisconsin Investment Bd.*, 677 N.W.2d 443, 448, n.6 (Minn. Ct. App. 2004).

33. Accordingly, the first step is to estimate the future cash flow. This involves projections of future revenue and expenses. The expenses are often broken down by accountants into "cost of goods or services sold," and "operating expenses" (overhead, including rent, utilities, and management). The formula is revenue minus cost of services equals gross income or profit. When operating expenses are also subtracted, the result is net income or profit. From there, consideration of working capital and noncash items such as depreciation and amortization yields cash flow.

34. A line-by-line comparison of the valuations shows where the valuation experts disagree. Of the three appraisers, Strachota is the most optimistic, projecting revenue growth of 12% declining to 5% over the next five years. Heidebrecht has a

similar pattern, while Cobb is the most conservative at 5% to 3%. The gross profit margins (revenue minus cost of services sold) are tightly grouped from 26–28% of revenue. This narrow band is to be expected because it effectively represents the W-2 or 1099 expense for MCI's IT consultants, an expense level that has been fairly consistent.

35. Differences in projected operating expenses account for much of the divergence among the appraisers. Cobb assumes operating expenses of 22% and Heidebrecht's varies, but averages slightly higher. Strachota, however, reduces operating expenses by almost one-third, to 15.5%. Because any reduction in operating expenses literally drops to the bottom line, that change alone doubles the net income. Cobb assumes about 5% (of revenue) net income, Heidebrecht about the same, but Strachota's reduced operating expenses is the primary factor in yielding net income of 10.5%.

36. The next step is to consider depreciation, capital expenditures, and working capital to arrive at actual cash flow. In MCI's case, these are not significant items, or significant areas of dispute among appraisers, except for working capital. Cobb and Heidebrecht both "frontload" substantial increases in working capital in the first years of their projections, while Strachota spreads that expense more evenly. Frontloading additional working capital reduces cash flow in the early years and significantly reduces the ultimate valuation.

37. The final step is to take the projected cash flow and discount it to present value. This process involves assessment of the risks inherent in investing in this company. Thus, in addition to evaluating current interest rates, the buyer considers the risks specific to MCI. The appraisers employed fairly similar discount rates: 20% for

Cobb, 22% for Heidebrecht, and 18% for Strachota. The higher the discount rate, the lower the valuation, all else equal.

38. In summary, Strachota's valuation ($10.3 million) is the highest primarily because of aggressive revenue forecasts, very aggressive reductions in operating costs, and a slightly lower discount rate. All of these adjustments overwhelm the fact that his gross income margin is the lowest of the three, but only by one percent. Heidebrecht's number ($2.498 million) is the lowest despite revenue forecasts that are higher than Cobb's. The primary reason for this is that although all three applied similar levels of operating expenses, Heidebrecht reduced the cash flow to account for taxes. He did this even though MCI is a Subchapter S corporation, which means there are no taxes at the corporate level, unlike a C corporation. Neither of the other appraisers made that adjustment. Cobb's valuation ($4.1 million) reflects the most conservative revenue forecasts, the median operating-expense level, his working-capital reductions to cash flow, and the median discount rate.

39. A reasonable revenue forecast would be approximately what was forecast by Heidebrecht, which was consistent with management's expectations at the time. Higher revenue forecasts must be tempered by the reality that the recent jumps in revenue were mainly due to two large customers and that future growth cannot be extrapolated based on that unusual spike.

40. On the expense side, the cost of services sold was not a subject of significant dispute. Much of the trial focused on the appropriate level of future operating expenses. The centerpieces of this dispute were the appropriate allocation of shared

expenses among the McKinley companies, and the value of the management services provided by Sorenson or Ohlendorf.

41. As of the valuation date, and for several years beforehand, the various McKinley companies shared office space and employees, and therefore rent, overhead, and management expenses. In the companion fiduciary-duty suit, Beard challenged the allocation of these expenses, contending that MCI was shouldering an inappropriate share. In this appraisal action, Beard presented the same analysis, quantifying possible savings primarily through expert witness Don Gorowsky, whose analysis was the predicate for Strachota's dramatic reduction in future operating expenses. Beard's contention was that a reasonable buyer would discover during due diligence that expenses could be pared, increasing cash flow and thereby the value of MCI.

42. Originally, MCI and its affiliated McKinley companies allocated expenses on the basis of "headcount"—that is, the number of employees in each company. While that method was easy to apply, it did not always reflect economic reality. Even Cobb, MCI's expert, agreed that the 2009–12 allocation and reporting of shared expenses and vehicle, travel, and entertainment expenses were not "rigorous." When McKinley companies hired a controller in 2012, he applied a more rigorous and reliable allocation method.

43. Sharing of expenses among affiliated companies is a mixed bag for valuation purposes. On the one hand, it fosters efficiency by allowing companies to share the benefits of economies of scale. Instead of several companies each hiring either a part-time or full-time controller, for example, the McKinley companies were able to share one

and allocate his expense among the various companies. On the other hand, the allocation process is in some ways a "zero-sum" game that distorts economic reality. For example, at one point while the headcount system was the sole determinant of allocation, the other McKinley companies lost employees due to a downturn in business. As an automatic result, MCI suddenly was obligated to pay a greater share of expenses because its stable headcount became a higher percentage of the whole. Beard contends that a prospective buyer would realize that MCI could reduce these expenses once freed from the tether of the other McKinley companies.

44. The other part of the cost savings urged by Beard involved management expense. Before 2013, none of the three shareholders had a significant role in the management of MCI. It was run on a day-to-day basis by people experienced in the "temporary" side of the consultant-placement business. Sorenson, Ohlendorf, and even Beard were successful businesspeople but all three lacked IT experience. Indeed, their experience was on the "permanent" side of the employment business, which did not readily transfer to MCI's "temporary" IT consultant business.

45. After Beard was not re-elected to the Board of MCI in December 2012, Sorenson and Ohlendorf decided to designate themselves as Chief Executive Officer and Chief Talent Officer, respectively, of MCI. A substantial share of their compensation was allocated to MCI. Beard and his expert Gorowsky contended that a prospective buyer would realize that Sorenson and Ohlendorf did not contribute significantly to MCI. As a result, they argued, the prospective buyer would eliminate that management expense and thereby increase net income, making MCI more valuable.

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46. A prospective buyer would be able to reduce operating expenses somewhat, in part by reducing overhead and related expenses and in part by reducing management expense. Freeing the company from the McKinley orbit would allow MCI to reduce overhead and related operating expenses in an amount less than projected by Beard and his expert. While Sorenson and Ohlendorf provided some value to MCI, it was not commensurate with the compensation and benefits they received.

47. The appraisers' discount rates were similar, varying only in the amount of risk assigned specifically to an investment in MCI. MCI emphasized the risks posed by its highly competitive industry and its concentration of business within two major customers, both of which were associated with one salesperson. Beard, on the other hand, focused on recent revenue growth and a downturn in operating expenses. All of the appraisers were aware of all these factors and considered them in setting their discount rates.

48. On balance, the discount rate for MCI belongs in the mid to higher end of the appraisers' range because of MCI's unusually heavy dependence on one employee and her two customers. One salesperson, Susan Miller, accounted for about two-thirds of company revenue, mostly from two large clients.

Post-Valuation-Date Evidence

49. MCI argues that information it learned after the valuation date bears on the valuation because (a) it relates to pre-valuation-date events that would be material to a prospective buyer, or (b) it bears on the reasonableness of pre-valuation-date projections. Specifically, MCI claimed as to the former that it learned through discovery in the two

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lawsuits that Beard was telling MCI employees that he hoped to gain control of the company as the result of the SLC deliberations on his claims and that if that happened, he would make substantial changes.

50. MCI claims that Beard told Judge Borg, the SLC, before the valuation date that he expected some MCI employees would leave if he did not gain control. Although Beard did not register it, Judge Borg told him he was not getting control of the company through the SLC process. MCI relies heavily on this "newly discovered" evidence, which includes texts from Beard to MCI employees, to argue that all appraisals overstate the value of MCI because Beard was sowing seeds of discontent.

51. Key employees of MCI did leave after the valuation date. MCI fired one and two others left voluntarily. When the one employee was fired, Sorenson and Ohlendorf assumed that another key employee would soon leave as a result. Dissension within MCI was apparent as of the valuation date primarily because of changes to the employee compensation system mandated by Sorenson and Ohlendorf, which were resisted by other MCI executives and managers as counterproductive.

52. As of the valuation date, Beard was aware that some MCI employees were unhappy with management. But as of August 2014, Sorenson also believed that key employees would not remain at MCI for long. Indeed, the potential departure of Susan Miller, the key salesperson, was factored into Cobb's analysis, as was "dissonance" in the company.

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53. In summary, the additional pre-valuation-date intelligence obtained by MCI after the valuation date does not materially change the picture of MCI available to a prospective buyer and does not undermine the valuations offered by the appraisers.

54. To the extent the post-valuation-date evidence is offered to show that gloomy forecasts were reasonable as of the valuation date, it is disregarded. Most of the post-valuation-date events were self-inflicted, natural fallout from the merger itself, or the result of squabbling among management after the merger, all of which a prospective buyer likely could avoid.

55. MCI also contends that Beard deleted texts from his cellphone relating to communications with MCI employees and that this constitutes spoliation of evidence that should trigger an adverse inference against him. Beard did not text much and was not in the habit of retaining texts on his phone except for communications with members of his family. His texts to and from MCI employees are not a significant factor in the Court's valuation. No adverse inference is drawn.

Phantom Stock

56. MCI gave one of its executives phantom stock that included a provision that upon any sale of the company, that executive would receive 2.5% of the proceeds. MCI argues that this contractual payment should reduce the amount Beard receives for his stock. Cobb concluded that this was a cost of liquidating the business, similar to other sale (of the company) expenses such as legal, accounting, and broker fees. Heidebrecht considered this in his valuation and reduced Beard's net proceeds accordingly. Strachota did not.

57. The Court credits Cobb's testimony on this issue and finds that payment for this phantom stock is a cost of liquidating the investment, not an element of fair market value or enterprise value.

Tax-Affecting

58. According to MCI, much of the difference between its two appraisers is explained by Heidebrecht's decision to tax-affect his valuation and Cobb's refusal to do so. Heidebrecht considered that a C corporation purchasing MCI would pay less because under the C corporation's umbrella, MCI's income would be taxed at the corporate level, not at the shareholder level. Neither Cobb nor Strachota tax-affected the income of MCI.

59. MCI would be more likely to be bought by an S corporation or other entity that is not taxed at the entity level. A sale to that type of purchaser is more likely to maximize value for MCI's shareholders. It is reasonable not to tax-affect the enterprise value.

Fair Market Value

60. The calculations in Exhibit 257 illustrate the effect of varying the appraisers' assumptions regarding revenue growth and net profit margin.

61. MCI's enterprise value, or fair market value, as of the valuation date was $5,700,000.

CONCLUSIONS OF LAW

1. This is a petition to determine value pursuant to Minn. Stat. section 302A.473, subdivision 7.

2. The August 19, 2014 merger triggered a right for Beard to receive in cash the fair value of his shares in MCI pursuant to Minn. Stat. sections 302A.471–473.

3. Petitioner followed the statutory procedures set forth in Minn. Stat. sections 302A.471–473.

4. Beard fully complied with the provisions of Minn. Stat. section 302A.473 and is entitled to receive the fair value of his shares in MCI as of August 19, 2014, immediately before the effective date of the merger that cashed him out. Minn. Stat. § 302A.473, subd. 1(c).

5. Determination of the fair value of Beard's shares starts with determination of the fair market value of MCI as a going concern. *Advanced Communication Design, Inc. v. Follett*, 615 N.W.2d 285, 290 (Minn. 2000). To determine the fair market value, the Court must determine the price, in cash equivalents, that a willing buyer and willing seller would agree to as of the valuation date.

6. Under Minn. Stat. section 302A.473, subdivision 7, "[t]he court . . . shall determine the fair value of the shares, taking into account any and all factors the court finds relevant, computed by any method or combination of methods that the court, in its discretion, sees fit to use, whether or not used by the corporation or by a dissenter." The trial court has "broad discretion both in the process and ultimate determination of the 'fair value' of the shares to be sold." *Advanced Communication*, 615 N.W.2d at 290. The parties agree, and the Court concludes, that it is improper to apply discounts for a minority interest or lack of marketability. *See id.* No "extraordinary circumstances" exist to warrant an exception to the rule prohibiting marketability discounts in fair value

determinations. *Id.* It is also improper to consider post-valuation date evidence except in limited instances not present here. *See American Sharecom, Inc. v. LDB Int'l Corp.*, 1995 WL 321540 at *3 (Minn. Ct. App. May 30, 1995), *review denied* (July 27, 1995).

7. A court may reasonably rely primarily on a single valuation method, particularly where it is one used by all appraisers. *See, e.g., id.* (approving reliance primarily on discounted-cash-flow method). The factors set forth in Rev. Rul. 59–60, which the Court considered, are a helpful guide to the valuation of closely held companies. *Nardini v. Nardini*, 414 N.W.2d 184, 189–90 (Minn. 1987).

8. The Court has considered the issue of tax-affecting its valuation in light of MCI's S corporation status. Only one of the three appraisers recommended tax-affecting in the sense of reducing the overall valuation because an S corporation is taxed differently from a C corporation. Having reviewed *Gross v. Commissioner*, 78 T.C.M. (CCH) 201 (T.C. 1999), *aff'd*, 272 F.3d 333 (6th Cir. 2001); *Doerr v. Arundel*, No. EM 97-013502 (Minn. Dist. Ct. Oct. 1, 1999); *Bernier v. Bernier*, 873 N.E.2d 216 (Mass. 2007); *Delaware Open MRI Radiology Associates, P.A. v. Kessler*, 898 A.2d 290 (Del. Ch. 2006); and *Hamelink v. Hamelink*, 2013 WL 6839700 (Minn. Ct. App. Dec. 30, 2013) *review denied* (Feb. 26, 2014), the Court concludes that the value of MCI should not be tax-affected. Consistent with Judge Solum's analysis in *Doerr*, a prospective purchaser is more likely to be another S corporation, because MCI can maximize its return for its shareholders in that manner.

9. The decision not to tax affect a closely held company under the circumstances of this case is independently justified by the legislative policy to protect

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minority shareholders that underlies the dissenter's right statute. *Rainforest Café v. State of Wisconsin Investment Bd.*, 677 N.W.2d 443, 454 (Minn. Ct. App. 2004); *MT Props, Inc. v. CMC Real Estate Corp.*, 481 N.W.2d 383, 388 (Minn. Ct. App. 1992) (recognizing legislative aim of statute is to protect minority dissenting shareholder). The Court does not make this decision on the basis of judicial comments that corporate squeeze-outs are not to be encouraged, *see Advanced Communication*, 615 N.W.2d at 292, and that policy arguments for dissenters are "enlarged" in a squeeze-out. *MT Props.*, 481 N.W.2d at 388 n.5.

10. Under the Minnesota Business Corporations Act, "fair value . . . means the pro rata share of the value of the corporation as a going concern." *Advanced Communication*, 615 N.W.2d at 290. For this legal reason, in addition to the factual bases reflected in the Court's findings, the fair value that is owed Beard must not be reduced by the cost of phantom stock. *See American Sharecom*, 1995 WL 321540 at *2 (trial court properly disregarded unexercised options of speculative value).

11. The fair value of Beard's one-third interest in MCI as of August 19, 2014 is one-third of the enterprise value of $5,700,000, or $1,900,000.

12. Petitioner must pay the difference between $834,856.69, what it paid to Beard after the merger, and $1,900,000, plus interest at the rate of 4% per annum from August 24, 2014 until the judgment date. Minn. Stat. §§ 302A.473, subds. 7 & 1(d) and 549.09, subd. 1(c)(1).

13. Petitioner failed to comply substantially with Minn. Stat. section 302A.473 in that it paid Beard less than half of the fair value of his shares in MCI. *Spinnaker*

Software v. Nicholson, 495 N.W.2d 441, 446 (Minn. Ct. App. 1993) *review denied* (March 30, 1993); *American Sharecom*, 1995 WL 321540 at *3. Even by Cobb's valuation—*i.e.*, the valuation of Petitioner's own expert—Beard was underpaid by more than $500,000.

14. Because Petitioner failed to comply substantially with section 302A.473, the Court exercises its discretion to order that Petitioner must pay the reasonable fees and expenses of Beard's counsel and experts incurred in this proceeding. Minn. Stat. § 302A.473, subd. 8(b).

15. Beard is entitled to recover his costs and expenses incurred in this proceeding pursuant to Minn. Stat. section 302A.473, subdivision 8(a).

16. Since this action began, Petitioner Versique Acquisition, Inc. has been the subject of a second merger and has been renamed Versique, Inc. As the successor in interest, Versique, Inc. is liable for the judgment entered in Beard's favor and the caption will be amended accordingly.

17. To the extent any of the Court's findings contain conclusions of law, or any conclusions of law contain findings, those labels should be ignored.

ORDER

1. The caption in this case is amended to reflect the correct name of Petitioner, which is Versique, Inc.

2. Beard is awarded $ 1,900,000 for his shares of MCI as of August 19, 2014. He is entitled to receive interest on that amount at the rate of 4% since August 24, 2014.

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The amount Petitioner owes Beard is offset by its earlier payment of $834,856.69, which consists of $832,666.66 for his shares and $2,109.03 in interest.

3. Beard is also entitled to recover his costs, expenses, and fees incurred herein.

4. Beard must file and serve documentation of his costs, expenses and fees by December 22, 2015. Petitioner may file and serve any response by January 5, 2016. The Court will then determine the appropriate amount to be awarded and issue a final judgment.

BY THE COURT:

December 15, 2015

Thomas S. Fraser
District Court Judge