No. 23-146

In the Supreme Court of the United States

THOMAS A. CONNELLY, PETITIONER

v.

UNITED STATES OF AMERICA

ON WRIT OF CERTIORARI
TO THE UNITED STATES COURT OF APPEALS
FOR THE EIGHTH CIRCUIT

JOINT APPENDIX

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PETITION FOR A WRIT OF CERTIORARI FILED: AUGUST 15, 2023
CERTIORARI GRANTED: DECEMBER 13, 2023

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AMENDED AND RESTATED
STOCK PURCHASE AGREEMENT

THIS AGREEMENT made as of this 29 day of August, 2001, by and among CROWN C SUPPLY COMPANY, INC., a corporation organized under the laws of Missouri (hereinafter referred to as the "Company"); MICHAEL P. CONNELLY, TRUSTEE U/I/T DATED 8/15/90, MICHAEL P. CONNELLY, GRANTOR; AND THOMAS A. CONNELLY (hereinafter the above individuals are collectively referred to as "Stockholders" and individually as a "Stockholder").

WHEREAS, the Company now has issued and outstanding Five Hundred (500) shares of common stock (the "Shares"), which are owned as follows:

STOCKHOLDER:	SHARES
Michael P. Connelly, Trustee U/I/T dated 8/15/90, Michael P. Connelly, Grantor	385.90
Thomas A. Connelly	114.10

WHEREAS, the Shares are subject to that certain Stock Purchase Agreement ("Stock Agreement") effective as of January 1, 1983, by and among the Company, Mark Connelly, Michael P. Connelly and Thomas A. Connelly; and

WHEREAS, Mark Connelly's interest in the Company was terminated prior to the date hereof; and

WHEREAS, the Stockholders and the Company deem it to be in their respective best personal and business interests if the Shares remain closely held and not generally distributed on the open market; and

WHEREAS, the Stockholders desire to promote their mutual interests and the interests of the Company by amending and restating the Stock Agreement to impose certain restrictions and obligations on themselves, the Company and the Shares.

NOW, THEREFORE, in consideration of the mutual covenants herein contained and other good and valuable consideration, the receipt and sufficiency of which are hereby acknowledged, the parties hereto agree as follows:

ARTICLE I
SCOPE

A. Except as hereinafter provided, none of the Shares owned or hereafter acquired by any of the Stockholders shall be subject to any voluntary or involuntary transfer, by operation of law or otherwise, including, but not by way of limitation, encumbrance, sale, assignment, gift, pledge, disposal, hypothecation, bankruptcy, legal process, assignment for the benefit of creditors or any other transfer, in any manner whatsoever to any person, trustee, receiver, corporation, partnership, joint venture, association, charity or any other entity or person whatsoever.

B. Notwithstanding any other provision of this Agreement to the contrary, a Stockholder ("Transferor-Stockholder") shall be free to transfer his Shares to a trust ("Trust-Stockholder"), provided all of the following conditions are met:

(i) The Transferor-Stockholder shall notify the Company of the transfer of the relevant terms and conditions of such trust in advance of such transfer.

(ii) The Transferor-Stockholder is the then sole trustee of the trust.

(iii) The Transferor-Stockholder, in his capacity as trustee, signs an instrument, satisfactory to the Company, providing that the Trust-Stockholder is bound by all terms and provisions of this Agreement.

In the case of any such transfer of Shares to a trust, any event which would give rise to an option(s) to purchase or purchase of Shares owned by the Trust-Stockholder if the Transferor-Stockholder still held the Shares outright, i.e., the death of such Transferor-Stockholder, shall give rise to the same option(s) to purchase or purchase of the Trust-Stockholder's Shares under the same terms and conditions. Similarly, any rights or obligations a grantor may have under this Agreement shall be transferred to and become rights or obligations of the Trust-Stockholder. In addition, in the case of any such transfer of Shares to a trust, if the Transferor-Stockholder ceases to be the sole trustee of the trust, for whatever reason, such event shall be treated as if the Trust-Stockholder were an Offering Stockholder that provided Notice to the Company under Article II, and the Purchase Price shall be the price provided in Article VII.

C. In the event any Shares are attempted to be sold, pledged or transferred contrary to, or in violation of, the provisions of this Agreement, the purported purchaser or transferee thereof shall not be entitled to have such Shares transferred on the books of the Company, or be vested with any voting rights or other rights of the Stock-

holder. Such Shares shall remain subject to all the provisions in this Agreement, and such purported sale, transfer or pledge shall be null and void and of no force or effect.

D. Any additional Shares of capital stock of the Company acquired by any Stockholder subsequent to the date hereof shall be subject to this Agreement.

E. The Shares shall remain subject to this Agreement notwithstanding any transfer, and no transfer of Shares otherwise permitted hereunder shall be effective until and unless the purported transferee first becomes a party to this Agreement pursuant to a written instrument signed by the purported transferee, in form and substance satisfactory to counsel for the Company. Without limiting any of the foregoing provisions of this Article I, a transferee; by accepting any transferred Shares, shall be deemed to have become a party to this Agreement with respect to those transferred Shares, to the same extent as if the transferee had executed this Agreement as a Stockholder.

F. When the Company has an option to redeem the Shares of a Stockholder under this Agreement, the Company shall act thereon by a special meeting of the Stockholders, at which time the Shares owned by all the Stockholders, including the Stockholder whose Shares are subject to the option, shall have voting rights.

ARTICLE II
RIGHT OF FIRST REFUSAL

A. In the event any Stockholder (hereinafter referred to as "Offering Stockholder") desires to sell all and not less than all of his Shares ("Offered Shares") to a third-party from whom he receives a bona fide written offer to purchase all of such Offered Shares for cash and/or a promise to make deferred payments of cash (the "Offer"),

such Offering Stockholder shall promptly give written notice (the "Notice") to all Stockholders whose shares are not subject to said offer (the "Non-Offering Stockholders"). The Notice shall state the identity of the third-party offeror, the purchase price (the "Offer Price") and the other terms and conditions of the Offer. Each Non-Offering Stockholder shall then have an option ("Stockholder Option") to purchase from the Offering Stockholder his proportionate share ("Proportionate Share") of the Offered Shares. For purposes of this Agreement, the term Proportionate Share shall mean a percentage obtained by dividing the number of Shares owned by each Non-Offering Stockholder by the total number of Shares owned by all Non-Offering Stockholders. In the event a Non-Offering Stockholder elects to exercise his Stockholder Option, said Non-Offering Stockholder must provide written notice to the Offering Stockholder, the Company and all other Non-Offering Stockholders within thirty (30) days after his receipt of the Notice from the Offering Stockholder. If any one or more Non-Offering Stockholders fail to exercise their option to purchase their Proportionate Share, all of those Non-Offering Stockholders that have exercised their option to purchase their Proportionate Share shall have an option to purchase their Proportionate Share of the Shares allocated to the non-purchasing, Non-Offering Stockholders. This option may be exercised within ten (10) days following the lapse of the options of the non-purchasing, Non-Offering Stockholders in the same manner as the exercise of the Stockholder Options. This Process shall continue indefinitely until all of the Offered Shares have been purchased or offered for purchase and declined by each of the Non-Offering Stockholders. The purchase price to be paid by each Non-Offering Stockholder shall be his Proportionate Share of the purchase price provided in Article VII, the purchase price

shall be paid as per the terms provided in Article VIII, and the purchase of the Shares shall be closed on the Closing Date as provided in Article IX.

B. In the event that all of the Offered Shares are not purchased by the Non-Offering Stockholders in accordance with Paragraph A of this Article II, then the Offering Stockholder shall promptly give Notice to the Company. The Company shall then have an option to purchase from the Offering Stockholder the Offered Shares that were not previously purchased ("Company Option"). In the event the Company elects to exercise its Company Option, the Company must provide written notice to the Offering Stockholder within thirty (30) days after the Company's receipt of the Notice from the Offering Stockholder. The purchase price to be paid by the Company shall be the purchase price provided in Article VII, the purchase price shall be paid as per the terms provided in Article VIII, and the purchase of the Shares shall be closed on the Closing Date as provided in Article IX.

C. Notwithstanding the foregoing provisions in Paragraphs A and B of this Article II if the Non-Offering Stockholders and Company fail to exercise their options above to purchase all of the Offered Shares, then the Offering Stockholder shall have thirty (30) days from the date the Company Option expires to consummate the sale of all of the Offered Shares to the third party offeror pursuant to the terms of the Offer, and none of the sales referred to in Paragraphs A and B of this Article II shall take place. If the Offering Stockholder does not complete the sale to the third-party offeror within said thirty (30) day period, then all of the Offered Shares shall once again become subject to the terms of this Agreement and the right of first refusal set forth in the Agreement. If the sale to the third-party offeror is completed within said thirty

(30) day period, then such purchaser shall take all of the Offered Shares subject to all terms of this Agreement.

ARTICLE III
INVOLUNARY TRANSFERS

A. If, other than by reason of a Stockholder's death or disability, any Shares of a Stockholder ("Purported Transferor") are either transferred by operation of law or would be transferred by operation of law if such transfer ("Purported Transfer") was not rendered ineffective by virtue of this Agreement, to any person other than the Company or the other Stockholders (such as but not limited to a Stockholder's trustee in bankruptcy, a purchaser at any creditor or court sale, a spouse in any divorce or dissolution action or domestic relations property settlement, or to any conservator) (the "Purported Transferee"), the other Stockholders whose Shares are not subject to the Purported Transfer ("Remaining Stockholders") shall have the same series of Stockholder Options, as provided in Paragraph A of Article II to purchase the Shares subject to the Purported Transfer as if the Purported Transferor was an Offering Stockholder. Notice shall be deemed to have been given on the day the Purported Transfer is recorded on the books of the Company. In the event a Remaining Stockholder elects to exercise his or her Stockholder Option hereunder, said Remaining Stockholder must provide written notice to the Purported Transferor, and if known, the Purported Transferee within thirty (30) days following receipt of Notice of the Purported Transfer. The purchase of Shares and the payment of purchase Price by a Remaining Stockholder as provided for by this article shall be deemed to have occurred on the last day before such Purported Transfer. If one or more Remaining Stockholders fail to exercise their option, the Remaining Stockholders that do shall have the

same series of options to purchase the non-purchased Shares as in Paragraph A of Article II. The purchase price to be paid by each Non-Offering Stockholder shall be his Proportionate Share of the purchase price provided in Article VII, the purchase price shall be paid as per the terms provided in Article VIII, and the purchase of the Shares shall be closed on the Closing Date as provided in Article IX.

B. In the event that all of the Shares subject to the Purported Transfer are not purchased by the Remaining Stockholders as provided in Paragraph A of this Article III, then the Company shall then have the same Company Option as provided in Paragraph B of Article II to purchase all of the remaining Shares subject to the Purported Transfer not purchased by the Remaining Stockholders, as if the Purported Transferor was an Offering Stockholder. In the event the Company elects to exercise its Company Option, the Company must provide written notice to the Purported Transferor, and if known, the Purported Transferee within sixty (60) days following receipt of Notice of the Purported Transfer. The purchase of Shares and payment of purchase price by the Company as provided for by this Article shall be deemed to have occurred on the last day before such Purported Transfer. The purchase price to be paid by the Company shall be the purchase price provided in Article VII, the purchase price shall be paid as per the terms provided in Article VIII, and the purchase of the Shares shall be closed on the Closing Date as provided in Article IX.

C. The terms of this Agreement shall be binding on both the Purported Transferor and the Purported Transferee. It is the intent of the parties that Purported Transfers are rendered ineffective by virtue of this Agreement and that any sale under this Article III shall take place

between the Purported Transferor, the Remaining Stockholders and/or the Company. If however, in the opinion of counsel for the Company or pursuant to the final judgement of a court of competent jurisdiction, any such Purported Transfer is valid, the sale under this Article III shall take place between the Remaining Stockholders and/or the Company and the Purported Transferee.

ARTICLE IV
DISABILITY

A. In the event any employee-Stockholder becomes Disabled (as hereinafter defined) (hereinafter "Disabled Stockholder"), the Remaining Stockholders (for purposes of this Article IV, Remaining Stockholders shall mean the Stockholders who are not Disabled) shall have the same Stockholder Option as provided in Paragraph A of Article II to purchase, followed by the Company having the same Company Option as provided in Paragraph B of Article II to purchase, from the conservator, attorney-in-fact, or other legal representative of the Disabled Stockholder (hereinafter referred to collectively as the "Disability Representative"), all of the Disabled Stockholder's Shares as if the Disabled Stockholder was an Offering Stockholder thereunder. Notice shall be deemed to have been given on the day such Disabled Stockholder is deemed Disabled. The purchase price to be paid by each Remaining Stockholder shall be his Proportionate Share of the purchase price provided in Article VII, the purchase price shall be paid as per the terms provided in Article VII, and the purchase of the Shares shall be closed on the Closing Date as provided in Article IX.

B. If the Company or the Remaining Stockholders own a disability related policy the purpose of which is to fund a purchase of shares upon a Stockholder's disability

(the "Policy"), such Stockholder shall be deemed "Disabled" in accordance with the definition of disabled under the Policy. If such a Policy is not owned by the Company or the Remaining Stockholders, then a Stockholder shall become Disabled when the Stockholder (i) experiences a physical or mental incapacity or inability to perform his or her regular duties for a period of two (2) consecutive years; (ii) is adjudicated to be incompetent by a court of competent jurisdiction; or (iii) (a) an individual other than the Stockholder is voting the Shares of the Stockholder either pursuant to a trust or power of attorney and (b) disability is determined to be permanent disability by a physician of the Stockholder. If the Stockholder or his or her Disability Representative and the Company cannot agree on whether a Stockholder has become Disabled, as defined in clause (i) of the preceding sentence, then such a determination shall be made by a disinterested physician to be appointed by the Dean of the Medical School at Washington University in St. Louis, Missouri. The costs of such determination shall be borne by the Company and shall be made at either party's request.

ARTICLE V
DEATH

A. In the event of the death of a Stockholder ("Deceased Stockholder") the Remaining Stockholders (for purposes of this Article V, Remaining Stockholders shall mean the Stockholders who are not deceased) shall have the same series of Stockholder options as provided in Paragraph A or Article II to purchase the Shares as if the Deceased Stockholder was an Offering Stockholder; provided, however, that the Remaining Stockholders shall and must purchase from the Deceased Stockholder's personal representative, executor, administrator or successor trustee of any trust, as the case may be (collectively,

the "Legal Representative"), and the Legal Representative shall and must sell to the Remaining Stockholders, their Proportionate Share of the Deceased Stockholder's Shares up to the amount of any insurance proceeds that are received by the Remaining Stockholders as a result of the Deceased Stockholder's death. Said option period shall commence on the date of the Deceased Stockholder' death. In the event a Remaining Stockholder elects to exercise his or her Stockholder Option, or is required to purchase the Shares as per the terms of this Article, said Stockholder must provide written notice to the Legal Representative within thirty (30) days of the Deceased Stockholder's Death. If one or more Remaining Stockholders fail to exercise their option, the Remaining Stockholders that do shall have the same series of options to purchase the non-purchased Shares as in Paragraph A of Article II. The purchase price to be paid by each Remaining Stockholder shall be his Proportionate Share of the purchase price provided in Article VII, the purchase price shall be paid as per the terms provided in Article VIII, and the purchase of the Shares shall be closed on the Closing Date as provided in Article IX.

B. In the event that all of the Deceased Stockholder's Shares are not purchased by the other Stockholders, then the Company shall and must purchase from the Legal Representative and the Legal Representative must sell to the Company all of the Deceased Stockholder's Shares that are not purchased by the Remaining Stockholders. The purchase price to be paid by the Company shall be the purchase price provided in Article VII, the purchase price shall be paid as per the terms provided in Article VIII, and the purchase of the Shares shall be closed on the Closing Date as provided in Article IX.

ARTICLE VI

[INTENTIONALLY OMITTED]

ARTICLE VII
PURCHASE PRICE FOR SHARES

A. In the event Shares are purchased pursuant to the terms of this Agreement, the purchase price per Share (the "Purchase Price Per Share") shall be the amount per Share set forth in the Certificate of Agreed Value, as that term is defined in Paragraph B of this Article VII; provided, however, that in the event the Stockholder fail or refuse to execute a new Certificate of Agreed Value within eighteen (18) months following the date of the last executed Certificate of Agreed Value (i.e., the last executed Certificate of Agreed Value is more than eighteen (18) months old). The Purchase Price Per Share shall be the "Appraised Value Per Share," as that term is defined in Paragraph C of this Article VII. The purchase price ("Purchase Price") of a Selling Stockholder's Shares shall equal the Purchase Price Per Share (or the Appraised Value Per Share, as the case may be) times the number of Shares being sold and purchased.

B. For purposes of this Agreement, "Certificate of Agreed Value" means a certificate (in the form attached to this Agreement as Exhibit A) signed by all of the Stockholders and filed with the records of the Company, which establishes the agreed per Share value of the Shares or a method of ascertaining the same. Within thirty (30) days after the end of each tax year of the Company, all the Stockholders shall, by mutual agreement, determine the agreed value per Share by executing a new Certificate of Agreed Value in the form of Exhibit A. A Certificate of

Agreed Value shall be effective only when executed by all of the Stockholders.

C. For the purposes hereof, the "Appraised Value Per Share" of the Company shall be determined as follows: If the Certificate of Agreed Value is more than eighteen (18) months old, within ten (10) days after the date an option is exercised or a mandatory purchase is required ("Appraisal Date"), the transferring Stockholder or his successor in interest shall appoint an appraiser and the Company or purchasing Stockholder(s), as the case may be, shall appoint an appraiser. Both appraisers shall have at least five (5) years of experience in appraising business similar to the Company. If either party fails to name such an appraiser within the specified time, the other party may upon five (5) years of experience in appraising businesses similar to the Company. If either party fails to name such an appraiser within the specified time, the other party may upon five (5) days written notice to the failing party, select the second appraiser. Each appraiser shall independently determine and submit to the parties, in writing, with reasons therefor, an appraisal of the fair market value of the Company. The appraisers shall take into consideration the goodwill of the Company in determining the fair market value of the Company. The appraisers shall not take into consideration premiums or minority discounts in determining their respective appraisal values. Upon receipt by the parties of both appraisals, if the fair market value of the Company is determined to be the same or if the difference between the appraisals is less than ten percent (10%) of the lower of the appraised values, then the fair market value of the Company shall be the average of the two appraisals. If the appraisals so submitted differ by more than ten percent (10%) of the lower of the appraised values, the accountants then servicing the Company shall appoint a third appraiser. The third

appraiser so appointed shall, as promptly as possible, determine the value of the Company on the same basis as above set forth, and that prior appraisal which is loser in value to such third appraisal shall, thereupon, be the appraisal which is binding on all parties in interest hereunder. The "Appraised Value Per Share" shall equal the amount determined by diving the binder appraisal by the total number of Shares of the Company issues and outstanding as of the Appraisal Date. Each party shall pay the fee and expenses of the appraiser selected by such party and the fee of the third appraiser shall be borne equally by the parties appointing the two appraisers.

ARTICLE VIII
PAYMENT OF PURCHASE PRICE

A. The payment of the Purchase Price for Shares sold pursuant to this Agreement shall be made on the Closing Date as follows: one-third (1/3) of the Purchase Price shall be paid in cash on the Closing Date, and the balance of the Purchase Price shall be evidenced by the execution and delivery of a negotiable promissory note to the Stockholder or his Legal Representative or Disability Representative, as the case maybe, who is selling Shares (collectively "Selling Stockholder") in the form and having the substantive provisions of the "Promissory Note," attached hereto as Exhibit B and incorporated by this reference herein. The Promissory Note shall be payable in thirty-six (36) equal monthly installments of principal and interest, the first of which shall be payable one (1) month after the Closing Date, with interest thereon at the prime rate of interest publicly announced by Firstar Bank as of the date of the Promissory Note. The Promissory Note shall further provide that the maker shall have the right to prepay the whole or any part thereof prior to the ma-

turity date without any charge, penalty or additional interest, such prepayment to be applied first to interest and then to principal in the inverse order of maturity.

B. In the event of a sale and purchase under Article V (Death), and the proceeds collected from any life insurance owned by the surviving Stockholders or the Company on which the Decedent Stockholder was the insured are sufficient to pay the Purchase Price in full, the full amount of said Purchase Price shall be paid on the Closing Date to the Legal Representative of the Decedent Stockholder, and any remaining proceeds may be retained by the beneficiary thereof. If the Purchase Price exceeds the proceeds of any life insurance collected, the insurance proceeds shall be paid on the Closing Date directly to the Legal Representative of the Decedent Stockholder and the balance of the Purchase Price shall be evidenced by a promissory note identical (except for principal amount) to the Promissory Note described in Paragraph A or this Article VIII, which shall be delivered to and in favor of the estate of the Decedent Stockholder, with the maker being the Remaining Stockholder(s).

ARTICLE IX
CLOSING DATE

A. The closing date ("Closing Date") of any and all sales and purchases of Shares by the Remaining Stockholders under this Agreement shall be as follows and shall have an effective date ("Effective Date") for all purposes, including federal tax purposes, as follows:

(i) The Closing Date and the Effective Date under Article II (Right of First Refusal) shall be the last day of the month following the later of (a) the month in which the Remaining Stockholders elects to exercise their Stockholder Option or, (b) if the Remaining Stockholders

elect to purchase only some of the Shares and the Company elects to purchase the remaining Shares, the month in which the Company elects to exercise its Company Option, as provided in Paragraph B of Article II.

(ii) The Closing Date under Article III (Involuntary Transfers) shall be the last day of the month following the month in which the Remaining Stockholders elects to exercise their Stockholder Options as provided in Paragraph A of Article II.

(iii) The Closing Date under Article IV (Disability) shall be sixty (60) days after the appointment of a Disability representative, but in no event shall the Closing Date be more than one hundred twenty (120) days from the date a Stockholder is deemed Disabled. Notwithstanding the foregoing, the Effective Date of the purchase and sale of a Disabled Stockholder's Shares shall be the date the Stockholder is deemed Disabled.

(iv) The Closing Date under Article V (Death) shall be sixty (60) days after the Decedent Stockholder's death. Notwithstanding the foregoing, the Effective Date of the purchase of a Decedent Stockholder's Shares shall be the date of death.

(v) [INTENTIONALLY OMITTED]

B. The Closing Date and Effective Date of any and all sales and purchases of Shares by the Company shall be as follows:

(i) The Closing Date and Effective Date under Article II (Right of First Refusal) shall be the last day of the month following the month in which the Company elects to exercise its Company Option as provided in Paragraph B of Article II.

(ii) The Closing Date under Article III (Involuntary Transfers) shall be the last day of the month following the month in which the Company elects to exercise its Company Option as provided in Paragraph B of Article III.

(iii) The Closing Date and the Effective Date under Article IV (Disability), Article V (Death) and Article VI (Termination of Employment) shall be the same as provided in Paragraphs A (iii), and A (iv) of this Article.

C. In the event the Purchase Price has not been determined by the Closing Date, the Closing Date shall be three (3) days after the Purchase Price is determined. On the Closing Date, certificates for all Shares being sold shall be transferred to the purchaser duly endorsed in blank for transfer by the Selling Stockholder, or accompanied by an appropriate irrevocable stock power, duly endorsed for transfer by the Selling Stockholder. The Selling Stockholder shall execute an agreement at Closing wherein the Selling Stockholder represents and warrants that it owns the Shares free and clear of all liens and encumbrances whatsoever, and agrees to indemnify the purchaser for any breach or inaccuracy of said representations and warranties. Unless otherwise agreed by the parties, all closings shall take place at the offices of the Company at 10:00 A.M. Central Time.

ARTICLE X
INSURANCE

A. Each Stockholder and/or the Company shall have the right to purchase in his or its sole discretion, life insurance policies of whatever kind insuring the life of any Stockholder to this Agreement, along with the right to substitute or withdraw any life insurance policy subject to this Agreement.

B. In the event that a Stockholder or the Company decides to purchase life insurance on any Stockholder, each Stockholder herby agrees to cooperate fully by performing all the requirements of the life insurer which are necessary conditions precedent to the issuance of life insurance policies. The Stockholder or the Company shall be the sole owner of the policies issued to him or it, and he or it may apply any dividends toward the payment of premiums.

C. If any Stockholder withdraws from the Company during his lifetime or if this Agreement terminates before the death of a Stockholder, then each Stockholder shall have the right to purchase any policy or policies on his life owned by the other Stockholders or the Company by paying an amount equal to the cash surrender value as of the date of transfer, less any existing indebtedness charged against the policy or policies. This right shall lapse if not exercised within sixty (60) days after such withdrawal or termination.

D. Notwithstanding the provisions of this Agreement, any life insurance company which has issued a policy of life insurance subject to the provisions of this Agreement is hereby authorized to act in accordance with the terms of such policies as if the Agreement did not exist, and the payment or other performance of its contractual obligations by any such insurance company in accordance with the terms of any such policy shall completely discharge such life insurance company from all claims, suits and demands of all persons whatsoever.

ARTICLE XI
EXECUTION AND DELIVERY OF DOCUMENTS

An Offering Stockholder, Purported Transferor, Disability Representative or Legal Representative, as the

case may be, shall execute and deliver any and all documents or legal instruments necessary or desirable to carry out the provisions of this Agreement.

ARTICLE XII
TERMINATION

The agreements and obligations of this Agreement shall terminate upon the occurrence of any of the following events:

A. the bankruptcy, receivership, dissolution, assignment for the benefit of creditors or other similar event of the Company,

B. the death of all the signatory Stockholders simultaneously, or

C. the mutual agreement of the Stockholders owning all of the issued and outstanding Shares of the Company.

ARTICLE XIII
ENDORSEMENT

Upon the execution of this Agreement, the certificates of Shares subject hereto shall be endorsed as follows:

> "This certificate is transferable only upon compliance with the provisions of the Amended and Restated Stock Purchase Agreement dated, 2001. A copy of said Agreement is on file at the Company's principal place of business. By accepting these shares of stock evidenced by this Certificate, the holder agrees to be bound by said Agreement."

ARTICLE XIV
GUARANTY OF CORPORATE OBLIGATIONS TO THE COMPANY OR REMAINING STOCKHOLDER

In the event the stockholder selling his Shares to the Company or Remaining Stockholders (hereinafter referred to as "Selling Stockholder") has personally guaranteed any corporate obligations, or has become a co-maker on any corporate notes, the Company and Remaining Stockholder shall take such steps as shall be or become necessary to remove said Selling Stockholder and/or his estate and spouse from liability for any of said obligations and shall secure the return of any collateral deposited in connection therewith by either renegotiation or said obligations or, failing to accomplish the foregoing after a good faith effort, shall execute a written document reasonably satisfactory to the Selling Stockholder, signed by the Company and Remaining Stockholder, holding such Selling Stockholder and/or his estate and spouse harmless and agreeing to indemnify, hold harmless and defend the Selling Stockholder and/or his estate and spouse from and against any of said obligations.

ARTICLE XV
SET-OFF

In the event a Stockholder is indebted to the Company at the time of a sale of his Shares to the Company hereunder, the debt shall mature as of such sale and purchase, and the amount of such debt (including accrued interest), not in excess of the Purchase Price for the Shares, shall serve as a set-off against and decrease the amount of the Purchase Price due the Stockholder hereunder. In the event of a cross-purchase, the purchasing Stockholder shall assume such obligation of the selling Stockholder to

the Company, the selling Stockholder shall be thereby released, and the amount of the Purchase Price due the selling Stockholder shall be accordingly reduced.

ARTICLE XVI

[INTENTIONALLY OMITTED]

ARTICLE XVII
MISCELLANEOUS

A. Counterparts. This Agreement may be signed in any number of counterparts, each of which shall be an original for all purposes, but all of which taken together shall constitute only one agreement.

B. Binding Nature. This Agreement shall be binding upon and inure to the benefit of the Stockholders and their respective heirs, legal representatives, successors, and assigns, and the Company and its successors, and assigns.

C. Specific Performance. Each of the parties hereto shall be entitled to specific performance of this Agreement upon compliance with all of its terms.

D. Law Governing. This Agreement shall be deemed to have been executed and delivered in Missouri and shall be governed, construed and enforced in accordance with the laws of the State of Missouri.

E. Amendment. This Agreement may be amended or terminated by a writing signed by the Company and all of its Stockholders.

F. Entire Agreement. This Agreement constitutes the entire agreement by the parties relative to the subject matter hereof, and all prior agreements, by and between the parties hereto, or any of them, pertaining to the retention and ownership of their Shares in the Company, shall

be deemed canceled and rescinded, void and held for naught.

G. Severability. If for any reason any immaterial provision(s) herein are determined to be invalid and contrary to any existing or future law, such invalidity shall not impair the operation of or affect those portions of this Agreement which are valid.

H. Authorization. The Company is authorized to enter into this Agreement by virtue of resolutions adopted at a meeting of its Directors held of even date herewith.

I. Notice. Each notice provided for by this Agreement shall be made in writing, either (i) by actual delivery of the notice into the hands of the party thereto entitled, or (ii) by the mailing of the notices in the United States Mails, to the last known address of the party entitled thereto, certified mail, return receipt requested. This notice shall be deemed to be received in case (i) above on the date of its actual receipt by the party entitled thereto and in case (ii) above two (2) days following the date of its mailing, unless such third day after mailing falls on a holiday or weekend, in which case it shall be deemed to be received on the next business day thereafter.

J. Exhibits. All Exhibits attached hereto shall be deemed a part hereof for all purposes.

K. Closing Days. If under this Agreement the day on which a Closing, the final date for a notice or some other day falls on a weekend or legal holiday, the applicable period shall be deemed extended so that such day falls upon the next regular business day.

L. Titles and Captions. All article, section and paragraph titles or captions contained in this Agreement are for convenience only and shall not be deemed part of the context nor affect the interpretation of this Agreement.

M. Pronouns and Plurals. All pronouns and any variations thereof shall be deemed to refer to the masculine, feminine, neuter, singular or plural as the identity of the person or persons may require.

IN WITNESS WHEREOF, the undersigned parties have executed this Agreement as of the day and year first hereinabove stated.

STOCKHOLDERS:

/s/ Michael P. Connelly
Michael P. Connelly,
Trustee U/I/T dated 8/15/90,
Michael P. Connelly, Grantor

/s/ Thomas A. Connelly
Thomas A. Connelly

COMPANY:

CROWN C SUPPLY COMPANY, INC.,
a Missouri Corporation

By: /s/ Michael P. Connelly
Title: President

[Duplicate Signature Page Omitted]

EXHIBIT A

CERTIFICATE OF AGREED VALUE

Pursuant to Article VII of the Amended and Restated Stock Purchase Agreement dated 29 August ~~(2000)~~ [2001], by and among CROWN C SUPPLY COMPANY, INC., a corporation organized under the laws of Missouri (hereinafter referred to as the "Company"), MICHAEL P. CONNELLY, TRUSTEE U/I/T DATED 8/15/90, MICHAEL P. CONNELLY, GRANTOR, AND THOMAS A. CONNELLY (collectively, the "Stockholders"); the Stockholders hereby determine and declare that the Purchase Price Per Share of the issued and outstanding common stock of the Company on this date is Ten Thousand Dollars ($10,000.00).

IN WITNESS WHEREOF, the Stockholders have signed this Certificate of Agreed Value the day of 29th day of August ~~(2000)~~ [2001] .

STOCKHOLDERS:

/s/ Michael P. Connelly
Michael P. Connelly,
U/I/T dated 8/15/90,
Michael P. Connelly, Grantor

[_____]

/s/ Thomas A. Connelly
Thomas A. Connelly

SALE AND PURCHASE AGREEMENT*

Now on this 13 day of November 2013, come now Michael P. Connelly, Jr., 3429 California, St. Louis, MO 63118, Thomas A. Connelly, Trustee of The Michael Connelly Irrevocable Trust dated 15 August 1990, Crown C Supply Co., Inc., a Missouri Corporation, Thomas A. Connelly, Individually, 5130 Manchester, St. Louis, MO 63110, Connelly Partnership/Connelly, LLC and 5200 Manchester, LLC and hereby covenant agree as follows:

WHEREAS, the parties seek to enter into an amicable agreement for the sale and purchase of the stock formerly held by Michael P. Connelly, Sr. and/or the Michael P. Connelly, Sr. Irrevocable Trust dated 15 August 1990; and

WHEREAS, the parties have resolved the issue of the sale price of the stock in as amicable and expeditious manner as is possible; and

WHEREAS, the parties seek to resolve the terms of the sale of Michael P. Connelly, Sr.'s ownership in Connelly Partnership/Connelly, LLC Main Warehouse and Office Building as well as resolve ownership of the "West Warehouse" and office building owned by 5200 Manchester, LLC.

NOW THEREFORE, the parties hereby covenant and agree:

---

* Handwritten additions are indicated with double underlining, and handwritten omissions are indicated with strikethrough. Initials attesting to the handwritten changes in this document have been omitted.

1. The parties have agreed that the value of the stock in Crown C Supply Co., Inc. is Three Million ~~Five Hundred Thousand~~ Dollars ($3,~~5~~000,000.00) and that life insurance is still available for payment of same. (A summary of the life insurance policies is attached hereto as Exhibit A and, by this reference is incorporated herein as if fully set forth herein.)

2. The parties further agree that Michael P. Connelly, Sr. has a one-half interest in the Main Warehouse and Office Building owned by Connelly, LLC which has a value (based upon an April 2013 appraisal) of One Million Two Hundred Thousand Dollars ($1,200,000.00) and that Michael P. Connelly, Sr.'s one half interest is Six Hundred Thousand Dollars ($600,000.00). (A copy of that appraisal is attached hereto as Exhibit B.)

3. The parties further agree that the Three Million ~~Five Hundred Thousand~~ ($3,~~5~~000,000.00) be paid in full promptly when those insurance proceeds are received. The Six Hundred Thousand ($600,000.00) shall be paid first from insurance proceeds available for that purpose and the balance to be paid in cash over a Thirty-Six (36) month period as allowed in the Buy/Sell Agreement.

4. Thomas A. Connelly covenants and agrees that he will prepare and enter into a purchase agreement between himself and Michael P. Connelly, Jr. wherein Michael P. Connelly, Jr. will have the right to eventually purchase all of Thomas A. Connelly's shares in Crown C Supply Company, Inc. for the purchase price of Four Million ~~Six~~ <u>One</u> Hundred Sixty-Six Thousand Six Hundred Sixty-Six Dollars ($4,~~6~~66,666.00 <u>4,166,666</u>). This right shall remain in full force and effect for Eighteen (18) months from the date of the execution of this Agreement. After the Eighteen (18) months referred to hereinabove has

elapsed, the purchase price shall then be set by a Certificate of Agreed Value as agreed to by Michael P. Connelly, Jr. and Thomas A. Connelly, or their respective trusts. That new Certificate amount shall remain in full force and effect for an additional Eighteen (18) month period, i.e., for Thirty-Six (36) months after the date of execution of this Agreement. Thereafter, the purchase price shall be set by a new Certificate of Agreed Value or by using the same valuation method contained in the Crown C Supply Co., Inc. buy/sell agreement in effect at the time of Michael, Sr.'s death (a copy of which is attached hereto as Exhibit C and, by this reference is incorporated herein as if fully set forth herein). ALL OF THE ABOVE NOT WITHSTANDING, Michael, Jr. has the irrevocable right to purchase the shares of Thomas upon his death.

5. Thomas A. Connelly also agrees to enter into an Irrevocable Agreement to sell the Main Warehouse and Office Building for the sum of One Million Two Hundred Dollars ($1,200,000.00). That agreed amount shall remain in full force and effect for a period of Eighteen (18) months after the execution date of this Agreement. Thereafter it shall be valued by either a Certificate of Agreed Value or by a real estate appraisal performed by a neutral real estate appraiser.

6. Michael P. Connelly, Sr. also had a Fifty Percent (50%) interest in the "West" warehouse and office building owned by 5200 Manchester, LLC which value is unknown at this time. An appraisal is presently being performed and, once that appraisal is completed, Michael, Jr. and/or Kelly A. Connelly shall have the exclusive right to determine whether or not the wish to be paid in cash for Michael P. Connelly, Sr.'s one-half net interest in that property or, alternatively, become a manager of 5200

Manchester, LLC succeeding to his/their father's one-half interest therein.

7. Thomas A. Connelly further guarantees that, if Crown C Supply Company, Inc. is sold, within Ten (10) years of the date of this Agreement, he will, after deduction of the amounts set forth hereunder for the purchase of his shares and interests, distribute any gain over that amount Fifty/Fifty (50/50) with the appropriate distributee(s). Any future purchaser of Thomas A. Connelly's interest(s) shall make a similar guarantee to him or his successors or heirs.

8. Documents will be prepared reflecting this Agreement and, any deviation between those documents and the terms contained herein are controlled by the terms of this Agreement.

9. If there is a determination made to succeed to Michael Sr.'s ownership interest in 5200 Manchester, LLC, then the parties hereto agree to enter into a binding buy/sell agreement to purchase the one-half interest of a deceased or selling member under the same terms and conditions contained herein for the valuation and sale of the Main Warehouse and Office Building.

10. Thomas A. Connelly covenants and agrees that he will use his best efforts to obtain insurance to fund the buy/out of all of his interests in both his stock in Crown C. Supply Company, Inc., the Main Warehouse and Office Building owned by Connelly, LLC and the East warehouse and office building owned by 5200 Manchester, LLC.

11. Payment in full for Thomas A. Connelly's interests shall occur upon his death. Any amounts of insurance in

excess of the then agreed or determined value of his interests shall be paid in full without reduction to his heirs, trustees or successors.

12. The right to purchase shall be triggered either 1) upon the death of Thomas A. Connelly; or 2) upon the determination by Thomas A. Connelly, in his absolute sole discretion, which discretion is not to be challenged, that Michael, Jr. has achieved the experience and ability to capably manage the company effectively. Michael, Jr. further agrees ~~to the establishment of an advisory board to assist in his development and education.~~ that [illegible] shall serve as president in the event of Thomas A. Connelly's inability, disability, or death before Michael, Jr. is ready to be president. The Crown Corporate board shall be [illegible] to assist in the development and education of Michael, Jr.

13. Michael, Jr. may at any time, elect to waive his rights under this Agreement in his sole discretion.

14. The parties hereto agree that the terms hereof are binding upon their heirs and successors.

GIVEN UNDER OUR HANDS this date first above written.

/s/ Thomas A. Connelly
Thomas A. Connelly, Trustee
of the Michael P. Connelly Sr.
Irrevocable Trust dated 15 August 1990

/s/ Michael P. Connelly, Jr.
Michael P. Connelly, Jr.

/s/ Thomas A. Connelly
Connelly, LLC, a Missouri
Limited Liability Company

/s/ Thomas A. Connelly
5200 Manchester, LLC
a Missouri Limited Liability Company

/s/ Thomas A. Connelly
Crown C Supply Co., Inc., President
a Missouri corporation

/s/ Thomas A. Connelly
Thomas A. Connelly

RECUSAL CERTIFICATE

Comes now Thomas A. Connelly, Trustee of the Michael P. Connelly, Sr. Irrevocable Trust dated 15 August 1990, and Thomas A. Connelly, Trustee of the Michael P. Connelly, Sr. Irrevocable Trust for Molly C. Connelly, and hereby recuses himself from all matters touching upon the sale, pricing, negotiation and transaction of any sale of the stock of Michael P. Connelly, Sr.'s interest in Crown C Supply Company, Inc. and/or Michael P. Connelly, Sr.'s interest in the warehouse and office building presently occupied by Crown C Supply Company, Inc.

According to the express terms of the aforementioned Trust Agreements, Kelly A. Connelly will be the Trustee for those two trusts relevant to the matters set forth hereinabove.

GIVEN UNDER MY HAND this 13 day of November 2013.

/s/ Thomas A. Connelly
Thomas A. Connelly, Trustee
of the Michael P. Connelly,
Sr. Irrevocable Trust dated
15 August 1990

/s/ Thomas A. Connelly
Thomas A. Connelly, Trustee
of the Michael P. Connelly,
Sr. Irrevocable Trust for
Molly C. Connelly

/s/ Kelly A. Connelly
Kelly A. Connelly

UNITED STATES DISTRICT COURT
EASTERN DISTRICT OF MISSOURI

No. 4:19-cv-01410-SRC

THOMAS A. CONNELLY, IN HIS CAPACITY AS EXECUTOR OF THE ESTATE OF MICHAEL P. CONNELLY, SR.,
PLAINTIFF

v.

THE UNITED STATES OF AMERICA, DEPARTMENT OF THE TREASURY, INTERNAL REVENUE SERVICE,
DEFENDANT

Filed: December 22, 2020

FIRST STIPULATION

WHEREAS, this is a federal estate tax refund case involving a dispute over the fair market value of Michael P. Connelly, Sr.'s interest in Crown C Supply, Inc., as of October 1, 2013;

WHEREAS, the parties stipulate as follows:

1. Michael P. Connelly, Sr., and Thomas A. Connelly (collectively the "Connelly Brothers" and each a "Connelly Brother") made a business decision to execute the Amended and Restated Stock Purchase Agreement, dated August 29, 2001 (the "Stock Purchase Agreement," previously marked as Exhibit C);

2. The Connelly Brothers executed the Stock Purchase Agreement, in part, to ensure that their family continued to own and operate Crown C Supply Company, Inc. (the "Company");

3. The Connelly Brothers executed the Stock Purchase Agreement to satisfy their respective estate planning objectives;

4. The Stock Purchase Agreement generally provided that upon one Connelly Brother's death, the surviving brother had the right to purchase the deceased brother's Company stock. But if the surviving brother did not elect to purchase the stock, then the Company was obligated to purchase the deceased brother's Company stock;

5. The Connelly Brothers agreed that when the first brother died, that the surviving brother could waive his right to purchase the deceased brother's Company stock so that the Company would be obligated to purchase the deceased brother's stock;

6. The Connelly Brothers caused the Company to fund its Stock Purchase Agreement obligations by employing life insurance policies payable upon each Connelly Brother's death;

7. Article VIII(B) of the Stock Purchase Agreement also provides: in the event of a sale and purchase under Article V (Death), and the proceeds collected from any life insurance owned by the surviving Stockholders or the Company on which the Decedent Stockholder was the insured are sufficient to pay the Purchase Price in full, the full amount of said Purchase Price shall be paid on the Closing Date to the Legal Representative of the Decedent Stockholder, and any remaining proceeds may be retained by the beneficiary thereof. If the Purchase Price

exceeds the proceeds of any life insurance collected, the insurance proceeds shall be paid on the Closing Date directly to the Legal Representative of the Decedent Stockholder and the balance of the Purchase Price shall be evidenced by a promissory note identical (except for principal amount) to the Promissory Note described in Paragraph A of this Article VIII, which shall be delivered to and in favor of the estate of the Decedent Stockholder, with the maker being the Remaining Stockholder(s)."

8. The Connelly Brothers intended that, after the first of them died, the Company would buy the deceased brother's Company stock from the deceased brother's estate with the life insurance policy proceeds the Company received after the brother's death.

9. After Michael P. Connelly, Sr., died, the Company purchased his Company stock;

10. After Michael P . Connelly, Sr., died, the Company purchased his Company stock from his estate with the life insurance policy proceeds the Company received after his death.

Date: December 15, 2020

/s/ Robert L. Devereux
ROBERT L. DEVEREUX
Danna McKitrick, P.C.
7701 Forsyth Blvd., Suite 1200
St. Louis, MO 63105
Phone: 314.726.1000
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ATTORNEY FOR PLAINTIFF THOMAS A. CONNELLY, IN HIS CAPACITY AS EXECUTOR OF THE

ESTATE OF MICHAEL P. CONNELLY, SR.

JEFFREY B. JENSEN
United States Attorney

RICHARD E. ZUCKERMAN
Principal Deputy Assistant Attorney General

/s/ James F. Bresnahan II
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ATTORNEYS FOR DEFENDANT UNITED STATES

UNITED STATES DISTRICT COURT
EASTERN DISTRICT OF MISSOURI

No. 4:19-cv-01410-SRC

THOMAS A. CONNELLY, IN HIS CAPACITY AS EXECUTOR OF THE ESTATE OF MICHAEL P. CONNELLY, SR.,
PLAINTIFF

v.

THE UNITED STATES OF AMERICA, DEPARTMENT OF THE TREASURY, INTERNAL REVENUE SERVICE,
DEFENDANT

Filed: December 22, 2020

SECOND STIPULATION

WHEREAS, this is a federal estate tax refund case that requires the Court to determine the value of Michael P. Connelly, Sr.'s (the "Decedent") taxable estate, which necessarily takes in account the Amended and Restated Stock Purchase Agreement (the "Agreement," previously marked as Exhibit C) that was in full force and effect at the time of the Decedent's death. The paramount issue is whether the $3,000,000 of life insurance death benefits proceeds that Crown C Supply Company, Inc. ("Crown C") received upon the Decedent's death and then used to fulfill its obligation under the Agreement to redeem the Decedent's shares should be included in the value of

Crown C and the Decedent's Crown C stock. Put another way the issue is, how to account for the life insurance proceeds, payable on the Decedent's death, that were used to redeem the Decedent's Crown C stock (the "Life Insurance Issue");

WHEREAS, the parties stipulate as follows:

1. This stipulation does not involve the Life Insurance Issue and has no effect thereon;

2. The plaintiff will not owe any additional federal estate taxes; and

3. At the conclusion of this case—whether by decision of this Court, the Court of Appeals for the Eighth Circuit, or Supreme Court—if the plaintiff is due a federal estate tax refund, for the purpose of determining the amount of such refund, the fair market value of the Decedent's interest in the Company was $3,100,000 (three million one hundred thousand dollars), as of October 1, 2013 as opposed to the $2,982,000 estimate of value submitted by the Decedent's estate to the IRS during the audit phase.

Date: December 15, 2020

/s/ Robert L. Devereux
ROBERT L. DEVEREUX
Danna McKitrick, P.C.
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St. Louis, MO 63105
Phone: 314.726.1000
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ATTORNEY FOR PLAINTIFF THOMAS A. CONNELLY, IN HIS CAPACITY AS EXECUTOR OF

THE ESTATE OF MICHAEL P. CONNELLY, SR.

JEFFREY B. JENSEN
United States Attorney

RICHARD E. ZUCKERMAN
Principal Deputy Assistant Attorney General

/s/ James F. Bresnahan II
JAMES F. BRESNAHAN II
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ATTORNEYS FOR DEFENDANT UNITED STATES

UNITED STATES DISTRICT COURT
EASTERN DISTRICT OF MISSOURI
EASTERN DIVISION

No. 4:19-cv-01410-SRC

THOMAS A. CONNELLY, IN HIS CAPACITY AS EXECUTOR OF THE ESTATE OF MICHAEL P. CONNELLY, SR., PLAINTIFF

v.

THE UNITED STATES OF AMERICA, DEPARTMENT OF THE TREASURY, INTERNAL REVENUE SERVICE, DEFENDANTS

EXPERT REPORT OF KEVIN P. SUMMERS[*]

I. Introduction

A. My name is Kevin P. Summers. I am a Certified Public Accountant in St. Louis, Missouri. I am a partner in the firm of Anders Minkler Huber & Helm LLP. My Curriculum Vitae is attached hereto and incorporated herein by reference (see Exhibit 1). Also included with this report is a listing of the matters in connection with which I have given a sworn statement within the past four

[*] The exhibits to the Expert Report of Kevin P. Summers have been omitted.

years (see Exhibit 2) and presentations on technical topics within the past ten years (see Exhibit 1).

B. I have been retained by Danna McKitrick, P.C. on behalf of their client, Thomas A Connelly, in his capacity as Executor of the Estate of Michael P. Connelly, Sr. ("Plaintiff") to review certain information and provide opinions in connection with this matter. The opinions I have formed are set forth herein and are those opinions that I hold to a reasonable degree of certainty and probability. A listing of the documents which I considered in forming the opinions that are set forth in this report is attached hereto and incorporated herein by reference (see Exhibit 3).

C. I have prepared this report to summarize the opinions which I may express at deposition and/or trial in this matter. My opinions are based upon the documents I reviewed, the assumptions and facts set forth herein, and my professional experience, education and training. It is usual and customary for a Certified Public Accountant who is Accredited in Business Valuation and Certified in Financial Forensics to rely on such information in forming opinions.

D. This engagement has been performed in accordance with the Statement on Standards for Forensic Services No. 1 issued by the American Institute of Certified Public Accountants.

E. This report is based upon information available and facts known by me at the time of its presentation. I reserve the right to amend or supplement this report if relevant information becomes available to me at a later date.

F. If requested by counsel, I may create trial exhibits based upon information and opinions contained in this report.

G. Throughout this report, the words "I", "me" and "my" shall mean myself or persons working under my direct supervision and control.

H. Compensation for my time and for personnel assisting me in this engagement is based upon hourly rates ranging from $250 per hour to $513 per hour. My hourly rate is $513 per hour.

I. This report is confidential, intended solely for use in connection with the above referenced matter and may not be inspected, copied or used for any other purpose.

II. Background

A. Complaint

1. As stated in Complaint, Plaintiff, Thomas A. Connelly, in his capacity as Executor of the Estate of Michael P. Connelly, Sr., brings this action for the recovery of $1,027,041.77 erroneously, illegally, and excessively assessed against and/or collected from Plaintiff as federal estate tax in his capacity as the Executor for the Estate of Michael P. Connelly, Sr., together with interest as provided by law.[1]

2. Plaintiff is the Executor of the Estate of Michael P. Connelly, Sr., late of St. Louis County, State of Missouri, having been appointed as such by the St. Louis County Circuit Court, Probate Division, and Letters Testamentary issued on October 1, 2013.[2]

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[1] Complaint filed May 23, 2019, at §5

[2] *Id.* at §1

3. Defendant is The United States of America, Department of the Treasury, Internal Revenue Service.[3]

4. At the time of Decedent's death, The Michael Patrick Connelly Indenture of Trust dated August 15, 1990 owned 385.90 shares of stock in Crown C Supply Company, Inc. (hereinafter "Crown C Supply"), which constituted 77.18 percent of the outstanding shares of Crown C Supply. The Decedent's Crown C Supply stock was subject to an Amended and Restated Stock Purchase Agreement dated as of August 29, 2001. Subsequent to the Decedent's death, in accordance with the requirements under the Amended and Restated Stock Purchase Agreement, Crown C Supply redeemed all of the Decedent's Crown C Supply stock for $3,000,000 pursuant to a Sale and Purchase Agreement dated November 13, 2013.[4]

5. An issue was raised during the course of the audit of the Decedent's Form 706 as to whether or not the value of Decedent's Crown C Supply stock shown on Form 706 was accurate. As a result of the issue involving the value of Decedent's Crown C Supply stock, Plaintiff obtained a calculation of value of the Decedent's Crown C Supply stock as of October 1, 2013, from Anders Minkler Huber & Helm, LLP ("Anders Firm"). This calculation of value determined that Decedent's Crown C Supply stock as of the date of Decedent's death was $2,982,000.[5]

B. Second Stipulation

1. Plaintiff and Defendant are in the process of finalizing a "Second Stipulation". The most recent draft of the "Second Stipulation" reads as follows:

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[3] *Id.* at §2

[4] *Id.* at §14

[5] *Id.* at §15

"Whereas, this is a federal estate tax refund case that requires the Court to determine the value of Michael P. Connelly, Sr.'s (the "Decedent") taxable estate, which necessarily takes in account the Amended and Restated Stock Purchase Agreement (the "Agreement," previously marked as Exhibit C) that was in full force and effect at the time of the Decedent's death. The paramount issue is whether the $3,000,000 of life insurance death benefits proceeds that Crown C Supply Company, Inc. ("Crown C") received upon the Decedent's death and then used to fulfill its obligation under the Agreement to redeem the Decedent's shares should be included in the value of Crown C and the Decedent's Crown C stock. Put another way the issue is, how to account for the life insurance proceeds, payable on the Decedent's death, that were used to redeem the Decedent's Crown C stock (the "Life Insurance Issue");

Whereas, the parties stipulate as follows:

1. This stipulation does not involve the Life Insurance Issue and has no effect thereon;

2. The plaintiff will not owe any additional federal estate taxes; and

3. At the conclusion of this case—whether by decision of this Court, the Court of Appeals for the Eighth Circuit, or Supreme Court—if the plaintiff is due a federal estate tax refund, for the purpose of determining the amount of such refund, the fair market value of the Decedent's interest in the Company was $3,100,000 (three million one hundred thousand dollars), as of October 1, 2013 as opposed to the $2,982,000 estimate of

value submitted by the Decedent's estate to the IRS during the audit phase."[6]

C. Amended and Restated Stock Purchase Agreement

1. On August 29, 2001, an Amended and Restated Stock Purchase Agreement ("Stock Purchase Agreement") was executed by and among Crown C Supply, a corporation organized under the laws of Missouri; Michael P. Connelly, Trustee U/I/T dated 8/15/90, Michael P. Connelly, Grantor; and Thomas A. Connelly.[7]

2. Article V (Death) of the Stock Purchase Agreement states the following:[8]

> "A. In the event of the death of a Stockholder ("Deceased Stockholder") the Remaining Stockholders (for purposes of this Article V, Remaining Stockholders shall mean the Stockholders who are not deceased) shall have the same series of Stockholder options as provided in Paragraph A of Article II to purchase the Shares as if the Deceased Stockholder was an Offering Stockholder; provided, however, that the Remaining Stockholders shall and must purchase from the Deceased Stockholder's personal representative, executor, administrator or successor trustee of any trust, as the case may be (collectively, the "Legal Representative"), and the Legal Representative shall and must sell to the Remaining Stockholders, their Proportionate Share of the Deceased Stockholder's Shares up to

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[6] Second Stipulation dated November XX, 2020 (Draft Version as of Monday, December 7, 2020 at 8:47 AM)

[7] Amended And Restated Stock Purchase Agreement Dated August 29, 2001 (IRS ADMIN-0000068-0000090)

[8] *Id.* (IRS ADMIN-0000076-0000077)

the amount of any insurance proceeds that are received by the Remaining Stockholders as a result of the Deceased Stockholder's death. Said option period shall commence on the date of the Deceased Stockholder's death. In the event a Remaining Stockholder elects to exercise his or her Stockholder Option, or is required to purchase the Shares as per the terms of this Article, said Stockholder must provide written notice to the Legal Representative within thirty (30) days of the Deceased Stockholder's Death. If one or more Remaining Stockholders fail to exercise their option, the Remaining Stockholders that do shall have the same series of options to purchase the non-purchased Shares as in Paragraph A of Article II. The purchase price to be paid by each Remaining Stockholder shall be his Proportionate Share of the purchase price provided in Article VII, the purchase price shall be paid as per the terms provided in Article VIII, and the purchase of the Shares shall be closed on the Closing Date as provided in Article IX.

B. In the event that all of the Deceased Stockholder's Shares are not purchased by the other Stockholders, then the Company shall and must purchase from the Legal Representative and the Legal Representative must sell to the Company all of the Deceased Stockholder's Shares that are not purchased by the Remaining Stockholders. The purchase price to be paid by the Company shall be the purchase price provided in Article VII, the purchase price shall be paid as per the terms provided in Article VIII, and the purchase of the Shares shall be closed on the Closing Date as provided in Article IX."

3. Article VII (Purchase Price For Shares) of the Stock Purchase Agreement states the following:[9]

> "A. In the event Shares are purchased pursuant to the terms of this Agreement, the purchase price per Share (the "Purchase Price Per Share") shall be the amount per Share set forth in the Certificate of Agreed Value, as that term is defined in Paragraph B of this Article VII; provided, however, that in the event the Stockholders fail or refuse to execute a new Certificate of Agreed Value within eighteen (18) months following the date of the last executed Certificate of Agreed Value (i.e., the last executed Certificate of Agreed Value is more than eighteen (18) months old), the Purchase Price Per Share shall be the "Appraised Value Per Share," as that term is defined in Paragraph C of this Article VII. The purchase price ("Purchase Price") of a Selling Stockholder's Shares shall equal the Purchase Price Per Share (or the Appraised Value Per Share, as the case may be) times the number of Shares being sold and purchased.
>
> B. For purposes of this Agreement, "Certificate of Agreed Value" means a certificate (in the form attached to this Agreement as Exhibit A) signed by all of the Stockholders and filed with the records of the Company, which establishes the agreed per Share value of the Shares or a method of ascertaining the same. Within thirty (30) days after the end of each tax year of the Company, all the Stockholders shall, by mutual agreement, determine the agreed value per Share by executing a new Certificate of Agreed Value in the form of Exhibit A. A Certificate of Agreed Value

[9] *Id.* (IRS ADMIN-0000077-0000079)

shall be effective only when executed by all of the Stockholders.

C. For the purposes hereof, the "Appraised Value Per Share" of the Company shall be determined as follows: If the Certificate of Agreed Value is more than eighteen (18) months old, within ten (10) days after the date an option is exercised or a mandatory purchase is required ("Appraisal Date"), the transferring Stockholder or his successor in interest shall appoint an appraiser and the Company or purchasing Stockholder(s), as the case maybe, shall appoint an appraiser. Both appraisers shall have at least five (5) years of experience in appraising businesses similar to the Company. If either party fails to name such an appraiser within the specified time, the other party may upon five (5) days written notice to the failing party, select the second appraiser. Each appraiser shall independently determine and submit to the parties, in writing, with reasons therefor, an appraisal of the fair market value of the Company. The appraisers shall take into consideration the goodwill of the Company in determining the fair market value of the Company. The appraisers shall not take into consideration premiums or minority discounts in determining their respective appraisal values. Upon receipt by the parties of both appraisals, if the fair market value of the Company is determined to be the same or if the difference between the appraisals is less than ten percent (10%) of the lower of the appraised values, then the fair market value of the Company shall be the average of the two appraisals. If the appraisals so submitted differ by more than ten percent (10%) of the lower of the appraised values, the accountants then servicing the Company shall appoint a third appraiser. The third ap-

praiser so appointed shall, as promptly as possible, determine the value of the Company on the same basis as above set forth, and that prior appraisal which is closer in value to such third appraisal shall, thereupon, be the appraisal which is binding on all parties in interest hereunder. The "Appraised Value Per Share" shall equal the amount determined by dividing the binding appraisal by the total number of Shares of the Company issued and outstanding as of the Appraisal Date. Each party shall pay the fee and expenses of the appraiser selected by such party and the fee of the third appraiser shall be borne equally by the parties appointing the two appraisers."

4. Article VIII (Payment of Purchase Price) of the Stock Purchase Agreement states the following:[10]

"A. The payment of the Purchase Price for Shares sold pursuant to this Agreement shall be made on the Closing Date as follows: one-third (1/3) of the Purchase Price shall be paid in cash on the Closing Date, and the balance of the Purchase Price shall be evidenced by the execution and delivery of a negotiable promissory note to the Stockholder or his Legal Representative or Disability Representative, as the case may be, who is selling Shares (collectively "Selling Stockholder") in the form and having the substantive provisions of the "Promissory Note," attached hereto as Exhibit B and incorporated by this reference herein. The Promissory Note shall be payable in thirty-six (36) equal monthly installments of principal and interest, the first of which shall be payable one (1) month after the Closing Date, with interest thereon at the prime rate of interest publicly announced by

[10] *Id.* (IRS ADMIN-0000079-0000080)

Firstar Bank as of the date of the Promissory Note. The Promissory Note shall further provide that the maker shall have the right to prepay the whole or any part thereof prior to the maturity date without any charge, penalty or additional interest, such prepayment to be applied first to interest and then to principal in the inverse order of maturity.

B. In the event of a sale and purchase under Article V (Death), and the proceeds collected from any life insurance owned by the surviving Stockholders or the Company on which the Decedent Stockholder was the insured are sufficient to pay the Purchase Price in full, the full amount of said Purchase Price shall be paid on the Closing Date to the Legal Representative of the Decedent Stockholder, and any remaining proceeds may be retained by the beneficiary thereof. If the Purchase Price exceeds the proceeds of any life insurance collected, the insurance proceeds shall be paid on the Closing Date directly to the Legal Representative of the Decedent Stockholder and the balance of the Purchase Price shall be evidenced by a promissory note identical (except for principal amount) to the Promissory Note described in Paragraph A of this Article VIII, which shall be delivered to and in favor of the estate of the Decedent Stockholder, with the maker being the Remaining Stockholder(s)."

D. Estate of George C. Blount v. Commissioner of Internal Revenue

1. In *Estate of George C. Blount v. Commissioner of Internal Revenue*, the United States Court of Appeals, Eleventh Circuit ("Court of Appeals") held as follows: "We AFFIRM the Tax Court's determination that the stock-purchase agreement does not fall within the statu-

tory exception, which would allow the parties to conclusively establish the value of the corporation for taxation purposes at an agreed upon purchase price. Because the Tax Court should not have added the insurance proceeds to the value of the corporation when calculating its fair market value, we REVERSE the court's computation of that value."[11]

2. The following background and discussion excerpts are from the Court of Appeals opinion:

a. Blount Construction Company ("BCC") is a closely held Georgia corporation that constructs roads and similar projects for private entities and Georgia municipalities. In 1981, the corporation's only shareholders, William C. Blount and James M. Jennings, and BCC entered into a stock-purchase agreement that required shareholder consent to transfer stock and established that BCC would purchase the stock on the death of the holder at a price agreed upon by the parties or, in the event that there is no agreement, for a purchase price based on the book value of the corporation.[12]

b. In the early 1990s, BCC purchased insurance policies solely for the purpose of ensuring that the business could continue operations, while fulfilling its commitments to purchase stock under the agreement. These policies would pro-

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[11] *Estate of George C. Blount v. Commissioner of Internal Revenue,* 428 F.3d 1338, 1340 (United States Court of Appeals, Eleventh Circuit, 2005)

[12] *Id.*

vide roughly $3 million, respectively, for the repurchasing of Jennings and Blount's stock. In 1992, BCC also began an employee stock ownership program ("ESOP") to which the company made annual contributions, either by purchasing stock from Blount and Jennings or by new issuances. Annual valuations were completed by a third party to facilitate the ESOP purchases. For example, as of January 1995, BCC was valued at roughly $7.9 million.[13]

c. In January 1996, Jennings died owning 46% of BCC's outstanding shares. BCC received about $3 million from the insurance proceeds, and paid a little less than $3 million to Jennings's estate. BCC used the previous year's book value to determine the amount to be paid to Jennings's estate.[14]

d. In October 1996, Blount was diagnosed with cancer, and his doctor predicted only a few months to live. Concerned that the buyout requirement of the 1981 stock-purchase agreement would deprive BCC of the liquidity it needed to function, he commissioned several studies regarding the amount of money his estate could receive for his shares and still leave the company in a healthy financial condition. Apparently, Blount was not concerned about

[13] *Id.*

[14] *Id.*

his family, because they were wealthy independent of the proceeds from the sale of his BCC stock.[15]

e. In November 1996, Blount executed an amendment to the 1981 stock purchase agreement that bound himself and BCC to exchange $4 million for the shares that Blount owned at his death. The 1996 agreement was substantially similar to the subsection in the 1981 agreement regarding the purchase of shares upon the death of the holder. Unlike the 1981 agreement, however, the 1996 agreement did not provide for future price adjustments in accordance with book value, which functionally locked the price at the January 1996 value of BCC. The 1996 agreement also differed from the 1981 agreement by removing the ability of BCC to pay its obligation in installments.[16]

f. When Blount died in September 1997, he owned 43,080 shares, or roughly 83% of BCC. BCC paid $4 million to the estate of Blount ("Taxpayer") in November of that year "in accordance with the November 11, 1996 Shareholders Agreement." [17]

g. In 1997, the Taxpayer filed a return declaring $4 million as the value of the shares, and the IRS filed a notice of deficiency claiming that the stock was worth $7,921,975. Implicit in this valuation of Blount's shares is a claim that

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[15] *Id.*

[16] *Id.* at 1340-1341

[17] *Id.* at 1341

BCC's fair market value exceeded $9.5 million. The Tax Court held that the 1981 agreement, as modified by the 1996 amendment, was to be disregarded for the purpose of determining the value of the shares. *Estate of Blount v. Comm'r*, 87 T.C.M. 1303, 1312, 2004 WL 1059517 (2004). The court also held that the amount of tax should have been calculated by adding the insurance proceeds to the other assets of BCC in order to arrive at the fair market value of the corporation. *Id.* at 1322.[18]

h. On the issue of the fair market value of BCC, each party offered one expert. The IRS's expert, James Hitchner, concluded that the company was worth $7 million, and the Taxpayer's expert, Gerald Fodor, computed the value at $6 million. Both experts used a blend of asset-based and income-based approaches to determine fair market value.[19]

i. The Tax Court began with Fodor's estimate but concluded that the expert should not have offset the value by the ESOP buyout obligation-for which Fodor made a $750,000 downward adjustment—and that BCC, therefore, was worth $6.75 million. The court found that Hitchner overvalued BCC's cash reserves and that, when this overvaluation was corrected, Hitchner's analysis also would value the company near $6.75 million. Thus, the Tax Court concluded

[18] *Id.*

[19] *Id.*

that both experts essentially reached the same base value for the corporation.[20]

j. Taking this base value of $6.75 million, the Tax Court found that the proper value of the stock was $9.85 million, adding the insurance proceeds of $3.1 million to compute the fair market value of the company. *Id.* at 1322. This meant that the value of Blount's stock for estate tax purposes was $8.2 million, but the Tax Court limited the amount assessed to the value determined by the IRS in its original notice of deficiency, that is, just less than $8 million. *Id.* As a result of the Tax Court's valuation of the BCC stock, additional taxes of approximately $1.36 million were paid by the Taxpayer to cover the deficiency.[21]

k. We review *de novo* the Tax Court's rulings on the interpretation and application of the tax code. *Roberts v. Comm'r*, 329 F.3d 1224, 1227 (11th Cir. 2003) (per curiam). The Tax Court's fact findings are reviewed for clear error. *Davenport Recycling Assocs. v. Comm'r*, 220 F.3d 1255, 1258 (11th Cir. 2000). In this case, we conclude that the $6.75 million valuation for BCC is not clearly erroneous. However, we find the conclusion of the Tax Court, that the insurance proceeds of $3.1 million should be added to the value of BCC, to be in error.[22]

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[20] *Id.* at 1342

[21] *Id.*

[22] *Id.*

l. To establish the fair market value of BCC, the Tax Court blended the analyses of the experts to arrive at a value of $6.75 million. The IRS and the Taxpayer, albeit alternatively, agree that this is the base value for the assets and liabilities of BCC as of the date of Blount's death. We accept the accuracy of this value as not clearly erroneous. The Tax Court then added the insurance proceeds that BCC would receive on Blount's death to the value of the company, concluding that the value of BCC would have been $9.85 million. In doing so, the Tax Court erred.[23]

m. In valuing the corporate stock, "consideration shall also be given to nonoperating assets, including proceeds of life insurance policies payable to or for the benefit of the company, to the extent that such nonoperating assets have not been taken into account in the determination of net worth." Treas. Reg. §20.2031-2(f)(2). The limiting phrase, "to the extent that such nonoperating assets have not been taken into account," however, precludes the inclusion of the insurance proceeds in this case. Likewise, in *Estate of Cartwright v. Commissioner*, the Ninth Circuit approved deducting the insurance proceeds from the value of the organization when they were offset by an obligation to pay those proceeds to the estate in a stock buyout. 183F .3d 1034, 1038 (9th Cir. 1999); see also

[23] *Id.* at 1345

Estate of Huntsman v. Comm'r, 66 T.C. 861, 875, 1976 WL 3635 (1976).[24]

n. The rationale in Cartwright is persuasive and consistent with common business sense. BCC acquired the insurance policy for the sole purpose of funding its obligation to purchase Blount's shares in accordance with the stock-purchase agreement. Even when a stock-purchase agreement is inoperative for purposes of establishing the value of the company for tax purposes, the agreement remains an enforceable liability against the valued company, if state law fixes such an obligation. Here the law of Georgia required such a purchase.[25]

o. Thus, we conclude that the insurance proceeds are not the kind of ordinary nonoperating asset that should be included in the value of BCC under the treasury regulations. To the extent that the $3.1 million insurance proceeds cover only a portion of the Taxpayer's 83% interest in the $6.75 million company, the insurance proceeds are offset dollar-for-dollar by BCC's obligation to satisfy its contract with the decedent's estate. We conclude that such nonoperating "assets" should not be included in the fair market valuation of a company where, as here, there is an enforceable contractual obligation that offsets such assets. To suggest that a reasonably competent business person, interested in ac-

[24] *Id.*

[25] *Id.*

quiring a company, would ignore a $3 million liability strains credulity and defies any sensible construct of fair market value.[26]

E. General Overview—Guidelines for Estate, Gift, and Income Valuations

1. The following excerpts are from *Financial Valuation: Applications and Models* (Fourth Edition)[27] by James R. Hitchner, who served as the IRS' expert in the *Estate of George C. Blount v. Commissioner of Internal Revenue* matter:

a. For estate, gift, and income tax planning purposes, minimization of taxes is one of the primary objectives for owners of closely held businesses. This chapter presents a general overview of the guidelines for estate, gift, and income tax valuations as set forth in the Internal Revenue Code, Treasury Regulations, and Internal Revenue Service ("IRS") Revenue Rulings.[28]

b. General guidelines for estate and gift valuations are primarily set forth in the Internal Revenue Code ("IRC"), Treasury Regulations, and Revenue Rulings. Additional guidance is found in the IRS positions as set forth in Technical Advice Memorandums and Private Letter Rulings. Court cases are also very helpful.[29]

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[26] *Id.* at 1346

[27] James R. Hitchner, *Financial Valuation: Applications and Models*, 4th ed. (New Jersey: John Wiley & Sons, Inc., 2017)

[28] *Id.* at pg. 681

[29] *Id.*

c. The IRC provides general guidance on the valuation of closely held companies as well as the applicable valuation dates for estate and gift taxes.[30]

d. Treasury Regulations represent the interpretation of the IRC by the U.S. Department of the Treasury. Key Treasury Regulations address the applicable standard of value for estate and gift taxes, guidelines for valuing closely held businesses, and disclosure requirements for gift tax returns.[31]

e. Revenue Rulings provide official interpretation of IRC, related statutes, tax treaties, and regulations by the IRS and application of the law to a specific set of facts.[32]

f. The IRS may publish Actions on Decisions in its weekly Internal Revenue Bulletins and provides a complete list of Actions on Decisions from 1997 to the present online. The IRS describes an Action on Decision ("AOD") as "a formal memorandum prepared by the IRS Office of Chief Counsel that announces the future litigation position the IRS will take with regard to the court decision addressed by the AOD." Action on Decisions for selected cases are prefaced by the following description:

> The recommendation in every Action on Decision will be summarized as acquies-

[30] *Id.* at pg. 682

[31] *Id.* at pg. 683

[32] *Id.* at pg. 686

> cence, acquiescence in result only, or nonacquiescence. Both "acquiescence" and "acquiescence in result only" mean the that the Service accepts the holding of the court in a case and the Service will follow it in disposing of case with the same controlling facts. However, "acquiescence" indicates neither approval nor disapproval of the reasons assigned by the court for its conclusions; whereas "acquiescence in result only" indicates disagreement or concern with some or all of those reasons. Nonacquiescence signifies that the Service does not agree with the holding of the court and, generally will not follow the decision in disposing of cases involving other taxpayers. In reference to an opinion of a circuit court of appeals, a nonacquiescence indicates that Service will not follow the holding on a nationwide basis. However, the Service will recognize the precedential impact of the opinion on cases arising within the venue of the deciding circuit.[33]

III. Opinions

A. Based upon the background information provided above, my review of the documents and information as listed in Exhibit 3, and my professional experience, education, and training as a Certified Public Accountant who is Accredited in Business Valuation and Certified in Financial Forensics, my opinions are as follows.

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[33] *Id.* at pg. 780

B. Stock Purchase Agreement

1. The draft Second Stipulation states that the Stock Purchase Agreement was in full force and effect at the time of the Decedent's death. I am unaware of any claims by Defendant that the Stock Purchase Agreement was not an enforceable contract under Missouri law. Therefore, I have assumed that the Stock Purchase Agreement was an enforceable contract under Missouri Law.

2. Section VIII(B) of the Stock Purchase Agreement required that in the event of a sale and purchase under Article V (Death), the proceeds collected from any life insurance owned by the surviving stockholders or the Company on which the decedent stockholder was the insured must be used to pay the purchase price. If the purchase price was less than the insurance proceeds, then the remaining proceeds may be retained by the beneficiary. If the purchase price exceeds the life insurance proceeds, then the insurance proceeds must be paid on the closing date to the legal representative of the decedent stockholder and the balance of the purchase price must be evidenced by a promissory note.[34]

3. Here, Crown C Supply was the owner and beneficiary of life insurance on Michael P. Connelly, Sr. ("Mr. Connelly"). Thus, according to Section VIII(B) of the Stock Purchase Agreement, upon the death of Mr. Connelly on October 1, 2013, Crown C Supply had an enforceable contractual obligation to use the life insurance proceeds to purchase Mr. Connelly's stock in Crown C Supply.

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[34] Amended And Restated Stock Purchase Agreement Dated August 29, 2001 (IRS ADMIN-0000079-0000080)

C. Estate of George C. Blount v. Commissioner of Internal Revenue

1. Like in *Blount*, Crown C Supply owned life insurance policies for the sole purpose of funding its enforceable contractual obligation under the Stock Purchase Agreement.[35] The life insurance proceeds provided liquidity to Crown C Supply so that the company could meet its enforceable contractual obligation to purchase a decedent stockholder's shares in accordance with the Stock Purchase Agreement.[36] The approach Crown C Supply took in order to fund an enforceable contractual obligation under the Stock Purchase Agreement with life insurance is consistent with common business sense.

2. Applying the Court of Appeals holding in *Blount*, the life insurance proceeds received by Crown C Supply were not the kind of ordinary nonoperating asset that should be included in the value of Crown C Supply. As such, the life insurance proceeds should be offset dollar-for-dollar by Crown C Supply's obligation to satisfy its contractual obligation with Mr. Connelly's estate. Thus, such nonoperating "assets" should not be included in the fair market value of Crown C Supply due to the enforceable contractual obligation that offsets such assets.

3. As referenced in Section II(E)1(f) above, I personally searched the IRS' Action on Decisions database.[37] Using both the "Decision" category and the "Issue" category, I entered the term "Blount" in the "Find Box" and received a message that "No Results Were Found That Match Your Entry In The "Find" Field". Next, I searched

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[35] Discussion with Tom Connelly, December 9, 2020

[36] *Id.*

[37] https://apps.irs.bov/app/picklist/list/actionsOnDecisions

both the "Decision" category and the "Issue" category using the term "Life Insurance" in the "Find Box" and again I received a message that "No Results Were Found That Match Your Entry In The "Find" Field". Due to the fact the IRS has not issued an AOD with regards to the *Blount* case or the issue of life insurance, Plaintiff should be allowed to rely on the Court of Appeals decision in *Blount*.

D. IRS Disregards Obligation To Pay Life Insurance Proceeds To The Estate

1. As stated in the Internal Revenue Service "Examining Officer's Activity Record", on October 26, 2016, Richard McChesney, the IRS examining officer, called Stephen Dybas, an appraiser for the IRS.[38] Mr. McChesney's notes read as follows:

> "Called Steve Dybas. He pointed out that the purchase and sale agreement required the stockholders to purchase the stock. The company would only purchase the stock if the stockholders did not. Therefore, the life insurance proceeds should not be reduced by $3,000,000. Worked on response to Cheryl Beebe-Snell's letter."[39]

2. However, on November 28, 2016, upon receiving additional information about the ownership of the life insurance policies, Mr. Dybas' position changed regarding Crown C Supply's requirement to purchase the shares. Mr. McChesney's notes read as follows:

> "Steve Dybas E-mailed me, asking if I had copies of the life insurance policies that reflected that the other

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[38] "Department of the Treasury—Internal Revenue Service—Report of Estate Tax Examination Changes", pg. 7 (IRS ADMIN-0000551)

[39] Internal Revenue Service "Examining Officer's Activity Record", entry dated October 26, 2016 (IRS ADMIN-0001125)

stockholders were the owners of the policies. I responded that, per the Forms 712, Crown C Supply was the owner. He responded that, because Crown C Supply was the owner, based on Article V of the 2001 stock purchase agreement, Crown C Supply was required to purchase the shares."[40]

3. Per an email dated November 28, 2016, Mr. Dybas explains his interpretation of the stock purchase agreement as follows:

"Richard,

This is my interpretation of the language in the stock purchase agreement.

If the Remaining Shareholders were not the beneficiaries then they did not receive any insurance proceeds and, therefore, were not obligated to purchase the shares. Per the language below of the stock purchase agreement, the obligation to purchase the shares would then go the Company.

Per Article V

B. In the event that all of the Deceased Stockholder's Shares are not purchased by the other Stockholders, then the Company shall and must purchase from the Legal Representative and the Legal Representative must sell to the Company all of the Deceased Stockholder's Shares that are not purchased by the Remaining Stockholders. The purchase price to be paid by the Company shall be the purchase price provided in Article VII, the purchase price shall be paid as per the terms provided in Article VIII, and the purchase of the

[40] *Id.*, entry dated November 28, 2016 (IRS ADMIN-0001127)

> Shares shall be closed on the Closing Date as provided in Article IX.
>
> If my understanding is not accurate please let me know.
>
> Steve"[41]

4. Per an email dated December 22, 2016, Mr. Dybas provided the following update to Mr. McChesney:

> "Hi Richard,
>
> Just following up on this case.
>
> If the company had the purchase obligation then the only other potential argument, in my opinion, would be as to the reasonableness of a 6% specific company risk premium the valuator included in his cost of equity.
>
> Merry Christmas!
>
> Steve"[42]

5. Finally, on March 3, 2017, Mr. Dybas was asked the following question by Mr. McChesney: "If the $3,000,000 obligation to pay the life insurance proceeds to the estate is disregarded, is it still your position that, using the net asset value approach, the $3,000,000 in life insurance proceeds should be added to the value of the corporation?" Mr. Dybas responded as follows:

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[41] Email from Steven M. Dybas to Richard P. McChesney dated November 28, 2016 (IRS ADMIN-0001152)

[42] Email from Steven M. Dybas to Richard P. McChesney dated December 22, 2016 (IRS ADMIN-0001152)

"Hi Richard,

Yes, you advised previously that, per the Forms 712, Life Insurance Statements, completed by the life insurance companies, Crown C Supply, and not the other stockholder, is the beneficiary of the life insurance policies. This being the case, then the insurance proceeds are an asset of the corporation.

If the obligation for the corporation to pay the life insurance proceeds to the estate is disregarded, then the corporation would retain the proceeds as an asset.

If you need anything else just let me know.

Steve"[43]

6. Based on the notes and emails described above, it appears Mr. Dybas, the IRS appraiser, agreed that Crown C Supply had an enforceable contractual obligation to use the life insurance proceeds to purchase Mr. Connelly's stock in accordance with the Stock Purchase Agreement. However, by simply disregarding Crown C Supply's liability associated with its enforceable contractual obligation, despite the Court of Appeals decision in *Blount*, the Defendant takes a position that is not consistent with common business sense and results in the fair market value of Crown C Supply being overstated by $3 million.

Respectfully submitted,

ANDERS MINKLER HUBER & HELM LLP

/s/ Kevin P. Summers

Kevin P. Summers, JD, CPA/ABV/CFF, CVA, CDFA, CEPA

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[43] Email from Richard P. McChesney to Steven M. Dybas (and response) dated March 3, 2017 (IRS ADMIN-0001150)

Partner

St. Louis, Missouri
December 9, 2020

UNITED STATES DISTRICT COURT
EASTERN DISTRICT OF MISSOURI
EASTERN DIVISION

No. 4:19-cv-01410-SRC

THOMAS A. CONNELLY, IN HIS CAPACITY AS EXECUTOR OF THE ESTATE OF MICHAEL P. CONNELLY, SR., PLAINTIFF

v.

THE UNITED STATES OF AMERICA, DEPARTMENT OF THE TREASURY, INTERNAL REVENUE SERVICE, DEFENDANT

DECLARATION OF EVAN K. COHEN*

I. INTRODUCTION

A. QUALIFICATIONS AND BACKGROUND

1. My name is Evan K. Cohen, and my business address is One Beacon Street, Ste. 2600, Boston, Massachusetts, 02108, United States of America. I am a Principal of The Brattle Group ("Brattle"), a global economic consulting firm headquartered in Boston, Massachusetts with additional offices in London, Rome, Madrid, Brussels, Sydney, Toronto, Chicago, Washington, D.C., New York, and

* The table of contents and exhibits to the Declaration of Evan K. Cohen have been omitted.

San Francisco. I have an MBA from the MIT Sloan School of Management with a concentration in financial engineering. I received my Charted Financial Analyst from the CFA Institute in 2013. I was an investment banking analyst in corporate finance at Dillon, Read & Co. and UBS.

2. I have extensive experience in corporate finance, valuation, structured finance, and tax disputes. I have assisted private businesses, the U.S. Department of Justice, and the Internal Revenue Service in developing economic and financial testimony in a variety of finance and tax litigation disputes. I have been retained by government and private counsel to provide expert and summary testimony in various venues, including federal district court, the Court of Federal Claims, and state regulatory bodies. I served as a valuation and damages expert for a class of shareholders in litigation arising from the $22 billion leveraged buyout by the Archstone-Smith REIT. I have played central roles in some of the landmark tax, economic substance, and transfer pricing cases of the past 15 years, including *Long Term Capital Holdings vs. U.S.*, *GlaxoSmithKline Holdings, Inc. vs. Commissioner*, *BB&T Corp. vs. U.S.*, *Fifth Third Bancorp & Subsidiaries vs. U.S.*, *Historic Boardwalk Hall, LLC vs. Commissioner*, *Pritired 1, LLC, et al. vs. U.S.*, *Bank of N.Y. Mellon Corp vs. Commissioner*, *Salem Financial, Inc. vs. U.S.*, *Buyuk LLC vs. Commissioner*, *U.S. vs. Ogbazion*, *U.S. vs. ITS Financial, and Eaton v. United States.*

3. Prior to joining Brattle, I spent six years as a consultant at Cambridge Finance Partners, LLC, where I served as a consultant on complex business and tax litigation cases in the financial services, pharmaceutical, electric, and gas industries. I was also formerly a cofounder

and Chief Financial Officer of NextCourier Networks, Inc.

4. I have presented at professional conferences and published articles on valuation. My detailed curriculum vitae, provided in Appendix 1, includes testimony I have provided and all of my publications for the past ten years.

5. Brattle is being compensated for my work on this case at my standard rate of $625 per hour. My compensation is not contingent upon my testimony or on the result of this proceeding.

6. Appendix 2 provides a list of documents I considered in preparing this report. I reserve the right to supplement or otherwise modify this report as new evidence is presented in this matter.

B. Overview and Assignment

7. Michael P. Connelly, Sr. ("Connelly"), President and majority shareholder of Crown C Supply Company ("Crown C Supply" or the "Company"), died on October 1, 2013.[1] At the time of his death, Connelly owned 385.9 shares of stock in Crown C Supply, representing 77.18% of the Company's outstanding shares.[2] Thomas A. Connelly, Connelly's brother and the executor of Connelly's estate (collectively, Connelly and Thomas A. Connelly are

[1] Exhibits A and B, Original and Amended Form, 706, United States Estate (and Generation Skipping) Tax Return of the Estate of Michael P. Connelly, Sr., line 5; Plaintiff's Response to United States Request for Admission ("U.S. RFA") Nos. 1-4, 34, 35.

[2] Plaintiff's Response to U.S. RFA No. 52.

the "Company Shareholders"), owned the remaining 114.1 shares or 22.82% of the Company.[3]

8. Pursuant to the Amended and Restated Stock Purchase Agreement, dated August 29, 2001, Crown C Supply was obligated to purchase the Company Shareholders' interests upon their respective deaths.[4] Crown C Supply was also the beneficiary of three life insurance policies payable upon Connelly's death.[5] Consequently, after Connelly died on October 1, 2013, Crown C Supply received $3,503,894.74 from these three life insurance policies.[6] Additionally, pursuant to the Purchase and Sale Agreement dated November 13, 2013, Crown C Supply purchased Connelly's 77.18% interest in the Company, and did so for $3,000,000.[7]

9. On October 7, 2016, Anders Minkler Huber & Helm LLP ("Anders Minkler") prepared a calculation of value report[8] that concluded Connelly's Company stock

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[3] Plaintiff's Response to U.S. RFA No. 53; Exhibit C, Amended and Restated Stock Purchase Agreement (C000310-C000332), p. 1.

[4] Plaintiff's Response to U.S. RFA Nos. 88 and 89; Exhibit C, Amended and Restated Stock Purchase Agreement (C000310-C000332), Article V (C0003180-C000319).

[5] Exhibit T, $1,000,000 AXA Term Life Insurance Policy No. 109021548 (C001647-C001692) at C001655; Exhibit U, $1,000,000 AXA Term Life Insurance Policy No. 109021767 (C001827-C001875) at C001830; Exhibit V, $1,500,000 AXA Universal Life Insurance Policy No. 159211555 (C001699-C001756) at C001726; Exhibit W, AXA Life Insurance Policy Documents (C002612–C002616) at C002616.

[6] Plaintiff's Response to U.S. RFA Nos. 166-181.

[7] Exhibit N, Sale and Purchase Agreement, dated November 13, 2013, ¶ 3 (not labeled).

[8] For convenience, I occasionally refer to the Anders Minkler Report as a valuation, however it is not a valuation report. Specifically,

was worth $2,982,000 as of October 1, 2013 (the "Anders Minkler Report").[9] When performing this analysis, Anders Minkler relied on a capitalized cash flow method, adding back "non-operating assets to arrive at [its estimate of] the fair market value of the Company's equity on a controlling, non-marketable basis."[10] These non-operating assets included, among other items, $503,915 in "Life Insurance Proceeds Retained by Company (Michael Connelly)."[11] However, these insurance proceeds were $2,999,980 less than the actual proceeds received,[12] approximating the $3,000,000 spent on the repurchase of Connelly's shares.

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the Anders Minkler Report was written in response to a "calculation engagement" which it describes as "[a]n engagement to estimate value wherein the valuation analyst and the client agree on the specific valuation approaches and valuation methods that the valuation analyst will use. . . A calculation engagement generally does not include all of the valuation procedures required for a valuation engagement. If a valuation engagement had been performed, the results might have been different." Exhibit L, Anders Minkler Report (C000613-C000640) at C000614.

[9] Exhibit L, Calculation of Value Regarding 77.18% Ownership Interest in Crown C Supply, Inc., as of October 1, 2013, by Anders Minkler Huber & Helm LLP, as of October 1, 2013 (C000613-C000640) at p. 5 (C000618); Plaintiff's Response to U.S. RFA Nos. 30-32.

[10] Exhibit L, Anders Minkler Report (C000613-C000640) at pp. 4-5 (C000617-C000618), Exhibit 6 (C000640).

[11] Exhibit L, Anders Minkler Report (C000613-C000640) at Exhibit 6 (C000640).

[12] Crown C Supply received $3,503,894.74 from the life insurance policies. $2,999,980 ≈ $3,503,894.74 – $503,915. Plaintiff's Response to U.S. RFA Nos. 166-181. After spending $3,000,000 purchasing shares from Connelly's estate, this leaves $503,894.74. In contrast, the Anders Minkler Report includes $503,915 in retained life insurance pro-

10. Counsel for the United States asked me to opine on the fair market value of a 77.18% equity interest in Crown C Supply, as of October 1, 2013—i.e., the fair market value of Connelly's Company stock as of his date of death. Counsel for the United States instructed me to accept Anders Minkler's conclusions regarding the value of Connelly's Company ownership interest, except for Anders Minkler's treatment of the life insurance proceeds that Crown C Supply used to purchase Connelly's Company stock.[13] For simplicity, I ignore the $20.26 overstatement and assume that the Anders Minkler Report excluded exactly $3,000,000 of insurance proceeds from its analysis.

C. Summary of Opinions

11. Crown C Supply's purchase of Connelly's 385.9 Company shares was a purchase of equity, and valuation of those shares should have been consistent with general equity valuation principles. In a fair market equity valuation, the insurance proceeds would be included in the value of Crown C Supply as a non-operating asset, distributable to the shareholders based on their respective equity interests in the Company. Accordingly, Connelly's 77.18% interest in Crown C Supply was worth $5,297,496, as of October 1, 2013.[14]

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ceeds. Exhibit L, Anders Minkler Report (C000613-C000640) at Exhibit 6 (C000640). This appears to be an overstatement of $20.26. $20.26 = $503,915.00 – $503.894.74.

[13] Functionally, that means I have not been asked to opine on the Anders Minkler Report's conclusion that the Company's equity value without $3,000,000 in insurance proceeds was $3,863,819.

[14] Note that, if I assumed that the Anders Minkler Report did not exclude exactly $3,000,000 of insurance proceeds, but rather $2,999,980, this value would fall to $5,297,480. $5,297,480 = 77.18% x ($3,863,819 + $2,999,980).

12. The alternative of allowing the repurchase obligation to offset $3,000,000 of insurance proceeds undervalues Crown C Supply's equity, undervalues Connelly's equity interest in Crown C Supply (*i.e.*, his stock), and violates well-established equity valuation principles because the resultant share price creates a windfall for a potential buyer that a willing seller would not accept. Indeed, by purchasing Connelly's shares at a $3,000,000 price, Crown C Supply created a windfall for Thomas A. Connelly at Connelly's expense.

II. GENERAL BACKGROUND

A. Introduction to Crown C Supply

13. Founded in 1980,[15] Crown C Supply is a roofing and siding materials supply company operating primarily in the St. Louis, Missouri area.[16] As of October 1, 2013, Crown C Supply relied on a variety of facilities in its operations, including a corporate headquarters, a showroom for displaying products samples, and a 75,000 square foot warehouse.[17] The Company leased these facilities from two related parties, 5200 Manchester, LLC and Connelly, LLC.[18]

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[15] Exhibit L, Anders Minkler Report (C000613-C000640) at C000615; *see also* Exhibit D, Crown C Supply Company, Inc. and Subsidiary, Consolidated Financial Statements, for the years ended September 30, 2012 and 2013 (C0000397-C000413), Item 2 (C000408).

[16] Exhibit L, Anders Minkler Report (C000613-C000640) at pp. 2-3 (C000615-C000616).

[17] *Id.*, p. 3 (C000616).

[18] *Id.* The annual financial statements for Crown C Supply and 5200 Manchester, LLC were produced on a consolidated basis, since these companies were jointly owned by Connelly and Thomas A. Connelly.

14. Prior to October 1, 2013, Connelly was the president of Crown C Supply.[19] On a standalone basis, Crown C Supply's annual gross and net incomes were somewhat variable. Between 2009 and 2013, Crown C Supply generated between $22,000,000 and $38,000,000 in annual revenue, leading to net annual income ranging from a loss of - 168,787 in 2010 to a profit of $1,181,064 in 2012.[20]

B. LIFE INSURANCE ASSETS

15. Crown C Supply acquired life insurance policies for both Connelly and Thomas A. Connelly.[21] From 2009 to 2013, the Company's annual consolidated financial statements show that Crown C Supply: (1) spent between $125,550 and $186,070 annually on life insurance premiums,[22] and (2) included the cash surrender value of these life insurance policies as an asset, reporting $851,870 as of

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Exhibit D, Crown C Supply Company, Inc. and Subsidiary, Consolidated Financial Statements, for the years ended September 30, 2012 and 2013, Item 1 (C000406).

[19] Plaintiff's Response to U.S. RFA No. 34.

[20] Exhibit L, Anders Minkler Report (C000613-C000640) at Exhibit 2 (C000629-C000631). *See also* Exhibit P, Crown C Supply Company, Inc. and Subsidiary, Consolidated Financial Statements, for the years ended September 30, 2009 and 2010 (Anders 388-Anders 407) at (Anders 393); Exhibit Q Crown C Supply Company, Inc. and Subsidiary, Consolidated Financial Statements, for the years ended September 30, 2010 and 2011 (Anders 408-Anders 421) at (Anders 412); Exhibit R, Crown C Supply Company, Inc. and Subsidiary, Consolidated Financial Statements, for the years ended September 30, 2011 and 2012 (Anders 422-Anders 435) at (Anders 426); Exhibit D, Crown C Supply Company, Inc. and Subsidiary, Consolidated Financial Statements, for the years ended September 30, 2012 and 2013 (C000403).

[21] *See* footnote 5 above; *see also* Plaintiff's Response to U.S. RFA Nos. 57 and 62.

[22] Exhibit L, Anders Minkler Report (C000613-C000640) at Exhibit 2 (C000636).

September 30, 2013.[23] In total, Crown C Supply received $3,503,894.74 from the three life insurance policies it owned with respect to Connelly after his death.[24]

C. Transaction Overview

16. In August of 2001, the Company Shareholders entered into an Amended and Restated Stock Purchase Agreement (the "2001 Agreement").[25] This agreement gave the Company Shareholders—i.e., the Connelly brothers—the right of first refusal for the other's shares. If one Company Shareholder received a bona fide offer for all of his shares from a third party and planned to sell those shares, the other Connelly brother had the option to purchase all the shares in lieu of the third party.[26] The 2001 Agreement also gave the Company Shareholders similar rights in the event of one brother's death, adding that, "[i]n the event that all of the Deceased Stockholder's Shares are not purchased by the other Stockholders, then the Company shall and must purchase from the Legal Representative and the Legal Representative must sell to the Company all of the Deceased Stockholder's Shares that are not purchased by the Remaining Stockholders."[27]

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[23] Exhibit D, Crown C Supply Company, Inc. and Subsidiary, Consolidated Financial Statements, for the years ended September 30, 2012 and 2013, Item 4, (C000409). Note that, on an unconsolidated basis, the Anders Minkler Report also includes $851,870 of "Cash Value of Life Insurance" as an asset. Exhibit L Anders Minkler Report, Exhibit 1 at C0000627.

[24] Plaintiff's Response to U.S. RFA Nos. 166-181; C001647-C001692; C001827-C001875; C001699-C001776; C002613-C002616.

[25] Exhibit C, Amended and Restated Stock Purchase Agreement (C000310-C000332).

[26] *Id.*, Article II (C000313-C000315).

[27] *Id.*, Article V (C000318-C000319).

That is, if any of the deceased Company shareholder's shares were not purchased by other stockholders, the 2001 Agreement *required* the Company to purchase them.

17. In the event that Crown C Supply was required to purchase the shares of a deceased stockholder, the 2001 Agreement specified that "the purchase price per Share . . . shall be the amount per Share set forth in the Certificate of Agreed Value," where "'Certificate of Agreed Value' means a certificate . . . signed by all of the Stockholders and filed with the records of the Company, which establishes the agreed per Share value of the Shares or a method of ascertaining the same."[28]

18. Further, the 2001 Agreement stated that "in the event the Stockholders fail or refuse to execute a new Certificate of Agreed Value within eighteen (18) months following the date of the last executed Certificate of Agreed Value . . . the Purchase Price Per Share shall be the 'Appraised Value Per Share.'"[29] The 2001 Agreement set forth the process for retaining an appraiser(s) to determine the "Appraised Value Per Share."[30]

19. When Connelly died on October 1, 2013, the Company was then obligated to purchase his shares according to the 2001 Agreement. However, the Company Shareholders (i.e., the Connelly brothers) had not executed a Certificate of Agreed Value within the last 18 months.[31]

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[28] Exhibit C, Amended and Restated Stock Purchase Agreement (C000310-C000332), Article VII (C000319-C000321).

[29] *Id.*

[30] *Id.*

[31] Plaintiff's Response to U.S. RFA No. 91.

Further, an appraiser was not retained at the time of death to determine the "Appraised Value Per Share."[32]

20. On November 13, 2013, Connelly's son, Michael P. Connelly Jr. ("Connelly, Jr."), and Thomas A. Connelly entered into "the 2013 Purchase Agreement" "for the sale and purchase of the stock formerly held by Michael P. Connelly, Sr."[33] In this document, the parties "agreed that the value of the stock in Crown C Supply Co., Inc. is Three Million Dollars ($3,000,000) and that life insurance is available for payment of the same," and further agreed that payment for the shares would be made upon receipt of the life insurance proceeds.[34] Additionally, the parties agreed that Connelly, Jr. had the right to purchase all of Thomas A. Connelly's shares "either 1) upon the death of Thomas A. Connelly; or 2) upon the determination by Thomas A. Connelly . . . that Michael, Jr. has achieved the experience and ability to capably manage the company effectively."[35] Based on this agreement, Crown C Supply purchased Connelly's 385.9 shares for $3,000,000.[36]

21. According to the Anders Minkler Report, Connelly's 385.9 Company shares were worth $2,982,000 on October 1, 2013.[37] The Anders Minkler Report included

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[32] Plaintiff's Response to U.S. RFA No. 92.

[33] Exhibit N, Sale and Purchase Agreement Dated November 13, 2013, p. 1.

[34] *Id.*, pp. 1-2.

[35] *Id.*, pp. 4-5.

[36] *Id.*, p. 1.

[37] Exhibit L, Anders Minkler Report (C000613-C000640) at C000618.

$503,915 in "Life Insurance Proceeds Retained by Company (Michael Connelly),"[38] or approximately $3,000,000 less than the amount of life insurance proceeds received by Crown C Supply.

22. In the following sections I evaluate whether this exclusion prevented the Anders Minkler Report from arriving at a fair market value for the 385.9 shares. First, I review some basic principles of valuation and discuss how these guide the appropriate treatment of life insurance proceeds owned by the Company. Second, I affirmatively show that the fair market value of the equity of the Company, as of October 1, 2013, was $6,863,819, making Connelly's shares worth $5,297,496. Finally, I show that excluding the insurance proceeds when valuing the Company leads to outcomes that would not arise in an arm's length transaction because it creates a windfall to a potential buyer that no willing seller would accept.

III. VALUATION PRINCIPLES

23. Valuation of companies, property, intangibles, and other assets is a common form of analysis used throughout the finance and investment industry.[39] Subsequently, there are "well-accepted methods or valuation models that managers and investors commonly use to measure

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[38] Exhibit L, Anders Minkler Report (C000613-C000640) at Exhibit 6 (C000640).

[39] As Holthausen and Zmijewski write, "[m]anagers and investors decide whether or not to make an investment by comparing their assessment of the value—or valuation—of the future cash flows they expect to earn from an investment to the amount they must invest." Robert W. Holthausen and Mark E. Zmijewski, *Corporate Valuation: Theory Evidence & Practice*, First Edition, (Cambridge Business Publishers, 2014), p. 4.

value,"[40] as well as extensive discussion of these methods and models in financial textbooks and other academic literature. I consider these methods in the context of the Anders Minkler Report's exclusion of the $3,000,000 in insurance proceeds from their valuation of the Company. I conclude that the Anders Minkler Report violates three standard "valuation principles" that are central to all arm's length equity valuations. Violation of these principles is an indication that the valuation did not result in a market-driven price (or fair market value, see definition below). In this section, after discussing some basic valuation definitions, I lay out these three valuation principles which any arm's length equity valuation should follow. Later in my report, I refer back to these principles to ascertain if the valuation of Connelly's shares conformed to fair market valuation principles.

A. Valuation Definitions

24. **Fair Market Value:** The fair market value of an asset is the price at which it would be sold in the market between two willing, well-informed unrelated parties, neither being under compulsion to participate.[41] While there

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[40] Robert W. Holthausen and Mark E. Zmijewski, *Corporate Valuation: Theory Evidence & Practice*, First Edition, (Cambridge Business Publishers, 2014), p. 4.

[41] *See, e.g.*, the OECD's definition for fair value, "[t]he price at which an asset would change hands between a willing buyer and a willing seller, neither being under any compulsion to buy or to sell and both having reasonable knowledge of relevant facts." Available online at https://stats.oecd.org/glossary/detail.asp?ID=5332, accessed October 29, 2020. This is consistent with the definition provided in IRS Revenue Ruling 59-60 which references regulations defining fair market value as "the price at which the property would change hands between a willing buyer and a willing seller when the former is not under any compulsion to buy and the latter is not under

are many different approaches to estimating fair market value, several common approaches start by examining the asset's expected cash flow. As Aswath Damodaran writes, "the price we pay for any asset should reflect the cash flows it is expected to generate."[42] A profit-maximizing buyer is not willing to pay more for an asset than its cash flows are worth, while a profit-maximizing seller is not willing to accept a price below what the cash flows are worth.[43] Therefore, willing, well-informed unrelated parties will generally accept a price which is consistent with an asset's expected cash flows.

25. **Firm Value:** When estimating the fair market value of a company, an analyst can either value the whole company—its firm value—or the value that equity holders

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any compulsion to sell, both parties having reasonable knowledge of relevant facts." IRS Revenue Ruling 59-60, § 2, available online at https://www.pvfllc.com/files/IRS_Revenue_Ruling_59-60.pdf. *See also* U.S. Treasury Regulation § 20.2031-1(b).

[42] Aswath Damodaran, *Damodaran on Valuation: Security Analysis for Investment and Corporate Finance*, Second Edition, (Hoboken, New Jersey: John Wiley & Sons, 2006), p. 1. Similarly, Holthausen and Zmijewski write, "[t]he value of an asset depends on the magnitude, timing, and risk of the cash flows the investor expects it to generate." Robert W. Holthausen and Mark E. Zmijewski, *Corporate Valuation: Theory Evidence & Practice*, First Edition, (Cambridge Business Publishers, 2014), p. 9.

[43] Note that "worth" here is as measured by the buyer and seller, respectively. It is possible that a buyer and seller will disagree slightly on the value of an asset and, indeed, "transactions are more likely to occur when the buyer believes a company is worth more than the seller believes it is." However "valuation models should approximate the observed market value of the company so long as the inputs used reflect both a specific valuation context and the information and expectations of the buyers and sellers engaged in market transactions." Robert W. Holthausen and Mark E. Zmijewski, *Corporate Valuation: Theory Evidence & Practice*, First Edition, (Cambridge Business Publishers, 2014), p. 5.

can expect to recover—its equity value (discussed below). Firm value reflects the fair market value of the company's assets without deducting its liabilities, and encompasses all of the firm's assets, including non-operating assets.[44]

26. **Equity Value:** Equity value (or common equity value) is the fair market value of a company's equity (or common equity). Equity investors provide a primary source of funding for a firm and, in return, receive an interest in all cash flows and assets available after other non-equity interests have been paid. As Fuhrmann and Lamba write, "[w]hen the company issues equity securities, it is not contractually obligated to repay the amount it receives from shareholders, nor is it contractually obligated to make periodic payments to shareholders for the use of their funds. Instead, shareholders have a claim on the company's assets after all liabilities have been paid. Because of this residual claim, equity shareholders are considered to be owners of the company."[45]

27. Consistent with equity's status as a residual claim on value, analysts often start an equity valuation by estimating firm value and then deducting all non-equity obligations. As Damodaran writes, "we can always get from the former (firm value) to the latter (equity value) by netting out the value of all nonequity claims from firm value.

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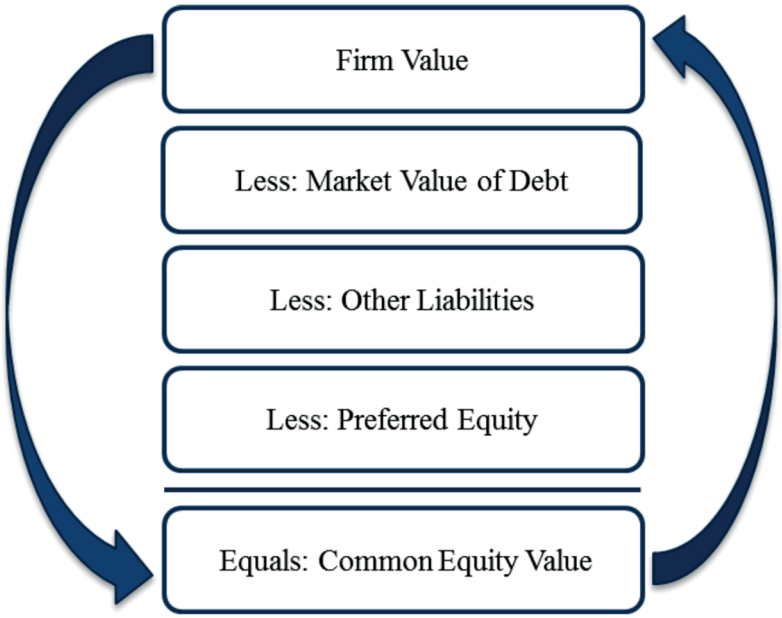
[44] As Aswath Damodaran writes, "[t]here are two ways in which we can approach DCF valuation. The first is to value the entire business, with both assets in place and growth assets; this is often termed firm or enterprise valuation. . . . The second way is to just value the equity stake in the business, and this is called equity valuation." Aswath Damodaran, *Damodaran on Valuation: Security Analysis for Investment and Corporate Finance*, Second Edition, (Hoboken, New Jersey: John Wiley & Sons, 2006), pp. 11-12.

[45] Ryan C. Fuhrmann and Asjeet S. Lamba, "Overview of Equity Securities," *Equity Asset Valuation* Fourth Edition, Jerald E. Pinto, et al. Ed., (Hoboken, New Jersey: Wiley, 2020), p. 8.

Done right, the value of equity should be the same whether it is valued directly (by discounting cash flows to equity at the cost of equity) or indirectly (by valuing the firm and subtracting out the value of all nonequity claims)."[46] Figure 1 below depicts the transformation from firm value to equity value.

Figure 1: Starting from the Equity Value or Firm Value to Derive the Other



28. Note also that an analyst can go in the opposite direction and use valuation techniques or markets to find the equity value, then follow Figure 1 to find firm value. For public companies, for example, analysts might start with an observation of the equity as valued by the stock

[46] Aswath Damodaran, *Damodaran on Valuation: Security Analysis for Investment and Corporate Finance*, Second Edition, (Hoboken, New Jersey: John Wiley & Sons, 2006), p. 12.

market, then add back non-common equity claims and liabilities to get to firm value.

B. Valuation Principle #1: Firm Value Reflects Cash Flows from All Assets

29. Total firm valuation should account for all cash flows associated with the firm's assets. For companies, this includes both the cash generated by regular business operations as well as any cash available from non-operating assets. Explaining this, Wessels, Goedhart, and Koller write, "[m]any companies own assets that have value but whose cash flows are not part of the operations of the business and are not included in accounting revenue or operating profit. As a result, the cash generated by these assets is not part of free cash flow and must be valued separately."[47]

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[47] David Wessels, Marc H. Goedhart, and Tim Koller, *Valuation: Measuring and Managing the Value of Companies*, University Edition, Sixth Edition, (Hoboken, NJ: Wiley Finance, 2015), p. 149. Similarly, when discussing the capitalized cash flow method, the National Association of Certified Valuators and Analysts writes, "[i]t is important that any income or expense items generated from non-operating assets and liabilities be removed from estimated future benefits prior to applying this method. The fair market value of net non-operating assets and liabilities is then added to the value of the business derived from the capitalization of earnings." National Association of Certified Valuators and Analysts, BVTC Course 1: Fundamentals, Techniques, and Theories, "Chapter 6: Commonly Used Methods of Valuation," 2012, p. 6.

30. Life insurance proceeds, such as the proceeds at issue here, provide a lump-sum cash payment to a company and represent such a non-operating asset that must be added to firm's operating value in any firm valuation.[48]

C. Valuation Principle #2: Common Equity Captures All Residual Value After All Other Obligations Are Satisfied

31. Because common equity is the residual claim on a company's assets, all other obligations need to be satisfied before equity holders can begin to recoup their investment. This means that in order to estimate the fair market value of common equity starting from firm value, an analyst must deduct all of the other obligations as described in Figure 1.

32. Indeed, the Anders Minkler Report took this approach, valuing first the ongoing operations of the Crown C Supply and then deducting the fair market value of its

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[48] Life insurance proceeds are received as cash, where any cash exceeding what is needed for day-to-day operations is considered a non-operating asset. For example, Wessels, Goedhart, and Koller write, "companies often hold more cash and marketable securities than they need to run the business on a daily basis. You need to make an estimate of how much the business needs for operations. The remaining cash and marketable securities are treated as nonoperating." David Wessels, Marc H. Goedhart, and Tim Koller, *Valuation: Measuring and Managing the Value of Companies*, University Edition, Sixth Edition, (Hoboken, NJ: Wiley Finance, 2015), p. 319. Similarly, Damodaran writes "[n]onoperating assets include all assets whose earnings are not counted as part of the operating income. The most common of the nonoperating assets is cash and marketable securities, . . . and the value of these assets should be added to the value of the operating assets." Aswath Damodaran, *Damodaran on Valuation: Security Analysis for Investment and Corporate Finance*, Second Edition, (Hoboken, New Jersey: John Wiley & Sons, 2006), p. 197.

debt.[49] This approach is appropriate as long as all assets are included and the debt deducted includes all non-equity claims, and no equity claims.

33. As part of this principle, once the residual value is determined, it belongs to all common equity holders based upon the number shares held. Each share is entitled to its proportional claim on that residual value; no individual common equity share is worth more than another. This makes common equity shares fully interchangeable.

D. Valuation Principle #3: Fair Market Transactions Do Not Make Either Party Worse Off

34. As noted above, the fair market value reflects the value that would be accepted in a market transaction between two willing, well-informed unrelated parties. In order for both parties to be willing, this means that an asset must be priced so that neither party in an exchange is made worse off by transacting. For example, if I buy a baseball card trading at $100, then when I exchange $100 of cash with the card owner, she has merely converted the value of the card into a different asset. On her personal balance sheet, that asset has been transformed from a $100 baseball card into $100 in cash. On my personal balance sheet, the $100 in cash has been transformed into a $100 baseball card. In other words, our economic positions are unchanged.

35. In an exchange like the purchase of the baseball card, where the asset is not worth more because of a change in ownership, the principle that neither party is worse off means that there is no transfer of wealth between the parties and neither party is made better or

[49] Exhibit L, Anders Minkler Report (C000613-C000640) at Exhibit 6 (C000640).

worse off. Acquiring a company worth $10,000,000 by paying $10,000,000 in cash leaves neither the buyer nor the seller with new wealth; their portfolio compositions have merely shifted. In general, fair market transactions do not change the wealth of participating parties unless the asset is worth more when owned by one of the participating parties.

36. Having established these principles, I next move to evaluating the fair market value of Crown C Supply as of October 1, 2013.

IV. UNDER GENERALLY ACCEPTED VALUATION PRINCIPLES, THE FAIR MARKET VALUES OF THE COMPANY'S EQUITY AND CONNELLY'S COMPANY STOCK ON OCTOBER 1, 2013 WERE $6,863,819 AND $5,297,496, RESPECTIVELY

A. The Company's Purchase Obligation Should Not Be Deducted from Crown C Supply's Total Equity Value

37. Crown C Supply paid Connelly's estate $3,000,000 for 385.9 Company shares.[50] This purchase was necessitated by the 2001 Agreement, which states, "[i]n the event that all of the Deceased Stockholder's Shares are not purchased by the other Stockholders, then the Company shall and must purchase from the Legal Representative and the Legal Representative must sell to the Company all of the Deceased Stockholder's Shares that are not purchased by the Remaining Stockholders."[51]

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[50] Exhibit N, Sale and Purchase Agreement Dated November 13, 2013, p. 1 Plaintiff's Response to U.S. RFA No. 52.

[51] Exhibit C, Amended and Restated Stock Purchase Agreement (C000310-C000332), Article V, (C000319).

38. The payment from Crown C Supply to Connelly's estate was compensation for a transfer of Company shares, an equity asset. As such, this payment represents a payment to equity rather than a non-equity claim, and the price should have reflected the fair market valuation principles for equity valuation described above.

39. Importantly, a proper valuation should include all the assets before calculating the residual value held by the equity holders. The Anders Minkler Report excludes an asset, approximately $3 million of the insurance proceeds, before estimating the total equity value of Crown C Supply, leading to an undervaluation of Connelly's Company shares. In the next section I correct the Anders Minkler Report's estimate of value to arrive at a fair market value of Connelly's Company shares.

B. Accounting for the Full Value of the Insurance Proceeds Received, 385.9 Shares Of Crown C Supply Were Worth $5,297,496 on October 1, 2013

40. The Anders Minkler Report concludes that Crown C Supply's equity—i.e., 100% of the Company shares—was worth $3,863,819 as of October 1, 2013.[52] This value includes $503,915 in life insurance proceeds the Company

[52] Exhibit L, Anders Minkler Report (C000613-C000640) at Exhibit 6 (C000640). See the line item "Fair Market Value of Equity On A Controlling, Non-Marketable Basis As Of October 1, 2013." I have not evaluated the value conclusion of this report aside from its treatment of the life insurance proceeds received tied to Connelly's death. At the direction of counsel, I accept all other considerations as fair estimations throughout this report.

received upon Connelly's death, but excludes an approximate $3,000,000 of these same life insurance proceeds.[53] As discussed above, the purchase of Connelly's shares was payment on an equity claim, and thus should not be subtracted from the estimate of its equity value.

41. The proper valuation of the Company's equity should include the full $3,503,894.74 of life insurance proceeds the Company received upon Connelly's death—both the $503,915 included in the Anders Minkler report and the roughly $3,000,000 excluded amount. Thus, beginning with the value of the Company's shares estimated by the Anders Minkler Report (the "Anders Minkler Estimated Company Equity Value") and adding in the excluded insurance proceeds increases Crown C Supply's total equity value from $3,863,819 to $6,863,819 on October 1, 2013.[54] Accounting for this correction, Connelly's 77.18% equity ownership in Crown C Supply was worth $5,297,496 as of October 1, 2013.[55]

42. One way to confirm whether Connelly's shares were worth $5,297,496 is to test whether parties other than Crown C Supply would have paid this price. I examine this question by determining: (1) how much Thomas A. Connelly would have paid for his brother's Company

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[53] The Company received $3,503,894.74 in life insurance proceeds as a consequence of Connelly's death (*see* footnote 5 above) and approximately $500,000 in proceeds were included and labeled as "Retained by Company." The difference, implicitly, is the amount which was spent repurchasing stock from Connelly's estate. Exhibit N, Sale and Purchase Agreement Dated November 13, 2013, p. 1; Exhibit D, Crown C Supply Company, Inc. and Subsidiary, Consolidated Financial Statements, for the years ended September 30, 2012 and 2013 (C000413).

[54] $6,863,819 = $3,863,819 + $3,000,000.

[55] $5,297,496 = $6,863,819 x 0.7718.

shares; and (2) the price an unrelated third-party buyer would have been willing to pay for all of Crown C Supply's shares.

1. If Thomas A. Connelly Had Purchased Connelly's Shares on October 1, 2013, the Fair Market Value Would Have Been $5,297,496

43. Under the 2001 Agreement, Thomas A. Connelly held the right of first refusal to purchase Connelly's shares.[56] If Thomas A. Connelly had elected to purchase Connelly's 77.18% equity interest in the Company, this would have eliminated the Company's obligation to purchase Connelly's shares.[57] In this hypothetical scenario, it is readily apparent that Crown C Supply's equity value was $6,863,819. Crown C Supply would have still received the entire $3,503,894.74 of life insurance proceeds—this insurance payment was not contingent on Thomas A. Connelly's share purchase decisions—but the Company would not have been obligated to purchase any of Connelly's

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[56] Exhibit C, Amended and Restated Stock Purchase Agreement (C000310-C000332), Article V (C000318-C000319).

[57] The person owning all of the Company shares (regardless of the actual number of shares), whether Thomas A. Connelly or a hypothetical third-party purchaser, had complete control over the $3,000,000 of insurance proceeds at issue. That 100% owner could have either: (1) left the 2001 Agreement in place, whereby the Company would have purchased the 385.9 shares for $3,000,000; or (2) terminated the Company's repurchase obligation under Article XII of Exhibit C, Amended and Restated Stock Purchase Agreement (C000325) and caused the Company to distribute the $3,000,000 of insurance proceeds. In either situation, the 100% owner would have owned $6,863,819 of assets—$3,000,000 cash and 100% of the Company that Anders Minkler valued at $3,863,819. A similar situation is discussed in Section IV.B.2.

shares. Based on the Anders Minkler Report, the Company's equity value was $6,863,819 in this scenario.[58] Therefore, if Thomas A. Connelly had elected to directly purchase his brother's 385.9 shares, a fair price for those shares would have been $5,297,496.[59]

44. Figure 2 illustrates this hypothetical transaction. The depiction in Section "A" of Figure 2 captures the ownership interest of Crown C Supply after Connelly's death, but before any sale of Connelly's Company shares. Connelly owned 77.18% of the Company, and Thomas A. Connelly owns the remaining 22.82%. Without any repurchase obligation, the Anders Minkler Report's Company equity value would be $6,863,819, making Thomas A. Connelly's initial interest worth $1,566,323.[60] The illustration in Section "B" of Figure 2 captures the transfer of shares and the resulting ownership, whereby Thomas A. Connelly would have paid $5,297,496 for Connelly's 385.9 Company shares, giving Thomas A. Connelly full equity ownership of Crown C Supply, which was worth $3,863,819 without the excluded insurance proceeds, and control of the $3,000,000 of insurance proceeds that the Anders Minkler Report excluded.

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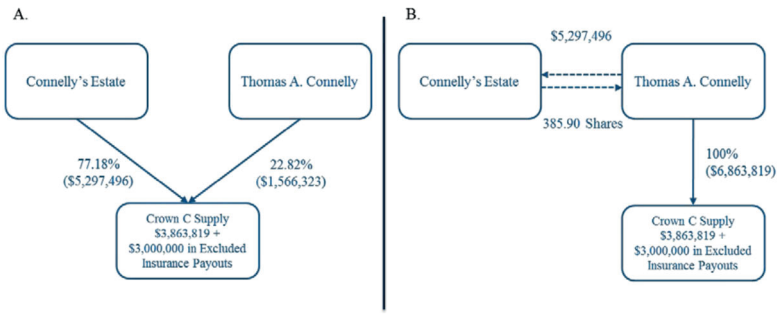
[58] *See* footnote 54 above.

[59] $5,297,496 = $6,863,819 x 77.18%.

[60] $1,566,323 = $6,863,819 x 0.2282.

Figure 2: Thomas A. Connelly's Potential Purchase of 385.9 Shares



45. Note that this hypothetical transaction satisfies all of the principles of equity valuation described above. It takes into account the fair market value of all of the Company's assets. The residual value subtracts out all non-equity claims from firm value and is distributed to all common equity holders. Thus, no shares are worth more than any other.[61] Finally, we can also see that Thomas A. Connelly's economic wealth is unchanged by the purchase. Before the purchase, he had a $1,566,323 interest in the company and $5,297,496 in cash,[62] totaling $6,863,819.[63] After the purchase, he has a 100% interest in $6,863,819 of Company equity, but no longer holds the $5,297,496 in cash. That is, at a price of $5,297,496 the transaction would not

[61] In this transaction, all shares are worth $13,727.64 each: $13,727.64 ≈ $1,566,323 / 114.10; $13,727.64 ≈ $5,297,496 / 385.90; and $13,727.64 ≈ $6,863,819 / 500.

[62] Here I use cash as a simplification for assets available to purchase Crown C Supply; in reality Thomas A. Connelly could have used cash, sold assets, or borrowed money to finance the purchase of Crown C Supply.

[63] Note that this only includes Thomas A. Connelly's personal holdings related to the Company.

have increased or decreased the value of Thomas A. Connelly's economic position, consistent with the baseball card example above. Similarly, the $5,297,496 price would not create nor destroy wealth for Connelly's estate; a $5,297,496 interest in the Company would be exchanged for $5,297,496 in cash. Because this exchange would not transfer wealth between the Company Shareholders, it is consistent with the third equity valuation principle and thus a fair market value exchange. In contrast, a $3,000,000 purchase price (instead of a $5,297,496 purchase price) would have shifted $2,297,496 in wealth from Connelly's estate to Thomas A. Connelly.[64] In other words, Thomas A. Connelly's economic position would have increased by $2,297,496 because he would have started with $1,566,323 of Company shares and $3,000,000 in cash,[65] totaling $4,566,323, but ended with a 100% interest in the Company worth $6,863,819.[66]

46. In both this hypothetical scenario and the actual transaction, Connelly's estate transfers all of its equity interest for cash and Thomas A. Connelly becomes the sole equity holder of the Company. However, in the actual transaction, Connelly's estate transferred its stock to the Company for $3,000,000, leaving Thomas A. Connelly with the only remaining outstanding shares and, as a consequence, 100% equity ownership of Crown C Supply.[67] In

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[64] $2,297,496 = $5,297,496 – $3,000,000.

[65] Again, I use cash as a simplification for assets available to purchase Crown C Supply; in reality Thomas A. Connelly could have used cash, sold assets, or borrowed money to finance the purchase of Crown C Supply.

[66] $2,297,496 = $6,863,819 – $4,566,323.

[67] Of course, in this scenario Thomas A. Connelly owns 114.1 shares of Crown C Supply which in turn owns the remaining 385.9 shares.

principle, since these two scenarios transfer the same equity interest, the fair market value of the transfer should be the same. That is, the share price should not depend upon which Thomas A. Connelly-controlled entity pays for the shares—the Company, which at the close of the transaction he fully owned, or Thomas A. Connelly himself from his personal wealth. Only a price of $5,297,496 for Connelly's stake reconciles both transactions. Therefore, the fair market value for the 77.18% equity interest in Crown C Supply was $5,297,496 on October 1, 2013.

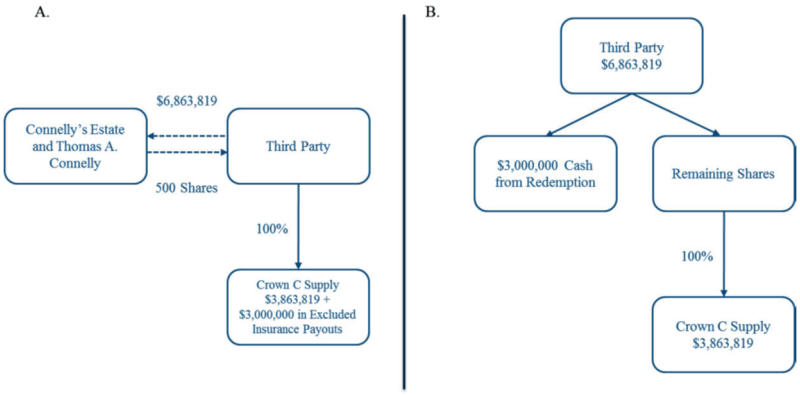
2. If an Unrelated Third Party Had Purchased All of Crown C Supply's Shares, the Fair Market Value Would Have Been $6,863,819

47. Another way to confirm that the fair market value of Crown C Supply's equity should include the full value of the insurance proceeds is to consider the perspective of a third-party buyer and what the buyer would have willingly paid for all of the Company Shareholders' equity interests. To examine this, I consider a third-party buyer's perspective in purchasing all of the Company Shareholders' interests in Crown C Supply, without affecting any repurchase obligations (i.e., after Connelly's death but before the Company purchased his shares). For simplicity, this scenario assumes that Company Shareholders' interests are transferred without any modification, the third-party receives all 500 outstanding shares, and the Company subsequently purchases the Connelly shares for $3,000,000.

48. Using the corrected equity value, the third party would have transferred $6,863,819 in cash in exchange for the 500 Company shares (i.e., all equity interests in the Company), including the shares held by Connelly's estate that the Company was required to purchase. Assuming

the third party did not modify the 2001 Agreement,[68] and the Company (which at this point is fully owned by the third party) purchased the 385.9 shares that Connelly previously owned, the third party would have received $3,000,000 from the Company. After selling those shares back to the Company, the third party would still own a company worth $3,863,819 according to the Anders Minkler Report, but also have $3,000,000 in cash. That is, based on the Anders Minkler Report, the Company Shareholders' equity interests in the Company would produce $6,863,819 in value for a third party. *See* Figure 3. Consequently, if a third party had purchased all equity interests in the Company for only $3,863,819, it would have received a $3,000,000 windfall from the sale at the expense of the Connelly brothers.[69]

Figure 3: Outcome of a Hypothetical Third-Party Sale



[68] Exhibit C, Amended and Restated Stock Purchase Agreement (C000310-C000332), Article XII (C000325). The owner of all Company stock can terminate the agreement.

[69] $3,000,000 = $6,863,819 – $3,863,819.

49. Like this hypothetical third party, the Company Shareholders (i.e., the Connelly brothers) extracted $6,863,819 of total value from Crown C Supply. In the observed transaction, Connelly's estate received $3,000,000 in cash as payment for its shares and Thomas A. Connelly received full equity control of a company which, after deducting the cost of the $3,000,000 payment, was worth an estimated $3,863,819. In combination, these recoveries total $6,863,819. Consequently, at the correct price, this hypothetical third-party transaction does not make any party worse off. Any price greater or less than $6,863,819 would be incorrect because it would violate equity valuation principles by making one party worse off.

50. Despite this, the Anders Minkler Report suggests that the Company Shareholders' combined equity in the Company was only $3,863,819. The difference between the hypothetical $3,863,819 valuation and the actual $6,863,819 valuation does not reflect an underlying change in the Company's fair market value; it reflects the fact that the Anders Minkler Report excluded approximately $3,000,000 in non-operating assets which belonged to the Connelly brothers as equity owners of the Company. Since the Anders Minkler Company Equity Value does not reflect all of the cash flows and residual value the Company Shareholders had the right to receive as a consequence of their equity ownership, it does not reflect the fair market value of their equity.

C. Deducting the Value of Insurance Proceeds Leads to a Price Which Fails to Capture the Full Equity Value Of Crown C Supply

51. The analyses above demonstrate that, following standard valuation principles, the at-issue shares were worth $5,297,496 and that the corresponding share price

would have been the only acceptable fair market value in both of the alternative transactions: direct purchase by Thomas A. Connelly and direct purchase by an unrelated third party. In both of the hypothetical scenarios, a price of $3,000,000 for 385.9 shares does not reflect the fair market value of the shares being transferred.

52. Indeed, the methodology for arriving at a $3,000,000 purchase price for the 385.9 shares is flawed and in violation of equity valuation principles. First, the actual transaction transferred significant wealth from Connelly's estate to Thomas A. Connelly, an outcome which is not consistent with the equity valuation principles and which demonstrates that it did not occur at a fair market value. Second, applying the same logic in a hypothetical where both Company Shareholders die simultaneously shows that allowing the estates to deduct share repurchase expense from a company's equity value leads to an impossible scenario of a company with residual value but no shares or shareholders.

1. Selling the Shares for $3,000,000 Produced a Windfall for Thomas A. Connelly

53. The $3,000,000 price that the Company paid to purchase Connelly's shares is problematic because it created a windfall for Thomas A. Connelly, even based on the Anders Minkler Estimated Company Equity Value. That is, accepting an estimated Company equity value of $3,863,819 leads to a stock repurchase agreement which creates a substantial transfer of wealth from one brother to another. Based on the Anders Minkler Estimated Company Equity Value, Connelly's estate and Thomas A. Connelly owned shares worth $2,982,095 and $881,723, respectively. However, after the Company purchased Connelly's 385.9 shares, Thomas A. Connelly, without any personal investment, became the sole equity owner of a

company with an estimated equity value of $3,863,819.[70] Based on these numbers, the Company's stock repurchase increased the value of Thomas A. Connelly's portfolio by $2,982,095 *under the assumptions of Anders Minkler Report*.[71] There is no reasonable explanation for this increase to Thomas A. Connelly's portfolio because the Company's repurchase of Connelly's shares should have reduced the total value of the Company equity and left the value of Thomas A. Connelly's shares unchanged, assuming the Company's shares were correctly priced. This increase, however, to Thomas A. Connelly's portfolio is a consequence of Anders Minkler excluding $3,000,000 of Company assets in its equity valuation.

54. Analyzing Thomas A. Connelly's position using a corrected equity value of $6,863,819 similarly demonstrates that the $3,000,000 purchase price created a windfall for Thomas A. Connelly. Applying the corrected Company equity value of $6,863,819, Thomas A. Connelly's shares were initially worth $1,566,323.[72] After the Company purchased Connelly's shares for the below market price, Thomas A. Connelly held shares worth $3,863,819, for an increase of $2,297,496.[73] That is, regardless of whether an analyst relies on the Anders Minkler Estimated Company Equity Value or the corrected Company equity value of $6,863,819, a $3,000,000 purchase price for

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[70] According to the Anders Minkler Report, Crown C Supply's ongoing operations and non-operating assets, excluding approximately $3,000,000 in insurance proceeds, were worth a collective $3,863,819 on October 1, 2013.

[71] $2,982,095.50 = $3,863,819 – $881,723.50.

[72] $1,566,323 = $6,863,819 x 0.2282.

[73] $2,297,496 = $3,863,819 – $1,566,323.

Connelly's shares creates a windfall for Thomas A. Connelly.

55. Thomas A. Connelly received a windfall because the Company underpaid for Connelly's shares, causing a decline in value of the Connelly estate's portfolio of at least $2,297,496.[74] This violates the third principle of equity valuation, since the transfer makes Thomas A. Connelly better off and Connelly's estate worse off. An unrelated, well-informed party would not willingly agree to this decrease in portfolio value, suggesting $3,000,000 cannot be the fair market value for Connelly's shares.

2. Accepting a Deduction for Share Repurchase Obligations Leads to an Illogical Result when All Stock is Repurchased

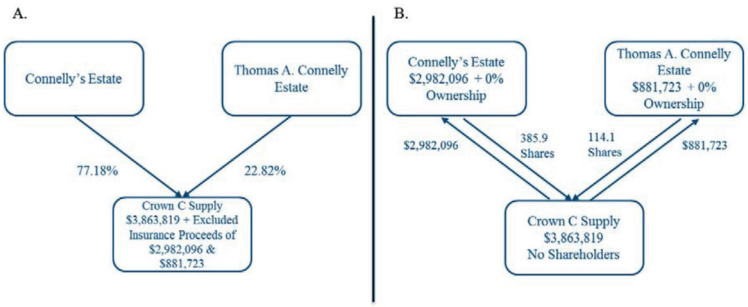
56. In the observed transaction, approximately $3,000,000 in insurance proceeds were excluded from the equity valuation in connection with a stock repurchase. This type of exclusion, when applied to all equity repurchases as in the hypothetical transaction described below, leads to an outcome which violates the principles of equity valuation.

57. To demonstrate the problem caused by allowing the exclusion, I consider a scenario in which (1) the Company has a $3,863,819 equity value (i.e., the Anders Minkler Estimated Equity Value) prior to receiving any insurance proceeds; and (2) the Company owns life insurance policies which will pay out proceeds equal to each

[74] At a corrected Company equity value of $6,863,819, Connelly's estate sells shares worth $5,297,496 for $3,000,000.

brother's pro rata interest in the Company's pre-insurance equity.[75] Further, this scenario assumes that Crown C Supply plans to repurchase the Company Shareholders shares using these insurance proceeds upon their death, much the way the Company purchased Connelly's shares in the actual transaction. Figure 4 depicts this scenario.

Figure 4: Hypothetical Scenario with Simultaneous Repurchase



58. In this scenario, if both Company Shareholders were to die simultaneously, Crown C Supply would receive $3,863,819 in insurance proceeds and use just this amount to repurchase *both* brothers' shares in the Company. As depicted in Section "A" of Figure 4, including the insurance proceeds in the valuation suggests the Company is worth $7,727,638.[76] If equity prices were based on

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[75] The actual Anders Minkler Report $3,863,819 valuation includes $458,083 which may represent the cash value of life insurance for Thomas A. Connelly. For simplicity and ease of illustration, I assume in the hypothetical scenario that the $3,863,819 excludes life insurance proceeds and that the proceeds paid exactly equal the calculated equity value.

[76] $7,727,638 = $3,863,819 + $2,982,095.50 + $881,723.50. These values represent the assumed equity value excluding any insurance

a valuation which deducts any repurchase obligations from the Company's equity value, in line with the Anders Minkler Report, Crown C Supply would use only $3,863,819 to repurchase the Company Shareholders' shares. Connelly's 385.9 shares would be repurchased for $2,982,095.50, and Thomas A. Connelly's 114.1 shares would be repurchased for $881,723.50.[77] In this scenario, all outstanding equity in the Crown C Supply would be repurchased, leaving the Company with no owners. However, as depicted in Section "B" of Figure 4, Crown C Supply, without any shareholders, would still have an ongoing equity value of $3,863,819, since insurance proceeds alone were sufficient to cover any cash required by the repurchases that occurred at prices that did not reflect the fair market value of the shares.

59. This outcome violates the second principle of equity valuation discussed above—the equity owners do not recover all residual value after all non-equity claims have been paid. This reflects the fundamental problem that arises if funds earmarked for share repurchase obligations are excluded from equity values. Share repurchases are one method through which common equity owners recover their investment in a company; excluding share repurchases reliably undervalues a company's equity because it ignores a portion of the equity value owners should recover.

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proceeds, the insurance proceeds from Connelly's life insurance policy, and the insurance proceeds from Thomas A. Connelly's life insurance policy, respectively.

[77] $2,982,095.50 = $3,863,819 x 0.7718. $881,723.50 = $3,863,819 x 0.2282.

D. Deducting the Value of Insurance Proceeds Violates Equity Valuation Principles

60. Accepting the Anders Minkler Estimated Company Equity Value violates all three valuation principles laid out in Section III above. The first principle is that valuation of the firm needs to take into account all assets. The $3,863,819 Anders Minkler Estimated Company Equity Value violates this principle by excluding approximately $3,000,000 of life insurance proceeds. Specifically, the Anders Minkler Report adds $503,915 to its equity value for Crown C Supply, noting these funds as "Life Insurance Proceeds Retained by Company (Michael Connelly)."[78] Including life insurance proceeds in valuing a firm is consistent with the principle that non-operating assets are added to estimates of operating value to calculate the fair market value of a firm or its equity. However, including only a portion of Crown C Supply's life insurance proceeds is not consistent with fair market valuation.

61. The second principle is that common equity is the residual claim after all other obligations have been satisfied, where the fair market value of each owner's claim is proportional to the number of shares held. The $3,000,000 in insurance proceeds is a company asset excluded by the Anders Minkler Report in connection with a common equity purchase. The insurance payment is a new asset owned by the equity holders, who should divide it based on their ownership shares. The purchase of the 385.9 shares for $3,000,000 equals a per share price of $7,774.[79]

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[78] Exhibit L, Anders Minkler Report (C000613-C000640) at Exhibit 6 (C000640).

[79] $7,774 ≈ $3,000,000 / 385.9.

Thomas A. Connelly's 114.1 shares retained the remaining $3,863,819 of Company equity, which comes out to $33,863 per share.[80] This result—excluding assets from calculated equity values and having some Company shares allegedly worth 336% more than the price of identical shares—violates this second principle.

62. Finally, the third principle is that transactions that occur at fair market value do not make any of the participants worse off. Because the 385.9 shares were undervalued relative to the full equity value of the company, under the Anders Minkler Report approach, Connelly's estate was made worse off as a result of this transaction. Indeed, Thomas A. Connelly's boon described in Section IV.C.1 came fully at the expense of Connelly's estate. Because one party was made worse off in this transaction, it did not occur at fair market value and thus violated the third principle described above.

V. CONCLUSION

63. The Anders Minkler Report valued Crown C Supply's equity at $3,863,819 on October 1, 2013, excluding approximately $3,000,000 in insurance proceeds held by the Company from the Company's equity value. Excluding these proceeds is inconsistent with equity valuation principles and undervalues Crown C Supply's equity by the same $3,000,000, since these insurance proceeds represented an asset which is recoverable by the Company's equity owners. Correcting this omission leads to a $6,863,819 equity value for Crown C Supply, implying the 77.18% interest owned by Connelly's estate was worth $5,297,496 on October 1, 2013. I can confirm this corrected equity value is the fair market value because unlike the

[80] $33,863 ≈ $3,863,819 / 114.1.

$3,863,819 original valuation, this valuation does not violate the rules of equity valuation. It takes into account all the assets of the Company, it takes into account the full residual value and values all common shares equally, and transactions based on this value do not cause a transacting party to suffer a wealth loss.

I declare under penalty of perjury that the foregoing is true and correct. 28 U.S.C. § 1746(2). Executed in Boston, Massachusetts, on this 18th day of December, 2020.

/s/ Evan K. Cohen
Evan K. Cohen

UNITED STATES COURT OF APPEALS
FOR THE EIGHTH CIRCUIT

No. 21-3683

THOMAS A. CONNELLY, IN HIS CAPACITY AS EXECUTOR OF THE ESTATE OF MICHAEL P. CONNELLY, SR.,
PLAINTIFF-APPELLANT

v.

UNITED STATES OF AMERICA, DEPARTMENT OF TREASURY, INTERNAL REVENUE SERVICE,
DEFENDANT-APPELLEE

Filed: June 2, 2023

Before: SMITH, Chief Judge, GRUENDER and STRAS, Circuit Judges.

OPINION

GRUENDER, Circuit Judge.

Brothers Michael and Thomas Connelly were the sole shareholders of a corporation. The corporation obtained life insurance on each brother so that if one died, the corporation could use the proceeds to redeem his shares. When Michael died, the Internal Revenue Service assessed taxes on his estate, which included his stock inter-

est in the corporation. According to the IRS, the corporation's fair market value includes the life insurance proceeds intended for the stock redemption. Michael's estate argues otherwise and sued for a tax refund. The district court[1] agreed with the IRS, and so do we.

I.

Before Michael died, he and Thomas owned Crown C Corporation, a building-materials company in St. Louis. Michael owned 77.18 percent of the 500 shares outstanding (385.9 shares); Thomas owned 22.82 percent (114.1 shares). To provide for a smooth transition of ownership upon either's death, the brothers and Crown together entered into a stock-purchase agreement. If one brother died, the surviving brother had the right to buy his shares. If the surviving brother declined, Crown itself had to redeem the shares. In this way, control of the company would stay within the family. The brothers always intended that Crown, not the surviving brother, would redeem the other's shares.

The stock-purchase agreement provided two mechanisms for determining the price at which Crown would redeem the shares. The principal mechanism required the brothers to execute a new Certificate of Agreed Value at the end of every tax year, which set the price per share by "mutual agreement." If they failed to do so, the brothers were supposed to obtain two or more appraisals of fair market value. The brothers never executed a Certificate of Agreed Value or obtained appraisals as required by the stock-purchase agreement. At any rate, to fund the redemption, Crown purchased $3.5 million of life insurance on each brother.

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[1] The Honorable Stephen R. Clark, Chief Judge, United States District Court for the Eastern District of Missouri.

After Michael died in 2013, Crown received the life insurance proceeds and redeemed his shares for $3 million. The actual redemption transaction was part of a larger, post-death agreement between Thomas and Michael's son, Michael Connelly, Jr., resolving several estate-administration matters. No appraisals were obtained pursuant to the stock-purchase agreement. Instead, the Connellys declared that they had "resolved the issue of the sale price of [Michael's] stock in as amicable and expeditious [a] manner as is possible" and that they "have agreed that the value of the stock" was $3 million. That figure effectively valued Crown, based on Michael's 77.18 percent share, at $3.89 million. The rest of the proceeds, about $500,000, went to fund company operations.

Thomas is the executor for Michael's estate. In 2014, the estate filed a tax return reporting that Michael's shares were worth $3 million. To value the shares, Thomas relied solely on the redemption payment, rather than treating the life insurance proceeds as an asset that increased the corporation's value and hence the value of Michael's shares. All told, this resulted in an estate tax of about $300,000, which was paid.

The IRS audited the estate's return. It concluded that the estate had undervalued Michael's shares by simply relying on the $3 million redemption payment instead of determining the fair market value of Crown, which should include the value of the life insurance proceeds. Taking the proceeds into account, Crown was worth $3 million more than the estate had determined—about $6.86 million.[2] So according to the IRS, just before redemption,

[2] This figure comes from the IRS's own valuation of Michael's interest in Crown plus the $3 million in proceeds used for redemption. The IRS independently determined that Michael's shares were worth

Michael's estate actually had a 77.18 percent stake in a $6.86 million company—worth about $5.3 million. As a result, the IRS sent a notice of deficiency to the estate for $1 million in additional tax liability. The estate paid the deficiency and sued for a refund. *See* 26 U.S.C. § 7422; 28 U.S.C. § 1346(a)(1).

The estate claims that the redemption transaction, made in furtherance of the stock-purchase agreement, determined the value of Crown for estate-tax purposes, so there is no need to conduct a fair-market-value analysis. Alternatively, the estate argues that Crown's fair market value should not include the life insurance proceeds used to redeem Michael's shares because, although the proceeds were an asset, they were immediately offset by a liability—the redemption obligation. In other words, the proceeds added nothing to Crown's value. By contrast, the IRS argues that the stock-purchase agreement should be disregarded and that any calculation of Crown's fair market value must account for the proceeds used for redemption.

The district court granted summary judgment to the IRS. The court first concluded that the stock-purchase agreement did not affect the valuation. The court then determined that a proper valuation of Crown must include the life insurance proceeds used for redemption because they were a significant asset of the company. In doing so, the district court declined to follow *Estate of Blount v.*

$2,982,000 exclusive of the proceeds. At Michael's 77.18 percent share, that represents a company value of $3.86 million—slightly less than the $3.89 million figure arrived at by deeming Michael's shares to be worth $3 million as the redemption transaction effectively did. Because the estate does not challenge this *sans*-proceeds value on appeal, we accept it for our purposes. In any event, it does not affect the issue of how to treat the life insurance proceeds used for stock redemption.

Commissioner, 428 F.3d 1338 (11th Cir. 2005), relying instead on the tax code, Treasury regulations, and customary valuation principles. The estate appeals.

II.

A federal tax applies to the transfer of a decedent's estate, which comprises the gross estate minus applicable deductions. 26 U.S.C. §§ 2001, 2051; *Comm'r v. Est. of Hubert*, 520 U.S. 93, 99-100 (1997). A decedent's gross estate includes "the value at the time of his death of all property, real or personal, tangible or intangible, wherever situated" in which he had an interest. §§ 2031(a), 2033. Property includes stocks. *See* 26 C.F.R. §§ 20.2031-1, 20.2031-2. For Michael's gross estate, the only issue on appeal is the value of his Crown shares.

The parties dispute whether Crown's value, and hence the value of Michael's shares, should include the life insurance proceeds used for redemption. If not, then the estate is entitled to a refund. If the proceeds should be included, as the district court determined, then the IRS is correct and summary judgment was proper. With this in mind, we review the district court's grant of summary judgment *de novo*. *Westerman v. United States*, 718 F.3d 743, 746 (8th Cir. 2013). In refund actions, "[t]he [IRS's] determination of a tax deficiency is presumptively correct, and the taxpayer bears the burden of proving that the determination is arbitrary or erroneous." *Day v. Comm'r*, 975 F.2d 534, 537 (8th Cir. 1992).

We first consider whether the stock-purchase agreement controls how the company should be valued. Finding that it does not, we then consider whether a fair-market-value analysis of Crown must include the life insurance proceeds used for redemption. It must.

A.

Generally, the value of any property for tax purposes is determined "without regard to any option, agreement, or other right to acquire . . . the property at a price less than the fair market value" or to "any other restriction on the right to sell or use such property." 26 U.S.C. § 2703(a). These sorts of agreements are commonly used by closely held corporations to keep control among a small group of people. *See* 3 James D. Cox & Thomas Lee Hazen, *Treatise on the Law of Corporations* § 18:13 (3d ed. Dec. 2022 update). Section 2703(a) tells us to ignore these agreements unless they meet the criteria in subsection (b). Under § 2703(b), to affect valuation, the agreement must (1) be a bona fide business arrangement, (2) not be a device to transfer property to members of the decedent's family for less than full and adequate consideration, and (3) have terms that are comparable to other similar arrangements entered into in arm's length transactions. Here, the estate argues that we should look to the stock-purchase agreement to value Michael's shares because it satisfies these criteria.

But the estate glosses over an important component missing from the stock-purchase agreement: some fixed or determinable price to which we can look when valuing Michael's shares. After all, if § 2703 tells us when we may "regard" agreements to acquire stock "at a price less than the fair market value," we naturally would expect those agreements to say *something* about value in a definite or calculable way. *See Est. of Lauder v. Comm'r*, 64 T.C.M. (CCH) 1643, 1656 (1992) ("It is axiomatic that the offering price must be fixed and determinable under the agreement."); *see also Est. of Amlie v. Comm'r*, 91 T.C.M. (CCH) 1017, 1027 (2006) (reviewing the comparability of *price terms* to determine whether the agreement satisfied

§ 2703(b)(3)). Otherwise, why look to the agreement to value the shares?

Further, the Treasury regulation that clarifies how to value stock subject to a buy-sell agreement refers to the *price* in such agreements and "[t]he effect, if any, that is given to the . . . price in determining the value of the securities for estate tax purposes." 26 C.F.R. § 20.2031-2(h). The regulation also states that "[l]ittle weight will be accorded a price" in an agreement where the decedent was "free to dispose of" the securities at any price during his lifetime. *Id.* Courts thus recognize that an agreement must contain a fixed or determinable price if it is to be considered for valuation purposes. *Est. of Blount v. Comm'r*, 428 F.3d 1338, 1342 (11th Cir. 2005); *Est. of True v. Comm'r*, 390 F.3d 1210, 1218 (10th Cir. 2004); *Est. of Gloeckner v. Comm'r*, 152 F.3d 208, 213 (2d Cir. 1998); *see also St. Louis Cnty. Bank v. United States*, 674 F.2d 1207, 1210 (8th Cir. 1982) (describing when restrictive buy-sell agreements "may *fix the value* of property for estate-tax purposes" (emphasis added)). Congress enacted § 2703 against the backdrop of 26 C.F.R. § 20.2031-2(h), which has remained substantially unchanged, and courts have since interpreted the two in tandem. *See Amlie*, 91 T.C.M. (CCH) at 1024 ("[R]egardless of whether section 2703 applies to a restrictive agreement, the agreement must satisfy the requirements of pre-section-2703 law to control value for Federal estate tax purposes."); *Blount*, 428 F.3d at 1343 n.4 ("[C]ourts generally agree that the limitation in . . . § 2703 should be read in conjunction with the court-created rule."); *True*, 390 F.3d at 1231 (describing § 2703 as "essentially codif[ying] the rules laid out in § 20.2031-2(h)" that had existed before § 2703 was added in 1990).

We need not resolve the precise contours of what counts as a fixed or determinable price because, wherever

that line may be, the stock-purchase agreement here falls short given that the brothers and Crown ignored the agreement's pricing mechanisms. It suffices for our purposes to think of a determinable price as one arrived at by "formula," *see Gloeckner*, 152 F.3d at 213, as by a "fair, objective measure," *see Lauder*, 64 T.C.M. (CCH) at 1659, or "calculation," *see True*, 390 F.3d at 1213.

Here, the stock-purchase agreement fixed no price nor prescribed a formula for arriving at one. It merely laid out two mechanisms by which the brothers might agree on a price. One was the Certificate of Agreed Value, which appears to be nothing more than price by "mutual agreement"—essentially, an agreement to agree. The other was an appraisal process for determining the fair market value of Crown. Although this second mechanism seems to carry more objectivity, there is nothing in the stock-purchase agreement, aside from minor limitations on valuation factors, that fixes or prescribes a formula or measure for determining the price that the appraisers will reach. Instead, the agreement required only that the appointed appraisers "independently determine and submit" their "appraisal[s] of the fair market value of the Company." The brothers were then supposed to average the results or consult a third appraiser as a tiebreaker. None of this was ever done. *See St. Louis Cnty. Bank*, 674 F.2d at 1211 (noting that upon death, the provisions of the stock-purchase agreement were not invoked and that post-death conduct may be relevant to understanding the nature of the agreement). Thus, "under the circumstances of th[is] particular case," neither price mechanism constituted a fixed or determinable price for valuation purposes. *See* 26 C.F.R. § 20.2031-2(h). If anything, the appraisal mechanism calls for a rather ordinary fair-market-value analysis, which § 2031 and § 2073(a) essentially

require anyway. Nothing therefore can be gleaned from the stock-purchase agreement.[3]

Thomas tries to get around this problem by directing us to the price fixed by the redemption transaction—the $3 million that Crown actually paid for Michael's shares. In his view, this is an appropriate valuation because the redemption transaction links back to the stock-purchase agreement and was done pursuant to it. We are not convinced. For one, the $3 million price was chosen *after* Michael's death. *See* 26 U.S.C. § 2031(a) (requiring that value be determined "at the time of [the decedent's] death"); *True*, 390 F.3d at 1218 (noting that "the terms of the agreement [must be] binding throughout life and death"). And second, the $3 million price came not from the mechanisms in the stock-purchase agreement but rather from Thomas and Michael Connelly, Jr.'s "amicable agreement" resolving outstanding estate-administration matters. Thus, Crown's value must be determined "without regard" to the stock-purchase agreement. *See* § 2703(a).

B.

We now consider the fair market value of Michael's shares. The key question is whether the life insurance proceeds received by Crown and intended for redemption

[3] The estate does not argue that the stock-purchase agreement otherwise controls the fair market value of Crown by virtue of its restriction on the transfer of shares (i.e., through non-price-related means). *Compare* § 2703(a)(2), *with* § 2703(a)(1). And even if we understood the estate to make this argument, we find it indistinguishable from the estate's fair-market-value argument that we address in Part II.B below.

should be taken into account when determining the corporation's value at the time of Michael's death.[4] Two principles guide the analysis. The first deals with valuing property in general, and the second addresses companies whose stock prices cannot be readily determined from an exchange, as is the case with closely held corporations.

Generally, the value of property in the gross estate is "the price at which the property would change hands between a willing buyer and a willing seller, neither being under any compulsion to buy or to sell and both having reasonable knowledge of relevant facts." 26 C.F.R. § 20.2031-1(b); *see also United States v. Cartwright*, 411 U.S. 546, 551 (1973) ("The willing buyer-willing seller test of fair market value is nearly as old as the federal income, estate, and gifts taxes themselves. . . .").

To this end, for closely held corporations, the share value "shall be determined by taking into consideration, in addition to all other factors, the value of stock or securities of corporations engaged in the same or a similar line of business which are listed on an exchange." 26 U.S.C. § 2031(b). Treasury regulations have interpreted this as a "fair market value" analysis. 26 C.F.R. § 20.2031-2(a). The fair market value depends on the company's net worth, prospective earning power and dividend-paying capacity, and other relevant factors like "the good will of

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[4] We focus on this moment in time—after Michael's death but before his shares are redeemed. *See Bright's Est. v. United States*, 658 F.2d 999, 1006 (5th Cir. 1981) (en banc) ("[T]he estate tax is an excise tax on the transfer of property at death and accordingly . . . the valuation is to be made as of the moment of death and is to be measured by the interest that passes, as contrasted with the interest held by the decedent before death or the interest held by the legatee after death."). Regardless of the timing, no one argues that the proceeds were ever in doubt. Crown expected to receive $3.5 million from the policy, most of which would be used to buy Michael's shares.

the business; the economic outlook in the particular industry; the company's position in the industry and its management; [and] the degree of control of the business represented by the block of stock to be valued." 26 C.F.R. § 20.2031-2(f)(2); *see also Est. of Huntsman v. Comm'r*, 66 T.C. 861, 876 (1976) ("[W]e . . . determine the fair market value of the decedent's stock . . . by applying the customary principles of valuation . . . .").

Setting aside for the moment the life insurance proceeds used to redeem Michael's shares, so far as Crown's operations, revenue streams, and capital are concerned, we know its value—about $3.86 million. *See supra* n.2.

But in valuing a closely held corporation, "consideration shall also be given to nonoperating assets, including proceeds of life insurance policies payable to or for the benefit of the company, to the extent such nonoperating assets have not been taken into account in the determination of net worth, prospective earning power and dividend-earning capacity." 26 C.F.R. § 20.2031-2(f)(2). This need to "take[] into account" life insurance proceeds appears again in a nearby regulation, 26 C.F.R. § 20.2042-1(c)(6). That regulation clarifies 26 U.S.C. § 2042, which has to do with life insurance proceeds that go to beneficiaries other than the decedent's estate. Understanding the relationship between § 2031 (defining the gross estate) and § 2042, along with their corresponding regulations, helps further illuminate what it means to "take[] into account" life insurance proceeds.

Section 2042 says that the value of a decedent's gross estate includes life insurance proceeds received directly by the estate as well as proceeds received by other beneficiaries under insurance policies in which the decedent "possessed at his death any of the incidents of ownership." For example, if Michael obtained a life insurance policy

for the benefit of Crown, the value of that policy's proceeds would be included in Michael's gross estate. *See* § 2042(2). Yet here, Crown obtained the policy for its own benefit.

Now, there might be a plausible argument that under § 2042 Michael possessed "incidents of ownership" in the life insurance policy through his controlling-shareholder status. If that were the case, then § 2042 would *require* that Michael's gross estate include the proceeds used for his stock redemption. But that is not the case. Treasury regulation § 20.2042-1(c)(6) clarifies that a decedent does not possess the "incidents of ownership" described in § 2042 merely by virtue of being a controlling shareholder in a corporation that owns and benefits from the policy.

Still, although § 2042 does not require that the proceeds be included here, it does not *exclude* them either. We are cautioned to "[s]ee § 20.2031-2(f) for a rule providing that the proceeds of certain life insurance policies shall be considered in determining the value of the decedent's stock." 26 C.F.R. § 20.2042-1(c)(6). Thus, although the life insurance proceeds intended for redemption do not directly augment Michael's gross estate by way of § 2042, they may well do so indirectly through a proper valuation of Crown. Indeed, the $500,000 of proceeds *not* used to redeem shares and which simply went into Crown's coffers undisputedly increased Crown's value according to the principles in § 2031 and 26 C.F.R. § 20.2031-2(f)(2).

We must therefore consider the value of the life insurance proceeds intended for redemption insofar as they have not already been taken into account in Crown's valuation and in light of the willing buyer/seller test. In this sense, the parties agree that this case presents the same fair-market-value issue as *Estate of Blount v. Commissioner*, 428 F.3d at 1345-46, from the Eleventh Circuit.

But they disagree on whether *Blount* was correctly decided. Like here, *Blount* involved a stock-purchase agreement for a closely held corporation. Although the court referenced the requirement in 26 C.F.R. § 20.2031-2(f)(2) that proceeds be "taken into account," it concluded that the life insurance proceeds *had* been accounted for by the redemption obligation, which a willing buyer would consider. 428 F.3d at 1345. In balance-sheet terms, the court viewed the life insurance proceeds as an "asset" directly offset by the "liability" to redeem shares, yielding zero effect on the company's value.[5] The court summarized its conclusion with an appeal to the willing buyer/seller concept: "To suggest that a reasonably competent business person, interested in acquiring a company, would ignore a $3 million liability strains credulity and defies any sensible construct of fair market value." *Id.* at 1346.

Like the estate in *Blount*, Thomas argues that life insurance proceeds do not augment a company's value where they are offset by a redemption liability. In his view, the money is just passing through and a willing buyer and seller would not account for it. The IRS counters that this assumption defies common sense and customary valuation principles, as reflected in Treasury regulations.

The IRS has the better argument. *Blount*'s flaw lies in its premise. An obligation to redeem shares is not a

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[5] *Blount* cited favorably the Ninth Circuit's decision in *Estate of Cartwright v. Commissioner*, 183 F.3d 1034, 1038 (9th Cir. 1999), which employed similar reasoning. Like the Eleventh Circuit in *Blount*, the Ninth Circuit's analysis was limited—one paragraph citing 26 C.F.R. § 20.2031-2(f)(2) and the tax-court decision in *Estate of Huntsman v. Commissioner*, 66 T.C. at 875, which merely emphasized that life insurance proceeds are to be considered according to § 20.2031-2(f)(2).

liability in the ordinary business sense. *See* 6A Fletcher Cyclopedia of the Law of Corporations § 2859 (Sept. 2022 update) ("The redemption of stock is a reduction of surplus, not the satisfaction of a liability.").

Treating it so "distorts the nature of the ownership interest represented by those shares." *See Est. of Blount v. Comm'r*, 87 T.C.M. (CCH) 1303, 1319 (2004), *aff'd in part and rev'd in part*, 428 F.3d at 1338. Consider the willing buyer at the time of Michael's death. To own Crown outright, the buyer must obtain all its shares. At that point, he could then extinguish the stock-purchase agreement or redeem the shares *from himself*. This is just like moving money from one pocket to another. There is no liability to be considered—the buyer controls the life insurance proceeds. A buyer of Crown would therefore pay up to $6.86 million, having "taken into account" the life insurance proceeds, and extinguish or redeem as desired. *See* 26 C.F.R. § 20.2031-2(f)(2). On the flip side, a hypothetical willing seller of Crown holding all 500 shares would not accept only $3.86 million knowing that the company was about to receive $3 million in life insurance proceeds, even if those proceeds were intended to redeem a portion of *the seller's own shares*. To accept $3.86 million would be to ignore, instead of "take[] into account," the anticipated life insurance proceeds. *See id.*

To further see the illogic of the estate's position, consider the resulting windfall to Thomas. If we accept the estate's view and look to Crown's value exclusive of the life insurance proceeds intended for redemption, then upon Michael's death, each share was worth $7,720 before redemption.[6] After redemption, Michael's interest is extinguished, but Thomas still has 114.1 shares giving him

[6] $3.86 million divided by 500 shares.

full control of Crown's $3.86 million value. Those shares are now worth about $33,800 each.[7] Overnight and without any material change to the company, Thomas's shares would have quadrupled in value.[8] This view of the world contradicts the estate's position that the proceeds were offset dollar-by-dollar by a "liability." A true offset would leave the value of Thomas's shares undisturbed. *See* Cox & Hazen, *supra*, § 21:2 ("When a corporation purchases its own stock, it has depleted its assets by whatever amount of money or property it gave in exchange for the stock. There is, however, an increase in the proportional interest of the nonselling shareholders in the remaining assets of the corporation."). In sum, the brothers' arrangement had nothing to do with corporate liabilities. The proceeds were simply an asset that increased shareholders' equity. A fair market value of Michael's shares must account for that reality.

III.

For the foregoing reasons, we affirm the district court's grant of summary judgment to the IRS.

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[7] $3.86 million divided by 114.1 shares.

[8] No one has argued that Michael's death and Thomas's subsequent sole ownership of Crown accounts for such an increase. *Cf. Huntsman*, 66 T.C. at 879 ("The decedent was the dominant force in both businesses, and his untimely death obviously reduced the value of the stock in the two corporations.").

UNITED STATES DISTRICT COURT
EASTERN DISTRICT OF MISSOURI

No. 4:19-cv-01410-SRC

THOMAS A. CONNELLY, IN HIS CAPACITY AS EXECUTOR OF THE ESTATE OF MICHAEL P. CONNELLY, SR.,
PLAINTIFF(S)

v.

THE UNITED STATES OF AMERICA, DEPARTMENT OF THE TREASURY, INTERNAL REVENUE SERVICE,
DEFENDANT(S)

Filed: September 21, 2021

MEMORANDUM AND ORDER

CLARK, United States District Judge.

Brothers Michael and Thomas Connelly were the only shareholders in Crown C Supply, Inc., a closely-held family business that sold roofing and siding materials. As is typical in family businesses, the brothers entered into a stock purchase agreement that required the company to buy back the shares of the first brother to die, and the company bought life insurance to ensure it had enough cash to make good on the agreement. When Michael died in October 2013, Crown C repurchased his shares for $3 million, and Michael's Estate paid estate taxes on his

shares in Crown C. But the IRS assessed additional estate taxes of over $1 million. Thomas, as executor of Michael's Estate, paid the deficiency and filed this suit seeking a refund. At the core of the dispute lies the question of the proper valuation of Crown C on the date of Michael's death.

Aside from the life-insurance proceeds, Crown C was worth roughly $3.3 million on the date of Michael's death. On that date, Crown C had an obligation to repurchase Michael's shares from his Estate. Also on that date, Crown C received (or was about to receive) a cash infusion of $3.5 million from the life-insurance proceeds; without these proceeds, Crown C would have had to deplete its assets or borrow money (or both) to buy Michael's shares.

The parties dispute whether the portion of the life-insurance proceeds used to buy Michael's shares must be included in the value of the company for estate-tax purposes. Both parties moved for summary judgment on this issue and moved to exclude each other's expert witnesses. Because on the date of death, Crown C was entitled to receive the life-insurance proceeds to fund the purchase of Michael's shares, the Court holds that Crown C was worth roughly $3.5 million more than it was worth the day before Michael's death.

I. FACTS AND BACKGROUND

A. Undisputed Material Facts

Crown C sells roofing and siding materials in the St. Louis area. Doc. 58 at ¶ 10. Before his death, Michael[1] was the President, CEO, and majority shareholder. *Id.* at ¶ 9. The Connelly brothers together owned all of Crown

[1] The Court refers to the Connelly brothers by their first names to differentiate between them, not to imply familiarity.

C's 500 shares, with Michael owning 385.90 shares (77.18%) and Thomas owning 114.10 shares (22.82%). *Id.* at ¶ 11-12.

The Connelly brothers and Crown C signed a Stock Purchase Agreement (the "Stock Agreement") in 2001, to maintain family ownership and control over the company and to satisfy their estate-planning objectives. *Id.* at ¶¶ 13-14. The Stock Agreement provided that upon one brother's death, the surviving brother had the right to buy the decedent's shares, but the Stock Agreement required Crown C itself to buy (i.e., redeem) the deceased brother's shares if the surviving brother chose not to buy them. *Id.* at ¶ 15. When the brothers signed the Stock Agreement, they always intended that Crown C, not the surviving brother, would redeem the deceased brother's shares. *Id.* at ¶ 16.

To fund its redemption obligation, Crown C bought $3.5 million in life-insurance policies on both Connelly brothers. *Id.* at ¶¶ 17-22. Article VII of the Stock Agreement provided two mechanisms for determining the price at which Crown C would redeem the shares. *Id.* at ¶ 23. Article VII specified that the brothers "shall, by mutual agreement, determine the agreed value per share by executing a new Certificate of Agreed Value" at the end of every tax year. *Id.* at ¶ 24; Doc. 53-4, Art. VII., Sec. A-B. If the brothers failed to execute a "Certificate of Agreed Value[,]" the brothers would determine the "Appraised Value Per Share" by securing two or more appraisals.[2]

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[2] Article VII, Section C of the Agreement sets forth a comprehensive appraisal process:

> For the purposes hereof, the "Appraised Value Per Share" of the Company shall be determined as follows: If the Certificate of Agreed Value is more than eighteen (18) months old,

within ten (10) days after the date an option is exercised or a mandatory purchase is required ("Appraisal Date"), the transferring Stockholder or his successor in interest shall appoint an appraiser and the Company or purchasing Stockholder(s), as the case may be, shall appoint an appraiser. Both appraisers shall have at least five (5) years of experience in appraising businesses similar to the Company. If either party fails to name such an appraiser within the specified time, the other party may upon five (5) days written notice to the failing party, select the second appraiser. Each appraiser shall independently determine and submit to the parties, in writing, with reasons therefor, an appraisal of the fair market value of the Company. The appraisers shall take into consideration the goodwill of the Company in determining the fair market value of the Company. The appraisers shall not take into consideration premiums or minority discounts in determining their respective appraisal values. Upon receipt by the parties of both appraisals, if the fair market value of the Company is determined to be the same or if the difference between the appraisals is less than ten percent (10%) of the lower of the appraised values, then the fair market value of the Company shall be the average of the two appraisals. If the appraisals so submitted differ by more than ten percent (10%) of the lower of the appraised values, the accounts then servicing the Company shall appoint a third appraiser. The third appraiser so appointed shall, as promptly as possible, determine the value of the Company on the same basis as set forth, and that prior appraisal which is closer in value to such third appraisal shall, thereupon, be the appraisal which is binding on all parties in interest hereunder. The "Appraised Value Per Share" shall equal the amount determined by dividing the binding appraisal by the total number of Shares of the Company issued and outstanding as of the Appraisal Date. Each party shall pay the fee and expenses of the appraiser selected by such party and the fee of the third appraiser shall be borne equally by the parties appointing the two appraisers.

Doc. 53-4.

Doc. 53-4, Art. VII., Sec. A, C. The Connelly brothers never signed a single Certificate of Agreed Value under the Stock Agreement. Doc. 58 at ¶¶ 25-36.

Upon Michael's death on October 1, 2013, Crown C received about $3.5 million in life-insurance proceeds. *Id.* at ¶ 39. Thomas chose not to buy Michael's shares, so Crown C used a portion of the life-insurance proceeds to buy Michael's shares from Michael's Estate. *Id.* at ¶ 16, 39-40. Crown C and the Estate did not obtain appraisals for the value of Michael's shares under the Stock Agreement, instead entering a Sale and Purchase Agreement (the "Sale Agreement") for the price of $3 million. *Id.* at ¶¶ 37-38, 64. Through the Sale Agreement, (1) the Estate received $3 million in cash; (2) Michael P. Connelly, Jr., Michael's son, secured a three-year option to purchase Crown C from Thomas for $4,166,666; and (3) in the event Thomas sold Crown C within 10 years, Thomas and Michael Jr. agreed to split evenly any gains from the future sale.[3] *Id.* at ¶¶ 64-66.

Thomas, as executor of Michael's Estate, filed an estate-tax return valuing Michael's Crown C shares at $3 million as of October 1, 2013 and included that amount in the taxable estate. *Id.* at ¶ 70. The IRS audited the Estate, challenging the $3 million value of Michael's Crown C shares. *Id.* at ¶ 71. The IRS determined that as of October 1, 2013, the fair market value of Crown C should have included the $3 million in life-insurance proceeds used to redeem the shares, resulting in a higher value for Michael's Crown C shares than reported on the Estate's return. *Id.* at ¶ 40, 82. The IRS issued a Notice of Deficiency, assessing over $1 million in additional estate taxes.

[3] For purposes of distinguishing father and son, the Court refers to the decedent/father as "Michael" and son as "Michael P. Connelly, Jr." or "Michael Jr."

Id. at ¶ 82; Doc. 1 at ¶¶ 8-9, 16. During the IRS audit, the Estate obtained a calculation of value report on Crown C's fair market value from Anders Minkler Huber & Helm, LLP. Doc. 1 at ¶ 15. And in May 2019, Thomas filed this suit on behalf of the Estate, seeking a refund of over $1 million. *See id.* at ¶ 5.

The parties stipulated that, if the Estate is due a federal-estate-tax refund, for the purpose of determining the amount of such refund, the fair market value of Michael's Crown C shares was $3.1 million as of October 1, 2013. Doc. 48. The stipulation expressly leaves aside the dispute over how to account for the life-insurance proceeds used to redeem Michael's shares, so the stipulation only controls the value of Crown C exclusive of those life-insurance proceeds. *Id.*; Doc. 71 at 31-33.

B. Experts

1. The Estate's expert, Kevin P. Summers

Kevin P. Summers is a CPA and a partner at accounting firm Anders Minkler Huber & Helm, LLP. Doc. 55-1 at p. 1. Summers offered an opinion on the proper fair market value of Crown C as of the date of Michael's death. *See id.* He stated that the Stock Agreement created "an enforceable contractual obligation to use the life-insurance proceeds to purchase [Michael] Connelly's stock in Crown C Supply" upon Michael's death. *Id.* at p. 11. Relying on the Eleventh Circuit's holding in *Estate of Blount*, Summers opined that the life-insurance proceeds used to redeem Michael's shares should be excluded from the fair market value of Crown C. *See id.* at pp. 11-12 (citing *Estate of Blount v. Comm'r*, 428 F.3d 1338, 1342-43 (11th Cir. 2005)). Summers advised that the IRS improperly disregarded Crown C's obligation to redeem Michael's shares under *Estate of Blount* and that the IRS's

decision was inconsistent with "common business sense." Doc. 55-1 at p. 14. Summers concluded that inclusion of the insurance proceeds in Crown C's fair market value resulted in an overstated value for Crown C by $3 million, as well as an inflated estate-tax bill for Michael's estate. *Id.*

2. The IRS's expert, Evan K. Cohen

Evan K. Cohen is a Charted Financial Analyst and a principal at an economic consulting firm, Brattle Group. Doc. 53-19 at ¶ 1. Cohen offered an opinion on the fair market value of Crown C and Michael's shares as of the date of Michael's death. *Id.* at ¶ 10. Cohen stated that "[i]n a fair market equity valuation, the insurance proceeds would be included in the value of Crown C Supply as a non-operating asset." *Id.* at ¶ 11. He opined that allowing the redemption obligation to offset the insurance proceeds "undervalues Crown C Supply's equity, undervalues [Michael's] equity interest in Crown C Supply (i.e., his shares), and violates well-established equity valuation principles because the resultant share price creates a windfall for a potential buyer that a willing seller would not accept." *Id.* at ¶ 12. Cohen concluded that the fair market value of Crown C was $6.86 million, rather than $3.86 million, a $3 million difference. *Id.* at ¶ 63.

II. STANDARD

Summary judgment is proper if the evidence, viewed in the light most favorable to the nonmoving party, demonstrates no genuine issue of material fact exists and the moving party is entitled to judgment as a matter of law. Fed. R. Civ. P. 56(c); *Cordry v. Vanderbilt Mortg. & Fin., Inc.*, 445 F.3d 1106, 1109 (8th Cir. 2006) (citing *Bockelman v. MCI Worldcom, Inc.*, 403 F.3d 528, 531 (8th Cir. 2005)).

Here, the parties agree that no disputed material facts exist and that the Court should decide the case on the cross motions without a trial. Docs. 45, 51, and 66. The Court may decide a case as a matter of law when there are no disputed issues of fact. *See* Fed. R. Civ. P. 56(a); *see also Sprint Communications Company v. Bernsten*, 152 F. Supp. 3d 1144, 1150 (S.D. Iowa Dec. 30, 2015) ("Because there is no genuine dispute of fact in this case, the Court must determine which movant is entitled to judgment as a matter of law."); *Essick Air Products, Inc. v. Crane USA Inc.*, 2018 WL 9963828, at *1 (E.D. Ark. July 12, 2018) (granting summary judgment where the parties agreed that there were no material factual disputes). The Court held argument on April 8, 2021. Doc. 70.

In a tax refund action under 28 U.S.C. § 1346(a)(1), the district court must determine the plaintiff's tax liability. *Lewis v. Reynolds*, 284 U.S. 281, 283, *modified,* 284 U.S. 599 (1932). The district court must make a *de novo* determination as to whether the plaintiff is entitled to a federal-estate-tax refund. *See, e.g.*, *Blansett v. United States*, 283 F.2d 474, 478 (8th Cir. 1960). The notice of tax deficiency carries a presumption of correctness, requiring the taxpayer to demonstrate that the deficiency is incorrect. *See Lesser v. United States*, 368 F.2d 306, 310 (2d Cir. 1966) (en banc). The taxpayer bears the burden of persuading the trier of fact that the assessment is incorrect. *Pizzarello v. United States*, 408 F.2d 579, 583 (2d. Cir.), *cert. denied*, 396 U.S. 986 (1969).

III. DISCUSSION

Congress imposes a federal estate tax on a decedent's taxable estate. *See* 26 U.S.C. § 2001. The estate tax is a property tax levied on the taxable estate a decedent transfers at death. *See* 26 U.S.C. §§ 2001(a), 2033; *see also Estate of McClatchy v. Comm'r*, 147 F.3d 1089, 1091 (9th Cir.

1998). A decedent's taxable estate is the value of a decedent's gross estate, minus all authorized deductions. *See* 26 U.S.C. § 2051. The decedent's gross estate includes the decedent's "property, real or personal, tangible or intangible," as of the decedent's date of death, as defined by statutes and regulations. *See* 26 U.S.C. §§ 2031(a), 2033; 26 C.F.R. § 20.2031-1(b). The value of the gross estate "shall be determined by including . . . the value at the time of his death of all property, real or personal, tangible or intangible, wherever situated[,]" as further fleshed out in the Internal Revenue Code. 26 U.S.C. § 2031(a). Treasury regulations provide that the "value of stocks . . . is the fair market value per share . . . on the applicable valuation date." 26 C.F.R. § 20.2031-2(a).

The parties dispute the value of Crown C, and of Michael's shares, as of the date of Michael's death. The Estate argues that the Stock Agreement determines the value of Crown C for estate-tax purposes, so the Court need not determine Crown C's fair market value. Doc. 46 at 7. The Estate also argues, alternatively, that Crown C's fair market value does not include $3 million of the life-insurance proceeds, because the Stock Agreement created an offsetting $3 million obligation for Crown C to redeem Michael's shares. *Id.* at 4.

The IRS disagrees, arguing that the Stock Agreement fails to meet the requirements under the Code, Treasury regulations, and applicable caselaw to control the valuation of Crown C, and that under applicable law and customary valuation principles, the life-insurance proceeds used to redeem Michael's shares increased Crown C's fair market value by $3 million. Doc. 52 at 5; Doc. 61 at 4.

A. Stock Agreement

The value of the taxable estate is the fair market value of the decedent's property at the date of death. 26 U.S.C. §§ 2031(a), 2033; 26 C.F.R. § 20.2031-1(b); *see also United States v. Cartwright*, 411 U.S. 546, 550-51 (1973). Under 26 U.S.C. § 2703(a), the IRS generally determines the fair market value of any property without regard to a buy-sell agreement, but certain kinds of buy-sell agreements fall under an exception to this general rule. *See* 26 U.S.C. § 2703(b); *St. Louis County Bank v. United States*, 674 F.2d 1207, 1210 (8th Cir. 1982); *Estate of True v. Comm'r*, 390 F.3d 1210, 1218 (10th Cir. 2004).

To control the value of a decedent's property for estate-tax purposes, a buy-sell agreement must meet the three statutory requirements of 26 U.S.C. § 2703(b): "(1) [i]t is a bona fide business arrangement[;] (2) [i]t is not a device to transfer such property to members of the decedent's family for less than full and adequate consideration in money or money's worth[; and] (3) [i]ts terms are comparable to similar arrangements entered into by persons in an arms' length transaction." 26 U.S.C. § 2703(b); *see also* 26 C.F.R. § 25.2703-1(b). As developed in caselaw and embodied in Treasury Regulation 26 C.F.R. § 20.2031-2(h), a buy-sell agreement must also meet several additional requirements: (1) the offering price must be fixed and determinable under the agreement; (2) the agreement must be legally binding on the parties both during life and after death; and (3) the restrictive agreement must have been entered into for a bona fide business reason and must not be a substitute for a testamentary disposition for less than full-and-adequate consideration. *Estate of True*, 390 F.3d at 1218 (citing 26 C.F.R. § 20.2031-2(h)); *see also St. Louis County Bank*, 674 F.2d at 1210. The effect of a buy-sell agreement's offering

price "in determining the value of the securities for estate-tax purposes depends upon the circumstances of the particular case." 26 C.F.R. § 20.2031-2(h).

The parties dispute whether the Stock Agreement meets all of the requirements necessary to determine the valuation of Crown C's shares for purposes of estate-tax valuation. If it doesn't meet all of the requirements, then the fair market value of the shares will determine the valuation. *See* 26 C.F.R. §§ 25.2703-1(b)(2); 20.2031-2(h). The Estate urges that the Stock Agreement meets all of the requirements, Doc. 46 at p. 7, while the IRS argues that "(1) the price of [Michael's] Company stock is not determinable from the Stock Purchase Agreement; (2) the Stock Purchase Agreement's terms were not binding throughout [Michael's] life and after his death; (3) the Stock Purchase Agreement is not a bona fide business arrangement and its terms are not comparable to similar arrangements that have been negotiated at arms' length; and (4) the Stock Purchase Agreement is an impermissible substitute for a testamentary disposition [that] transferred . . . wealth to [Michael's] family[.]" Doc. 64 at p. 6.

The Court begins by observing that the Estate's arguments all turn on the same premise. The Estate argues that the company sold Michael's shares at fair market value, Doc. 65 at p. 7, which in turn relies on the assumption that the Estate's valuation expert correctly valued Michael's shares. The Estate's valuation expert, Kevin P. Summers, excluded $3 million in life-insurance proceeds from the valuation, presuming that the Eleventh Circuit's decision in *Estate of Blount* controls. Doc. 55-1 at pp. 11-12. And, even though the parties to the Sale Agreement did not value Michael's shares using the valuation mechanisms set forth in Article VII of the Stock Agreement, the Estate nonetheless argues that the very

existence of the Stock Agreement—the parties' failure to adhere to it notwithstanding—provides sufficient basis for the Court to accept Thomas and the Estate's *ad hoc* valuation as the proper estate-tax value of Michael's shares. Doc. 46 at pp. 8-9. For the reasons explained below, the Court rejects this premise but nonetheless first analyzes whether the Stock Agreement fits into the buy-sell-agreement exception to the fair-market-valuation rule. The Court begins by analyzing the statutory requirements in 26 U.S.C. § 2703(b), and then the additional requirements from 26 C.F.R. § 20.2031-2(h) and applicable caselaw. *See Estate of True*, 390 F.3d at 1218.

1. Statutory requirements in 26 U.S.C. § 2703(b)

a. Bona fide business arrangement

The IRS argues that the Stock Agreement is not a bona fide business arrangement, so it should not control the value of Michael's stock. Doc. 61 at pp. 10-11. The IRS admits that the Connelly brothers entered into the Stock Agreement to ensure their family continued to own Crown C and to satisfy certain estate-planning objectives but argues that these purposes do not, by themselves, make the Stock Agreement a bona fide business arrangement. *Id.* at p. 10. The IRS explains that the Connelly brothers did not genuinely follow the Stock Agreement in good faith. *Id.* Specifically, the IRS points to the Connelly brothers' disregard for the pricing mechanisms set out in Article VII of the Stock Agreement as well as Michael Jr.'s retained interest in Crown C's future sale under the Sale Agreement. *Id.* at pp. 10-11.

"The ultimate question of whether there was a bona fide business arrangement is a question of fact[.]" *See*

Holman v. Comm'r, 601 F.3d 763, 769 (8th Cir. 2010) (citing *Estate of True*, 390 F.3d at 1218-19). Courts have recognized the validity of agreements to maintain family ownership and control over closely-held businesses. *St. Louis Cty. Bank*, 674 F.2d at 1210. To establish that the Stock Agreement was a bona fide business *arrangement*, the Estate needed only to show that the Connelly brothers entered the Stock Agreement for a bona fide business *purpose*. *See id.* ("We have no problem with the District Court's findings that the stock-purchase agreement . . . had a bona fide business purpose—the maintenance of family ownership and control of the business."); *Estate of Lauder v. Comm'r*, 1992 WL 386276, *21 (T.C. 1992) (buy-sell agreements had a bona fide business purpose because the "agreements, on their face, serve the legitimate business purpose of preserving family ownership and control of the various Lauder enterprises. We are persuaded that these concerns were a motivating factor in the Lauders' decision to enter into the agreements."); *Estate of Gloeckner v. Comm'r*, 152 F.3d 208, 214 (2d Cir. 1998) ("[W]e agree with the tax court that the Gloeckner agreement represents a bona fide business arrangement. This test is sufficiently satisfied when the purpose of a restrictive agreement is to maintain current managerial control—whether by family or outsiders.").

The parties here have stipulated that the Connelly brothers entered the Stock Agreement for the purpose of ensuring continued family ownership over Crown C. Doc. 47 at ¶¶ 1-3. The IRS does not provide any support for its contention that the Estate's actions taken after Michael's death alter the purpose of the Stock Agreement, making it no longer a bona fide business arrangement. Doc. 61 at p. 12. Based on the parties' stipulation, the Court deems the Stock Agreement a bona fide business arrangement for purposes of summary judgment.

Assuming that the IRS could explain its position in light of its stipulation to the business purpose of the Stock Agreement, the "bona fide business arrangement" issue would otherwise have to be resolved by the factfinder at trial. *See Holman*, 601 F.3d at 769. Even so, resolution of this issue is ultimately unnecessary because the Stock Agreement fails to meet the other requirements under 26 U.S.C. § 2703(b).

b. Device to transfer property to family for less than full-and-adequate consideration

The IRS argues that the Stock Agreement is a device to transfer wealth to Michael's family members for less than full-and-adequate consideration. Doc. 61 at pp. 7-9. The IRS states that the $3 million redemption price is not full-and-adequate consideration because the price did not account for all of the insurance proceeds, allowing Thomas to obtain a financial windfall at the expense of Michael's Estate. *Id.*

For a buy-sell agreement to control the value of property for estate-tax purposes, it must not be a substitute for a testamentary disposition, ensuring that transactions between family members reflect full-and-adequate consideration. *See* 26 C.F.R. § 25.2703-1(b)(4) (price must be comparable to what an unrelated third party would pay, taking into account fair market value); *Estate of Lauder*, 1992 WL 386276, *21 (plaintiff must demonstrate full-and-adequate consideration in money or money's worth). The existence of a bona fide business purpose does not exclude the possibility that a buy-sell agreement is a testamentary device. 26 C.F.R. § 25.2703-1(b)(2); *see also St. Louis County Bank*, 674 F.2d at 1210. Further, "intrafamily agreements restricting the transfer of stock in a closely held corporation must be subjected to greater scrutiny

than that afforded similar agreements between unrelated parties." *Estate of Lauder*, 1992 WL 386276, *20 (citing *Dorn v. United States*, 828 F.2d 177, 182 (3d Cir. 1987)); *see also Hoffman v. Comm'r*, 2 T.C. 1160, 1178-1179 (T.C. 1943), *affd. sub nom. Giannini v. Comm'r*, 148 F.2d 285 (9th Cir. 1945) ("[T]he fact that the option is given to one who is the natural object of the bounty of the [decedent] requires substantial proof to show that it rested upon full-and-adequate consideration.").

Despite the legitimate business purpose of the Stock Agreement, the Estate bears the burden of proving that the Stock Agreement was not also a device to pass Crown C shares to members of the Connelly family for less than full-and-adequate consideration. *See Estate of Lauder*, 1992 WL 386276, *21. The Estate asserts that the Stock Agreement was not a testamentary device because (1) Crown C redeemed Michael's shares for fair market value, as established by the parties' stipulation to the value of Michael's shares, (2) the Stock Agreement was binding, because Crown C redeemed Michael's shares, and (3) the Connelly brothers were in good health when they executed the Stock Agreement. Doc. 65 at p. 7.

The Estate failed to show that the Stock Agreement was not a device to transfer wealth to Michael's family members for less than full-and-adequate consideration. First, the $3 million redemption price was not full-and-adequate consideration. The parties' stipulation explicitly left aside the life-insurance issue when it otherwise agreed to the $3.1 million fair market value of Michael's Crown C shares. Doc. 48. Therefore, the stipulation only aids the Estate if the Court finds that the fair market value excludes the $3 million in life-insurance proceeds used to redeem Michael's shares. In other words, the $3

million redemption price is only equivalent to the fair market value of the shares ***if*** the Court were to find that the $3 million in life-insurance proceeds are not included in Crown C's value. As discussed in section III.B.1 below, the Court follows the reasoning from the Tax Court in *Estate of Blount*, so the life-insurance proceeds are included in Crown C's fair market value. *Estate of Blount v. Comm'r*, 2004 WL 1059517, at *26 (T.C. 2004), a*ff'd in part, rev'd in part on other grounds*, 428 F.3d 1338 (11th Cir. 2005).

Second, even though Crown C fulfilled the purpose of the agreement by redeeming Michael's shares, Thomas and the Estate's process in selecting the redemption price indicates that the Stock Agreement was a testamentary device. *See Estate of Gloeckner*, 152 F.3d at 216 ("[C]ourts scrutinize the processes employed in reaching the share price contained within the redemption agreement to shed light on the nature of the relationship between the decedent and the person to whom the stock was conveyed.") (citing *Estate of Lauder*, 1992 WL 386276, *21-22 and *Cameron W. Bommer Revocable Trust v. C.I.R.*, 1997 WL 473161, at *13 (T.C. 1997)). Thomas and the Estate excluded a significant asset (the life-insurance proceeds) from the valuation of Crown C, failed to obtain an outside appraisal or professional advice on setting the redemption price, Doc. 58 at ¶¶ 23-38; Doc. 51 at p. 4, and as discussed further below, disregarded the appraisal requirement in Article VII of the Stock Agreement, *see* Section III.A.2.a-b, *infra*. *See also Estate of Lauder*, 1992 WL 386276, *21-22 (exclusion of major intangible assets, absence of a formal appraisal, and failure to obtain professional advice may mean the agreement is a testamentary device); *St. Louis County Bank*, 674 F.2d at 1211 (lack of regular enforcement of the buy-sell agreement's terms

may mean the agreement is a testamentary device); *Estate of True*, 390 F.3d at 1222 ("[W]here the price term in a buy-sell agreement is reached in an arbitrary manner, is not based on an appraisal of the subject interest, or is done without professional guidance or consultation, courts draw an inference that the buy-sell agreement is a testamentary substitute.").

Additionally, the Stock Agreement's lack of a minority discount for Thomas's shares and corresponding lack of a control premium for Michael's shares substantially overvalues Thomas's shares and undervalues Michael's shares. The Stock Agreement required that in determining the appraised value of the shareholders' shares in Crown C, "[t]he appraisers shall not take into consideration premiums or minority discounts[.]" Doc. 53-4, Art. VII., Sec. C. The Stock Agreement's lack of a control premium for Michael's majority interest indicates that the price was not full-and-adequate consideration. *See* 26 C.F.R. § 20.2031-2(f)(2) (fair market value for a corporation's stock is determined by "the company's net worth, prospective earning power and dividend-paying capacity, and other relevant factors" including "the degree of control of the business represented by the block of stock to be valued . . ."); *Bright's Estate v. U.S.*, 658 F.2d 999, 1006-7 (5th Cir. 1981) (a willing buyer would account for a controlling interest or a minority interest in a closely-held corporation); *Estate of True v. Comm'r*, 2001 WL 761280, at *100 (T.C. 2001) ("[Plaintiff's] 58.16-percent interest represented a majority of the shares entitled to vote; therefore, [Plaintiff] owned a controlling interest in Black Hills Trucking at his death. Accordingly, [the expert] should have added a control premium to compute entity value . . ."); *see also Zaiger's Estate v. Comm'r*, 64 T.C. 927, 945-46 (T.C. 1975) ("Petitioner's experts applied discounts to their valuations to reflect the minority interest

involved and to compensate for the fact that voting control would not be in the hands of the purchaser. Such considerations were proper and discounts were appropriate.").

While the Connelly brothers' good health when they executed the Stock Agreement weighs in favor of the Estate's argument, the parties' abject disregard of the Stock Agreement so as to undervalue the company and underpay estate taxes, as well as the Stock Agreement's lack of a control premium or minority discount, demonstrates that the Stock Agreement was a testamentary device to transfer wealth to Michael's family members for less than full-and-adequate consideration. *See* Section III.A.2.a-b, *infra*.[4]

c. Comparability to similar arrangements

The IRS argues that the Stock Agreement is not comparable to similar arrangements negotiated at arms' length because Thomas and the Estate did not account for the insurance proceeds in the valuation of Michael's Crown C shares and because the Stock Agreement itself undervalued Michael's 77.18% majority interest. Doc. 61 at pp. 11-12. The IRS claims that an unrelated majority shareholder operating at arms' length would not have allowed Crown C to create a windfall for a minority shareholder at the expense of the majority shareholder's estate. *Id.*

The Estate does not show that the Stock Agreement is comparable to similar agreements negotiated at arms'

[4] Were the Court to consider that the parties seemingly paved the way for Michael Jr. to purchase the company at a below-market price, it would reinforce this conclusion. But as noted in Section III.A.2.b.ii, the parties did not fully develop this point and the Court does not consider it.

length. Courts treat a contractual restriction as comparable to similar agreements if it "could have been obtained in a fair bargain among unrelated parties in the same business dealing with each other at arm's length." 26 C.F.R. § 25.2703-1(b)(4) (this determination considers factors such as "the expected term of the agreement, the current fair market value of the property, anticipated changes in value during the term of the arrangement, and the adequacy of any consideration given in exchange for the rights granted."). The question is whether, "[a]t the time the right or restriction is created, the terms of the right or restriction are comparable to similar arrangements entered into by persons in an arm's length transaction." 26 C.F.R. § 25.2703-1(b)(1)(iii); *Holman v. Comm'r*, 130 T.C. 170, 197 (T.C. 2008), *aff'd*, 601 F.3d 763 (8th Cir. 2010) ("Comparability is determined at the time the restriction is created.").

In *Blount*, the Tax Court held that to show comparability, the estate had to produce evidence "that the terms of an agreement providing for the acquisition or sale of property for less than fair market value are similar to those found in similar agreements entered into by unrelated parties at arm's length in similar businesses." *Estate of Blount*, 2004 WL 1059517, at *17 (T.C. 2004), *aff'd in part, rev'd in part on other grounds*, 428 F.3d 1338 (11th Cir. 2005); *see also Holman*, 130 T.C. at 198-99. The Tax Court relied on the text of 26 U.S.C. § 2703(b)(3), legislative history, and the text of the applicable regulations, 26 C.F.R. § 25.2703-1(b)(4).

The Court agrees with this analysis. The statutory text of 26 U.S.C. § 2703(b)(3) uses terms that require a comparison of the agreement at issue to others ("comparable to similar arrangements") and that those other

agreements must be the product of "arm's length transaction(s)." In the face of this plain text, legislative history need not be consulted, but even so, the Senate committee report supports this textual analysis. *See* 136 Cong. Rec. 15683 (Oct. 18, 1990) (discussing consideration of various factors, including "the demonstration of general practice(s) of unrelated parties," and expert testimony). The regulations also track the "general practice(s) of unrelated parties" language of the Senate committee report, and further require the showing of comparables from similar businesses. 26 C.F.R. 25.2703-(1)(b)(4).

The Estate claims that the Stock Agreement was comparable to similar arrangements negotiated at arms' length simply because the $3 million redemption price here was equal to what the Estate claims is the fair market value of Michael's shares, and because closely-held family corporations often use life-insurance proceeds to redeem a shareholder's stock. Doc. 46 at pp. 12-13. In support of its position on the fair market valuation, the Estate presents the calculation-of-value report from Anders Minkler, as well as the expert report and testimony of Kevin P. Summers. *Id.*

Even assuming that the Anders Minkler valuation and Summers's testimony were admissible in their present form, the Court does not find them persuasive. The Anders Minkler calculation of value and Summers's opinions both rely on the reasoning of the 11th Circuit opinion in *Estate of Blount*, which held that life-insurance proceeds used to redeem a stockholder's shares do not count towards the fair market value of the company when valuing those same shares. Doc. 58 at ¶¶ 73-74; Doc. 55-1 at p. 14; *see also Estate of Blount*, 428 F.3d at 1344. Thus neither valuation answers the question of whether the $3 million

price was below fair market value, and both valuations ignore the detailed valuation mechanism in the Stock Agreement. The Estate does not explain how these contra-agreement valuations have any bearing on whether the Stock Agreement or its valuation mechanism was comparable to similar arm's-length agreements.

As discussed further in section III.B.1 below, the Court includes the life-insurance proceeds in the fair market value of Crown C and of Michael's shares. Other than the Anders Minkler report and Summer's testimony, the Estate failed to provide any evidence of similar arrangements negotiated at arms' length. That closely-held family corporations generally use life-insurance proceeds to fund redemption obligations does not establish that this particular Stock Agreement was comparable to an arm's-length bargain, particularly when the $3 million valuation was so far below fair market value. Doc. 53-19 at ¶¶ 12, 45; *see also Estate of Blount*, 2004 WL 1059517, at *19 (T.C. 2004) ("[W]e assign no weight to [the expert's] testimony that the $4 million purchase price set forth in the [agreement] was a fair market price value. Accordingly, his conclusion that the [agreement] established a price comparable to those of similar arrangements entered into at arm's length by people in similar businesses is flawed.").

The Court also observes that here the Stock Agreement's prohibition of control premiums or minority discounts results in an undervalued majority interest for Michael's shares. *See* 26 C.F.R. § 20.2031-2(f)(2); Section III.A.1.b, *supra*. Thus, the Stock Agreement is not comparable to similar arrangements negotiated at arms' length.

2. Additional requirements under regulation and caselaw

a. Fixed and determinable offering price

The IRS contends that the price of Michael's Crown C shares was not fixed and determinable under the Stock Agreement because Thomas and the Estate ignored the agreement's pricing mechanisms and came up with a valuation of their own. Doc. 52 at p. 7; Doc. 61 at p. 5. The Stock Agreement required shareholders Michael and Thomas to agree on and sign "Certificates of Agreed Value" every year to establish the price-per-share; but in the 12 years the agreement was in place before Michael's death, they never agreed on the value, or created or signed such certificates. Doc. 61 at p. 5; Doc. 53-4, Art. VII., Sec. A-B. Under the Stock Agreement, the failure of the shareholders to do so triggered the obligation to obtain the Appraised Value Per Share through a very specific process involving multiple professional appraisers. Doc. 53-4, Art. VII., Sec. C. But Thomas and the Estate never followed that specific process and never determined the Appraised Value Per Share; instead, they chose to come up with their own *ad hoc* valuation of $3 million. Doc. 58 at ¶¶ 23-38; Doc. 51 at p. 4.

The Court finds that Crown C's share price was not "fixed and determinable" from the 2001 Stock Agreement. *See Estate of Lauder*, 1992 WL 386276, *18 ("Several requirements have evolved for testing whether the *formula price set forth in such restrictive agreements* is binding for purposes of the Federal estate tax. It is axiomatic that *the offering price* must be fixed and determinable under the agreement." (emphasis added)); *see also* 26 C.F.R. § 20.2031-2(h) ("The effect, if any, that is given to the op-

tion or contract price in determining the value of the securities for estate-tax purposes depends upon the circumstances of the particular case.").

The $3 million redemption price that Thomas and the Estate set forth in the Sale Agreement did not come from any formula or other provisions in the Stock Agreement, rendering the Estate's proposed share price, for estate-tax-valuation purposes, neither fixed nor determinable from the Stock Agreement. Doc. 58 at ¶¶ 23-38. The parties did not rely on a Certificate of Agreed Value or follow the detailed appraisal mechanism of the Stock Agreement to determine the price-per-share; instead, they completely disregarded the Stock Agreement and negotiated their own value, which not surprisingly was less than the value of the life-insurance proceeds. *Id.* at ¶¶ 23-38, 64-65; *see also* 26 C.F.R. § 20.2031-2(h).

The Estate argues that the mere existence of a pricing formula in the Stock Agreement satisfies the requirement that the offering price be "fixed and determinable" by the preexisting agreement. Doc. 46 at pp. 8-9 (citing *Estate of Gloeckner*, 152 F.3d at 213). But the Estate does not ask the Court to apply one of the price-setting mechanisms set out in the Stock Agreement; it wants the $3 million price to control estate-tax valuation, even though that price has no mooring in the Stock Agreement. *Id.* Further, the Estate's citation to *Estate of Gloeckner* is unpersuasive, as in *Estate of Gloeckner*, the Commissioner conceded that the buy-sell agreement at issue had a "fixed and determinable" offering price. 152 F.3d at 213 ("The Commissioner does not dispute that the restrictive agreement affecting Gloeckner's shares meets the first three requirements. That is, it concedes the stock price at issue was fixed within the redemption agreement . . .").

The Estate represented to the Court that the pricing mechanisms in the Stock Agreement are not mandatory because it "talks about situations if the parties don't agree." Doc. 71 at p. 38. This argument lacks merit. The Stock Agreement clearly states that "[t]he purchase price to be paid by the Company ***shall be*** the purchase price provided in Article VII . . ." Doc. 53-4, Art. V, Sec. B (emphasis added). The appraisal obtained by the IRS here provides some evidence that the valuation mechanism in Article VII of the Stock Agreement would have rendered a much higher valuation than $3 million, which seems motivation enough for Thomas and the Estate to disregard it. *See* Doc. 53-19 at ¶¶ 12, 45.

The Estate argues that the $3 million price "resulted from extensive analysis of Crown C's books and the proper valuation of assets and liabilities of the company. Thomas Connelly, as an experienced businessman extremely acquainted with Crown C's finances, was able to ensure an accurate appraisal of the shares." Doc. 51 at p. 4. Leaving aside Thomas's obvious self-interest in arriving at a below-market valuation, this argument reveals the frailty of the Estate's position: the Estate didn't believe that the very specific valuation mechanism in the Stock Agreement produced an accurate value that bound the Estate, but the Court should treat it as if it did. The Court finds this position as untenable as it is unpersuasive.

b. Binding during life and after death

The IRS next argues that the Stock Agreement's terms were not binding throughout Michael Connelly's life and after his death, because Michael, Thomas, and the Estate ignored their obligations under the Stock Agreement. Doc. 61 at pp. 6-7. For twelve years, Michael and Thomas failed to execute an Annual Certificate of Value

as required under the Stock Agreement; and at Michael's death, Thomas and the Estate ignored the appraisal mechanism in the Stock Agreement. Doc. 58 at ¶¶ 23-38. The IRS also argues that the Stock Agreement was not binding because Michael Jr. retained a profits interest in the company, as he and Thomas agreed to split evenly any gains from the future sale of Crown C, so the stock redemption did not actually account for Michael Sr.'s entire interest in Crown C. Doc. 61 at pp. 6-7; Doc. 52 at p. 8.

i. During life

As discussed in section III.A.2.a, above, the Stock Agreement required shareholders Michael and Thomas to agree on and sign "Certificates of Agreed Value" every year to establish the price-per-share, but they never agreed on the value, or created or signed such certificates. Doc. 61 at p. 5; Doc. 53-4, Art. VII., Sec. A-B. During life, the parties did not treat that aspect of the Stock Agreement as binding, but the Stock Agreement (for reasons unknown) anticipated that they might not comply with Certificates-of-Agreed-Value provision; accordingly, and insofar as the binding-during-life-and-death analysis goes, the Court does not find the parties' failure in this regard entirely dispositive. *See* Doc. 53-4, Art. VII., Sec. C. The Court therefore turns to the question of whether the Stock Agreement was binding after death.

ii. After death

The parties' own conduct demonstrates that the Stock Agreement was not binding after Michael's death. Thomas and the Estate failed to determine the price-per-share through the formula in the Stock Agreement. *See St. Louis County Bank*, 674 F.2d at 1210-11 (parties' post-execution conduct can determine whether the court ap-

plies the terms of a buy-sell agreement for estate-tax purposes); *Estate of Lauder*, 1992 WL 386276, *19 (allowing some minor deviations from the buy-sell agreement's terms, but finding that the family still considered the agreement's terms to be binding because the family executed formal waivers and modifications as the buy-sell agreement required). As already discussed in section III.A.2.a, Thomas and the Estate did not consider the Stock Agreement to be binding or enforceable on them; they ignored the price mechanism in Article VII and sold Michael's shares for $3 million without first obtaining any appraisals for Crown C.

The Estate argues that the appraisal process in Article VII was only meant to determine the value of the shares if the parties disagreed over the value, so the $3 million price negotiated between Thomas and the Estate still complied with the Stock Agreement. Doc. 71 at p. 38; *see also* Doc. 53-4, Art. VII., Sec. C. The Stock Agreement itself belies this argument, completely. The Stock Agreement mandates that if the surviving brother did not buy the deceased brother's shares, "the Company ***shall and must*** purchase . . . all of the Deceased Stockholder's Shares[.]" Doc. 53-4, Art. V, Sec. B (emphasis added). The Stock Agreement further states that "The purchase price to be paid by the Company ***shall*** be the purchase price provided in Article VII, the purchase price ***shall be paid*** as per the terms provided in Article VIII, and the purchase of the Shares ***shall be closed*** on the Closing Date as provided in Article IX." *Id.* (emphasis added).

The Stock Agreement does not contain an optional dispute-resolution mechanism; it uses mandatory language ("shall," and "shall and must," which in this context is redundantly mandatory). Doc. 53-4, Art. V, Sec. B. This language admits of no discretion or exception, dictating

that Crown C redeem Michael's shares, the price at which it must do so, and the timing and terms of its payment. Thomas and the Estate utterly ignored these mandatory terms, indicating if not demonstrating that the Stock Agreement was not binding after Michael's death. *See St. Louis County Bank*, 674 F.2d at 1210-11; *Estate of Lauder*, 1992 WL 386276, *19.

The Estate also argues that it negotiated a fair redemption price for Michael's shares, based on the Anders Minkler calculation of value and the stipulation with the IRS affirming the $3.1 million valuation for Crown C. Doc. 59 at pp. 4-5. But these points are not relevant to whether the Stock Agreement bound the parties. The supposed fairness of the redemption price does not mitigate Thomas and the Estate's failure to follow the pricing mechanism in the Stock Agreement. Thomas and the Estate did not consider the Stock Agreement to bind their behavior after Michael's death, so the Stock Agreement cannot control the value of Michael's Crown C shares for estate-tax purposes. *See St. Louis County Bank*, 674 F.2d at 1210-11; *Estate of Lauder*, 1992 WL 386276, *19.

The Court observes that a more likely explanation exists for parties' scrapping the Stock Agreement in favor of the after-the-fact Sale Agreement. As noted above, the evidence indicates that the valuation under the Stock Agreement's comprehensive appraisal mechanism in Article VII would have been much higher than $3 million. *See* Doc. 53-19 at ¶¶ 12, 45. Regardless of whether that is true, Thomas paid nothing to increase his ownership from 22.82% to 100% of Crown C. Doc. 58 at ¶ 65. Additionally, the *post hoc* Sale Agreement created an option for Michael Jr. to buy all of Thomas's shares at a below-market value. *Id.* at ¶¶ 64-66. If allowed, these maneuvers would effectively: a) reduce the Estate's taxes, b) increase the

amount of cash Thomas and Michael Jr. received at the time of sale, c) potentially reduce the taxes Thomas or his estate would eventually pay by setting a below-market price for Michael Jr.'s later purchase of his shares, and d) seemingly defer the larger tax bills for Thomas, Michael, Jr., and Crown C to later tax periods. *See id.*; Doc. 53-19 at ¶¶ 12, 45, 48, 52, 53-55, 61, and 62 (explaining the "windfall" to Thomas, on which Thomas presumably paid no taxes). Because the parties do not squarely address these collateral tax effects, the Court does not consider them in its analysis but simply notes them for the record.

c. Bona-fide business reason and not a substitute for a testamentary disposition for less than full-and-adequate consideration

The Court already discussed whether the Stock Agreement had a bona-fide business reason and whether it was a substitute for a testamentary disposition for less than full-and-adequate consideration, so the Court need not duplicate the analysis here. *See* Section III.A.1.a-b, *supra*; *see also Holman*, 601 F.3d at 772 (observing that *St. Louis County Bank*, 674 F.2d at 1210, set out the "bona fide business reason" and "testamentary disposition" factors, which Congress "subsequently adopted" in 26 U.S.C. § 2703(b)).

Based on the undisputed facts in the record, the Court concludes that the Stock Agreement does not establish Crown C's value for estate-tax purposes.

B. Fair market value

Because the Stock Agreement does not control the value of Michael's Crown C shares, the Court must determine the fair market value of Crown C. *See Estate of True*, 390 F.3d at 1218. Fair market value is "the price at

which the property would change hands between a willing buyer and a willing seller, neither being under any compulsion to buy or to sell and both having reasonable knowledge of relevant facts." *See* 26 C.F.R. § 20.2031-1(b). Courts determine the fair market value of property based on the willing-buyer-willing-seller test. *See* 26 C.F.R. § 20.2031-1(b); *Cartwright*, 411 U.S. at 551 ("Under this test, [it] is clear that if the decedent had owned ordinary corporate stock listed on an exchange, its 'value' for estate tax purposes would be the price the estate could have obtained if it had sold the stock on the valuation date . . ."). Fair market value of a decedent's stock is determined by applying "customary principles of valuation." *Estate of Huntsman v. Comm'r*, 66 T.C. 861, 876 (T.C. 1976). "The ultimate determination of fair market value is a finding of fact. The question of what criteria should be used to determine value is a question of law[.]" *Estate of Palmer v. C.I.R.*, 839 F.2d 420, 423 (8th Cir. 1988).

In valuing shares of closely-held businesses for which no market exists, courts consider factors such as "the company's net worth, prospective earning power and dividend-paying capacity, and other relevant factors." 26 C.F.R. § 20.2031-2(f)(2). This valuation includes the proceeds of life-insurance policies owned by the corporation: "consideration shall also be given to nonoperating assets, including proceeds of life-insurance policies payable to or for the benefit of the company, to the extent that such nonoperating assets have not been taken into account in the determination of net worth." *Id.*

The parties agree that the facts relating to Crown C's fair market value are undisputed, so the only remaining issue is how to allocate the life-insurance proceeds. Doc. 46 at 15; Doc. 61 at 16. The parties' stipulation affirms that the fair market value of Michael's shares was roughly

$3.1 million, assuming the exclusion of the life-insurance proceeds from the Crown C valuation. Doc. 48 at ¶¶ 1-3. The Estate and the IRS therefore agree that the fair market value of Crown C was approximately $3.86 million, exclusive of the $3 million in life-insurance proceeds used to redeem Michael's shares. *Id.*; Doc. 58 at ¶ 43, 79-81. The IRS claims, however, that those proceeds must be included in Crown C's value under 26 C.F.R. § 20.2031-2(f)(2), resulting in a $6.86 million fair market value for Crown C.

1. Treatment of the life-insurance proceeds

The Estate urges that the fair market value of Crown C does not include the $3 million in life-insurance proceeds at issue because those proceeds "were off-set dollar for dollar by the obligation to redeem [Michael's] shares" under the Stock Agreement. Doc. 65. According to the Estate, a hypothetical "willing buyer" of Crown C would have to account for substantial liabilities like Crown C's redemption obligation. *See, e.g., Estate of Dunn v. C.I.R.*, 301 F.3d 339, 352 (5th Cir. 2002) (the value of a corporation's assets is discounted by the corporation's capital-gains liability); *Eisenberg v. Comm'r*, 155 F.3d 50, 57 (2d Cir. 1998) (a hypothetical buyer would pay less for shares in a corporation because of the buyer's "inability to eliminate the contingent tax liability"). The Estate emphasizes that a willing buyer would pay less for a company encumbered with a stock-purchase agreement, to account for the company's future decrease in assets when fulfilling the contractual obligation. *See Estate of Blount*, 428 F.3d at 1346.

The parties agree that the facts of this case present the same fair-market-value issue as *Estate of Blount*, 2004 WL 1059517, at *26 (T.C. 2004), a*ff'd in part, rev'd in part*, 428 F.3d 1338 (11th Cir. 2005). Doc. 52 at 12; Doc. 46 at 6-

7. In *Estate of Blount*, a closely-held family company entered into a stock purchase agreement with its shareholders, intending that the company would use life-insurance proceeds to redeem a key shareholder's shares upon his death. 428 F.3d at 1340. When one of the shareholders died, his estate argued that the life-insurance proceeds should not be included in the value of the company, for purposes of determining fair market value of the redeemed shares, because of the company's offsetting contractual obligation to redeem those shares from the estate. *Id.* at 1345.

The Tax Court in *Estate of Blount* included the life-insurance proceeds in the value of the company and the shareholders' shares, determining that the redemption obligation was not like an ordinary liability because the redemption involved the very same shares being valued. 2004 WL 1059517, at *26. The Eleventh Circuit reversed on this issue, holding that the fair market value of the closely-held corporation did not include life-insurance proceeds used to redeem the shares of the deceased shareholder under a stock purchase agreement. *Estate of Blount*, 428 F.3d at 1346. The Eleventh Circuit reasoned that the stock-purchase agreement created a contractual liability for the company, offsetting the life-insurance proceeds. *Id.* at 1345-46. The Eleventh Circuit concluded that the insurance proceeds were "not the kind of ordinary nonoperating asset that should be included in the value of [the company] under the treasury regulations" because they were "offset dollar-for-dollar by [the company's] obligation to satisfy its contract with the decedent's estate." *Id.* at 1346 (citing 26 C.F.R. § 20.2031-2(f)(2)).

The IRS urges the Court to reject the Eleventh Circuit's holding in *Estate of Blount* and apply the Tax

Court's reasoning. Doc. 52 at 12-14. The IRS contends that the Eleventh Circuit's approach violates customary valuation principles, resulting in a below-market valuation for Crown C and a windfall for Thomas at the expense of Michael's estate. *Id.* According to the IRS, a willing buyer and seller would value Crown C at approximately $6.86 million, rather than $3.86 million, because on the date of Michael's death, Crown C possessed the $3 million in life-insurance proceeds that were later used to redeem Michael's shares. *Id.* at 19. This, in turn, would make Michael's 77.18% interest in Crown C worth about $5.3 million. *Id.* The Estate disagrees, somewhat reflexively arguing that under the Eleventh Circuit's holding in *Estate of Blount*, the Court should not include the $3 million in life-insurance proceeds in the valuation of Crown C because of the redemption obligation in the Stock Agreement. Doc. 46 at p. 6. But other than citing the Eleventh Circuit's holding and its own expert opinions (which essentially say that holding controls), the Estate does not really explain *why* it believes the Eleventh Circuit's holding is correct. *Id.*

Life-insurance proceeds are nonoperating assets that generally increase the value of a company. 26 C.F.R. § 20.2031-2(f)(2); *Estate of Huntsman*, 66 T.C. at 874. Here, the parties agree that the proceeds are a nonoperating asset that would have increased Crown C's value, but they dispute whether Crown C's redemption obligation was a liability that offset the proceeds for valuation purposes. Doc. 52 at pp. 14-15; Doc. 46 at pp. 5-6. Therefore, to determine the fair market value of Michael's shares as of the date of his death, the Court analyzes whether Crown C's outstanding redemption obligation was a corporate liability that reduced the fair market value of Crown C.

Under the willing-buyer-willing-seller principle, a redemption obligation does not reduce the value of a company as a whole or the value of the shares being redeemed. A redemption obligation requires a company to buy its own shares from a shareholder, and just like any other contractual obligation, a redemption obligation expends company resources. But as the Tax Court observed in *Estate of Blount*, a redemption obligation is not a "value-depressing corporate liability when the very shares that are the subject of the redemption obligation are being valued." 2004 WL 1059517, at *25.

Consider what a hypothetical "willing buyer" would pay for a company subject to a redemption obligation. *See* 26 C.F.R. § 20.2031-1(b). The willing buyer would not factor the company's redemption obligation into the value of the company, because with the purchase of the entire company, the buyer would thereby acquire all of the shares that would be redeemed under the redemption obligation; in other words the buyer would pay all of the shareholders the fair market value for all of their shares. The company, under the buyer's new ownership, would then be obligated to redeem shares *that the buyer now holds*. Since the buyer would receive the payment from the stock redemption, the buyer would not consider the obligation *to himself* as a liability that lowers the value of the company *to him*. *See Estate of Blount*, 2004 WL 1059517, at *25 (T.C. 2004) ("To treat the corporation's obligation to redeem the very shares that are being valued as a liability that reduces the value of the corporate entity thus distorts the nature of the ownership interest represented by those shares.").

A willing buyer purchasing Crown C on the date of Michael's death would not demand a reduced purchase price

because of the redemption obligation in the Stock Agreement, as Crown C's fair market value would remain the same regardless. The willing buyer would buy all 500 of Crown C's outstanding shares (from Michael's Estate and Thomas) for $6.86 million, acquiring Crown C's $3.86 million in estimated value plus the $3 million in life-insurance proceeds at issue. If Crown C had no redemption obligation, the willing buyer would then own 100% of a company worth $6.86 million.

But even with a redemption obligation, Crown C's fair market value remains the same. Once the buyer owned Crown C outright, the buyer could either: 1) cancel the redemption obligation to himself and own 100% of a company worth $6.86 million, or 2) let Crown C redeem Michael's former shares—the buyer (and not Michael's Estate) would receive roughly $5.3 million in cash and then own 100% of a company worth the remaining value of about $1.56 million, leaving the buyer with a total of $6.86 million in assets. Therefore, with or without the redemption obligation, the fair market value of Crown C on the date of Michael's death was $6.86 million.

The Estate urges the Court to follow the Eleventh Circuit's reasoning in *Estate of Blount*, which declared that "nonoperating assets should not be included in the fair market valuation of a company where, as here, there is an enforceable contractual obligation that offsets such assets." 428 F.3d at 1346 (quotation marks omitted). But as the IRS points out, the Court must determine the fair market value of Crown C on the date of Michael's death, not the value in its post-redemption configuration. *See* 26 U.S.C. § 2031. Excluding the insurance proceeds from Crown C's value impermissibly treats Michael's shares as both outstanding and redeemed at the same time, reducing Crown C's value by the redemption price of the very

shares whose value is at issue. This approach ignores the ownership interest represented by Michael's shares; construing a redemption obligation as a corporate liability only values Crown C post redemption (i.e., excluding Michael's shares), not the value of Crown C on the date of death (i.e. including Michael's shares).

Demonstrating this point, exclusion of the insurance proceeds from the fair market value of Crown C and valuing Michael's shares at $3 million results in drastically different share prices for Michael's shares compared to Thomas's. If on the date of his death, Michael's 77.18% interest was worth only $3 million ($7,774/share), that would make Thomas's 22.82% interest worth $3.86 million ($33,863/share) because Thomas owned all other outstanding shares and the residual value of Crown C was $3.86 million. *See* Doc. 53-19 at ¶ 61. The residual value of Crown C is the value of the company apart from the $3 million of insurance proceeds at issue. The parties have agreed that this value was $3.8 million. Doc. 48 at ¶¶ 1-3; Doc. 58 at ¶¶ 43, 79-81. Because Thomas was the only other shareholder of Crown C, his ownership interest must therefore equal the residual value of Crown C: $3.8 million. This outcome violates customary valuation principles because Thomas's shares would be worth 336% more than Michael's *at the exact same time*. *See* Doc. 53-19 at ¶ 61. A willing seller of Michael's shares would not accept this bargain, as it creates a windfall for the buyer (Crown C of which Thomas would now have 100% control), while undervaluing Michael's shares in comparison.

Only by including the insurance proceeds in the fair market value of Crown C do Michael's and Thomas's shares hold an equal value on the date of Michael's death. Michael's 77.18% interest in a $6.86 million company would be worth $5.3 million ($13,782/share) and Thomas's

22.82% interest would be worth $1.56 million ($13,782/share). This outcome tracks customary valuation principles, because the brothers' shares have the same value-per-share. A willing seller of Michael's shares would only accept this outcome, because it assigns the same value to Michael's shares as to Thomas's and neither party's economic position changes through the transaction.

The Eleventh Circuit declared in *Estate of Blount* that 26 C.F.R. § 20.2031-2(f)(2) precludes the inclusion of insurance proceeds in the corporate value when the proceeds are used for a redemption obligation. 428 F.3d at 1345 ("The limiting phrase, 'to the extent that such nonoperating assets have not been taken into account,' however, precludes the inclusion of the insurance proceeds in this case." (citing 26 C.F.R. § 20.2031-2(f)(2))). But, 26 C.F.R. § 20.2031-2(f)(2) begins with a discussion of the factors considered in determining the fair market value of a closely-held corporation, including "the company's net worth, prospective earning power and dividend-paying capacity, and other relevant factors." The regulation goes on to state that "[i]n addition to the relevant factors described above, consideration shall also be given to nonoperating assets, including proceeds of life insurance policies payable to or for the benefit of the company, to the extent such nonoperating assets have not been taken into account in the determination of net worth." *Id.*

While in *Estate of Huntsman* the Tax Court ultimately rejected the Commissioner's valuation as not following customary valuation principles, the court found this regulation to mean that the court "must determine the fair market value of the decedent's stock . . . by applying customary principles of valuation and by giving 'consideration' to the [life-]insurance proceeds." 66 T.C. at

875. The Eleventh Circuit's holding in *Estate of Blount* notwithstanding, the text of the regulation does not indicate that the very presence of an offsetting liability means that the life-insurance proceeds have already been "taken into account in the determination of a company's net worth." *See* 26 C.F.R. § 20.2031-2(f)(2). By its plain terms, the regulation means that the proceeds should be considered in the same manner as any other nonoperating asset in the calculation of the fair market value of a company's stock. *See id.* And as already discussed, a redemption obligation is not the same as an ordinary corporate liability. *See supra* at pp. 29-31.

The Eleventh Circuit's opinion in *Estate of Blount* relied heavily on *Estate of Cartwright*, 183 F.3d 1034, 1037 (9th Cir. 1999), which excluded insurance proceeds from the fair market value of a company when the proceeds were offset by an obligation to pay those proceeds to a shareholder's estate. *Estate of Blount*, 428 F.3d at 1345. But *Estate of Cartwright* is distinguishable. As the Tax Court in *Estate of Blount* explained about *Estate of Cartwright*:

> The lion's share of the corporate liabilities in that case which were found to offset the insurance proceeds were *not obligations of the corporation to redeem its own stock*. Rather, we determined that approximately $4 million of the $5 million liability of the corporation was to compensate the decedent shareholder for services; i.e., for his interest in work in progress. Thus, a substantial portion of the liability was no different from any third-party liability of the corporation that would be netted against assets, including insurance proceeds, to ascertain net assets.

2004 WL 1059517, at *27 (emphasis added). Unlike in *Estate of Cartwright*, Crown C's redemption obligation

simply bought Michael's shares. *See id.* The redemption did not compensate Michael for his past work, so it was not an ordinary corporate liability. *See Estate of Blount*, 2004 WL 1059517, at *27 (T.C. 2004). While some of the life-insurance proceeds in *Estate of Cartwright* were used for a stock redemption, *Estate of Cartwright* mainly discussed how the insurance proceeds compensated the shareholder for past work, not for his shares in the company. *See Estate of Cartwright*, 1996 WL 337301, at *7-8 (T.C. 1996), *aff'd in part, rev'd in part by*, 183 F.3d 1034, 1037-38 (9th Cir. 1999). And to the extent that *Estate of Cartwright* excluded some of the life-insurance proceeds from the company's fair market value because of an offsetting redemption obligation, the opinion contains the same analytical flaw as *Estate of Blount*, 183 F.3d at 1037, i.e. considering a redemption obligation to be a corporate liability that depresses a company's value by ignoring the ownership interest represented by the redeemed shares.

The Court finds the Tax Court's reasoning in *Estate of Blount* persuasive. *Estate of Blount*, 2004 WL 1059517, at *24-27; *see also* Adam S. Chodorow, *Valuing Corporations for Estate Tax Purposes: A Blount Reappraisal*, 3 Hastings Business Law Journal 1, 25 (2006) ("Taking redemption obligations into account leads the court to value the wrong property . . . redemption obligations are different from other types of corporate obligations in that a redemption obligation both shrinks the corporate assets and changes its ownership structure."). A redemption obligation is not an ordinary corporate liability—a stock redemption involves a change in the ownership structure of the company, where the company buys a shareholder's interest—so a redemption obligation does not change the value of the company as a whole *before the shares are redeemed*. Nor can a redemption obligation diminish the value of the same shares being redeemed; the shareholder

is essentially "cashing out" his share of ownership in the company and its assets. Moreover, a stock redemption results in the company (and more specifically its remaining shareholder(s)) getting something of equal value for the cash spent, i.e. the decedent's share of ownership in the company; the exchange increases the ownership interest for each of the company's outstanding shares, i.e. the surviving shareholders' shares.

For these reasons, the Court respectfully finds that the Eleventh Circuit's opinion in *Estate of Blount* is "demonstrably erroneous" and there are "cogent reasons for rejecting [it]." *Keasler v. United States*, 766 F.2d 1227, 1233 (8th Cir. 1985) ("[T]he tax decisions of other circuits should be followed unless they are demonstrably erroneous or there appear cogent reasons for rejecting them." (internal quotation marks and citation omitted)). Accordingly, the Court holds that the $3 million in life-insurance proceeds used to redeem Michael's shares must be included in the fair market value of Crown C and of Michael's shares.

2. Accounting for the insurance proceeds

The parties stipulated that the fair market value of Michael's shares was $3.1 million, aside from the life-insurance proceeds. Doc. 48. The parties further represented, in their briefs and in the hearing on their motions for summary judgment, that the only remaining issue between the parties was how to allocate the life-insurance proceeds. Doc. 46, 52; *see also* Doc. 71 at 3 (The Estate's counsel: "[I]t doesn't appear that there are really any factual disputes before the Court, and the real issue is whether the insurance proceeds that were received are excluded from the valuation of the company."). Because the insurance proceeds are not offset by Crown C's obligation to redeem Michael's shares, the fair market value

of Crown C at the date of date of death and of Michael's shares includes all of the insurance proceeds. Therefore, based on the undisputed facts in the record, the Estate failed to prove that the IRS's tax determination is incorrect and that it is entitled to a tax refund.

IV. CONCLUSION

The Court grants the IRS's motion for summary judgment, Doc. 51, and denies the Estate's motion for summary judgment, Doc. 45. The Court further denies both parties' motions to exclude expert testimony as moot. Docs. 49, 54.

So Ordered this 21st day of September 2021.

s/ Stephen R. Clark
STEPHEN R. CLARK
UNITED STATES DISTRICT JUDGE