

NO. A11-399

State of Minnesota
In Supreme Court

Berry & Co., Inc.,

Relator,

v.

County of Hennepin,

Respondent.

RELATOR'S REPLY BRIEF

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RELATOR'S STATEMENT OF THE ISSUES

1. Did the facts sufficiently support the Tax Court's decision?

Result below: The Tax Court ruled incorrectly.

Most apposite authorities: Hedberg & Sons Co. v. County of Hennepin, 232 N.W.2d 743 (Minn.1975); Evans v. County of Hennepin, 548 N.W.2d 277 (Minn. 1996); Minn. Stat. §§ 273.08, 273.11.

LEGAL ARGUMENT

I. RESPONDENT AGREES EXISTENCE OF PUD IS CRITICAL TO OPINION OF VALUE. PROBLEM IS, NO PUD EXISTED.

Respondent goes to great lengths to establish that a Planned Unit Development (“PUD”) was approved for development of the Subject Property and argues that the property value is significantly increased by its development potential. However, in order to accept Respondent’s argument, the Court must ignore the facts—namely, that the Subject Property alone was never approved for a PUD, that the PUD that was approved was not the PUD requested by the property owners, that under the plan proposed by the City the Subject Property could not be developed without the neighboring parcel, and is development of the property is not economically feasible under the required highest and best use argument.

As detailed in Relator’s opening brief, under the zoning restrictions in place now and on the relevant valuation dates, the owner of the Subject Property can only erect a two-story building with a maximum height of 30 feet. In addition, this two-story building is further restricted by the availability of parking, (i.e. there must be five parking spaces per 1000 square feet of building), limited curb exposure (the lot is excessively deep), and high water levels that prevent below ground development. These restrictions necessitate involvement of the neighboring property owner in any development plans. Standing alone, without deviating from the zoning restrictions, the property is virtually undevelopable. Thus, the property owner attempted to maximize the potential of the property by working with the adjoining land owner to develop their properties together as

one development. This potential development still required alternative zoning, but use of both properties overcame some of the more pronounced issues, such as parking. The proposed PUD submitted to the City for approval included a three-story office/retail building with a rear parking ramp that straddled both properties. The City rejected the proposed PUD, but did approve development of the properties with 15 substantial changes. These changes included a requirement that any buildings erected on the properties be three-story structures consisting of first level retail, second level office and third level residential. Unfortunately, the economics of building such a structure far outweighed the potential return, and the property owners abandoned the idea. In short, the approval of a PUD was no approval at all, a fact admitted by Respondent's expert.

Nevertheless, Respondent relied, and the Tax Court accepted, this so called approved PUD to reach the excessive value decided by the lower court. Again, this position is contrary to the facts and law. Hedberg & Sons Co. v. Hennepin County, 232 N.W.2d 743 (Minn. 1975) explored a similar situation. There, as here, the elevated assessed value of the property was based on the assumption that zoning restrictions would be modified to accommodate the proposed development of the property and that such development was the highest and best use. The Hedberg court concluded that although the probability of future zoning modification is a factor to be considered by the trier of fact if there is sufficient proof that the zoning laws will indeed be changed, development of the property under the existing zoning was remote and speculative and therefore the appraisal was not adopted and in fact the Court gave no consideration to the ultimate nature of the use to which the property would be devoted. Id. Contrary to

Respondent's argument, Hedberg is not a situation where the appraisal relied on zoning restrictions that did not exist. Rather the appraiser in Hedberg assumed zoning would be modified—an assumption not allowed by the Court for purposes of determining value. Here, as in Hedberg, there is no evidence in the record that the zoning laws will be modified.

Next, Respondent acknowledges that this PUD that never existed with regard to the Subject Property alone and had expired prior to the 2008 assessment date, but argues it would have been renewed. Respondent bases this argument solely upon its expert's guess that he "ha[d] no doubt that if he [Relator] went in and asked for a three-story approval that they would give it to him." (Trial Trans. at p. 334, Reply Brief at p. 8). Under cross examination, the expert admitted that he had never participated in the decision-making process and that he had no authority to approve any such deviation from zoning laws. (Id.) Moreover, Respondent's expert qualified his testimony that a PUD would be approved for the Subject Property by stating that Relator would have to develop the property the way the City wanted it developed.

Q: But it's pure speculative --

A: No, it's --

Q: -- because it's never been applied for and it's never been approved, correct?

A: When I see it happening over and over again it's not speculative.

Q: So are you suggesting that he would be entitled to that zoning change?

A: I'm saying that if he -- if he applied for that and he did the

development the way the City wants, they would in all likelihood give him a three-story building there. I don't think that is speculative at all.

Q: But you don't know, do you?

A: 100 percent, no; but I don't think it's a speculative thing. I think it's very likely that that is what would happen.

Q: Mr. Bennett, with all due respect, you don't participate in decision making, you have no authority with regard to what is approved and what isn't approved, correct?

A: That is correct.

(Trial Trans. pp. 334-335).

Other than this testimony, Respondent gives no support for its position. It is wholly improper for the Tax Court to ignore Hedberg and its progeny on the guess of a biased witness. Accordingly, the Tax Court decision must be over tuned.

II. HIGHEST AND BEST USE.

When undertaking to appraise the value of commercial real estate, the appraiser must perform a highest and best use analysis. The highest and best use of real estate is defined as:

The reasonably probable and legal use of vacant land or an improved property that is physically possible, appropriately supported and financial feasible and that results in the highest value.

Highest and best use of land or site as though vacant. Among all reasonable, alternative uses, the use that yields the highest present land value, after payments are made for labor, capital, and coordination. The use of a property based on the assumption that the parcel of land is vacant or can be made vacant by demolishing any improvements.

Highest and best use of property as improved. The use that should be made of the property as it exists. An existing improvement should be renovated

or retained as is so long as it continues to contribute to the total market value of the property, or until the return from a new improvement would more than offset the cost of demolishing the existing building and constructing a new one.

(Trial Ex. 101, p. 32/APP0227).

Further, the appraiser must consider whether the use of the property is legally permissible, physically possible, financially feasible and maximally productive.

Legally permissible: Primary considerations are private restrictions, zoning ordinances, building codes, historic district controls and environmental regulations.

Physically possible: Consideration is given to the size, shape, topography/soils and accessibility of the property.

Financially feasible: The use must generate a positive return.

Maximally Productive: The use that generates the highest return.

It is undisputed that to maximize the value of the Subject Property, it must be redeveloped. However, as discussed at length in Relator's opening brief, such development was not, and will not be, financial feasible for at least the near term future. The Subject Property owner, Bradley Hoyt, testified in detail as to the cost to develop this property. Hoyt is the only individual who actually undertook to determine the cost to develop the property, standing alone, based on the restrictions imposed by the City and the limitations of the land itself, such as excessive depth, ground water issues, and soil conditions. Conversely, Respondent's expert did not do a full analysis of the cost to develop the Subject Property, but instead based his estimates on the PUD with the adjoining property, made uneducated guesses (he has no experience developing property and has never owned commercial property) and spoke to only one individual about cost

in a hypothetical situation:

Q: Bill Kwasny. And what information did you give him to determine -
- so that he could calculate the piles that would be used or need to be
used?

A: I told him the ground floor area of the structure. He knew what the
building was basically going to be, the three-story building, and he
gave me an estimate. He gave me a pile quantity estimate based on -
- I asked him about if the building was 12,500 square feet the ground
floor area.

Q: Did you submit any structural drawings?

A: No.

Q: So it's a completely hypothetical situation that you have?

A: The 12,500 was hypothetical, yes.

(Trial Trans. p. 345)

Further, Respondent's expert admittedly failed to include all the costs to develop the
property:

Q: Okay. And would you agree with me that more things needed to be
done than pilings to fix the soil problem?

A: Well, the pilings are going to fix the soil. You're still going to need
a foundation, if that's what you're talking about.

Q: Actually I am referring to Mr. Kramer's testimony that in addition to
the pilings there is going to be other -- there is going to be other
necessary steps that have to be taken. For example, he testified that
the plumbing and all of the utilities would have to be hung from the
structure underneath because of the ground water.

A: Well, the report that I used they say in there that the utility lines
should be piled. They didn't talk about any suspension.

Q: And that is also because there were never structural drawings
completed, correct?

A: I don't think they knew where the -- yeah, I'm not aware of where the utility lines are going to be. Yeah, I have got in my notes here it says utility lines need to be piled. They don't know where they're going to be, where they're going to run, so that is true.

Q: So there are other costs that you haven't considered?

A: Well, I've considered it. I know there is going to be additional costs besides the pilings.

Q: And did you undertake to do any analysis of how much those additional costs might be?

A: No.

(Trial Trans. pp. 346-348).

Finally, Respondent's expert based his financial feasibility analysis, in part, on the fact that another property owner had built a building similar to the three-story structure he believed the City would approve. Respondent's expert never spoke to the developer, did not know the cost of the development and did not know that the development is in financial distress:

Q: And what analysis did you undertake to determine that it was financially feasible?

A: Well, I guess there is a couple of things that I used to determine that Lowell Zitzloff was doing -- in '07 he did the 315 Lake building, which is the same mixed use as I'm concluding to here, and in '08 he was also trying to do the Five Swans with the three same uses. I guess another piece of info is --

Q: So did you actually do an analysis, or are you basing this on the fact that he was developing his land, is that the extent that --

A: I am basing it on the fact that he's a smart guy, he's a player down there, he felt it was prudent to --

Q: Okay. So --

A: -- he thought the market was right for that type of --

Q: Do you have any idea if the cost of that development could be supported by the income it would generate?

A: I don't think Lowell would have --

Q: I didn't ask about Mr. Zitzloff. I asked about you, do you have any idea?

* * *

A: I guess my answer would be I'm just assuming that he didn't do that to lose money. He built one building in order to make money. He's a smart guy.

Q: So you don't know?

A: ...no, I don't I guess.

(Trial Trans. pp. 361-363).

Q: Do you know what the status of Mr. Zitzloff's building is?

A: The 315?

Q: Yes.

A: Well, I know that he has vacancy in there.

Q: He has never sold a condo, has he?

A: But he's -- it's the timing. The timing was bad. But he went -- the thing about it is is that hasn't panned out probably the way he wanted to, but in mid-2008 he was trying to develop the Five Swans property in the same way, so I think that he feels that that concept is feasible. Just because one of his projects maybe didn't turn out quite as well as he hoped, that doesn't mean that it's not feasible.

(Trial Trans. p. 317).

When determining the financial feasibility of the use of commercial property for appraised value purposes, the appraiser must utilize factual data, not conjecture and assumption. Here, Respondent relied on incomplete data and make-believe scenarios to support his appraised value. Therefore, the Tax Court's reliance on his opinion cannot stand as it is not founded on the facts.

III. RESPONDENT FAILS TO PROVIDE FACTUAL SUPPORT FOR FAILURE TO MAKE ADJUSTMENTS.

When using the comparative sale method of valuation, under the Uniform Standards of Professional Appraisal Practice ("USPAP"), it is necessary to make adjustments to comparable sales so as to make the comparables as similar to the subject property as possible. In this case, Respondent failed to make the appropriate adjustments, which resulted in an inflated value for the Subject Property. When confronted with this fact, Respondent in its brief attempts to confuse this Court by repeatedly citing to the record, but providing no reasonable explanation or support for its expert's decision not to make the appropriate adjustments. In other words, Respondent acknowledges the accusation, but then simply quotes testimony that fails to explain why the appropriate adjustments were not made.

For example, the Subject Property has approximately 35,000¹ usable square feet and the "comparables" used by Respondent's expert were between 4,900 square feet and 15,600 square feet. When discussing the failure to make an adjustment for size, Respondent states that no adjustment was made because "there is no evidence out there

¹ One of the facts in dispute is the usable square footage of the Subject Property. Relator claims it is 34,598. Respondent claims it is 44,107.

that you can really find out if an adjustment should or shouldn't be made."

(Respondent's Brief at p. 11 citing Trial Trans. p. 357). Respondent goes on to discuss how its expert charted each of the properties on Lake Street that sold during the relevant time period, "determined the contract price divided by the square feet for every property," and based on this chart decided no size adjustment was necessary. However, when questioned about this analysis at trial, (which showed great disparities in the purchase price per square foot) Respondent's expert had this to say:

Q: And wouldn't you agree with me that a smaller property is more valuable?

A: Normally you would assume that, but I don't think that is the case on Lake Street.

Q: And you base that on what?

A: Well, I looked at all the properties on Lake Street -- first of all, there is no evidence out there that you can really find out if an adjustment should or shouldn't be made on this.

Q: So it's based on your personal, professional opinion, and it's highly subjective, correct?

A: No, it's anything but subjective. I mean it's subjective in a way, but I think I have a good basis to why I didn't make an adjustment --

Q: Okay.

A: -- based on the market. If you look at the --I put every property on Lake Street from one end to the other on a spreadsheet, and I sorted them by size, and you have a majority of the properties are small out there.

Q: What spreadsheet are you referring to, sir?

A: It's a spreadsheet in my files here.

Q: So it's not a document that is in evidence?

- A: It's not in my appraisal, no; but it's something that I used to decide not to make a size adjustment.
- Q: Okay. Well, let me ask you it look at Page 54 of your appraisal.
- A: Okay.
- Q: When you look at, for example, you have got 801 Lake Street, which looks like it traded twice during the time period that you have considered on this chart, correct?
- A: The Wayzata Bay Center, yes.
- Q: That is 628,747 square feet of usable?
- A: Correct.
- Q: That traded between \$24 and \$38 or at 24.25 and 38.17?
- A: Right.
- Q: Then if you look at, for example, 332 Broadway, it's 4,906 square feet, and that was \$244.60 per square foot?
- A: Right.
- Q: Doesn't that evidence that smaller properties sell for a much higher amount per square foot?
- A: No, because there is numerous differences between these properties. That doesn't prove a thing.

(TT. pp. 357-359). Obviously, based on Respondent's expert's own analysis, the size of the property, affects the value. The failure to adjust for the size differential is clearly error.

Likewise, when discussing the failure to adjust for razing costs, Respondent states that no such adjustment was necessary because the cost to raze the buildings was

comparable. What Respondent fails to acknowledge is that its expert had no experience estimating razing costs and even stated that developers in Wayzata are not concerned with tens of thousands.

Q: I believe you testified earlier that you didn't include any razing costs adjustments, excuse me, you didn't include any adjustments for razing costs, correct?

A: Right.

Q: And that was because you believe that each of those comparables has structures on them that need to be razed, and those razed structures are comparable and cost about the same?

A: I think in relation to the land, yeah, they're in the same ballpark.

Q: Wouldn't a potential buyer consider that in the amount that they'd be willing to pay for the property?

A: All of these razing costs are such a miniscule amount, I don't think these guys would even think about it. They're worried about hundred of thousands of dollars, not 10,000.

(Trial Trans. 366-367). This is the sole justification; Wayzata developers are so wealthy that they cannot be bothered with costs in the tens of thousands of dollars. Wayzata developers would probably be dismayed to find out that their City assessor, when valuing their property, does not account for the tens of thousands of dollars they must spend to correct property in order to develop it. This is another clear violation of the appraisal standards that requires reversal of the Tax Court's decision.

When confronted with the admission that its expert miscalculated the usable land area by failing to include the wetland buffer zone, Respondent quotes its expert's testimony, "you don't subtract out setbacks when you calculate usable." (Trial Trans. p.

328-329). However, this testimony was never substantiated. When pressed further on cross examination, Respondent's expert attempted to qualify this claim by saying he did not know what was on the other properties...a statement that is irrelevant to the question posed. Respondent then states that its expert did not include the buffer zone because he wants the sales comparables to be "apples to apples." Respondent goes on to claim that Relator's inclusion of the buffer zone is tantamount to comparing apples and oranges because he excludes the wetland buffer zone when calculating the comparable property usable land area resulting in a double deduction. This conclusion is patently false. Relator's expert did not include any wetland buffer zone in the comparable sales because there is no evidence that there are wetland zones in any of the comparable sales. Again, Respondent is relying on confusion, and in this case piecemeal citations, to create facts where none exist.

Finally, the most compelling argument made in Respondent's brief is the argument that it fails to make. Namely, Respondent does not even address the fact that in order for the Tax Court's decision to be upheld, the reviewing Court must find that the law and facts support its ruling. Respondent cannot make this argument. The sole purpose of the appraisal is to determine the market value of the Subject Property on the assessment dates. In short, market value is the most probable price that a property should bring in a competitive and open market. When questioned about his determination of the market value of the Subject Property, Respondent's expert admitted that "no one would pay" the value he had attributed to the property because the value is quite simply too high. Accordingly, the Tax Court's adoption of Respondent's appraised value is clearly

erroneous.

CONCLUSION

The Tax Court's determination of the value of the Subject Property is not supported by Minnesota law or the facts presented at trial. Relator respectfully requests that this Court reverse the decision of the Tax Court for the reasons set forth above.

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Date: May 9, 2011

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**CERTIFICATE OF
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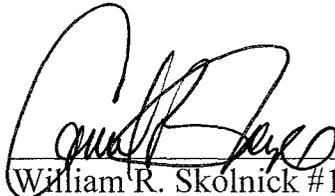
**Appellate Court
Case No: A11-399**

I hereby certify that this brief conforms to the requirements of Minn. R. Civ. App. P. 132.01. subds. 1 and 3, for a brief produced with a proportional font. The length of this brief is 3,523 words, and the font size is 13 point. This brief was prepared using Microsoft Word 2000 software.

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