IN THE SUPREME COURT OF IOWA
NO. 20-1290

NATIONWIDE MUTUAL INSURANCE COMPANY,
PLAINTIFF-APPELLANT,

v.

POLK COUNTY BOARD OF REVIEW,
DEFENDANT-APPELLEE.

APPEAL FROM THE IOWA DISTRICT COURT
FOR POLK COUNTY
THE HONORABLE PAUL SCOTT
DISTRICT COURT JUDGE
CASE NO. CVCV054470

APPELLANT'S FINAL BRIEF

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ROUTING STATEMENT

This case presents this Court with the opportunity to enunciate or change legal principles on a substantial question regarding the proper valuation of commercial real estate. See Iowa R. App. P. 6.1101(2)(f). This case -- a property tax valuation dispute involving two single tenant office buildings in downtown Des Moines – requires the Iowa Supreme Court's guidance on the proper interpretation of Iowa law when valuing buildings like these given this Court's decision in *Wellmark, Inc. v. Bd. of Review*, 875 N.W.2d 667 (Iowa 2016.) In *Wellmark* this Court held that market analysis is the preferred method of determining actual value, and "other factors" may be considered *if, and only if,* market value cannot be readily established through the preferred market analysis. Since this Court's decision in *Wellmark*, several District Courts have struggled in determining when to abandon market analysis and use other factors. A clear position from this Court regarding a proper interpretation of *Wellmark* will help property owners and their respective Boards of Review resolve these issues efficiently and amicably. Plaintiff-Appellant Nationwide Mutual Insurance Company respectfully requests the Iowa Supreme Court retain this case.

STATEMENT OF THE CASE

Nature of the Case

Plaintiff Nationwide Mutual Insurance Company ("Nationwide") appeals from an Order upholding the Board of Review's assessment of 1100 and 1200 Locust for the 2017 tax year. Nationwide argues the District Court failed to consider the substantial evidence presented at trial by Nationwide regarding the market valuation of these properties as required by Iowa law and this Court's decision in *Wellmark*. In contrast, the Defendant Board of Review ("Board") failed to introduce *any* evidence that complied with the standard set in *Wellmark*, and instead introduced flawed valuations based on the replacement costs of both buildings. Further, even though the District Court found Nationwide had presented competent evidence and utilized the appropriate methods for valuing property for tax purposes, and the Board failed to present any evidence recognized as competent by *Wellmark*, the District Court inexplicably found the Board's evidence more competent and credible. Wellmark asserts it presented competent evidence of the fair market value of the properties at issue and has easily met its burden.

Course of Proceedings

On July 12, 2017, Nationwide filed its Petition for Judicial Review of the Board's decision to reject its protest of the valuations assigned to

Nationwide's office buildings located at 1100 and 1200 Locust. The matter was tried beginning on February 18, 2020 and concluding on February 20, 2020. Final post trial briefs were submitted on May 4, 2020, and on September 22, 2020 the District Court issued its Findings of Fact, Conclusions of Law, and Order upholding and affirming the Board's assessment of $87,050,000 for 1100 Locust and $44,910,000 for 1200 Locust. This appeal followed.

STATEMENT OF THE FACTS

A. <u>Minimum Assessment Agreement.</u>

Nationwide's buildings at 1100 and 1200 Locust were some of the first buildings constructed in the Des Moines Western Gateway, as part of the revitalization of the downtown area. On May 8, 2006, the Des Moines City Council approved an Urban Renewal Development Agreement (Ex. I, App. 1375-1493) between the City and Nationwide which laid out the requirements for the buildings in question, and also set forth the incentives Nationwide was to receive for going forward with the project. Under the Agreement, Nationwide:

1) Agreed to add a 280,000 square foot addition to its existing 500,000 square foot building at 1100 Locust and agreed to build a

360,000 square foot building at 1200 Locust. (Ex. I p. 3, App. 1380); and

2) Agreed to a 10-year minimum property tax assessment of $78.5 million for 1100 Locust and $36 million for 1200 Locust once the properties were completed. (Ex I p. 11, App. 1388).

In exchange, the City agreed to pay Nationwide economic incentives of approximately $28 million to help finance the project. (Ex. I, pp. 14-15, App. 1391-1392)

The Minimum Assessment Agreement was signed and recorded in 2007 and was to go into effect upon the city issuing certificates of completion for the respective properties. (Ex. J, App. 1494-1500). The Certificate of Completion for 1100 Locust was issued on February 28, 2008 (Ex. K, App. 1501-1503) and the Certificate of Completion for 1200 Locust was issued on December 8, 2008. (Ex. L, App. 1504-1505). Accordingly, the Minimum Assessment Agreement was in effect for the 2017 and 2018 tax years.

B. <u>Assessments for 2017 and 2018.</u>

For tax years 2017 and 2018, the Polk County Assessor increased its valuation on both properties. The valuation of 1100 Locust increased from $80,230,000 to $87,050,000. (Ex. 1, App. 0218-0224). The valuation of

1200 Locust increased from $41,390,000 to $44,910,000. (Ex. 4, App. 0225-0229).

Bryon Tack, the Director of Commercial Real Estate for the Polk County Assessor's Office, testified as to how he determined the 2017 valuations for both buildings. According to Tack, his initial 2017 assessments for 1100 and 1200 Locust were NOT based on any appraisals that took into consideration comparable sales, the income approach, or the cost approach. (Trans. Vol. IV p. 85, App. 0203). Instead, Tack testified that for 2017, the Assessor simply took the 2015 property tax valuations for all the buildings in the central business district ("CBD") and increased them by 8.5%. (Trans. Vol. IV p. 84, App. 0202).

Once the protests were filed, the Assessor went back and did a cost analysis using a state manual which estimates the cost of construction. (Trans. Vol. IV p. 85, App. 0203). Once the Assessor established the estimated cost of construction, he deducted physical depreciation based on the age of the buildings and arrived at a depreciated value. Unlike the professional appraisers engaged by Nationwide and the Board, the Assessor did not further reduce the cost by functional or external obsolescence. Since the value determined by the Assessor using the cost approach exceeded the assessed value of the properties, the Assessor determined that no adjustment to the valuation was necessary and the protests were denied.

C. Vaske Appraisals

Once the Board's decision was appealed to District Court, Nationwide engaged two appraisers to value the properties under Iowa law, one of whom was Don Vaske. Vaske is a Des Moines based appraiser with 26 years' experience valuing commercial property. To appraise the two buildings, Vaske relied on the definition of market value set forth in Iowa Code §441.21.

> The actual value of all property subject to assessment and taxation shall be the fair and reasonable market value of such property except as otherwise provided in this section. "Market value" is defined as the fair and reasonable exchange in the year in which the property is listed and valued between a willing buyer and a willing seller, neither being under any compulsion to buy or sell and each being familiar with all the facts relating to the particular property. Sale prices of the property or comparable property in normal transactions reflecting market value, and the probable availability or unavailability of persons interested in purchasing the property, shall be taken into consideration in arriving at its market value. In arriving at market value, sale prices of property in abnormal transactions not reflecting market value shall not be taken into account, or shall be adjusted to eliminate the effect of factors which distort market value, including but not limited to sales to immediate family of the seller, foreclosure or other forced sales, contract sales, discounted purchase transactions or purchase of adjoining land or other land to be operated as a unit.

(Ex. 9 p. 2, Vaske Appraisal of 1100 Locust, App. 0540)[1]. To arrive at an appraised value, Vaske's analysis included the development of the Cost Approach, the Sales Comparison Approach, and the Income Approach.

Vaske's appraisal valued a "fee simple" interest. A fee simple interest is defined as "Absolute ownership, unencumbered by any other interest or estate, subject only to the limitations imposed by the governmental powers of taxation, eminent domain, police power, and escheat." (Ex. 9 p. 3, Vaske Appraisal of 1100 Locust, App. 0541). As a result, Vaske avoided looking at sales comparisons that were sale-leaseback transactions or sales that involved a long-term lease already in place, since those would not be considered "fee simple" transactions. (Trans. Vol. II p. 46, App. 0168). Finally, Vaske appraised the property based on its "highest and best use." In his opinion, the highest and best use of the property as vacant was for some type of commercial or office use. The highest and best use of the property as improved was its current use as a single occupant building. (Ex. 9 pp. 47-48, Vaske Appraisal of 1100 Locust, App. 0585-0586).

[1] Vaske prepared separate appraisals for 1100 and 1200 Locust, exhibits 9 and 10, but the definitions and basis for the appraisals are identical in both.

1. <u>Vaske Cost Approach – 1100 Locust</u>

Using the Cost Approach, Vaske valued the land by looking at comparable sales in the CBD and arrived at a valuation of $8,794,000 for the bare land on which the building sits.

For the improvements, Vaske determined the replacement cost by using Marshal and Swift Valuation Service as a reference to determine the cost per square foot to actually build the building and arrived at a replacement cost of $137,852,835.

Since this figure is obviously greater than "market value" as defined in the Iowa Code, it is subject to depreciation. According to the Appraisal Institute, depreciation is defined as "The difference between the **<u>market value of an improvement</u>** and its reproduction or replacement cost at the time of appraisal. The depreciated cost of the improvement can be considered an indication of the improvement's contribution to the property's market value." (Ex. 9 p. 59, Vaske Appraisal of 1100 Locust, App. 0597). So, when applying depreciation under the Cost Approach, you must take into account the fair market value of comparable properties. Vaske did so by looking at sales data for two Des Moines owner-occupied properties that were comparable to 1100 and 1220 Locust and arrived at a depreciation figure of 67%.

In summary, Vaske's valuation of 1100 Locust using the cost basis was as follows:

Replacement Cost (including improvements)	$138,162,835
Deprecation 67%	($ 92,569,099)
Total Depreciated Cost Improvements	$ 45,593,736
Add Land Value	$ 8,794,000
Cost Approach Indicated Value	$ 54,387,736
Rounded to	$ 54,388,000

(Ex. 9 pp. 59-61, Vaske Appraisal of 1100 Locust, App. 0597-0599).

2. <u>Vaske Cost Approach – 1200 Locust</u>

Vaske used the same analysis for 1200 Locust that he used for 1100 Locust. However, since 1200 Locust was newer and smaller than 1100 Locust, the depreciation was lower. Under the analysis, Vaske's valuation of 1200 Locust using the Cost Approach was as follows:

Replacement Cost (including improvements)	$ 59,672,495
Deprecation 62%	($36,996,947)
Total Depreciated Cost Improvements	$ 22,675,548
Add Land Value	$ 3,974,000
Cost Approach Indicated Value	$ 26,649,548
Rounded to	$ 26,650,000

(Ex. 10 pp. 52-57, Vaske Appraisal of 1200 Locust, App. 0690-0695)

3. Vaske Sales Comparison Approach – 1100 Locust

Under the Sales Comparison Approach, recent sales of similarly improved properties are an indication of market value for the property after adjusting for differences. This recognizes the availability of competitive substitute properties in the market. The accuracy of this approach depends upon 1) there being a market for this type of property; and 2) comparable sales must be "arm's length" transactions between unrelated parties. (Ex. 9 p. 62, Vaske Appraisal of 1100 Locust, App. 0600).

In this case, Vaske identified 8 sales of office properties in the Des Moines area having greater than 100,000 square feet and meeting the criteria. Sales 1 through 5 are in the CBD, and sales 6, 7 and 8 are in West Des Moines. Vaske broadened his search and also identified sales 9 and 10, which are two properties over 500,000 square feet which are owner occupied corporate headquarters in Northfield Illinois and St. Paul Minnesota. After analyzing the sales, Vaske used 2, 8, 9 and 10 as comparable sales for his analysis.

Like the subject property, these properties are all examples of corporate home office properties originally developed for single use occupancy. The sales were purchased by entities acquiring the offices for owner occupancy. None of the sales used by Vaske were multi-tenant buildings or buildings located in high priced areas on the east or west coast. Vaske did not consider properties that were sale-leaseback transactions or leased fees since they are not comparable to the sale of a "fee simple" estate. Once those four sales were identified, they had to be adjusted based on the comparable properties' location, size, condition, land to building ratio, and parking.

After adjustments, the indicated value ranges of the comparable properties were $46.07 to $63.55per square foot (psf), and subject 2 located directly across the street from 1100 Locust was valued at $62.22 psf. For his final valuation, Vaske used $63.00 psf and multiplied that value by 765,674 square feet to arrive at a value of $48,236,642 for 1100 Locust, rounded to $48,237,000. (Ex. 9 pp. 65-67, Vaske Appraisal of 1100 Locust, App. 0603-0605).

4. <u>Vaske Sales Comparison Approach – 1200 Locust</u>

Vaske used the same analysis for 1200 Locust that he used for 1100 Locust. The adjustments were slightly different based on the age and size of 1200 Locust as compared to 1100 Locust. After adjustments, the indicated value ranges of the comparable properties were $52.66 to $72.62 psf, and subject 2 located directly across the street from 1100 was valued at $67.17 psf. For his final valuation, Vaske used $70.00 psf and multiplied that value by 371,290 square feet to arrive at a value of $26,034,400 for 1200 Locust, rounded to $26,034,000. (Ex. 10 pp. 61-63, Vaske Appraisal of 1200 Locust, App. 0699-0701)

5. **Vaske Income Approach – 1100 Locust**

Under the Income Approach the appraiser determines the value of the property based on its ability to produce income over a period of time and considers investors' expectations of future net income it is expected to produce. To do that, the appraiser:

1) Determines the expected net revenue of the building based on rental income;
2) Allows for a reasonable vacancy rate on the property;
3) Estimates the expenses necessary to operate the building; and
4) Capitalizes the resulting net operating income ("NOI") by applying an expected overall rate of return ("OAR") to determine a reasonable value for the property.

(Ex. 9 p. 80, Vaske Appraisal of 1100 Locust, App. 0618)

In his analysis Vaske first determined market rent in the CBD and found a range of $6.48 to $9.50 psf with the largest property involving 86,000 square feet. Since 1100 Locust had 722,824 square feet of rentable space, Vaske arrived at a rental rate at the low end of the range and used a figure of $7.25 psf. (Ex. 9 pp. 82-83, Vaske Appraisal of 1100 Locust, App. 0620-0621).

For a vacancy rate, Vaske used the Greater Des Moines Real Estate Market Survey and looked at the vacancy rate for class A and B office buildings. The two Nationwide properties at issue in this case comprise 20% of the CBD office inventory. Considering the size and location of the property, Vaske forecasted a vacancy rate of 9%, and variable annual expenses of $91,442. (Ex. 9 pp. 83-85, Vaske Appraisal of 1100 Locust, App. 0621-0623).

Using the information discussed above, Vaske arrived at a projected NOI as follows:

Gross Income (722,824 sf x $7.25 psf)	$5,240,474
Less Vacancy rate 9%	($ 471,643)
Gross Income	$4,786,831
Less Variable expenses	($ 919,442)
Net Operating Income	$3,849,389

Vaske then selected an 8% capitalization rate using the effective capitalization rates of the properties he identified in the Sales Comparison approach and also using a mortgage equity analysis. (Ex. 9 pp. 86-87, Vaske Appraisal of 1100 Locust, App. 0624-0625). Dividing the NOI of $3,849,389 by the 8% cap rate results in an indicated value of $48,117,363, which rounds to a value of $48,117,000. (Ex. 9 p. 85, Vaske Appraisal of 1100 Locust, App. 0623).

6. <u>Vaske Income Approach – 1200 Locust</u>

Vaske used the same analysis for 1200 Locust that he used for 1100 Locust. The differences are due to 1200 Locust being half the size of 1100 Locust. As a result, Vaske used a rental rate of $8.00 psf instead of $7.25; a vacancy rate of 7% instead of 9%, and lower variable annual expenses of $418,461 due to the size of the building. (Ex. 10 pp. 78-81, Vaske Appraisal of 1200 Locust, App. 0716-0719).

Using the information discussed above, Vaske arrived at a projected NOI as follows:

Gross Income (326,508 sf x $8.00 psf)	$2,612,064
Less Vacancy rate 7%	<u>($ 182,844)</u>
Gross Income	$2,429,220
Less Variable expenses	<u>($ 414,461)</u>
Net Operating Income	$2,010,759

Vaske used the same analysis to select a capitalization rate of 8%. Dividing the NOI of $2,010,759 by the 8% cap rate results in an indicated value of $25,134,488, which rounds to a value of $25,134,000. (Ex. 10 p. 83, Vaske Appraisal of 1200 Locust, App. 0721).

7. **Vaske Reconciliation**

Vaske testified that the Cost Approach is most accurate with new construction, but in the case of these two buildings, there is functional and external obsolescence that makes them less reliable. (Trans. Vol. II p. 62, App. 0169; Ex. 9 p. 86, Vaske Appraisal of 1100 Locust, App. 0624). The Income Approach is most accurate when properties are bought for their income producing potential, but since these are owner occupied buildings, that weakens the reliability of the income approach.

Under the Sales Comparison Approach, Vaske relied on sales of large corporate home offices in Des Moines and in Midwest. The adjustments are reasonable and Vaske testified this approach deserves the most weight. There is nothing unique about these buildings, and if they were put up for sale they would be marketed nationally and may take time to sell. But the price a national buyer would pay will be based on the Des Moines market, not on what the building would sell for on the east or west coast. (Trans. Vol. II pp. 63-64, App. 0170-0171).

In sum, Vaske opined that the fair market value of the 1100 Locust property is $49,000,000, and the fair market value of the 1200 Locust property is $26,000,000. Below is a chart summarizing the two appraisals and the three approaches Vaske used to reach his determination of value.

	1100 Locust	**1200 Locust**
Cost Approach	**$54,385,000**	**$26,650,000**
Sales Comps	**$48,237,000**	**$26,034,000**
Income	**$48,117,000**	**$25,134,000**
Reconciliation	**$49,000,000**	**$26,000,000**

D. Scaletty Appraisals

Nationwide's other appraiser is Tom Scaletty. Scaletty is based in Kansas City with 23 years' experience valuing commercial property. To appraise the two buildings, Scaletty relied on the definition of market value contained in Iowa Code § 441.21 and appraised the property as a fee simple estate. (Ex. 7 p. 7, Scaletty Appraisal of 1100 Locust, App. 0240)[2]. Since he was appraising a fee simple, Scaletty testified:

> "I looked for sales of ideal single-tenant buildings that were being sold for use as office. **I excluded – attempted to exclude buildings that were leased at the time, because buildings that are built to suit or sale leased-back property are not indicative of the fee simple interest, which is what we're charged with estimating here**. Those sales of leased buildings equate value to the lease or the income stream that's guaranteed by that lease."

[2] Scaletty prepared separate appraisals for 1100 and 1200 Locust, exhibits 7 and 8, but the definitions and basis for the appraisals is identical in both.

(Trans. Vol. I pp. 85-86, App. 0146-0147). In his analysis, Scaletty specifically avoided looking at sales comparisons that were sale-leaseback transactions or second generation leased fees, since a significant portion of the sale price was reflective of the lease, and not the fee simple estate itself. (Trans. Vol. I pp. 87-88, App. 0148-0149).

Scaletty found that the highest and best use of the property as vacant was not to build a commercial office building, but instead to hold for later development unless significant government assistance was available to help finance the project, similar to the assistance received by Nationwide. As improved, Scaletty found the highest and best use was as a single tenant office with the potential of multi-tenancy in the future. (Trans. Vol. I pp. 79-80, App. 0144-0145). Scaletty's methods and analysis was similar to the analysis performed by Vaske. Accordingly, his conclusions are summarized below.

1. <u>Scaletty Cost Approach – 1100 Locust</u>

Scaletty looked at comparable sales in the CBD and arrived at a valuation of $8,790,000 for the real estate. For the improvements, Scaletty determined the replacement cost to be $175,848,992. (Ex. 7 pp. 47-50, Scaletty Appraisal of 1100 Locust, App. 0280-0283).

To determine physical deterioration Scaletty looked at the useful life of the property for short term and long term items. To determine functional and external obsolescence, Scaletty compared the cost method with the values derived from the sales and income approaches and determined that demand for such properties does not justify the development costs. (Ex. 7 pp. 51-52, Scaletty Appraisal of 1100 Locust, App. 0284-0285). His conclusion was as follows:

Replacement Cost (including entrepreneurial profit)	$175,848,992
Short-Lived Deprecation	($ 2,520,717)
Long-Lived Deprecation	($ 30,826,764)
External Obsolescence	($111,821,512)
Total Depreciated Cost Improvements	$ 30,676,999
Add Land Value	$ 8,790,000
Cost Approach Indicated Value	$ 39,466,999
Rounded to	$ 39,470,000

(Ex. 7 pp. 51-52, Scaletty Appraisal of 1100 Locust, App. 0284-0285).

2. **Scaletty Cost Approach – 1200 Locust**

Scaletty used the same analysis for 1200 Locust:

Replacement Cost (including entrepreneurial profit)	$77,858,199
Short-Lived Deprecation	($ 1,114,672)
Long-Lived Deprecation	($10,919,494)
External Obsolescence	($46,754,033)
Total Depreciated Cost Improvements	$19,070,000
Add Land Value	$ 4,370,000
Cost Approach Indicated Value	$ 23,440,000

Rounded to $ 23,440,000

(Ex. 8 pp. 56-63, Scaletty Appraisal of 1200 Locust, App. 0434-0441).

3. Scaletty Sales Comparison Approach – 1100 Locust

Scaletty identified six properties with similar characteristics to the Nationwide buildings: three in Des Moines, one in Little Rock Arkansas, one in Northfield Illinois, and one in Lenexa Kansas. Five of the properties were owner occupied properties and the sale was of a fee simple estate. None involved sale leaseback transactions or leased fees. One property -- 400 Locust in Des Moines -- is a multi-tenant building and was sold as a leased fee. The five single tenant properties are all examples of corporate home office properties originally developed for single use occupancy. (Ex. 7 pp. 53-61, Scaletty Appraisal of 1100 Locust, App. 0286-0294).

After adjustments for time of sale, size of the property, age/condition, parking, and location, the indicated value ranges of the comparable properties were $32.25 to $65.44 psf, with an average of $52.26 psf. For his final valuation, Scaletty used $50.00 psf and multiplied that value by 787,724 square feet to arrive at a value of $39,386,200 for 1100 Locust, rounded to $39,390,000. (Ex. 7 p. 67, Scaletty Appraisal of 1100 Locust, App. 0300).

4. Scaletty Sales Comparison Approach – 1200 Locust

Scaletty used the same analysis for 1200 Locust that he used for 1100 Locust. The adjustments were different based on the age and size of 1200 Locust as compared to 1100 Locust. After adjustments, the indicated value ranges of the comparable properties were $37.02 to $89.10 psf with an average of $64.86 psf. For his final valuation, Scaletty used $65.00 psf and multiplied that value by 348,335 square feet to arrive at a value of $22,641,775 for 1200 Locust, rounded to $22,640,000. (Ex. 8 p. 78, Scaletty Appraisal of 1200 Locust, App. 0456).

5. Scaletty Income Approach – 1100 Locust

Scaletty's Income Approach model differed from the models used by the other appraisers. Scaletty used the "Argus" software program which is specifically designed as a real estate investment and leased fee tool, but was still based on determining an estimated NOI for the property and applying a reasonable capitalization rate. (Ex. 7 p. 70, Scaletty Appraisal of 1100 Locust, App. 0303). Using that model and a discounted cash flow analysis, Scaletty estimated a value of $39,550,000. (Ex. 7 p. 90, Scaletty Appraisal of 1100 Locust, App. 0323).

6. <u>Scaletty Income Approach – 1200 Locust</u>

Scaletty used the same analysis for 1200 Locust that he used for 1100 Locust, with the major differences being due to the size and age of the building. Using the Argus model and a discounted cash flow analysis, Scaletty estimated a value of $24,240,000. (Ex. 8 p. 101, Scaletty Appraisal of 1200 Locust, App. 0479).

7. <u>Scaletty Reconciliation</u>

Scaletty testified he assigned no weight to the Cost Approach. It's an *indication* of value, but he has "never talked with any investor or developer that has ever used the cost approach to estimate what they should pay for something." (Trans. Vol. I p. 99, App. 0150). He gave less weight to the Income Approach because "there's a lot of pitfalls going on with a property like this. It's so large, that finding a single tenant to occupy it is very problematic, and so it requires a different type of analysis." (Trans. Vol. I pp. 99-100, App. 0150-0151). Scaletty testified he "relied significantly on the sales comparison approach, <u>**because it specifically focuses on single tenant buildings that were sold for continued single office use**</u>." (Trans. Vol. I p. 99, App. 0150). Like Vaske, Scaletty focused on true comparable sales of large corporate home offices in Des Moines and in the region. Accordingly, Scaletty "weighted the sales and income 60/40 in my analysis and came up with a value of $39,450,000." (Trans. Vol. I p. 100, App. 0151). Scaletty used the same analysis in reconciling the appraisal methods for 1200 Locust where he came up with a value of $23,280,000. (Trans. Vol. I p. 105, App. 0152)

Below is a chart summarizing the two appraisals and the three approaches Scaletty used to reach his determination of value.

	1100 Locust	**1200 Locust**
Cost Approach	**$39,470,000**	**$23,440,000**
Sales Comps	**$39,390,000**	**$22,640,000**
Income	**$39,550,000**	**$24,240,000**
Reconciliation	**$39,450,000**	**$23,280,000**

E. Kenney Appraisal

The Board of Review engaged two of its own appraisers to value the properties. The first to testify was Mark Kenney, an appraiser from Philadelphia who provided a single combined appraisal for both 1100 and 1200 Locust. Unlike the other three appraisers who testified, Kenny did not base his determination of market value on the definition contained in Iowa Code § 441.21. Instead, Kenney included in his report a discussion of Iowa cases interpreting market value under a variety of scenarios. (Ex. A pp. 31-35, Kenney Appraisal, App. 0772-0776). Since the interpretation and application of Iowa law is a task for this Court, anything in Kenny's testimony or report regarding the proper measure of market value should be disregarded.

Kenney assumed that the subject properties, if sold, would continue to have access to and use of the parking ramp located at 1100 Walnut Street, despite the fact they are separately assessed, and also "assumes any necessary easements are in place." (Ex. A p. 40, Kenney Appraisal, App. 0781). However, there was no evidence presented at trial that a buyer would have any right or access to the separate parking ramp.

Kenny indicated in his report that he was appraising the "fee simple interest" in the subject properties, which is defined as "absolute ownership unencumbered by any other interest or estate, subject only to the limitations imposed by the government power of taxation, eminent domain, police power and escheat." However, at trial he testified that many of the comparable sales he used in his analysis were not "fee simple" sales but instead involved sales encumbered by leases or other interest. (Ex. A p. 46, Kenney Appraisal, App. 0787).

1. Kenney Sales Comparison Approach

Under this approach Kenney identified various corporate headquarters located throughout the United States and used them as "comparable sales" for his analysis. However, those sales were not truly comparable and of little use in determining fair market value. Kenny testified that Des Moines is the 88th largest metropolitan area in the United States, but he did not limit his search for comparable properties in nearby or similarly sized cities. Instead, he looked at properties in the largest metropolitan areas in the country and ignored any single occupant sales in Des Moines or Iowa. (Vol. III p. 41, App. 0185). Those sales Kenney did use have little in common with the subject property given their size, location, and the terms of the sales involved.[3]

Sales Comp 1 is a multi-building office complex located on a 101 acre campus in Tampa Florida. Citicorp was the existing tenant with a few years remaining on the lease and purchased it from the existing owners for $116 million. Included in the sale price were a fitness center, child care, salon, bank, convenience store, two parking ramps and a surface parking lot. It

[3] Kenney used the same comparable sales for 1100 and 1200 Locust.

sold for \$172.62 psf and Kenny "adjusted" it down to \$120.83 psf.[4] (Ex. A p. 109 and 120, Kenney Appraisal, App. 0850 and 0861).

Sales Comp 2 is the Facebook headquarters in the San Francisco area. It's a ten-building complex on 56 acres with 3,700 parking spaces. It was sold to Facebook (the tenant) for \$202 million with 10 years remaining on its lease of the property. The sale price was \$197.65 psf and \$100.77 after adjustments. Despite the fact it was purchased by its only tenant with 10 years remaining on the list, Kenney made no ownership interest adjustment. (Ex. A p. 110 and 120, Kenney Appraisal, App. 0851 and 0861).

Sales Comp 3 is a sales-leaseback arrangement involving the Verizon headquarters in New Jersey that sold for \$650 million in 2015. As part of the deal, Verizon agreed to a 20 year lease with renewal options for an additional 28 years. It was originally acquired by Verizon for \$99.5 million in 2005. It has 1.4 million square feet of rentable area on 139 acres. The property has a pond, covered parking, conference facilities and a full-service cafeteria. It sold for \$464.50 psf and \$195.09 after adjustments. (Ex. A p. 111 and 120, Kenney Appraisal, App. 0852 and 0861).

Sales Comp 4 is a State Farm operations center in Austin Texas and also represents a sale-leaseback between State Farm and the new owner.

[4] The adjusted psf for 1200 Locust is slightly different based on the size and age of the building compared to 1100 Locust, but the analysis is similar.

State Farm entered into a 15 year lease as part of the sale for $110 million. It has 448,000 square feet on 83 acres. It sold for $245.04 psf and $140.16 after adjustments. (Ex. A p. 112 and 120, Kenney Appraisal, App. 0853 and 0861).

Sales Comp 5 is the Rolls Royce building in Indianapolis and is the $79 million sale of two seven story office buildings with 10 years remaining on its lease with Rolls Royce. It has 400,000 square feet on 9 acres. It sold for $195.53 psf and $173.63 after adjustments, but Kenney made no adjustments based on the purchase of a leased fee. (Ex. A p. 112 and 120, Kenney Appraisal, App. 0853 and 0861).

Sales Comp 6 is the AON building in Lake County Illinois. The sale was for $148 million and included a six story office building with 818,686 rentable square feet on 30 acres. At the time of the sale, AON had 12.1 years remaining on its lease. It sold for $180.78 psf and $142.36 after adjustments, but Kenney once again made no adjustments based on the purchase of a leased fee. (Ex. A p. 112 and 120, Kenney Appraisal, App. 0853 and 0861).

Based on these comparable sales, Kenney determined the value of the properties under the Sales Comparison Approach was $107,000,000 for 1100 Locust, and $63,000,000 for 1200 Locust. However, all of Kenney's comparable sales are in much large metropolitan areas that are not indicative of the smaller Des Moines market. Further, most of his comparable sales involved properties subject to a long term lease, which clouds comparability and raises the question of whether the buyer was interested in the property or the income stream generated by an advantageous lease. Either way, Kenney's comparable sales are not helpful in determining the fair market value of the subject properties.

2. <u>Kenney Income Approach</u>

Kenney's Income Approach is similar to the Income Approach used by Vaske. First, he estimated the potential gross income based on a projection of rental and other income from the property. In his report, Kenney claimed the rentals he used for his analysis are "predicated on comparison with comparable properties in the subject's market….**<u>Market rental is the rental income that the space in question would most probably command on the open market</u>**…." After determining gross income, Kenney deducted an amount for vacancy and collection loss, as well as operating expenses, to arrive at net operating income. Once NOI was determined, Kenney applied a capitalization rate to arrive at a value for the property. (Ex. A p. 124, Kenney Appraisal, App. 0865).

Even though Kenney indicated he would look to "market rent" to arrive at gross income, his report considered the office rental rates at three buildings in the Austin Texas area and a separate building in Indianapolis. (Ex. A p. 127, Kenney Appraisal, App. 0868). Nowhere in his report or his testimony did Kenney reference office rental rates in Des Moines or in Iowa, and nowhere in his report or his testimony does he explain how he arrived at a rental rate of $10 psf for 1100 Locust and $13 psf for 1200 Locust. In fact, he did not think the market rates at Des Moines multi-tenant properties were even relevant. (See Vol. IV at pp. 6-7, App. 0187-0188). He testified that while he failed to explain what specific adjustments he made to the rental rate for those out of state properties to determine an appropriate rental rate, he made those adjustments based on his experience. (See Vol. IV at pp. 10-11, App. 0189-0190). Without more, the rental rates used by Kenney are not supportable.

Based on the rental rates relied upon by Kenney, he determined the value of the properties under the Income Approach was $80,000,000 for 1100 Locust, and $55,000,000 for 1200 Locust. However, since Kenney's rental rates are the starting point for any income analysis, and the office rates he used have no relationship to the Des Moines market, his calculation of expected net operating income and the resulting calculation of value based on a reasonable capitalization rate is useless. Even assuming Kenney's capitalization rate and estimated expenses are reasonable, a 10% difference in the rental rate would result in a 10% difference in the estimated value under the Income Approach. (Ex. A p. 134, Kenney Appraisal, App. 0875). As a result, it is an unreliable estimate of the fair market value of the properties.

3. Kenney Cost Approach

Kenney's Cost Approach was similar to the methods used by the other appraisers. He first valued the land by looking at comparable sales. He then determined the replacement cost of the improvements by using Marshal and Swift Valuation Service as a reference to determine the cost per square foot to actually build the building. Thereafter, Kenney reduced the value for physical depreciation and functional obsolescence.

All of the appraisers came up with similar land values for the bare ground and the costs of improvements were in the same range using the Marshall and Swift data. Physical deprecation was also similar among all the appraisals since it was based on the age of the buildings with economic lives of 55 and 60 years for the two buildings.

The biggest difference among the appraisers was how they calculated functional and external obsolescence. All the other appraisers separately calculated functional obsolescence for the two separate buildings. Kenney, however, calculated functional obsolescence on page 151 of his report by combining the two buildings (Ex. A p. 151, Kenney Appraisal, App. 0893) and then apportioning that obsolescence factor between the separate buildings on page 152 of his report. According to his direct testimony and his report, Kenney assigned functional obsolescence of $36,313,347 to 1100 Locust, which reduced the estimated value of the property to $99,000,000 under the Cost Approach. For 1200 Locust, the functional obsolescence was calculated to be $12,972,811, which reduced the estimated value of the property to $41,000,000. (Ex. A p. 152, Kenney Appraisal, App. 0894).

But at trial, Kenney admitted under cross-examination his calculations were in error. In fact, based on his calculations contained on page 151 of his report, the functional obsolescence for 1100 Locust should be $50 million instead of $36 million, which means the value under the Cost Approach should be $85 million, not $99 million. Here is his testimony regarding his calculation of functional obsolescence:

Q: And then if you divide that number by 7.7 percent, you get the obsolescence for 1100 Locust, and that comes to $50,029,117.

A: Yeah. 50 million, that's what I get too, yes.

> **Q:** Well, on page 152, which is your cost approach, final number, you assign functional and economic obsolescence of 36 million to 1100 Locust when really, under your analysis, it should be 50 million, shouldn't it?
>
> **A:** Well, yeah. I ended up – I allocated it differently.

(Vol IV pp. 45, App. 0193). And since the obsolescence is wrong, the value of 1100 Locust is overstated:

> **Q:** So your total accrued depreciation, instead of being 74 million, is going to be $88,543,273, which, when you subtract that from the 165 million number up above, leaves you with a total depreciated value of the improvements of $76,517,396 instead of 90 million you had.
>
> You add in the land value, and that gets you to $85 million 417 instead of the 99 million that you have; isn't that right?
>
> **A:** I'm not sure I got all the same numbers you – or I followed you 100 percent. If you did the math right, then those are the numbers.
>
> **Q:** Okay. So the cost approach as presented in your report, it's in error, isn't it?
>
> **A:** It's the way I did it at the time, yes.

(Vol IV pp. 45, App. 0193). Given the admitted $15 million error in Kenney's calculations of value under the Cost Approach, his calculations are unreliable as expert testimony.

4. Kenney Reconciliation

Kenney testified he gave the most weight to the Cost Approach, "because of the type of property it is and the fact that I had to go nationwide on both of the other approaches…" (Vol. III p. 26, App. 0184). He gave less weight to the Income Approach, and "very little weight" to the Sales Comparison Approach. Below is a chart summarizing the appraisals and the three approaches Kenney used to reach his determination of value.

	1100 Locust	**1200 Locust**
Cost Approach	**$99,000,000**	**$41,000,000**
Sales Comps	**$107,000,000**	**$63,000,000**
Income	**$80,000,000**	**$55,000,000**
Reconciliation	**$94,000,000**	**$47,000,000**

There are a number of problems with Kenney's analysis. First, as discussed above, Kenney gave very little weight to the Sales Comparison Approach, and in performing that analysis he used properties that are not truly comparable to the two Nationwide properties. Second, in performing his income analysis, Kenney ignored rental rates in the Des Moines market and instead relied on office rental rates from Texas and Indianapolis, which are appreciably higher than Des Moines, and then failed to explain how he adjusted those rates downward. Finally, Kenney testified he gives the most weight to the Cost Approach, yet he acknowledged a $15 million error in his calculations. Taken together, no weight should be given to Kenney's opinions or testimony.

F. Manternach Appraisals

The second appraiser to testify for the Board was Russ Manternach, who is based in Des Moines. Like Vaske and Scaletty, Manternach relied on the definition of market value contained in Iowa Code § 441.21. (Ex. B p. 5, Manternach 1100 Locust Appraisal, App. 1169). Manternach found that the highest and best use of the property as vacant was for "office, retail, and/or multiple family residential development". As improved, Manternach found the highest and best use for "continued office use." (Ex. B p. 53, Manternach 1100 Locust Appraisal, App. 1217).

Unlike the other three appraisers, Manternach did not find that the highest and best use of the property as improved was as a single tenant or owner occupied building. Instead, he treated the building as a multi-tenant building when performing his Sales Approach and Income Approach, and did not appear to differentiate between multi-tenant and single tenant properties. Otherwise, Manternach's methods and analysis was similar to the analysis performed by Vaske and is summarized below.

1. **<u>Manternach Cost Approach – 1100 Locust</u>**

Manternach looked at comparable sales in the CBD and arrived at a valuation of $7,910,000 for the real estate. He determined the replacement cost for the improvements was $144,414,128. (Ex. Z p. 60, App. 1516).

To determine physical depreciation Manternach looked at the useful life of the property and testified the appropriate straight line depreciation was 28 percent. (Vol. IV p. 150, App. 0210; Ex. Z p. 58, App. 1515). But for functional obsolescence, Manternach estimated a figure of 25% of the value <u>after</u> subtracting physical depreciation, so total depreciation of all kinds equaled 46%. He testified that his 25% figure for functional obsolescence – which amounted to $26 million -- was "based on extractions from sales, which I haven't shown here" (Vol. IV p. 151, App. 0211). But nothing in his report explains how he arrived at that figure. In comparison the Board's other appraiser calculated functional obsolescence of $50 million for 1100 Locust – a $27 million difference. In summary, Manternach's valuation of 1100 Locust using the cost basis was $86,100,000, but given his low estimate of external obsolescence it is inconsistent with every other appraisal associated with this case. (Ex. B p. 60, Manternach 1100 Locust Appraisal, App. 1224).

2. **Manternach Cost Approach – 1200 Locust**

Manternach used the same analysis for 1200 Locust that he used for 1100 Locust. He arrived at a valuation of $3,580,000 for the real estate, determined the replacement cost for the improvements was $58,800,000, and found physical depreciation was 28 percent based on straight line depreciation. (Ex. B p. 59, Manternach 1200 Locust Appraisal, App. 1223). Once again, however, Manternach's estimate of 20% external obsolescence was purely subjective and Manternach could not cite to any data to support it. In summary, Manternach's valuation of 1200 Locust using the cost basis was $44,000,000.

3. **Manternach Sales Comparison Approach – 1100 Locust**

Out of all the appraisers who testified, Manternach was to only one who made no attempt to identify single tenant buildings as comparable sales. At trial, he testified the four comparable sales he found were the "most comparable to the subject property", even though he considered all of them to be multi-tenant. (Vol. IV pp. 154-55, App. 0212-0213). However, since the Nationwide buildings in question are large single-occupant properties, any comparisons to multi-tenant buildings are not truly comparable and an appraiser is required to make significant adjustments to support his analysis. Further, three of the four comparable properties selected are leased fees, which are poor comparisons for a fee simple estate. As a result, Manternach's Sales Comparison Approach cannot readily establish the market value of the Nationwide properties.[5] A review of the specific properties and the adjustments required indicates why they are poor comparable sales. (Ex. B p. 62, Manternach 1200 Locust Appraisal, App. 1226)

Sales Comp 1 is a leased fee multi-tenant office building at 400 Locust in Des Moines that sold for $30,200,000 or $62.04 psf which Manternach adjusted up to $94.27 psf. Even though it is a leased fee and some of the purchase price should be attributable to the leases in place as opposed to the property itself, Manternach actually made an <u>upward</u> adjustment to the sale price based on the lease.

Sales Comp 2 is 909 Locust, a 225,654 square foot building located directly across the street from 1100 Locust. Manternach claims it is a fee simple sale that sold for $20,400,000 or $90.40 psf, which Manternach adjusted up to $108.38 psf. However, Manternach testified that $4.8 million of the sale price was for separately assessed parcels that were nearby

[5] Manternach used the same comparable sales for 1100 and 1200 Locust.

parking lots. (Vol. IV pp. 156-57, App. 0214-0215). Which means the purchase price of the separately assessed building was actually $15.6 million, or $69.13 psf. The price per square foot Manternach used as a starting point is obviously inflated by $20.

Sales Comp 3 is two leased fee buildings with 237,077 square feet of space and a 320 stall parking garage in Cedar Rapids that sold for $31,000,000 or $130.76 psf. Even though it is a leased fee with an 86% occupancy, Manternach made no downward adjustment in the purchase price for property rights conveyed. Instead, Manternach ended up adjusting the price upward to $147.35 psf, which is inconsistent with the typical adjustments.

Sales Comp 4 is a 197,658 square foot fully leased fee in Johnston Iowa that was built to suit for Pioneer as a tenant. It sold to an investor for $44,685,000 or $226.07 psf. It is so dissimilar to the Nationwide properties, it was adjusted down to $123.19 psf, losing almost one-half its "value". This is too large an adjustment to be a true comparable sale.

After adjustments, the indicated value ranges of the comparable properties were $94.00 to $147.00 psf, and Manternach valued subject 2 located directly across the street from 1100 at $108 psf (even though that was inflated by at $20 psf). For his final valuation Manternach used $108.00

psf and multiplied that value by 753,074 square feet to arrive at a value of $81,331,992 for 1100 Locust, rounded to $81,300,000. (Ex. B p. 65, Manternach 1200 Locust Appraisal, App. 1229).

4. **Manternach Sales Comparison Approach – 1200 Locust**

Manternach used the same analysis for 1200 Locust that he used for 1100 Locust. The adjustments were slightly different based on the age and size of 1200 Locust as compared to 1100 Locust. After adjustments, the indicated value ranges of the comparable properties was $105 to $162 psf, and subject 2 located directly across the street from 1100 was valued at $118.80. For his final valuation, Manternach used $115 psf and multiplied that value by 371,920 square feet to arrive at a value of $42,770,800 for 1200 Locust, rounded to $42,800,000. (Ex. B p. 64, Manternach 1200 Locust Appraisal, App. 1228).

5. **Manternach Income Approach – 1100 Locust**

Like his Sales Comparison approach, Manternach made no attempt to look at single tenant properties to determine an appropriate rental rate to use to arrive at an estimated net operating income for the building. Instead, he looked at a wide variety of multi-tenant properties with a number of different lease terms to arrive at his estimated triple net lease rental rate of

$11.00 psf. (Ex. B pp. 66-71, Manternach 1100 Locust Appraisal, App. 1230-1235).

But in doing so, he made no downward adjustments in his report for: a) the size of the property in comparison to the Nationwide buildings, b) the inclusion of a tenant improvements allowance in conjunction with the lease rate; or c) parking. Without those adjustments, the rates he looked at to arrive at a final rental rate of $11 psf were clearly inflated, which would result in an inflated NOI when calculating a value using the Income Approach. For example,

Lease # 1 included a $10 psf tenant improvement allowance.

Lease # 2 included a $30 to $40 psf tenant improvement allowance.

Lease # 4 included on-site parking.

Lease # 7 included a $20 psf tenant improvement allowance and on-site parking.

Lease # 8 had a multi-level parking structure and surface parking.

Lease #9 included a $15 psf tenant improvement allowance and on-site parking.

Nothing in Manternach's report or testimony indicates he made any downward adjustments for these factors.

Using rental income of $11 psf for 722,950 square feet of rentable space and an 8% vacancy rate, Manternach assumed gross income of $7,316,254, and Net Operating Income of $6,446, 401. When divided by his selected capitalization rate of 7.85%, the indicated value of the property was $82,100,000. (Ex. B pp. 72-77, Manternach 1100 Locust Appraisal, App. 1236-1241). If, however, the rental rate had been $10 psf instead of $11 psf, the indicated value would decline to less than $75 million if the other assumptions used by Manternach in his analysis stayed the same. A $1 change in the rental rate has a large impact on the indicated value.

6. **<u>Manternach Income Approach – 1200 Locust</u>**

Manternach used the same analysis for 1200 Locust that he used for 1100 Locust, with the major differences being due to the size of the building and the presence of retail properties on the first floor. He made no downward adjustments to the comparable rental rates for: a) the size of the property in comparison to the Nationwide buildings, b) the inclusion of a tenant improvements allowance in conjunction with the lease rate; or c) parking. Manternach used an office rental rate of $11.50 psf, and a retail rate of $14.00 psf, which resulted in an estimated value of $43,000,000.

7. **Manternach Reconciliation**

Manternach testified he gave the least weight to the Cost Approach, and relatively equal weight to the Sales and Income Approaches (Vol. IV pp. 167, App. 0216). Below is a chart summarizing the appraisals and the three approaches Manternach used to reach his determination of value.

	1100 Locust	**1200 Locust**
Cost Approach	**$89,300,000**	**$44,000,000**
Sales Comps	**$81,300,000**	**$42,800,000**
Income	**$82,100,000**	**$42,900,000**
Reconciliation	**$82,100,000**	**$43,000,000**

Manternach's Income and Sales Approach analyses both suffer from the same flaw: they look at comparable sales and comparable rents of multi-tenant buildings with little or no relationship to the two single occupant Nationwide buildings at issue in this case. In his Sales Comparison Approach, Manternach was the only appraiser who failed to use single occupant, fee simple comparable sales and instead relied on four multi-tenant properties requiring significant adjustments to make them "comparable" – three of which were leased fees.

Second, in performing his income analysis, Manternach made no indicated adjustments to his comparable rents for the size of the space being rented, the tenant improvements paid by the landlord, or the amount of parking included in the rent. Given the sales and rents utilized by Manternach in his analyses were not "comparable" to the Nationwide buildings at issue here, Manternach's appraisals are not helpful in determining the fair market value of the properties.

G. Combined Reconciliation of All Appraisals

1100 LOCUST – Assessed at $ 87,050,000

Minimum Assessment $78,500,000

	Vaske	Scaletty	Kenney	Manternach
Cost	**$54,385,000**	**$39,470,000**	**$99,000,000**	**$89,300,000**
Sales Comps	**$48,237,000**	**$39,390,000**	**$107,000,000**	**$81,300,000**
Income	**$48,117,000**	**$39,550,000**	**$80,000,000**	**$82,100,000**
Reconciliation	**$49,000,000**	**$39,450,000**	**$94,000,000**	**$82,100,000**

1200 LOCUST Assessed at $ 44,910,000

Minimum Assessment $36,000,000

	Vaske	Scaletty	Kenney	Manternach
Cost	**$26,650,000**	**$23,440,000**	**$41,000,000**	**$44,000,000**

Sales Comps	**$26,034,000**	**$22,640,000**	**$63,000,000**	**$42,800,000**
Income	**$25,134,000**	**$24,240,000**	**$55,000,000**	**$42,900,000**
Reconciliation	**$26,000,000**	**$23,280,000**	**$47,000,000**	**$43,000,000**

ARGUMENT

I. THE BOARD OF REVIEW FAILED TO PRESENT COMPETENT EVIDENCE IN SUPPORT OF ITS VALUATION OF 1100 AND 1200 LOCUST AS REQUIRED BY *WELLMARK v. BOARD OF REVIEW*.

Preservation of Error.

All issues raised in this appeal and in Appellant's argument herein were raised in Appellant's Proposed Findings of Fact and Conclusions of Law and supplemental briefing submitted to the District Court following trial. *See* App. 0005-0042.

Standard of Review.

Appeals from decisions of a local Board of Review are triable in equity and this Court's review of a tax protest is *de novo*. *Wellmark v. Bd. of Review* 875, N.W.2d 667, 672 (Iowa 2016); *Boekeloo v. Bd. of Review*, 529, N.W.2d 275, 276 (Iowa 1995). Weight is given to the District Court's findings of fact, but this Court is not bound by them. Iowa R. App. P. 6.904(3)(g); *Wellmark* at 672.

Merits.

Under Iowa law, "market analysis is the preferred method of determining actual value. If market analysis can provide a reliable estimation of value, the process is at an end. **"Other factors" may be considered *if, and only if,* market value cannot be readily established through the preferred market analysis.**" *Wellmark, Inc. v. Polk County Board of Review*, 875 N.W.2d 667, 679 (Iowa 2016.) The *Wellmark* decision did not change Iowa law regarding the preference for market analysis to set value.

At trial, Nationwide's experts presented competent evidence of value based on comparable sales, and the District Court found Nationwide had shifted the burden of proof to the Board to uphold the assessed value. (District Court Order p. 16, App. 0128). However, as demonstrated above, the Board of Review failed to produce any competent evidence of value using market analysis as required by Iowa law. As a result, Nationwide's valuations must be accepted as the correct assessed value for both properties. The District Court's decision finding the Board's experts more reliable simply ignores the Board's failure to abide by the Iowa Code and the decision in *Wellmark.* Accordingly, it must be reversed by this Court.

A. **The Comparable Sales Method is the Preferred Method of Determining Actual Value**

Iowa Code section 441.21, enacted in 1967, requires all taxable property to be assessed at its fair and reasonable market value:

> The actual value of all property subject to assessment and taxation shall be the fair and reasonable *market value* of such property. "*Market value* " is defined as the fair and reasonable exchange in the year in which the property is listed and valued between a willing buyer and a willing seller, neither being under any compulsion to buy or sell and each being familiar with all the facts relating to the particular property. Sale prices of the property or comparable property in normal transactions reflecting market value, and the probable availability or unavailability of persons interested in purchasing the property, shall be taken into consideration in arriving at its *market value.*

Iowa Code § 441.21 (1)(b); *Wellmark, Inc. v. Polk County Board of Review*, 875 N.W.2d 667, 678-79 (Iowa 2016.) Section 441.21(1)(b) recognizes the sales comparison approach as the preferred method to value property, so long as the comparable sales used are adjusted in consideration of the relative nature and condition of the assessed property. *Bartlett & Co. Grain v. Bd. of Review,* 253 N.W.2d 86, 87 (Iowa 1977).

The Supreme Court's decision in *Wellmark, Inc. v. Polk County Board of Review* reinforced this well-established law:

> "Under the 1967 legislation, then, market analysis is the preferred method of determining actual value. If market analysis can provide a reliable estimation of value, the process is at an end. **"Other factors" may be considered *if, and only if,* market value cannot be readily established through the preferred market analysis.**

Wellmark at 679 (emphasis added). Market analysis is clearly the preferred method.

In performing that analysis, abnormal transactions not reflecting market value, such as foreclosures or other forced sales, contract sales, sales to immediate family, or discount purchase transactions, or purchases of adjoining land or other land to be operated as a unit shall either be adjusted or not taken into account at all. Iowa Code § 441.21 (1)(b). In arriving at market value, an appraiser must consider "the probable availability or unavailability of persons interested in purchasing the property." Iowa Code § 441.21(1)(b). It's only if the market value cannot be readily established through market analysis that the Court may look at other factors to determine value. *Wellmark* at 682. Comparable sales are not strictly limited to a specific geographic area, and Iowa Courts allow sales of property in the geographic area that includes the Midwest "were sufficiently similar to amount to comparable sales." *Wellmark* at 681.

B. <u>Application of Principles to Nationwide Properties.</u>

Applying applicable Iowa law to the facts of this case, the maximum fair and reasonable market value for 1100 Locust is $49,000,000, and the maximum fair and reasonable market value for 1200 Locust is $26,000,000. Since a minimum assessment agreement is in place for both properties for the January 1, 2017 and January 1, 2018 tax years, the assessed value for 1100 Locust is $87,050,000, and the assessed value for 1200 Locust is $36,000,000.

1. <u>Nationwide's Experts Established Market Value Based on Market Analysis</u>

In the *Wellmark* case, the Supreme Court was faced with two types of appraisals attempting to determine market value.

> "Wellmark's experts utilized transactions from similar geographic markets**<u>, but the transactions involved office buildings dedicated to multitenant use.</u>** Further, Wellmark's experts were required to make substantial adjustments with respect to comparable sales in order to support their analysis.
>
> On the other hand, the Board's expert **<u>… presented single-occupant sales of large office buildings in large metropolitan areas that are simply not very indicative of the value of property in the much smaller Des Moines market</u>**. **<u>Further, some of his comparable sales involved property subject to a long-term lease, thus clouding comparability and raising the question of whether the buyer was interested in the property or the income stream generated by an advantageous lease.</u>** We therefore conclude that the district court correctly considered other factors in its effort to establish the value of the properties."

Wellmark at 682 (emphasis added). Given the fact none of the appraisers from either side was able to establish market value through comparable sales, the Court in *Wellmark* could look at other factors to determine value, and did so in that case. But, as the Supreme Court noted, it was **only** able to consider "other factors" because it found market value could not be established using comparable sales. *Wellmark* at 682. In this case, both Nationwide appraisers determined market value using actual comparable sales of single tenant office buildings and the District Court determined they utilized the appropriate method to determine value. Accordingly, there is no need to consider "other factors" to determine value in this case.

This Court should note that all four appraisers performed some type of comparable sales analysis for the two properties, but only Nationwide appraisers Vaske and Scaletty performed an analysis of comparable single occupant buildings in Des Moines and similar markets. In contrast, the Board's experts -- Kenney and Manternach – performed comparable sales analyses that were rejected by the Supreme Court in *Wellmark*.

Specifically, Vaske and Scaletty looked at single-occupant buildings in Des Moines and the Midwest where the sale was of a fee simple interest. They avoided multitenant buildings, buildings with leased fees, and buildings located in markets completely dissimilar to Des Moines to arrive at their suggested values. As Vaske testified, there is nothing unique about these buildings, and "if you drive around the Des Moines central business district, you drive around the business parts in West Des Moines, we're a banking and insurance market. There are plenty of examples of large corporate office buildings." (Vol. II p. 63, App. 0170). The approach used by the Nationwide experts clearly meets the standard set forth in *Wellmark* regarding comparable sales, and there is no need to look at "other factors."

The Board's appraisers not only failed to meet the comparable sales standards set forth in *Wellmark*, they explicitly violated them. Kenney ignored any sales in Iowa and only looked at sales of single occupant buildings in some of the largest markets in the United States that have nothing in common with the Des Moines market. Many of Kenney's comparable sales also involved long term leases or were buildings that were purchased by long term tenants which raises the question of whether the buyer was interest in the property, or the income stream associated with the property. This Court in Wellmark specifically rejected those types of comparable sales, and when you also consider the fact Kenney gave very little weight to the sales comparison approach, his report does not readily establish market value.

Further, even if this Court were to consider "other factors" due to the unavailability of a market approach, Kenney's methodology in his Cost Approach, which he relied on the most for his opinion, includes a $15 million error in his calculations which he admitted at trial. When you factor in Kenney's 1) failure to use a comparable sales method based on similar properties, 2) admission he gave no weight to the income method, and 3) flawed cost analysis that was off by over $15 million, his opinions should be given no weight by this Court.

Manternach's report has similar flaws. He used Des Moines office buildings as comparable sales, but only used multi-tenant properties requiring significant adjustments, which this Court in *Wellmark* specifically rejected as comparable properties for a single occupant building. Manternach also relied heavily on properties subject to long term leases, which also was rejected by *Wellmark*. Since this Court found in *Wellmark* that using multi-tenant comparable sales to value a single tenant office building constituted reversible error, Manternach's appraisals cannot be considered competent evidence of value and must be rejected. That leaves the expert appraisals submitted by Nationwide as the only competent evidence of market value for this Court to consider.

II. THE DISTRICT COURT ERRED BY FINDING THE BOARD OF REVIEW MET ITS BURDEN AND THE TESTIMONY SUBMITTED BY THE BOARD OF REVIEW'S EXPERT APPRAISERS WAS MORE CREDIBLE THAN THE REPORTS AND TESTIMONY SUBMITTED BY NATIONWIDE'S EXPERT APPRAISERS REGARDING THE VALUATION OF 1100 AND 1200 LOCUST.

Preservation of Error.

All issues raised in this appeal and in Appellant's argument herein were raised in Appellant's Proposed Findings of Fact and Conclusions of Law and supplemental briefing submitted to the District Court following trial. *See* App. 0005-0042.

Standard of Review.

Appeals from decisions of a local Board of Review are triable in equity and this Court's review of a tax protest is *de novo. Wellmark v. Bd. of Review* 875, N.W.2d 667, 672 (Iowa 2016); *Boekeloo v. Bd. Of Review*, 529, N.W.2d 275, 276 (Iowa 1995). Weight is given to the District Court's findings of fact, but this Court is not bound by them. Iowa R. App. P. 6.904(3)(g); *Wellmark* at 672.

Merits.

As demonstrated above, the Board failed to present any competent evidence to support its valuation of 1100 and 1200 Locust. But even if the appraisal evidence submitted by the Board was competent, the Board still has failed to shift the burden of proof in favor of Nationwide and the evidence it presented.

A. <u>Respective Burdens of the Parties</u>

There is no presumption "as to the correctness of the valuation of assessment" from which the appeal is taken. Iowa Code 441.39. Upon appeal to the district court the court may increase, decrease or affirm the amount of the assessment. Iowa Code 441.43

The initial burden of proof was on Nationwide to show that the assessment meets one of the grounds of protest provided under the stature. Iowa Code 441.37(1)(a)(1-5). Here Nationwide's protest was that the Property was assessed for more than the value authorized by law. Nationwide must prove its case merely by a preponderance of the evidence. *Post-Newsweek Cable, Inc. v. Board of Review of Woodbury County*, 497 N.W.2d 810, 813 (Iowa 1993). Nationwide has a twofold burden. First, it must prove that 1100 Locust and 1200 Locust were over-assessed. If it proves the two buildings were over-assessed, it must next establish what the correct valuation should be. *Boekeloo v. Board of Review of City of Clinton*, 529 N.W.2d 275, 276-277 (Iowa l995).

Once the property owner "offers competent evidence by at least two disinterested witnesses that the market value of the property is less than the market value determined by the assessor," the burden shifts to the board of review to uphold the assessed value. Iowa Code § 441.21 (3)(2011); *Boekeloo v. Board of Review*, 529 N.W.2d 275, 277 (Iowa 1995); *Wellmark, Inc. v. Polk County Board of Review*, 875 N.W.2d 667, 671 (Iowa 2016.) A witness is deemed to be disinterested if the witness "has no right, claim, title, or legal share in the cause or matter in issue, and who is lawfully competent to testify." *Post-Newsweek Cable, Inc. v. Bd. of Review*, 497 N.W.2d 810, 813 (Iowa 1993). Evidence is competent when it complies "with the statutory scheme for property valuation for tax assessment purposes." *Boekeloo v. Bd. of Review,* 529 N.W.2d 275, 279 (Iowa 1995). Evidence to be competent does not mean that it must be credible. *Soifer v. Floyd County Bd. of Review,* 759 N.W.2d 775, 784 (Iowa 2009).

Here, the District Court correctly found that Nationwide presented competent evidence that "the market value of the property was less than the market value determined by the Assessor" and that Nationwide's appraisers "utilized the <u>appropriate methods</u> for valuing property for tax purposes", thereby shifting the burden to the Board. (District Court Order p. 16, App. 0128). In reaching that conclusion, the District Court explained that both Vaske and Scaletty looked at comparable sales of other large single tenant buildings – the preferred method under Iowa law -- and gave the most weight to those sales in determining the fair market value of the Nationwide properties. (District Court Order pp. 7-10, App. 0119-0122).

In contrast, the District Court admits Appraiser Kenney gave little to no weight to the sales comparison approach and instead based his appraisal primarily on the cost method, while appraiser Manternach looked at multi-tenant properties as sales comparisons despite the lack of similarity with the Nationwide properties. (District Court Order pp. 7-10, App. 0119-0122). Despite the District Court's acknowledgment that the comparable sales method was the preferred method of valuing real property (District Court Order pp. 14-15, App. 0126-0127), and the District Court's admission the Board's appraisers did not rely on comparable sales as part of their opinions, the District Court gave more weight and consideration to the Board's appraisers. As demonstrated below, this decision has no basis in logic or law.

B. The District Court Failed to Properly Apply the Respective Burdens

A market analysis based on comparable sales is the bedrock principle for valuing real estate for property tax purposes in Iowa. Accordingly, in determining which party met its burden in this case, it was incumbent on the District Court to analyze the valuation methods utilized by both parties and come to a decision on how that burden was met. In this case, the District

Court gave "more weight and consideration to the reports and testimony of Kenney and Manternach in its attempt to determine the value of the property." (District Court Order p. 17, App. 0129). What the District Court fails to discuss is the basis for its conclusion. Given the Board's failure to use a market analysis acceptable to *Wellmark*, the District Court's decision is unsupportable.

Specifically, the District Court's decision correctly states that the Sales Comparison approach is the preferred method of determining value unless it cannot be utilized. (District Court Order p. 14-15, App. 0126-0127). The District Court also finds that Vaske and Scaletty primarily relied on the Sales Comparison approach based on single tenant buildings, and that their reports and testimony were competent evidence which shifted the burden to the Board.

In contrast, Kenney admitted at trial and in his report that in reaching his valuation, he gave the most weight to the Cost Approach (which contains a $15 million miscalculation), less weight to the Income Approach, and "very little weight" to the Sales Comparison Approach. Given the District Court's understanding that the Sales Comparison approach is the preferred method of valuation unless it cannot be utilized; its acceptance of Vaske and Scaletty's reports utilizing the Sales Comparison method; and Kenney's admission he did NOT use the Sales Comparison method, there is no possible basis for the District Court to give more weight to Kenney's testimony compared to the testimony of Vaske and Scaletty. Without an explanation from the District Court as to why it made this decision, it must be reversed.

The same analysis applies to the report and testimony of Manternach. It is undisputed that Manternach's Sales Comparison Approach used multi-tenant properties that were leased out at the time they were sold. This Court in *Wellmark* held that relying on those type of properties using a Sales Comparison method when valuing a single tenant building constituted reversible error. Despite the District Court's acknowledgment of the type of properties utilized by Manternach (District Court Order p. 12, App. 0124) and the plain holding of *Wellmark*, the District Court without explanation found Manternach's testimony more credible. As demonstrated above, this finding by the District Court is completely inconsistent with Iowa law.

C. The District Court's Ruling Cited Irrelevant Authority in Support of Its Decision.

In addition to referencing the testimony and evidence presented by the Board's experts, the District Court's ruling also made reference to other "authority" in support of its findings. None of these additional reasons cited by the District Court provide a proper basis for upholding the Board's assessment.

First, the District Court "notes Polk County denied Nationwide's appeal based on the cost reports developed by the Polk County Assessor's Office, which showed the assessed value of 1100 and 1200 Locust were not excessive." (District Court Order p. 12, App. 0124). Earlier in its decision, the District Court stated this analysis was performed by a county employee using a state manual that estimates the cost of construction and did not further reduce the cost of the buildings by functional or external obsolescence. (District Court Order p. 7, App. 0119). But the law is clear that the "the actual value of all property subject to assessment and taxation shall be the fair and reasonable ***market value*** of such property" (*see* Iowa Code § 441.21 (1)(b); *Wellmark* at 678-79) and both parties submitted expert testimony regarding market value under Iowa law. As a result, a county employee's opinion of value based on a process that does not take into account functional obsolescence is simply irrelevant, and the District Court fails to cite any authority to the contrary.

Finally, the District Court found support for the assessed values of 1100 and 1200 Locust based on Exhibits P which states the replacement cost for insurance purposes is $148,061,365 for 1100 Locust and $67,804,793 for

1200 Locust. According to the District Court, this information helps prove "by a preponderance of the evidence the assessments are not excessive." (District Court Order p. 7, App. 0119). This statement by the District Court has no basis in the law.

As stated in the affidavit of Mr. Pittello, these figures are what it would cost to replace the buildings from scratch in today's dollars, and reflects the value "for insurance purposes" in the event the buildings are destroyed and need to be rebuilt. It is **not** an estimate of the buildings' fair market value, and Nationwide's corporate VP for real estate Joe Baughman testified at trial that replacement cost for insurance purposes is in no way equivalent to fair market value. (Trans. Vol. I p. 69-70, App. 0142-0143). Further, as part of the Cost Approach, all four expert appraisers calculated the replacement cost for each building, and then reduced those costs substantially for depreciation and functional obsolescence to arrive at a fair market value for tax purposes. The value Nationwide puts on the properties in the event there is an insurance loss does not account for depreciation of functional obsolescence, and literally has nothing to do with the fair market value of those buildings for purposes of this dispute. As a result, the District Court has no basis to rely on the insurance value of the property to determine whether the Board's valuation should be upheld.

CONCLUSION

Under Iowa law, "market analysis is the preferred method of determining actual value. If market analysis can provide a reliable estimation of value, the process is at an end. **"Other factors" may be considered *if, and only if,* market value cannot be readily established through the preferred market analysis.**" *Wellmark, Inc. v. Polk County Board of Review*, 875 N.W.2d 667, 679 (Iowa 2016.)

The *Wellmark* decision did not change Iowa law regarding the preference for market analysis to set value. But it did set the framework for what types of properties to utilize when performing a market analysis for large single tenant properties. In this case, Nationwide's experts determined market value using comparable sales, the District Court found Nationwide had shifted the burden to the Board, and that should end the analysis. Accordingly, Nationwide respectfully requests that the decision of the District Court be reversed, and that this Court sets the assessed value of 1100 Locust at no more than $49,000,000, and set the assessed value of 1200 Locust at no more than $26,000,000, with the understanding the value for 2017 and 2018 is subject to a minimum assessment of $78,500,000 for 1100 Locust and $36,000,000 for 1200 Locust.

REQUEST FOR ORAL SUBMISSION

In accordance with Iowa Rule of Appellate Procedure 6.908(1), Appellants hereby request the Court submit this matter following oral argument.

Dated this 15th day of April, 2021.

/s/ *Sean Moore*

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CERTIFICATE OF SERVICE AND FILING

I hereby certify that on April 15, 2021, I electronically filed this Final Brief in accordance with Chapter 16 of the Iowa Rules of Court, which will electronically serve the attorneys of record.

/s/ *Angie Walker-Springer*

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