

# The Deal That Allegedly Never Died: Defending Against a Claimed Option to Purchase

Alexander C. Chae, Esq., and Audrey F. Momanaee, Esq.

*The case of M7 Capital, LLC, v. Ted Miller, which was tried in late 2013, is an example of the jury getting it right. In that case, the plaintiff, M7 Capital, LLC (“M7 Capital”), by and through its principal, John Miller, claimed to have a perpetual option to purchase an ownership interest in a company. The trial, which involved the theatrics of a crying John Miller of M7 Capital, lasted two weeks, and resulted in a verdict for Ted Miller, with M7 Capital taking nothing. In the case, the jury did not decide the value of the company at issue. This is because the jury found that there was no agreement to hold the purchase option indefinitely. Had the jury found the existence of such an agreement, however, issues of the appropriate valuation would have been paramount.*

## THE FACTS OF THE CASE

In the fall of 2002, Ted Miller, the former president, chief executive, and founder of Crown Castle, was approached by John Miller, a former chief executive of a publicly traded company and a Louisiana-based promoter, about coinvesting in an aircraft parts business in San Antonio and Virginia that was in bankruptcy.

The business opportunity that was initially proposed involved the purchase, out of bankruptcy, of the assets of three U.S. divisions of Fairchild Dornier. Fairchild Dornier was a manufacturer of turboprop-powered aircrafts that are primarily used by commuter airlines.

The three divisions in bankruptcy, Merlin Express Incorporated, Fairchild Gen-Aero Incorporated, and Metro Support Services, Inc., operated the Fairchild Dornier U.S. servicing and parts distribution center in San Antonio (the “FDUS Assets”).

Ted Miller, on behalf of 4M Investments (an entity controlled by Ted Miller), successfully bid for the FDUS Assets in an agreement dated December 17, 2002. The purchase price of the FDUS Assets was \$7.4 million. The interest in the FDUS Assets

was later assigned to M7 Aerospace LP, an entity controlled by Ted Miller.

In January 2003, due diligence was conducted on the feasibility of the purchase of assets that were owned by another subsidiary of Fairchild Dornier named Dornier Aircraft North America (“DANA Assets”). In February 2003, Ted Miller, on behalf of M7 Aerospace LP, made a successful bid in a Virginia bankruptcy court for the DANA Assets.

The purchase price of the DANA Assets was \$5.6 million. The interest in the DANA Assets was later assigned to M7 Aerospace II LP, an entity controlled by Ted Miller.

Ted Miller formed M7 Holdings on or about March 24, 2003. M7 Holdings held a 99.0 percent limited partnership interest in the following entities:

- M7 Aerospace LP
- M7 Aerospace II LP

Though he indicated an interest in doing so, because John Miller did not provide any capital to co-purchase the FDUS Assets and the DANA Assets, Ted Miller and his entities were forced to provide \$3.5 million of investment capital and to guarantee

a \$10 million loan from JP Morgan Chase in order to make the purchases.

From December 2002 to June 2003, John Miller and Ted Miller discussed various scenarios under which M7 Capital, an entity formed by John Miller, may acquire an interest in M7 Holdings and in the FDUS Assets and DANA Assets. During this time, John Miller was employed by M7 Holdings and was paid \$200,000 per year.

There was never any limited partnership or other written agreement between John Miller and Ted Miller or their respective entities. Further, neither John Miller nor M7 Capital, ever paid any consideration to Ted Miller or M7 Holdings for any ownership interest in M7 Holdings.

In a June 27, 2003, email, John Miller was notified that if he wished to proceed with the purchase of an interest in M7 Holdings, Ted Miller's attorney must have written confirmation of payment by no later than 5:00 p.m. on June 30, 2003. Nothing was received by M7 Holdings at that time.

However, at trial, John Miller testified that on or about June 30, 2003, \$750,000 was placed in an escrow account, allegedly on behalf of M7 Capital, to purchase a 20.48 percent ownership interest in M7 Holdings.

On July 10, 2003, and again on July 11, 2003, John Miller informed Ted Miller that he would not be moving forward with the purchase of the ownership interest in M7 Holdings.

Under Ted Miller's leadership, the newly formed company became very successful. And, in 2007, Ted Miller sold the company for a significant gain on his investment.

M7 Capital then filed suit, alleging that it was owed a share of the company's sale price. M7 Capital, through John Miller, claimed that he had identified and analyzed the business opportunity on his own time and proposed to Ted Miller that they should purchase the FDUS Assets out of bankruptcy. John Miller further claimed that around December 2, 2002, he and Ted Miller agreed that Ted would own at least a 51 percent controlling interest in the acquiring limited partnership, while an investment entity to be formed by John Miller would have the option to purchase up to a 49 percent ownership interest.

M7 Capital further claimed that on June 30, 2003, John Miller deposited \$750,000 into an escrow account representing payment for a 20.48 percent interest in the limited partnership, but that before the deal closed, Ted Miller amended a proposed limited partnership agreement. According to M7 Capital, the amended agreement contained unacceptable terms to John Miller and his investors,



which made it impossible for him to exercise his option to purchase an interest, even though he was ready, willing, and able to do so as of June 30, 2003.

The trial court granted a motion for summary judgment on failure of consideration grounds in favor of Ted Miller. However, the appellate court subsequently overturned the summary judgment.

Upon returning to the trial court, M7 Capital proceeded with claims of breach of contract and fraud, seeking over \$21 million based, in part, on its expert's valuation of 20.48 percent of M7 Holdings at \$5.8 Million.

Ted Miller moved for summary judgment on the fraud claims in the case. However, the court allowed that claim, along with the breach of contract claim, to proceed to trial.

On December 12, 2012, after a two week trial presided over by Judge Mike Miller in the 11th Judicial District Court of Harris County, the jury entered a verdict in favor of Ted Miller, finding no fraud in Ted Miller's actions. The jury also found that no contract had ever been created between Ted Miller and M7 Capital with the terms that M7 Capital had alleged.

## THE VALUATION

Though it became moot by the jury's findings, had the jury found the existence of a contract between Ted Miller and M7 Capital, the issue of damages would have been important. The two valuation analyst opinions on damages diverged. The court selected a valuation date as of July 9, 2003, which was the day prior to the date of the alleged breach.

### Ted Miller's Valuation Analyst

The valuation analyst for Ted Miller valued the alleged loss of a 20.48 percent interest in M7 Holdings using both an asset-based and a market-based approach. The expert determined that the value of such interest was less than \$700,000 given the results of the valuation under each of these approaches.

Using the asset-based approach, and valuing the assets of M7 Holdings as of July 9, 2003, the value of 100 percent of the M7 Holdings equity was \$4,419,074. M7 Holdings acquired the tangible assets approximately three months prior to the valuation date. This equity value represented the amount that was paid to purchase these assets out of bankruptcy less debt financing used for the asset acquisitions. Reducing this value by a 20 percent discount for lack of marketability and a 15 percent discount for lack of control resulted in a value of \$615,000 for a 20.48 percent interest in M7 Holdings.

Using the market approach and considering other transactions in the M7 Holdings ownership interests, which occurred from April through September of 2003, the defendant's valuation analyst estimated that the fair market value of a 20.48 percent interest in M7 Holdings was \$724,000.

### The M7 Capital Valuation Analyst

Not surprisingly, the valuation analyst for M7 Capital estimated the value of M7 Holdings to be far greater, estimating the value of a 20.48 percent interest in M7 Holdings at \$5.849 million. The valuation conclusion from the plaintiff's analyst was approximately \$35 million higher than the actual price paid by the defendant for the assets.

In his valuation, the plaintiff's analyst used the income approach based on defendant's business plan. The analyst also concluded that (1) the asset approach did not "reflect fair market value" because the assets were purchased out of bankruptcy at a discount and (2) there was not any transaction data available to apply a market approach analysis.

The plaintiff's analyst assumed that there was minimal risk with future cash flow even though the four entities were acquired by M7 Holdings through bankruptcy and had only been operated by M7 Holdings for three months. The business plan included significant changes in operating structure.

In his income approach analysis, and assuming annual earnings before interest, taxes, depreciation, and amortization (EBITDA) of \$6 million and an aggressive capitalization rate that was equivalent to an earnings multiple of 7, the plaintiff's analyst estimated the business value to be \$42 million. After applying a 20 percent discount for lack of control and a 15 percent discount for lack of marketability, the M7 Capital analyst estimated that the fair market value of a 20.48 percent interest in M7 Holdings was \$5,849,190.

Importantly, in his valuation, the plaintiff's analyst relied on data from transactions involving M7 Holdings that occurred in December 2003, well after the valuation date in the case. Legal counsel for Ted

Miller argued the impropriety of relying on such data based on the AICPA *Statement on Standards for Valuation Services*, which expressly requires, among other things, that "the valuation analyst should only consider circumstances existing at the valuation date and events occurring up to the valuation date . . ." Nevertheless, the court allowed the testimony, subject to cross-examination, to be presented to the jury.

### CONCLUSION

At the end of the day, the jury found in favor of Ted Miller, finding that no contract with a perpetual option existed between the parties, as alleged by M7 Capital.

Though the issue of value was never decided by the jury, from the perspective of the defendant, given the risk associated with the M7 Holdings assets and what was known at the time of the purchase of those assets out of bankruptcy, the proper valuation analysis was that prepared by the defendant's analyst. This analyst estimated the value of the company as of June 2003, and he did not consider future unknown events. Though it was not ultimately something that the jury relied upon in making their determination, we believe that the straightforward and reasonable nature of the analysis would have won the day.

---

*Alexander C. Chae is a trial partner of Gardere Wynne Sewell LLP. Mr. Chae's practice encompasses all areas of commercial litigation. Recently, Mr. Chae's trial skills in the courtroom resulted in a successful \$27.3 million victory on behalf of Curocom Energy LLC after a three-week trial. This multi-million dollar verdict was recognized as one of the National Law Journal's "Top 100 Verdicts of 2014." He was proud to represent Ted Miller in the M7 Capital case, alongside his co-counsel Robert Singleton Jr. of Singleton Cooksey PLLC and Audrey F. Momanaee of Gardere Wynne Sewell LLP. Mr. Chae can be reached at (713) 276-5539 or at [achae@gardere.com](mailto:achae@gardere.com).*

*Audrey F. Momanaee is a trial partner of Gardere Wynne Sewell LLP. Ms. Momanaee's practice encompasses all areas of commercial litigation, representing clients from varied industries including the energy, real estate, and chemical and refining industries. In addition to business and contractual disputes, Ms. Momanaee has been involved in a number of cases involving business dissolutions, shareholder suits, and class actions. She has also handled trade secret and patent infringement litigation. Ms. Momanaee was thrilled that the jury got it right in the M7 Capital case, and was proud to represent Ted Miller. Ms. Momanaee can be reached at (713) 276-5732 or at [amomanaee@gardere.com](mailto:amomanaee@gardere.com).*

