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Gregory L. Segall, Trustee

UNITED STATES BANKRUPTCY COURT
FOR THE EASTERN DISTRICT OF NEW YORK

IN RE:	)	Chapter 11
	)	Case Nos. 02-88564
	)	02-88565
MED DIVERSIFIED, INC., et al.	)	02-88568
	)	02-88570
Debtors.	)	02-88572
	)	02-88573
CHARTWELL LITIGATION TRUST)	
and GREGORY L. SEGALL AS	)	Jointly Administered
TRUSTEE OF CHARTWELL)	
LITIGATION TRUST,	)	Adversary Proceeding No.
	)	8-04-8680-288
Plaintiffs,)	
)	
v.	)	OPPOSITION OF PLAINTIFF
	)	CHARTWELL LITIGATION TRUST
ADDUS HEALTHCARE INC., et al.	)	AND GREGORY L. SEGALL,
	)	TRUSTEE OF THE CHARTWELL
Defendants.)	TRUST, TO DEFENDANTS' MOTION
)	TO STRIKE EXPERT REPORT OF
AND RELATED COUNTER-CLAIMS)	ROBERT J. CIMASI
)	

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Plaintiffs Chartwell Litigation Trust and Gregory L. Segall, Trustee of the Chartwell Litigation Trust (collectively, “Plaintiffs”), submit this opposition to the motion of defendants Addus Healthcare, Inc., et al. (“Defendants”) to strike the testimony and expert report (the “Report”) of Robert J. Cimasi.¹

The parties have extensively briefed the authority that governs this Court’s decision to admit or exclude expert testimony. *See* Fed. R. Evid. 702; *Ruggiero v. Warner-Lambert Co.*, No. 04-6674-CV, 2005 WL 2240999, at *4 (2d Cir. Sept. 16, 2005); *Amorgianos v. Nat'l R.R. Passenger Corp.*, 303 F.3d 256, 266 (2d Cir. 2002). The Court must ask whether the methodologies that Mr. Cimasi employed are reliable methodologies. *See Amorgianos*, 303 F.3d at 266. “A minor flaw in an expert’s reasoning or a slight modification of an otherwise reliable method will not render an expert’s opinion *per se* inadmissible. ‘The judge should only exclude the evidence if the flaw is large enough that the expert lacks ‘good grounds’ for his or her conclusions.’” *Id.* at 267 (quoting *In re Paoli R.R. Yard PCB Litig.*, 35 F.3d 717, 746 (3d Cir.1994)).

In their memorandum of points and authorities regarding proper methods for valuing closely held companies, filed on September 9, 2005 (the “Valuation Memorandum”), Plaintiffs provided the Court with authority from federal courts of appeal (including the Second Circuit), federal district courts, bankruptcy courts, tax courts, state courts, treatises,

¹ It is Plaintiffs’ understanding that Mr. Cimasi already has been admitted as an expert witness. 8/26/2005 Trial Transcript (“Tr.”) 134:23-24 (“THE COURT: All right. Well, I’m going to admit you as an expert witness.”). The only issue reserved by the Court was the admissibility of Mr. Cimasi’s report. *Id.* 135:1 (“But I’m not admitting your report yet.”).

business publications, and law review articles to support Mr. Cimasi’s methodology and assumptions. In their motion to strike Mr. Cimasi’s testimony, Defendants do not cite a single case in which the methodologies, techniques, or assumptions on which Mr. Cimasi relied were rejected.

Indeed, in their memorandum Defendants *cite no legal authority at all* and cite to only one publication: a book by Shannon Pratt (Mem. at 9) that, as explained below, Defendants take out of context. Defendants’ inability to cite any authority at all to buttress their attack on Mr. Cimasi’s opinion – particularly in view of the abundant authority cited by Plaintiffs to support Mr. Cimasi’s opinions and methodology – indicates the weakness of Defendants’ arguments.

Moreover, as a factual matter, Defendants’ attacks on Mr. Cimasi’s testimony and report are specious. In every instance, Defendants either have misstated or misconstrued Mr. Cimasi’s reasoning to construct strawmen to which they direct their arguments. Indeed, it is remarkable that despite the intense scrutiny applied to Mr. Cimasi’s report and the forceful interrogation of Mr. Cimasi, Defendants are unable to point out a single material flaw in Mr. Cimasi’s methodology or analysis.

I. BENCHMARKING ANALYSIS

A. Defendants misrepresent the purpose for Mr. Cimasi’s benchmarking analysis

In Schedule 3 of his report, Mr. Cimasi compared the historic operational and financial performance of Addus to the performance of similar companies. (Report § 5.2, p.2 & Sch. 3.). Mr. Cimasi called this a “benchmarking” analysis.

Mr. Cimasi used this benchmarking analysis for only one purpose: to measure “the relative risk of investment in [Addus] as compared to investment in other companies operating within the same or similar industry.” (Report § 5.2, p.2.) That is, he used it in the determination of the Operational Performance Risk premium for Addus, which is discussed in Section 5.12.5.1 of the Report (Section 5, p. 18). (“As illustrated in Schedule 3, [Addus] compared unfavorably to the industry benchmark in terms of profitability, liquidity, operating efficiency and leverage measures.”) *That is the only purpose for which the benchmarking analysis was used.*

Defendants falsely contend that Mr. Cimasi used the benchmarking analysis in connection with his selection of ratios for the Guideline Company method. (Mtn. 3, ¶ 6, at 3, bullet points 2 and 3.) In other words, they contend that Mr. Cimasi relied on the benchmarking analysis for his determination that Addus was not a “median” company under the Guideline Company method. He did not.

Mr. Cimasi’s application of the Guideline Company valuation method is reflected in Schedule 10 of his Report. As the Court will recall, in the Guideline Company method, Mr. Cimasi selected two multiples to apply to financial variables of Addus: market value of invested capital to revenue (MVIC/Revenue) and market value of invested capital to EBITDA (MVIC/EBITDA).² (Report § 5.15, at pp. 22-24 & Sch. 10.) As Mr. Cimasi’s report clearly states, Mr. Cimasi selected the ratios that he used in the application of the

² Unlike Scott Peltz’s use of a ratio based on “net cash flow provided by operating activities” – which the record shows has never been used by any analyst in a valuation other than by Mr. Peltz in this specific case – analysts commonly use MVIC/Revenue and MVIC/EBITDA multiples in applying the guideline company methodology. Cf. Shannon P. Pratt, THE MARKET APPROACH TO VALUING BUSINESSES 14-17 (John Wiley & Sons ed. 2001); *Okerlund v. U.S.*, 53 Fed. Cl. 341, 347-49 (Fed. Cl. 2002).

Guideline Company method *based solely on consideration of the operating margin (or profitability of Addus)* in comparison to the operating margins of the guideline companies that the selected as reflected in Schedule 9, Table B, of the Report. (See Report Sch. 9, footnotes 11 & 12; Report Sch. 10, footnotes 2 & 3.) To make this clear, we have reproduced Mr. Cimasi's Schedule 9 and Schedule 10 on the following two pages of this brief.

In Schedule 9, Mr. Cimasi calculated the weighted average of the operating margin for Addus and for the 13 guideline companies; that is, he analyzed the operating margin for each of the years 1999, 2000, and 2001, and, in the weighting, gave 50% of the weight to 2001, 30% to 2000, and 20% to 1999 (consistent with the view that the most weight should be given to the period closest in time to the "as of" valuation date). (See 8/29/2005 Tr. 87:4-9.) By doing this, Mr. Cimasi took into consideration and accounted for the fact that the adjustments to Addus' financial statements included non-recurring and extraordinary events. Defendants' assertion that Mr. Cimasi did not exclude deductions caused by non-recurring events (Mtn. 4) is simply false.

Addus Healthcare, Inc.
Analysis of Normalized EBITDA and Operating Margin

Schedule 9

Table A - EBITDA (1)

	A	B	C	D
1 Period (2)	2001	2000	1999	Weighted Average (5)
2 Weight (3)	50%	30%	20%	
3 Almost Family, Inc.	6.11%	7.12%	5.41%	6.27%
4 Amedisys, Inc.	9.90%	0.35%	0.45%	5.14%
5 American Homepatient, Inc.	8.29%	12.52%	7.76%	9.45%
6 Apria Healthcare Group, Inc.	23.28%	24.26%	23.46%	23.61%
7 Coram Healthcare Corporation	6.06%	7.76%	0.06%	5.37%
8 Gentiva Health Services, Inc.	3.60%	-6.54%	1.97%	0.23%
9 Lincare Holdings, Inc.	40.15%	38.79%	38.78%	39.47%
10 Mid-Atlantic Home Health Network, Inc.	3.50%	5.85%	5.81%	4.66%
11 National Home Health Care Corp.	11.13%	9.67%	7.64%	9.99%
12 New York Health Care, Inc.	2.40%	2.75%	0.77%	2.18%
13 Option Care, Inc.	9.88%	11.40%	10.01%	10.36%
14 Pediatric Services of America, Inc.	7.39%	5.41%	-3.52%	4.62%
15 Transworld Healthcare, Inc.	11.17%	0.46%	2.97%	6.32%
16 SUBJECT ENTITY (4)	-0.07%	5.46%	6.15%	2.83%

Table B - Operating Margin (6)

	A	B	C	D
17 Period (7)	2001	2000	1999	Weighted Average (10)
18 Weight (8)	50%	30%	20%	
19 Almost Family, Inc.	4.08%	4.95%	3.31%	4.19%
20 Amedisys, Inc.	6.77%	-2.91%	-2.69%	1.98%
21 American Homepatient, Inc.	4.62%	2.30%	-3.34%	2.33%
22 Apria Healthcare Group, Inc.	12.65%	13.63%	12.31%	12.88%
23 Coram Healthcare Corporation	0.80%	2.76%	-4.53%	0.33%
24 Gentiva Health Services, Inc.	1.67%	-8.64%	-0.28%	-1.81%
25 Lincare Holdings, Inc.	30.82%	29.19%	28.96%	29.96%
26 Mid-Atlantic Home Health Network, Inc.	2.86%	5.48%	5.44%	4.16%
27 National Home Health Care Corp.	9.68%	8.14%	5.80%	8.44%
28 New York Health Care, Inc.	1.84%	1.97%	-0.34%	1.45%
29 Option Care, Inc.	8.09%	9.25%	7.71%	8.36%
30 Pediatric Services of America, Inc.	3.95%	1.13%	-7.77%	0.76%
31 Transworld Healthcare, Inc.	7.56%	-4.46%	-1.54%	2.13%
32 SUBJECT ENTITY (9)	-1.95%	2.99%	3.54%	0.63%
33 Percentile of SUBJECT ENTITY to Guideline Companies	0.50% (11)			14.20% (12)

Notes:

- 1 The historical EBITDA of each of the guideline companies and the SUBJECT ENTITY.
- 2 The most recent 12-month period of operations.
- 3 The VALUATOR's weighting of the historical periods of companies' EBITDA.
- 4 The SUBJECT ENTITY's historical EBITDA (as a percentage of net revenue (See Schedule 1, Line 14).
- 5 Weighted average of historical periods *Columns A - C) based on weighting in Line 2.
- 6 The historical Operating Margin of each of the guideline companies and the SUBJECT ENTITY.
- 7 The most recent 12-month period of operations.
- 8 The VALUATOR's weighting of the historical periods of companies' operating margin.
- 9 The SUBJECT ENTITY's historical operating margin (as a percentage of net revenue (See Schedule 1, Line 9).
- 10 Weighted average of historical periods *Columns A - C) based on weighting in Line 18.
- 11 The lowest one-half (1/2) of the first percentile of selected MVIC/Revenue ratios was selected because both the SUBJECT ENTITY's actual 2001 operating operating margin (-1.95%) and normalized operating margin (0.63%) were below the range of the guideline companies' 2001 operating margins (Column A, Lines 19 - 31).
- 12 Calculated as the percentile of the SUBJECT ENTITY's 3-year weighted operating margin (0.63%) compared to the 3-year weighted operating margins of the guideline companies (Column D, Lines 19 - 31).

Schedule 10

Addus Healthcare, Inc.
Guideline Company Valuation Method - As of 1/8/02

	B	C	D	E	F	G	H	I	J	K	L	M	N
Guideline Companies (Publicly Traded)		Share Price as of 1/8/2002	Period Ending for Guideline Co. Data	Net Revenue	EBITDA (1)	Market Value of Capital (MVIC) (2)	Operating Margin	Weight	Outstanding Shares	MVIC to Revenue	MVIC to EBITDA	Weighted MVIC to Revenue	Weighted MVIC to EBITDA
1 Almost Family, Inc.	AFAM	\$16.10	12/31/2001	\$98,265,463	\$6,164,953	\$67,533,326	4.1%	2	3,317,674	0.69	0.035	10.95	0.56
2 Amerisys, Inc.	AMED	\$5.90	12/31/2001	\$110,174,000	\$5,665,688	\$75,379,249	6.8%	5	7,178,152	0.68	0.088	13.30	1.71
3 American Homepoint, Inc.	AHOM	\$0.84	12/31/2001	\$352,584,000	\$296,332,680	4.6%	5	16,327,000	0.84	0.108	8.90	1.14	
4 Alpha Healthcare Group, Inc.	AHGX	\$22.96	12/31/2001	\$1,151,195,000	\$267,285,674	12.7%	2	54,604,167	1.37	0.070	5.79	0.30	
5 Conam Healthcare Corporation	CRHEQ	\$0.53	12/31/2001	\$393,629,000	\$21,143,514	\$165,818,140	0.8%	4	49,638,000	0.42	0.043	7.84	0.80
6 Centiva Health Services, Inc.	GTIV	\$23.20	12/31/2001	\$1,171,767,000	\$17,178,594	\$354,923,021	1.7%	4	25,658,754	0.43	0.044	187.11	19.19
7 Linare Holdings, Inc.	LNCR	\$28.34	12/31/2001	\$812,442,000	\$320,661,533	\$327,722,215	30.8%	1	107,743,762	4.03	N/A	10.22	0.26
8 Mid-Atlantic Home Health Network, Inc.	MATHN	\$0.32	12/31/2001	\$28,336,732	\$1,321,646	\$905,145	2.9%	1	12,105,142	0.32	0.008	6.88	0.18
9 National Home Health Care Corp.	NHHC	\$12.60	10/31/2001	\$77,748,000	\$7,718,305	\$66,772,314	9.7%	5	5,267,644	0.86	0.110	8.60	1.10
10 New York Health Care, Inc.	BBAL	\$3.20	12/31/2001	\$34,330,710	\$748,559	\$12,000,347	1.8%	1	3,696,730	0.35	0.009	16.03	0.41
11 Option Care, Inc.	OPTN	\$19.05	12/31/2001	\$317,153,000	\$23,253,826	\$106,123,397	8.1%	1	16,037,024	1.41	0.036	13.60	0.35
12 Pediatric Services of America, Inc.	PSAI	\$9.68	12/31/2001	\$187,668,714	\$8,664,200	\$92,367,840	3.9%	4	6,713,000	0.49	0.050	10.66	1.09
13 Transworld Healthcare, Inc.	ARCI	\$3.36	12/31/2001	\$78,747,000	\$11,290,714	\$236,124,900	7.6%	4	17,555,000	1.32	0.135	20.91	2.14
Statistical Analysis													
14 MVIC/EBITDA Ratio			MVIC/EBITDA			Ratio	MVIC/EBITDA						
14 Arithmetic Mean MVIC/EBITDA Ratio	1.02		Arithmetic Mean MVIC/EBITDA Ratio			24.68							
15 Weighted Mean MVIC/Revenue Ratio	0.84		Weighted Mean MVIC/EBITDA Ratio			29.24							
16 Median MVIC/EBITDA Ratio	0.69		Median MVIC/EBITDA Ratio			10.66							
17 High MVIC/EBITDA Ratio	4.03		High MVIC/EBITDA Ratio			187.11							
18 Low MVIC/Revenue Ratio	0.32		Low MVIC/EBITDA Ratio			5.79							
19 Upper Quartile MVIC/Revenue Ratio	1.32		Upper Quartile MVIC/EBITDA Ratio			13.60							
20 Lower Quartile MVIC/Revenue Ratio	0.43		Lower Quartile MVIC/EBITDA Ratio			8.60							
21 Percentile Value Multiple Ratio (2)	0.32		Percentile Value Multiple Ratio (3)			7.55							
22 MVIC/Revenue technique Selected Ratio (4)	0.32		MVIC/EBITDA technique Selected Ratio (4)			7.55							
23 SUBJECT ENTITY		Net Revenue	SUBJECT ENTITY			EBITDA							
24		\$234,970,611					\$6,654,687	(8)					
25 Indicated Debt-Free Value of MVIC (5)		\$75,531,942	Indicated Debt-Free Value of MVIC (4)				\$59,148,558						
26 Weight of Methods (6)		0.60	Weight of Methods (7)				0.40						
27 Indicated Debt-Free Value of MVIC (5)							\$65,579,588	(9)					
28 Less Interest-Bearing Debt													
29 Unadjusted Value of Equity before Premiums and discounts													
30 Plus Control Premium, (10%)													
31 Less Discount for Marketability, (30%)													
32 Total Fair Market Value of the 100% Total Invested Capital of SUBJECT ENTITY													
C Share Price as of 1/8/02. Source: www.bighcharts.com													
D Period ending date of guideline public company utilized in columns E, F, G and J													
E Total Net Revenues for 12-month period ending in column D													
F Historical 3-year normalized earnings before interest, taxes, depreciation and amortization (See Schedule 9, Column D) multiplied by													
G Market Value of Invested Capital (MVIC) is calculated as market value of the common equity (Column C) x Column J plus preferred equity (Schedule 3, Line 17 plus interest-bearing debt (Schedule 3, Line 16).													
H 2001 operating margin of each public company (See Schedule 3, Line 38).													
I The VALUATOR's weighting of guideline companies based upon their similarity to the SUBJECT ENTITY, e.g., revenue size, scope of services, etc.													
J The number of outstanding common shares as of the date in column D.													
K Calculated as Column G divided by Column E.													
L Calculated as Column G divided by Column F.													
M Calculated as Column G divided by Column F.													
N Calculated as Column G weighted by weighting assigned in Column I.													
Notes by Column:													
1 Negative EBITDA values was given a MVIC/EBITDA of zero (\$0).													
2 Calculated as the lowest 1/2 of the first percentile of selected MVIC/Revenue ratios. Both the SUBJECT ENTITY's actual 2001 operating margin (-1.9%) and the normalized operating margin (0.63%) was below the range of the guideline companies' 2001 operating margins (See Schedule 3, Table B, Column A).													
3 Calculated as the 14.20 percentile of selected MVIC/EBITDA ratios. The SUBJECT ENTITY's 3-year weighted operating margin (0.63%) was the 14.20 percentile of selected company 3-year weighted operating margins (See Schedule 5, Table B, Column D).													
4 The percentile value of the MVIC/Revenue ratio and MVIC/EBITDA ratio (Line 21) was selected by the VALUATOR.													
5 Indicated value derived on a debt-free basis (TIC = Equity + Debt). Calculated by multiplying the selected ratio in (Line 22) by the SUBJECT ENTITY's level of ownership benefit (Line 24).													
6 The VALUATOR's weighting of the techniques based upon their applicability to the valuation engagement.													
7 The SUBJECT ENTITY's 2001 Net Revenues (See Schedule 1, Page 1 of 5, Column C Line 2).													
8 The SUBJECT ENTITY's Normalized Earnings Before Interest Taxes Depreciation and Amortization of 2.83% of net revenue (See Schedule 9, Line 16) multiplied by 2004 Net Revenue of \$234,070,611.													
9 Calculated as the indicated values in Line 25 weighted by weighting assigned in Line 26.													
10 The interest-bearing debt of the SUBJECT ENTITY as of the VALUATION DATE (See Schedule 2, Line 24).													
11 Indicated value derived on a net-of-debt basis (Assets-Debt-Equity). Calculated by subtracting interest-bearing debt (Line 23) from the debt-free (asset) value (Line 22).													
12 Application of a 10% control premium.													
13 Application of a 10% discount for lack of marketability.													
14 Value of the 100% interest in the shares (equity) of the SUBJECT ENTITY. (Line 29 plus Line 30 less Line 31)													

Notes by Column:

- Share Price as of 1/8/02. Source: www.bighcharts.com
- Period ending date of guideline public company utilized in columns E, F, G and J
- Total Net Revenues for 12-month period ending in column D
- Historical 3-year normalized earnings before interest, taxes, depreciation and amortization (See Schedule 9, Column D) multiplied by 2001 Revenue (Column E).
- The VALUATOR's weighting of guideline companies based upon their similarity to the SUBJECT ENTITY, e.g., revenue size, scope of services, etc.
- The number of outstanding common shares as of the date in column D.
- Calculated as Column G divided by Column E.
- Calculated as Column G weighted by weighting assigned in Column F.
- Calculated as Column G divided by Column F.
- Calculated as Column G weighted by weighting assigned in Column I.
- Calculated as Column G weighted by weighting assigned in Column J.
- Calculated as Column G weighted by weighting assigned in Column K.
- Calculated as Column G weighted by weighting assigned in Column L.
- Calculated as Column G weighted by weighting assigned in Column M.
- Calculated as Column G weighted by weighting assigned in Column N.
- Calculated as Column G weighted by weighting assigned in Column O.
- Calculated as Column G weighted by weighting assigned in Column P.
- Calculated as Column G weighted by weighting assigned in Column Q.
- Calculated as Column G weighted by weighting assigned in Column R.
- Calculated as Column G weighted by weighting assigned in Column S.
- Calculated as Column G weighted by weighting assigned in Column T.
- Calculated as Column G weighted by weighting assigned in Column U.
- Calculated as Column G weighted by weighting assigned in Column V.
- Calculated as Column G weighted by weighting assigned in Column W.
- Calculated as Column G weighted by weighting assigned in Column X.
- Calculated as Column G weighted by weighting assigned in Column Y.
- Calculated as Column G weighted by weighting assigned in Column Z.
- Calculated as Column G weighted by weighting assigned in Column AA.
- Calculated as Column G weighted by weighting assigned in Column BB.
- Calculated as Column G weighted by weighting assigned in Column CC.
- Calculated as Column G weighted by weighting assigned in Column DD.
- Calculated as Column G weighted by weighting assigned in Column EE.
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- Calculated as Column G weighted by weighting assigned in Column LL.
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- Calculated as Column G weighted by weighting assigned in Column NN.
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- Calculated as Column G weighted by weighting assigned in Column PP.
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Addus' *actual* operating margin for 2001 (-1.95%) and *weighted* operating margin for 1999-2001 (.63%) were below the operating margins of any of the 13 guideline companies in 2001. (Report, Sch. 9, Table B, columns A & D.) Moreover, Addus' 3-year weighted operating margin was in the 14.20 percentile of the 3-year weighted operating margin of the guideline companies. (Report, Sch. 9, Table B, column D.) Put simply, Addus was much less profitable than the median guideline companies.

As Mr. Cimasi's report indicates, the analysis in Schedule 9 was the sole basis for the selection of the ratios used in the Guideline Company method. The benchmarking analysis in Schedule 3 was irrelevant. Thus, in calculating his MVIC/Revenue ratio, Mr. Cimasi calculated a ratio as the lowest ½ of the first percentile of selected MVIC/Revenue ratios. He explained the basis for this in footnote 11 of Schedule 9:

- “The lowest one-half (1/2) of the first percentile of selected MVIC/Revenue ratios was selected because both the SUBJECT ENTITY's actual 2001 operating margin (-1.95%) and normalized operating margin (0.63%) were below the range of the guideline companies' 2001 operating margins (Column A, Lines 19-31).”

He repeated this explanation in footnote 2 of Schedule 10:

- “Calculated as the lowest ½ of the first percentile of selected MVIC/Revenue ratios. Both the SUBJECT ENTITY's actual 2001 operating margin (-1.95%) and the normalized operating margin (0.63%) was below the range

of the guideline companies' 2001 operating margins (See Schedule 9, Table B, Column A)."

In calculating his MVIC/EBITDA ratio, Mr. Cimasi calculated a ratio in the 14.20 percentile of the guideline companies' MVIC/EBITDA ratios. He explained the basis for this calculation in footnote 3 of Schedule 10:

- "Calculated as the 14.20 percentile of selected MVIC/EBITDA ratios. The SUBJECT ENTITY's 3-year weighted operating margin (0.63%) was the 14.20 percentile of selected company 3-year weighted operating margins (See Schedule 9, Table B, Column D)."

The "benchmarking" analysis in Schedule 3 had no bearing at all on the calculations in Schedules 9 and 10 or on the selection of the ratios used in the guideline company approach. Those ratios were selected based solely on Addus' lack of profitability in 2001 and over a three-year period from 1999-2001.

B. Mr. Cimasi's benchmarking analysis was not flawed

For the reasons given above, even if the Court were to completely discount Mr. Cimasi's benchmarking analysis, the only consequence to Mr. Cimasi's opinion is that it would decrease the operational performance risk discussed in Table 5-8 and Section 5.12.5.1 of the Report (p. 18). Mr. Cimasi added 300 basis points (3%) to the discount rate for this measure of specific risk related to Addus. *Ibid.* Therefore, discounting the benchmarking analysis would not materially change Mr. Cimasi's overall conclusion of value.

Nevertheless, Defendants are flatly wrong in asserting that Mr. Cimasi's application of the benchmarking analysis was flawed.

1. **Mr. Cimasi relied on information that was known or knowable as of January 8, 2002, his date of valuation**

Defendants first contend that the benchmarking analysis relies exclusively on information regarding Addus and other publicly held companies that was not available as of January 8, 2002. (Mtn. 4 ¶ 8 at 4.) As Mr. Cimasi explained, the financial information on which he relied was information that was either known or knowable at the “as of” date. (8/26/2005 Tr. 189:5-8 (“[B]ut I want to just clarify that – that we did not do this with hindsight, that the information that we relied on is information that could have been known or should have been known as of the date of the valuation.”).) The period for these financial statements had closed as of January 8, 2002, and the actual financial events for the period had occurred. Indeed, Mr. Cimasi addressed precisely the argument that Defendants raise during his cross-examination:

Q. None of those reports were actually available in their final form as of January 8th, 2002, were they?

A. The actual filings of the 10-K and 10-Q were not available as of that date, but the information that they contained as defined would have been known or knowable as of 12/31. The information existed. The operating – historical operating performance of the company in fact existed, and through adequate due diligence anything that appeared in the 10-K and 10-Q was known or knowable or could have been known or knowable at that date. (8/30/2005 Tr. 26:7-16.)

Mr. Cimasi provided further clarification of his point in response to the Court’s question:

“The concept is is [sic] that the information that ultimately goes into whatever the audited financial statements are does in fact exist. It is there. The point of entry data is what that’s referred to. You know, the actual performance data is there,

and the same types of tests and testing that an audit firm would perform in providing the certified audit for the company's books are techniques that are widely used, and sometimes even more intensely by, you know, a typical acquirer especially with a transaction of this size.

[A] big portion of the valuation process is in fact due diligence, and so it's likely – the underlying assumption is that it's likely that since information and data did exist and it's just a matter of it being uncovered, then the information was known or knowable at that time. (8/30/2005 Tr. 28:22-29:16; ellipses added.)

Defendants cite no authority at all to challenge Mr. Cimasi's use of Addus' 2001 audited financial statements and the 2001 financial statements of the comparable public companies, even though such information was not published until after the valuation date. On the contrary, his decision to do so is supported both by the caselaw and by the professional literature.³ It also should be noted that the fact that Addus' financial condition continued to decline in 2002 and 2003, as reflected in its 2002 and 2003 audited financial

³ See, e.g., *First Nat'l Bank of Kenosha v. United States*, 763 F.2d 891, 894 (7th Cir. 1985) ("[T]he only relevant facts are those that this hypothetical buyer and seller could reasonably have been expected to know at that time. Thus, subsequent events are not considered in fixing fair market value, *except to the extent that they were reasonably foreseeable at the date of valuation*") (emphasis added); *McKesson Corp. v. Islamic Republic of Iran*, 116 F. Supp. 2d 13, 22 (D.D.C. 2000) (proper use of information "available only after the valuation date would be to establish by inference the existence of a fact that would be known to an investor prior to that date"), *aff'd in relevant part and rev'd on other grounds*, 271 F.3d 1101 (D.C. Cir. 2001), *cert. denied*, 537 U.S. 941 (2002); *Hess v. Comm'r*, T.C. Memo 2003-251, 86 T.C.M. (CCH) 303 (U.S. Tax Ct. Aug. 20, 2003) ("as a general rule, subsequent events are not considered in fixing fair market value, except to the extent that they were reasonably foreseeable at the date of the valuation"); Robert F. Reilly, *Recent Judicial Decisions Guide Valuation Analysts*, 21-Sep AM. BANKR. INST. J. 26, Am. Bankr. Inst. J. Sept., 2002 ("It is a basic valuation principle that *unanticipated subsequent events* that occur after the relevant valuation date should be ignored in the valuation analysis.") (emphasis added).

statements (Trial Exs. 5, 6) corroborates Mr. Cimasi's appraisal and his valuation. *See Jacobson v. Comm'r*, T.C. Memo 1989-606, 58 T.C.M. (CCH) 645, T.C.M. (P-H) 89,606 (U.S. Tax Ct. Nov. 6, 1989) ("Subsequent events or facts may be used to corroborate an appraisal that is based on facts known as of the valuation date."); *Vesper v. Comm'r*, T.C. Memo 1989-358, 57 T.C.M. (CCH) 1035, T.C.M. (P-H) ¶ 89,358 (U.S. Tax Ct. Jul 24, 1989) (same).

2. **Mr. Cimasi accounted for the fact that the adjustments to Addus' financial statements included non-recurring events**

Defendants assert that Mr. Cimasi failed to adjust his valuation for certain non-recurring adjustments to Addus' financial statements. As Mr. Cimasi explained, he did make these adjustments as part of the process of normalizing Addus' operating results. (*See* Report § 5.3.2.2, at p. 4 (discussing normalization process); *id.* Sch. 5 (normalization of Addus operations); 8/30/2005 Tr. 41:12-19). Defendants simply assert, without authority or reasoning, that the normalization process does not factor in non-recurring items. (Mtn. 4 at n.1.) This assertion is belied by the report.

3. **Mr. Cimasi properly excluded outlier data points in his statistical analysis**

Defendants broadly assert that Mr. Cimasi inappropriately excluded certain data points in reaching his conclusions. (Mtn. 5.) These contentions, which are made in bullet-point fashion in the motion, are specious and easily addressed:

- First bullet point: Mr. Cimasi excluded outliers in his calculation of ratios in lines 24-46 of Schedule 3, because that is where the calculation is reflected.

No purpose would be served by excluding data from lines 1-23, which is just a summary of the information used to calculate lines 24-46. This would not affect any aspect of Mr. Cimasi's Report or conclusions, and Defendants do not contend otherwise.

- Second bullet point: The "standard deviation" is a measure of how spread specific data points are. *Waisome v. Port Authority of New York and New Jersey*, 948 F.2d 1370, 1376 (2d Cir. 1991); *Palmer v. Schultz*, 815 F.2d 84, 92 n.7 (D.C. Cir. 1987). Therefore, the choice of an appropriate standard deviation will depend on the data that is being analyzed; it is not "one size fits all." *See U.S. v. LaChance*, 788 F.2d 856, 866-67 (2d Cir. 1986); *Peightal v. Metropolitan Dade County*, 26 F.3d 1545, 1556 n.16 (11th Cir. 1994). As Mr. Cimasi explained in footnote 8 to Schedule 3 of his report, he did not use ratios more than one standard deviation from the mean. The reason for this decision is that the survey data from Risk Management Associates and Integra (Columns O and P of Schedule 3) used in the report already excludes outliers and therefore already is a measure of central tendency.⁴ In other words, this survey data is comprised of a statistical selection, as Mr. Cimasi explained in footnotes 3 & 4 of Schedule 3, which already eliminates wide dispersion of data. By contrast, in Schedule 11

⁴ "Central tendency is 'a value (as the mean or median) representative of an entire statistical distribution.'" *Erie County Geriatric Center v. Sullivan*, 952 F.2d 71, 75 n.2 (3d Cir. 1991) (quoting WEBSTER'S THIRD NEW INTERNATIONAL DICTIONARY, Unabridged (1966)).

(direct market comparable transaction method), Mr. Cimasi used data within two standard deviations, because there were only 11 companies and no survey data was used. In Schedule 10, there was no variation of data that required application of a standard deviation.

In sum, two points are clear: (1) Mr. Cimasi applied the same standard deviations to the same sets of data; and (2) Defendants do not explain (nor can they) why application of the same standard deviation throughout the Report would be appropriate regardless of the data set, what the appropriate deviation would be, and how this would alter the conclusions in the Report.

- Third through sixth bullet points: In their Motion, defendants criticize Mr. Cimasi for excluding “extreme outliers” from his benchmarking analysis. (Mtn. 5-6). Nowhere do Defendants cite any authority for the proposition that these “extreme outliers” should have been included. Indeed, it would have been inappropriate for Mr. Cimasi to *include* outliers regardless of the impact on his conclusions. *See Association of Oil Pipe Lines v. F.E.R.C.*, 281 F.3d 239, 246 (D.C. Cir. 2002) (“To the extent that FERC refused to exclude outliers on the ground that doing so changed the result, it obviously missed the whole point: the object of excluding outliers is to prevent extreme and spurious data from biasing an analysis, i.e., affecting its result adversely.”).

4. **Addus was not a “median” company**

One of the points that Defendants attempt to make in their brief (and attempted to make through Mr. Peltz’s testimony) was that Addus was a “median” company. The assertion that Addus was a “median” company is belied by the evidence in the record – *e.g.*, that Addus had a negative EBITDA in 2001 and only a marginally better EBITDA in 2002 and 2003; that Addus was eating into its working capital; that Addus was stretching out its creditors; that Addus’ HME division was hemorrhaging money; and that Addus required a \$4 million infusion of capital from Mr. Wright in 2002. It also is belied by Mr. Cimasi’s benchmarking analysis.

In his lines 38 through 46 of Schedule 3 (the benchmarking analysis), Mr. Cimasi compared four aspects of Addus’ operations to those of the comparable companies: profitability ratios, liquidity/solvency ratios, operating efficiency and activity ratios, and leverage ratios. Based on this analysis, Mr. Cimasi concluded that Addus was “less profitable, solvent, efficient and more leveraged than industry benchmarks.” (Report § 5.2, p. 2.) This conclusion is supported by the data in Schedule 3:

- As to profitability, Addus’ operating margin was -1.9%, while the industry average was 5.15%. (Report Sch. 3, lines 38-46, column R.) Therefore, Addus was materially less profitable than the industry average.
- As to solvency, Addus’ working capital ratio was 4.07% while the industry average was 9.75%. (Report Sch. 3, lines 38-46, column R.) Therefore, Addus was materially less solvent than the industry average.

- As to leverage ratios, Addus' debt ratio was .90, while the industry average was .62, and Addus' ratio of interest-bearing debt to total capitalization was 82.24%, while the industry average was 49.88%. (Report Sch. 3, lines 38-46, column R.) Therefore, Addus was materially more leveraged than the industry average.
- As to efficiency, Addus' days in accounts receivable were 68.84, while the industry average was 66.26, and Addus' capital expenditures to revenue ratio was 2.20%, while the industry average was 1.99%. (Report Sch. 3, lines 38-46, column R.) Thus, Addus' efficiency was inferior to the industry average as to these categories. In terms of total asset turnover and depreciation and ratios of amortization to revenue, Addus was equal or superior to industry average. Therefore, Addus either was marginally less efficient or was as efficient as the industry average. This is the only one of these four criteria where Addus was not materially inferior to the industry average.

C. Conclusion

Mr. Cimasi performed his benchmarking analysis appropriately. Defendants' attacks on that analysis are based on misrepresentations of the data and flawed reasoning. In any event, the benchmarking analysis only relates to one aspect of one of Mr. Cimasi's calculations: the "Operational Performance Risk" calculation in the derivation of the "Subject Entity Specific Risk Premium." (Report § 5.12.5 & 5.12.5.1, pp. 17 & 18.) It does *not* relate to his other opinions. Therefore, these attacks, even if justified (which they are not) would not materially alter Mr. Cimasi's analysis.

II. CONTROL PREMIUM AND DISCOUNT FOR LACK OF MARKETABILITY

A. Neither the control premium nor the discount for lack of marketability materially alter Mr. Cimasi's conclusion

Defendants do not contend that applying a control premium or a discount for lack of marketability is inappropriate. They concede that discounts and premiums are appropriate – indeed, Scott Peltz included both in his analysis. Instead, they quibble with the amount of the discount and the premium.

As Plaintiffs told the Court in their Valuation Memorandum, the debate over the appropriate discount and premium is largely irrelevant. As show below, using Mr. Cimasi's analysis, reproducing Table 5-11 on page 27 of Section 5 of the Report, the fair market value of Addus, *excluding* all discounts and premiums would be \$27,000,000:⁵

⁵ The conclusions in the table are based on the following calculations: Mr. Cimasi's indicated total present fair market value of the 100% interest in the equity of Addus before discounts and premiums under his Discounted Cash Flow Method was \$24,380,469. (Report, Sch. 8, line 20.) Under his Guideline Company method it was \$33,906,747. (Report, Sch. 10, line 29.) And under his Direct Market Comparable Transaction method (where he applied a 10% discount as a surrogate for transaction costs, *see* Report § 5.16.1, p. 25), it was \$23,144,635. Using the weighting of the methods reflected in Table 5-11 (Report § 5.17, at 27), the fair market value of Addus, excluding all discounts and premiums, would be \$27,114,769.

Table 5-11 Reconciliation, Correlation, and Synthesis of Approaches and Methods – Final Conclusion of Value of the SUBJECT INTEREST without Application of Discounts or Premiums

Method	100% Interest, on a Control, closely-held level of value	Weight	Value Results – FMV of the SUBJECT INTEREST (100%)
Discounted Cash Flow Method	\$24,380,469	60%	\$14,628,281
Guideline Company Valuation Method	\$33,906,747	30%	\$10,172,024
Direct Market Comparable Transaction Method	\$23,144,635	10%	\$2,314,464
FINAL OPINION OF VALUE OF SUBJECT INTEREST – 100%			\$27,114,769.00
FINAL OPINION OF VALUE OF SUBJECT INTEREST – 100% (ROUNDED)			\$27,000,000

The purchase price in this transaction was *at least* \$115 million according to Mr. Wright and Mr. Cimasi and, depending on other assumptions concerning the proper calculation of price under the Modification, may have been substantially higher. Therefore, the debate over discounts and premiums has no relevance to the issue of whether the transfer of \$7.5 million to Mr. Wright pursuant to the alleged First Amendment was a fraudulent conveyance under Section 548 of the Bankruptcy Code.

Nevertheless, Defendants' criticisms of Mr. Cimasi's calculation of the discounts and premium are flawed.

B. Mr. Cimasi's application of a 10 percent control premium is justified
 Defendants criticize Mr. Cimasi for excluding Med's 2001 acquisition of Tender Loving Care from the control premium surveys. Reprinted below is the Mergerstat Review

Control Premium Study for 2001. As Mr. Cimasi explained, the mean in this control premium study was 52%, the standard deviation was 69%, and Med paid a control premium of 185.7% in connection with the acquisition of TLC by Med, which was almost two standard deviations from the mean. (8/29/2005 Tr. 199:16-200:24.) Mr. Cimasi explained that he included the acquisition of Insight Health Services Corp. by Childs Associates, L.P., with a control premium of 2.9%, because this control premium was less than one standard deviation from the mean. (*Id.* 200:25-201:7 (“it wasn’t more than one standard deviation from the mean, and so the statistical test that we adopted here was if it was more than one standard deviation from the mean we considered it to be an outlier”)).

Mergerstat Review

Calculation of Control Premium Study
2001

	A	B	C
All Healthcare Transactions in Mergerstat Review with reported Control Premium (5)	Buyer	Seller	Control Premium
	1 Anam, LLC	NextHealth, Inc.	48.3%
	2 Childs(JW) Associates LP	Insight Health Services Corp	2.9%
	3 DIANON Systems, Inc.	UroCor, Inc.	4.7%
	4 e-MedSoft.com, Inc.	Tender Loving Care, Inc.	185.7%
	5 Private Group	US Medical Group, Inc. - 36.3%	20.0%
	6 Mean		52.3%
Conclusion of Review of All Transactions	7 Standard Deviation		68.6%
		Transaction #4, the Control Premium (185.7%) is greater than one (1) standard deviation from the mean, therefore it was excluded from our analysis.	
Analysis Utilized in HCC Report (4 transactions)	Buyer	Seller	Control Premium
	1 Anam, LLC	NextHealth, Inc.	48.3%
	2 Childs(JW) Associates LP	Insight Health Services Corp	2.9%
	3 DIANON Systems, Inc.	UroCor, Inc.	4.7%
	5 Private Group	US Medical Group, Inc. - 36.3%	20.0%
	6 Mean		19.0%

Defendants also criticize Mr. Cimasi for excluding Kohlberg Kravis Roberts & Co.’s (“KKR”) 1999 acquisition of Apollo Management LP from the control premium studies.

Reprinted below is the Mergerstat Review Control Premium Study for 1999. The mean in this control premium study was 52.8%, and the standard deviation was 58.3%. KKR paid a control premium of 220%, which was almost three standard deviations from the mean. Therefore, Mr. Cimasi properly excluded it.

**Mergerstat Review
Calculation of Control Premium Study
1999**

	A	B	C
	Buyer	Seller	Control Premium
1	Ion Beam Applications Sa	SteriGenics International, Inc.	52.1%
2	Kelso & Co	Unilab Corp - 93%	15.6%
3	Kohlberg Kravis Roberts & Co	Appollo Management LP	220.0%
4	Loab Holdings, Inc.	Lob One, Inc - REM 19%	10.3%
5	Landauer Hospital Supplies, Inc.	Community Care Services, Inc.	53.6%
6	National Nephrology Associates, Inc.	Renex Corp	50.9%
7	Private Group	InterDent, Inc.	15.2%
8	TA Associates	Physicians' Specialty Corp	23.5%
9	UICI	HealthPlan Services Corp	30.3%
10	Welsh, Carson, Anderson & Stowe	Concentra Managed Care, Inc. - REM 85.1%	56.3%
11	Mean		52.8%
12	Standard Deviation		58.3%
Conclusion of Review of All Transactions		Transaction #3, the Control Premium (220%) is greater than one (1) standard deviation from the mean, therefore it was excluded from our analysis.	
	A	B	C
	Buyer	Seller	Control Premium
1	Ion Beam Applications Sa	SteriGenics International, Inc.	52.1%
2	Kelso & Co	Unilab Corp - 93%	15.6%
4	Loab Holdings, Inc.	Lob One, Inc - REM 19%	10.3%
5	Landauer Hospital Supplies, Inc.	Community Care Services, Inc.	53.6%
6	National Nephrology Associates, Inc.	Renex Corp	50.9%
7	Private Group	InterDent, Inc.	15.2%
8	TA Associates	Physicians' Specialty Corp	23.5%
9	UICI	HealthPlan Services Corp	30.3%
10	Welsh, Carson, Anderson & Stowe	Concentra Managed Care, Inc. - REM 85.1%	56.3%
11	Mean		34.2%

Defendants next argue that the data on which Mr. Cimasi relied in the Report suggest that a control premium of greater than 10 percent would be appropriate. (Mtn. ¶¶ 18-20, at 8.) In his report, Mr. Cimasi expressly explained why he selected a control premium below the mean of these studies:

Accordingly, given the facts and circumstances of the SUBJECT ENTITY and the public market for the home healthcare industry segment within which it operates, as well as the VALUATOR's informed consideration as to the typical investor's perception as to whether ownership of a 100% interest would add incremental value to the aggregate value of the minority shares represented by the methodology utilized, it is reasonable to conclude that the methods that result in a control level of value of the SUBJECT INTEREST would receive, and should be subject to, the application of a control premium *below the mean of the studies described above.* (Report § 5.11.1, p. 10 (emphasis added).)

Thus, Mr. Cimasi expressly states in his report that his control premium departs from the median, and he explains why. Defendants argue that this conclusion is wrong, but they provide no evidence from any source to support this argument.

C. Mr. Cimasi's application of a 30 percent discount for lack of marketability is justified

Defendants' complaints about Mr. Cimasi's 30 percent discount for lack of marketability ("DLOM") ring hollow, given that they have introduced testimony by Mr. Peltz, who applies a 25% illiquidity discount in his "analysis." Moreover, Defendants have never argued that a DLOM is inappropriate or should not be applied, nor have they cited any evidence in support of that position. The only issue Defendants dispute is the magnitude of the discount.

Concerning the magnitude of the discount, Defendants assert that Mr. Cimasi relied exclusively on empirical pre-initial public offering ("IPO") studies relating to discounts applicable to minority interests, and they contend that Dr. Pratt asserts that such studies

“have no application in connection with the acquisition of controlling interests.” (Mtn. 9.)

Both statements are false.

First, as Mr. Cimasi explained in his testimony, in addition to the pre-IPO studies and the Mergerstat study, he relied on a number of empirical studies of illiquid public stock (so-called “restricted stock” studies). (8/30/2005 Tr. 154:6-13; Report § 5.11.2.1 & Table 5-3, p. 11.) These studies of restricted public stocks are different from the pre-IPO studies to which Chris Mercer and Dr. Pratt are referring.

Moreover, as Mr. Cimasi explained in his report, he did not simply rely on the stock studies in determining the appropriate discount but included factors specific to Addus in determining the appropriate discount for lack of marketability, including the financial performance of Addus and the feeble transactional marketplace for home health entities. (Report § 5.11.2.4, p. 14.)

Second, neither Dr. Pratt nor Mr. Mercer asserts that such empirical studies “have no application in connection with the acquisition of controlling interests,” as Defendants contend. What they assert is that the *magnitude* of the discount would be different. As Dr. Pratt states, “[d]iscounts for lack of marketability for controlling interests allowed in the U.S. Tax Court range from 3 to 33%, compared with the more typical 30 to 45% for minority interests.” Shannon P. Pratt, BUSINESS VALUATION DISCOUNTS AND PREMIUMS 167 (John Wiley & Sons, Inc. ed. 2001). Dr. Pratt further notes that “[t]he U.S. Tax Court clearly has recognized DLOMs for controlling interests. In fact, when DLOMs have been an issue in the U.S. Tax Court, they have been accepted far more often than they have been rejected.” *Id.* at 173.

In sum, neither Mr. Cimasi's control premium nor his discount for lack of marketability materially alter the conclusions in his report. Moreover, Defendants' criticisms of Mr. Cimasi's calculation of the appropriate control premium and discount for lack of marketability are unfounded.

III. MR. CIMASI'S ANALYSIS UNDER THE DISCOUNTED CASH FLOW METHOD IS SOUND

A. Defendants have neither alleged nor proven that the discounted cash flow method is an inappropriate method for valuing Addus

In their Motion, Defendants *assert* that Mr. Cimasi's analysis under the discounted cash flow method is flawed, but nowhere do they cite any evidence, either in the form of judicial opinions or scholarly literature, to support that assertion. This is an important point. Mr. Peltz did not use anything that he labeled a "discounted cash flow method"; therefore, there is no reason for Defendants to pull any punches in attacking this method or Mr. Cimasi's application of it, if they could muster any ammunition for such an attack. Nevertheless, Defendants' entire criticism of Mr. Cimasi's discounted cash flow analysis is reduced to three inconsequential points:

- (1) Mr. Cimasi used Addus' poor operational performance in the calculation of several of the "specific risk factors" in Section 5.12 of the Report, even though these risk factors are labeled as being distinct (Mtn. ¶ 30, at 11);
- (2) Mr. Cimasi added 1200 basis points when determining the weighted average cost of capital, because Mr. Wright personally guaranteed Addus' debt (Mtn. ¶ 31, at 11); and

(3) Mr. Cimasi assumed that a purchaser would move Addus to the industry average immediately, rather than gradually (Mtn. ¶¶ 32, 33, at 11-12).

Even if these assumptions were flawed (which, as explained below, they are not), Defendants do not even assert, let alone demonstrate, that any of these points undermine Mr. Cimasi's methodology or would have *any material impact at all* on Mr. Cimasi's opinion. Thus, despite the Court's expressed skepticism of the discounted cash flow method, the only evidence concerning that method is Mr. Cimasi's testimony and Plaintiffs' Valuation Memorandum, both of which support its validity.

B. There are no flaws in Mr. Cimasi's assumptions in his discounted cash flow analysis

Even the trivial attacks that Defendants do attempt to make on Mr. Cimasi's application of the discounted cash flow method miss the mark.

1. There is no overlap in Mr. Cimasi's specific risk categories

Despite Defendants' contention, there is no overlap in Mr. Cimasi's consideration of Addus' operational performance in his calculation of the specific risk premium attributable to Addus. (Report § 5.12 & Table 5-8, pp. 17-18.)

- Mr. Cimasi's "Operational Performance Risk" is based on the benchmarking analysis. (Report § 5.12.5.1, p. 18.)
- The "Depth of Management Risk" (Report § 5.12.5.2) is based on the testimony of Ron Ford and Mr. Wright that Mr. Ford's job responsibilities – as CFO, for oversight of the HME Division, for oversight of Arcadia, and for

due diligence – were too extensive for him to consistently keep his eye on the ball. (E.g., 8/26/2005 Tr. 163:2-15.)

- The “Market/Competition Risk” is based on the competition in *Addus*’ market from a small number of public companies and “the estimated five to seven thousand local and regional providers.” (Report § 5.12.5.3.) It has nothing to do with *Addus*’ operational performance.
- The “Financial Condition Risk” is based on the “significant errors and inconsistencies … in the SUBJECT ENTITY’s financial and management reporting systems.” (Report § 5.12.5.4.) While these errors certainly contributed to *Addus*’ poor operational performance, these are distinct risks.
- The “Reimbursement Risk” is based on the risk of reimbursement created by government regulations. (Report § 5.12.5.5.) Again, it has nothing to do with *Addus*’ operational performance.

2. **Mr. Cimasi’s addition of 1200 basis points when determining the weighted average cost of capital is valid**

In his testimony, Mr. Cimasi explained his rationale for the addition of 1200 basis points when determining his weighted average cost of capital. *Addus*’ debt was guaranteed. Because of the personal guaranties, *Addus*’ interest rate was lower than it otherwise would have been. An acquirer may be able to replace the debt without guaranties, but that acquirer would not compensate *Addus* (or give additional value to *Addus*) based on the acquirer’s credit-worthiness; that is, the acquirer will not pay for what the acquirer brings to the table.

(8/29/2005 Tr. 139:21-140:2, 142:8-23.)

3. Mr. Cimasi's assumptions concerning Addus moving to the industry average were appropriate and, in any event, Mr. Cimasi made the same assumptions concerning Addus' expenses

Defendants assert that Mr. Cimasi assumed that a hypothetical purchaser would move Addus to the industry average immediately and that this would increase the value of Addus. (Mtn. ¶¶ 32, 33, at 11-12.) Defendants offer no substantiation for their assertion. In fact, Mr. Cimasi also did not phase in industry expenses, which industry expense structure was lower than Addus' actual expense structure; if he had, it would have reduced the value of Addus. So this criticism is a non-issue.

IV. DEFENDANTS FAIL TO DEMONSTRATE ANY FLAWS IN MR. CIMASI'S APPLICATION OF THE GUIDELINE COMPANY METHOD

Defendants' attack on Mr. Cimasi's application of the Guideline Company method is premised entirely on their false assumption that Mr. Cimasi used the benchmarking analysis in the Guideline Company method. (Mtn. at 12-13.) As discussed in Part I, above, he did not. Defendants have no other criticisms of this method.

V. DEFENDANTS FAIL TO DEMONSTRATE ANY FLAWS IN MR. CIMASI'S APPLICATION OF THE DIRECT MARKET COMPARABLE TRANSACTION METHOD

Defendants attack Mr. Cimasi's selection of comparable transactions in his direct market comparable transaction method. In making these attacks, Defendants simply ignore the fact that the transactions that Mr. Cimasi considered were the *only* relevant ones.

The home healthcare market was in significant flux during the years immediately preceding the “as of” date of January 8, 2002. (See generally Report § 4.) Among other things, the prospective payment system (“PPS”) in home healthcare was implemented in October 2000. (Report § 4.7.1.2, p. 10.) The PPS had a dramatic effect on the home healthcare market and led to a significant decrease in the number of home healthcare agencies. (*Ibid.*) Thus, any market transactions that occurred significantly prior to the “as of” date and probably before October 2000 would be an unreliable indicator of the value of a transaction that was to be completed in 2002.

The only transactions of companies of any significant size that occurred in 2000 and 2001 were the Med acquisitions of Chartwell and TLC. (This fact is further support for Mr. Cimasi’s lack of marketability discount, as there was, during this period, a dearth of buyers for companies like Addus.) The Med transactions are inherently suspect; among other things, it is clear that Med paid a significant premium for TLC. In any event, prior Med transactions are inappropriate touchstones for the value of a third company (Addus) also being acquired by Med, as these prior Med transactions shed no objective light on what some party other than Med (that is, a hypothetical purchaser) would pay for Addus.

Thus, the transactions that Mr. Cimasi considered were the only relevant transactions in the marketplace. As Mr. Cimasi explained, the lack of comparable transactions, among other problems, caused Mr. Cimasi to accord this method only 10% of the weight in his overall valuation. (Report § 5.17.3; 8/29/2005 Tr. 230:18-231:232:23.)

**VI. DEFENDANTS' ASSERTIONS CONCERNING THE ABSENCE OF A
SYNERGY VALUE OF THE ADDUS TRANSACTION ARE LAWYERS'
ARGUMENTS THAT DO NOT UNDERCUT MR. CIMASI'S ANALYSIS,
REASONING, OR CONCLUSIONS**

Defendants assert that Mr. Cimasi's conclusion that no synergistic acquisition premium could be achieved between Med and Addus is flawed. (Mtn. 16-17.) First, it should be noted at the outset that Defendants have adduced no evidence at all that the acquisition would lead to a synergy value, beyond Mr. Wright's speculation concerning the impact of a computer software program that Mr. Magliochetti would not allow him to look at. Thus, Defendants' criticisms of Mr. Cimasi's conclusions once again ring hollow. In any event, they are unfounded.

As Defendants concede, Mr. Cimasi's conclusions about the absence of a synergistic premium for the Med acquisition are based on Med's track record. (Mtn. ¶ 52, at 16.) As he testified:

[T]he point is from that lesson is a practical reality, you know, in the investment community, and that's, you know, again serving as a proxy I will tell you that unless the acquiring entity has the ability, has the resources, the depth of management, the track record, you know, to be able to achieve those hoped for, intended, advertised, ballyhooed synergies and that, you know, unless they have that, then there's nothing else to talk about because it cannot exist as a matter of definitional – you know, Aristotle put it, A is A, A cannot be B, and so before you go to the step of trying to quantify whether or not the geographic markets would have meshed, and whether their services would have meshed, and whether they would have been able to achieve leverage in the market place, all the things we did look at, and in our report I'll show you where we talk about those things, but before you even get

to that point you don't get to that point unless you've crossed the first threshold, and the evidence is clear here. It's almost irrefutable evidence that Med's record -- track record at achieving any sort of synergies or any sort of efficiencies or any sort of things that would be related to an acquisition premium with their prior transactions was abysmal at best, and so for an investor -- a reasonably and typically informed investor, because that's what investors look at, they look -- and lenders look at, what is the track record of these folks? What have they done in the past?

So you don't get to even go to the next step of feasibility if you can't get past the first hurdle.

THE COURT: Mr. Cimasi, you've done a very good job of helping me readjust my perspective. In other words, I can't about third base, unless I get to first. If the management capacity isn't there and they don't have a demonstrated record, all the rest is nonsense?

THE WITNESS: That's pretty well held in our business, yes, your Honor. (8/26/2005 Tr. 199:20-201:4.)

Defendants do not dispute Mr. Cimasi's conclusion that the transaction, in fact, had no synergistic value or that Med, in fact, lacked the resources and ability to create synergy. Instead, they argue that Med's track record was not known as of January 8, 2002. (Mtn. ¶¶ 53, 54, at 16.) This is not true. As of January 8, 2002, Med had written off over \$200 million in goodwill as a consequence of failed transactions. (Ex. 151; Report § 6.4, at 4.) Med had no history at all of successful acquisitions. Defendants do not and cannot show that the Chartwell acquisition provided any such synergistic value. (Mtn. ¶ 57, at 17.)

**VII. DEFENDANTS' COMMENTS REGARDING INVESTMENT VALUE AND
MR. CIMASI'S OPTION VALUATION METHODOLOGY ARE BASED ON
A MISCHARACTERIZATION OF MR. CIMASI'S REPORT**

At the end of their Motion, Defendants direct two criticisms at Mr. Cimasi, both of which are based on a mischaracterization or misreading of Mr. Cimasi's report.

First, Defendants claim that there is a disconnect between Mr. Cimasi's definition of fair market value and this transaction, because the definition of fair market value assumes a cash purchase, and a significant portion of the price in the Stock Purchase Agreement was consideration other than cash. (Mtn. 17 ¶ 61.) This argument conflates the concepts of "value" and "price."

Fair market "value" is normally to be ascertained from "what a willing buyer would pay in *cash* to a willing seller."⁹ *Almota Farmers Elevator & Warehouse Co. v. U. S.*, 409 U.S. 470, 474 (1973) (emphasis added); *U.S. v. Shugart*, 176 F.3d 1373, 1375 (11th Cir. 1999) ("value is easy to determine: it's the actual cash value, or fair market value, of the item - that is, '[t]he fair or reasonable cash price for which the property could be sold in the market in the ordinary course of business.'") (quoting Black's Law Dictionary 35 (6th ed.1990)).

The fact that the *price* that Med agreed to pay included non-cash components has no effect on the value. To determine whether the price exceeded the value, one simply needs to calculate the cash value of the price, then compare the cash value of the price to the cash value of the business. Mr. Cimasi did this, and concluded that the cash value of the *price*

was at least \$115 million (8/29/2005 Tr. 9:16-23) and that the *cash value* of Addus was \$21 million.

Second, Defendants state that Mr. Cimasi “no longer stands behind his valuation” of the alleged First Amendment. (Mtn. ¶ 65, at 18.) This is false. As Mr. Cimasi explained, he valued the First Amendment at \$0 without applying Black-Scholes: “Assuming a hypothetical probability that an investor, acting in his or her rational economic self-interest, would enter into such an agreement, the VALUATOR has concluded that, under the assumed terms, no economic or financial value would exists that would accrue to or could be ascribed to the OPTION INTEREST.” (Report § 7.2, p 3.) Mr. Cimasi then went on and engaged in a *hypothetical* application of Black-Scholes assuming a purchase price of \$21 million, but no such price ever existed or was proposed.

Therefore, Mr. Cimasi has not rejected any aspect of his valuation methodology. He simply has concluded that, in this case, given the vast disparity between the fair market value of Addus and the price, the methodology has no real application. A rational hypothetical investor would not give any cash value for the First Amendment interest under the facts of this case.

VIII. CONCLUSION

In drafting their motion to strike Mr. Cimasi’s testimony, Defendants undoubtedly attempted to include every argument that they could cobble to challenge Mr. Cimasi’s opinion. It is remarkable, therefore, that Defendants have been unable to find any flaws with Mr. Cimasi’s methodology or any authority that controverts the basic premises or assumptions in his Report.

Instead, Defendants have pulled together a series of nit-picks that, for the most part, are based on a mischaracterization of Mr. Cimasi's Report. Beyond that, Defendants quibble with the magnitude of Mr. Cimasi's discounts and premiums; even assuming that those criticisms were valid, which they are not, the discounts and premiums do not materially alter the valuation conclusion in the Report.

Therefore, Plaintiffs respectfully request that Defendants' motion to strike be denied.

Dated: Los Angeles, California
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