

BEFORE THE  
INDIANA BOARD OF TAX REVIEW

UNITED STATES STEEL	)	On Appeal of Determination
CORPORATION,	)	of the Department of Local
	)	Government Finance
Petitioner,	)	
v.	)	Petitions: 45-001-02-9-3-00001, <i>et seq.</i>
	)	
DEPARTMENT OF LOCAL	)	
GOVERNMENT FINANCE,	)	Lake County, Calumet Township
	)	
Respondent.	)	
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LAKE COUNTY ASSESSOR,	)	
	)	On Appeal of Determination
Petitioner,	)	of the Department of Local
	)	Government Finance
v.	)	
	)	Petition: 45-001-02-9-3-00036A
	)	
DEPARTMENT OF LOCAL	)	
GOVERNMENT FINANCE,	)	Lake County, Calumet Township
	)	
Respondent.	)	
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April 1, 2005

**FINAL DETERMINATION FINDINGS AND CONCLUSIONS**

On March 29, 2005, the Indiana Board of Tax Review issued a final determination in the above-captioned matter. Because the final determination contains certain information deemed confidential under Indiana law, the Board has redacted certain information at the request of the Taxpayer. Redacted information is indicated by the use of asterisks (*i.e.*, “\*\*\*\*\*”).

BEFORE THE  
INDIANA BOARD OF TAX REVIEW

UNITED STATES STEEL CORPORATION,	)	On Appeal of Determination of the Department of Local Government Finance
Petitioner,	)	
v.	)	Petitions: 45-001-02-9-3-00001, <i>et seq.</i>
DEPARTMENT OF LOCAL GOVERNMENT FINANCE,	)	
Respondent.	)	Lake County, Calumet Township
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LAKE COUNTY ASSESSOR,	)	
Petitioner,	)	On Appeal of Determination of the Department of Local Government Finance
v.	)	Petition: 45-001-02-9-3-00036A
DEPARTMENT OF LOCAL GOVERNMENT FINANCE,	)	
Respondent.	)	Lake County, Calumet Township
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March 29, 2005

**FINAL DETERMINATION FINDINGS AND CONCLUSIONS**

The Indiana Board of Tax Review issues this determination in the above matter. It finds and concludes as follows:

**I. PROCEDURAL BACKGROUND AND FACTS**

1. On December 31, 2003, the Department of Local Government Finance (the “Department” or “DLGF”) issued a preliminary determination assessing the real property (land, buildings, site improvements) of United States Steel Corporation (“U.S. Steel” or “USS”) – Gary Works pursuant to Indiana Code § 6-1.1-8.5-8. The preliminary determination assessed the Gary Works real property at \$113,672,188, and gave U.S. Steel and the Lake County Assessor (“Lake County” or “LC”) an opportunity to provide additional information bearing on the assessment.

2. Representatives of U.S. Steel and Lake County each met with and provided additional information to the Department. On February 27, 2004, the Department issued a final determination assessing the Gary Works real property at \$113,664,100.

3. On March 26, 2004, Lake County appealed the Department’s final assessment determination. U.S. Steel timely filed multiple Forms 139 (one for each parcel), challenging the Department’s final assessment determination for the Gary Works real property.

4. The Indiana Board of Tax Review (the “Board” or “IBTR”) consolidated all petitions into one appeal and set the matter for hearing to begin the week of January 24, 2005.

5. Pursuant to Indiana Code §§ 6-1.1-8.5-11 and 15-4 through 15-8, the Board<sup>1</sup> conducted a hearing on Lake County Petition No. 45-001-02-9-3-00036A and U.S. Steel Petition Nos. 45-001-02-9-3-00001, *et seq.*, from January 24 through January 28, 2005.

6. Lake County was represented by Brian P. Popp, LASZLO & POPP, PC, Charles C. Meeker and Charles R. Raynal, IV, PARKER, POE, ADAMS & BERNSTEIN L.L.P., and John S. Dull, Lake County Attorney.

7. Thomas M. Atherton and David S. Suess, BOSE MCKINNEY & EVANS LLP., represented United States Steel Corporation.

8. Nandita G. Sheperd represented the Department of Local Government Finance.

9. The following persons were sworn as witnesses and presented testimony:

<b>For Lake County</b>	<b>For U.S. Steel</b>	<b>For the DLGF</b>
Dr. Frank Kelly	Michael Prendergast	C. Kurt Barrow
Sherry Stone	Jerrold F. Janata	
Ronald Grzybowski	Dean Anderson	
Roger Regelbrugge	Ronald Sloan	
Terrence Oetzel	Robert Stall	
Richard Kelley	Harold “Skip” Perry	
	Seth Kaplan	

<sup>1</sup> Commissioner Duga and Senior ALJ Michael Dart conducted the hearing. Senior ALJ Dart did not participate in this decision.

10. In addition, the parties each identified and submitted exhibits at the hearing that are listed at the end of these findings and conclusions. *See* Lake County Exhibits (Exhibit 1), U.S. Steel Exhibits (Exhibit 2), and DLGF Exhibits (Exhibit 3). Exhibits highlighted in bold were admitted into evidence. The remaining exhibits were identified, but not admitted in evidence.

11. The subject property is an integrated steel making facility known as the Gary Works, located at 1 North Broadway in Gary.

12. The Board did not conduct an on-site inspection of the subject property.

13. The Department assessed the Gary Works real property (land, buildings and site improvements) for the 2002 assessment at \$113,664,100.

14. U.S. Steel contends the assessed value of the subject property for the 2002 assessment should be \$84,100,000.

15. Lake County contends the assessed value of the subject property for the 2002 assessment should be \$382,570,000.

16. The Parties specifically did not stipulate to the value of the land, but they did stipulate to the following facts:

a. The Board should use \$216,515,600 as the replacement cost, less normal depreciation, of all improvements at the Gary Works pursuant to the assessment guidelines.

b. The Board should use 15,007,871 as the square footage of the buildings at the Gary Works.

c. The total area of the land at the Gary Works is 3,155 acres.

## II. QUALIFICATIONS OF WITNESSES

### A. For Lake County:

17. Frank Kelly. Mr. Kelly holds a Ph.D. in economics from Indiana University and from 1999 to the present has been President of the Nexus Group an Indiana Property Tax Research and Consulting firm. Mr. Kelly is a level one and level two assessor in the State of Indiana. Nexus provides property tax consulting services to approximately twenty Indiana counties. Mr. Kelly was accepted as an expert on assessment in the State of Indiana.

18. Sherry Stone. Ms. Stone is employed by the Lake County Assessor's Office as Director of Real Estate. She has worked for the Lake County Assessor for 13

years. In the course of her duties, she has become familiar with approximately 100 appeals filed in Lake County regarding the 2002 real property reassessment.

19. Ronald Grzybowski. Mr. Grzybowski has a Bachelor of Science and Engineering degree from the University of Michigan. He is employed by Delta Consulting Services, Inc. of Grand Rapids, Michigan, a firm that specializes in cost estimating and in machinery and equipment appraisals. Mr. Grzybowski holds a designation in machinery and equipment and technical evaluation from the American Society of Appraisers (“ASA”). Mr. Grzybowski has a great deal of experience in estimating the replacement cost of various types of industrial buildings, but he has not appraised or prepared a cost estimate involving a steel mill before. Mr. Grzybowski was accepted as an expert in building replacement cost analysis.

20. Roger Regelbrugge. Mr. Regelbrugge possesses a Masters Degree in Mechanical Engineering from Michigan State University. From 1977 through his retirement in 1997, Mr. Regelbrugge served as President and Chief Executive Officer of Georgetown Steel Corporation. Mr. Regelbrugge was on the Board of the American Iron and Steel Institute, an organization of steel company executives, and also served on the Board of Steel Manufacturers Association, an association of smaller steel manufacturers. Mr. Regelbrugge was accepted as an expert in the manufacture of steel, as well as acquisitions and sales of steel companies.

21. Terrence Oetzel. Mr. Oetzel is a designated M.A.I. appraiser by the Appraisal Institute and is President of the Oetzel-Williams Group in East Lansing, Michigan. He is a member of the American Society of Real Estate Counselors and holds appraisal licenses in Ohio, Indiana, Michigan and New York. He has been actively involved in the appraisal field since approximately 1971 and has appraised a wide variety of properties. He had not appraised a steel mill before this case. Prior to this case, Mr. Oetzel had never appraised any property other than Gary Works using Indiana’s market value-in-use concepts. Mr. Oetzel has not read the entire 2002 REAL PROPERTY ASSESSMENT MANUAL and REAL PROPERTY ASSESSMENT GUIDELINES FOR 2002 — VERSION A, nor has he taken any courses in the application of the Manual guidelines. In addition, Mr. Oetzel did not ask for any aid in interpreting the MANUAL or GUIDELINES from the Department or any Lake County Assessing Official. Mr. Oetzel was accepted as an expert in appraisal of real property.

22. Richard Kelley. Mr. Kelley has been affiliated with the Pomeroy Appraisal firm in Syracuse, New York for 48 years. He holds the M.A.I. designation from the Appraisal Institute and is a Counselor of Real Estate. He holds a real estate appraisal license in New York State and temporary Indiana license. Mr. Kelley has appraised a wide variety of industrial properties, including steel mills. He has also completed numerous appraisal reviews. Mr. Kelley was accepted as an expert in the appraisal of real property and review appraisals.

B. For U.S. Steel:

23. Michael Prendergast. Mr. Prendergast is Manager of Property Taxes for United States Steel. He possesses a Bachelor of Arts in Mathematics and a J.D. from the University of Virginia. Mr. Prendergast held various tax and accounting positions for U.S. Steel between 1976 and 1986 when he joined Aristech Chemical Corporation as Director of taxation, ultimately serving as Controller and Chief Financial Officer. Mr. Prendergast returned to U. S. Steel in 2002 and assumed his current position as Manager of Property Taxes.

24. Jerrold F. Janata. Mr. Janata is the Chief Executive Officer of the International Appraisal Company in Upper Saddle River, New Jersey. Mr. Janata holds a B.A. from Queens College of the City University of New York, a M.B.A. in Finance from Iona College and a J.D. from Fordham University School of Law. He holds the ASA designation from the American Society of Appraisers in Real Property. He is widely published in the field of property taxation, including serving as editor of PROPERTY TAXATION, 1<sup>st</sup>, 2<sup>nd</sup> and 3<sup>rd</sup> Editions published by the Institute for Professionals in Taxation, a publication often cited by Indiana Courts. Mr. Janata has actively been involved in the appraisal of real estate since 1964 and has appraised a wide variety of industrial properties, including integrated steel mills. Mr. Janata was accepted by the Board as an expert in the field of Appraisal of Real Property.

25. Dean Anderson. Mr. Anderson has been employed by U.S. Steel for 28 ½ years, and has worked at Gary Works since 1983. Mr. Anderson has worked as an engineer in every major process area of Gary Works during his tenure and was the manager of engineering at Gary Works between 1995 and 2003. In his over twenty years as a design engineer, Mr. Anderson has acquired personal knowledge and familiarity with the plant's history, technology, layout, design, and functional inefficiencies. Mr. Anderson is currently the regional manager of engineering for U.S. Steel.

26. Ronald Sloan. U.S. Steel has employed Mr. Sloan for the past 35½ years. He has worked in the accounting and financial analysis areas since 1978. Mr. Sloan has held various positions within the financial analysis department at Gary Works over a period of about 5 years. Mr. Sloan has been the controller of Gary Works since January 1, 2004. Mr. Sloan's primary functions are to supervise and oversee the accounting and financial analysis departments at Gary Works. Mr. Sloan has personal knowledge of the plant layout problems at Gary Works and their financial impact on the company.

27. Robert Stall. Mr. Stall is the National Director of the Capital Equipment and Evaluation Practice for Ernst & Young, a practice that specializes in valuation of heavy manufacturing facilities such as steel mills, mining operations, refineries and oil and gas properties. He holds a Bachelor of Science in Accounting and Finance from Miami University in Oxford, Ohio. Mr. Stall has served as an appraiser for Valuation Research Corporation in KPMG, as well as for Ernst & Young. Mr. Stall holds an ASA designation from the American Society of Appraisers. He has been personally involved

with the valuation of at least nine steel mills. Mr. Stall was accepted as an expert in appraisal of industrial facilities.

28. Harold “Skip” Perry. Mr. Perry is the National President of Ernst & Young’s Real Estate Advisory Services Group. He holds a B.A. from the University of Illinois and an M.B.A. from Loyola University. He holds the M.A.I. designation from the Appraisal Institute and is also a C.P.A. He has been an appraiser for more than 30 years. He is licensed as an appraiser in the States of Illinois and Wisconsin. He holds a temporary license in the State of Indiana and also possesses a Counselor of Real Estate designation. Mr. Perry was accepted as an expert in the field of real estate evaluation.

29. Seth Kaplan. Dr. Kaplan holds a Ph.D. in Economics; served on faculty at various educational institutions; served on the U.S. International Trade Commission as an economist from 1987 to 1991. Since 1988, Dr. Kaplan has been vice-president and co-director of International Trade and Practice at Charles River Associates, an economic consulting firm and business consulting firm with offices throughout the United States and abroad. He has testified or consulted in over 50 trade disputes, including approximately 20 cases involving steel products. He has worked for both domestic and foreign steel clients, testifying both for and against domestic steel interests. Dr. Kaplan is a member of the American Economic Association and the Royal Economic Society and has extensive publications and presentations. Dr. Kaplan was accepted as an expert in economics and market conditions affecting the steel industry.

C. For the Department:

30. C. Kurt Barrow. Mr. Barrow is Director of the Assessment Division of the Department. As such he is responsible for oversight of assessments in the State of Indiana and for providing training on the use of the 2002 REAL PROPERTY ASSESSMENT MANUAL (incorporated by reference at 50 IAC 2.3-1-2) and the REAL PROPERTY ASSESSMENT GUIDELINES FOR 2002—VERSION A to assessment officials throughout the state. He was a principle author of the Manual and Guidelines. Mr. Barrow is a graduate of Illinois State University with a degree in economics. He was an appraiser for the Illinois Department of Local Government Affairs, and eventually became Deputy Director of the Illinois Department of Revenue with oversight duties for the property taxation functions of that agency. He has been employed by a large appraisal firm, as well as operating his own appraisal firm and has appraised real estate ranging from single family homes to complex industrial properties. Before joining the State of Indiana, he served for five years as Education Director for the International Association of Assessing Officials. The Board accepted Mr. Barrow as an expert in the field of assessment administration and Indiana’s assessment MANUAL and GUIDELINES.

### III. STANDARD OF REVIEW

31. The Department is statutorily assigned the responsibility to assess the real property at Gary Works. *See* Ind. Code § 6-1.1-8.5-8. The taxpayer, U.S. Steel, and the Lake County Assessor have the right to appeal the assessment determination of the Department. *See* Ind. Code § 6-1.1-8.5-11. Accordingly, the Department is the “assessing official” whose determination is under review, while the Lake County Assessor and U.S. Steel are the parties challenging the assessment.

32. The parties challenging an assessment bear the initial burden of proof: “[T]he party challenging an assessment bears the burden of demonstrating that the assessment is unsupported by substantial evidence, constitutes an abuse of discretion, exceeds the State Board's statutory authority, or is arbitrary or capricious. . . . This burden can be met when the [challenging party] presents a prima facie case in support of its position.” *Canal Square Ltd. Partnership v. State Bd. of Tax Comm’rs*, 694 N.E.2d 801, 804 (Ind. Tax Ct. 1998).

33. A prima facie case “is a case in which the evidence is ‘sufficient to establish a given fact and which if not contradicted will remain sufficient.’” *GTE North Inc. v. State Bd. of Tax Comm’rs*, 634 N.E.2d 882, 887 (Ind. Tax Ct. 1994); *Clark v. State Bd. of Tax Comm’rs*, 694 N.E.2d 1230, 1233-35 (Ind. Tax Ct. 1998) (quoting *Thorntown Telephone Co. v. State Bd. of Tax Comm’rs*, 629 N.E.2d 962, 964 (Ind. Tax Ct. 1994)).

34. Once a petitioner has established a prima facie case, the burden shifts to the assessing official (here, the Department) to rebut the petitioner’s evidence. *See American United Life Ins. Co. v. Maley*, 803 N.E.2d 276, 281 (Ind. Tax Ct. 2004). Moreover, “when a [petitioner] presents a prima facie case of the existence of obsolescence and introduces evidence quantifying its effect on the property's value, the [Department] cannot simply ignore such evidence. Instead, ‘when a [petitioner] offers probative evidence, that evidence must be dealt with in some meaningful manner.’” *Canal Square*, 694 N.E.2d at 805 (citing *Clark*, 694 N.E.2d at 1235).

35. Under Indiana law, as the agency charged with interpreting the true tax value, the DLGF’s interpretation of true tax value must be given deference. In determining the appropriate deference to be accorded the Department's interpretation of its rules, our Supreme Court has directed all courts to “give great weight” to an administrative agency's interpretation of a statute (1) when the interpreting agency is charged with the duty of enforcing the statute interpreted and (2) the interpretation is not inconsistent with the statute itself. *See, e.g., LTV Steel v. Griffin*, 730 N.E.2d 1251, 1257 (Ind. 2000); *State Bd. of Registration for Professional Engineers v. Eberenz*, 723 N.E.2d 422 (Ind. 2000); *State Bd. of Tax Comm'rs v. Two Market Square Assoc., Ltd. Partnership*, 679 N.E. 2d 882 (Ind. 1997); *Indiana Dep't of State Revenue v. Bulkmatic Transport Co.*, 648 N.E.2d 1156, 1158 (Ind. 1995).



#### IV. DISCUSSION OF LAKE COUNTY'S CASE

36. Lake County submitted an appraisal by Mr. Terry Oetzel of the Oetzel-Williams Group. LC Ex. No. 18. Mr. Oetzel concluded "there is insufficient reliable market data to complete a sales comparison approach; therefore, I have not completed a sales comparison approach as part of this appraisal assignment." His opinion is based on the cost approach to value. Nevertheless, his appraisal applied a sales comparison approach to determine land value at the Gary Works. LC Ex. No. 18, p. 50-52. He identified a total of 12 comparable sales, but primarily relied on the first six sales identified in his report. None of them have water access. They have varying degrees of freeway access. Those sales average \$25,000 to \$26,000 per acre.

37. This appraisal discussed two adjustments to those sales prices. One to account for the fact that they were sales of much smaller properties than the subject and the other to account for "water access" because Gary Works is located adjacent to Lake Michigan. Mr. Oetzel's methodology did not actually apply the size adjustment as discussed. He explained his calculation as follows: "I took the first six sales, which were around the subject property, without any adjustments and averaged \$25,000 to \$26,000/acre and adjusted them 30 percent for water usage only; the indicated value of subject property would be approximately \$33,000/acre, rounded to \$35,000/acre." LC Ex. No. 18, p. 52.

38. Mr. Oetzel multiplied his \$35,000/acre price by 3,154.6 acres to arrive at a rounded value of \$110,400,000 as of March 1, 2002. *Id.* Adjusted to January 1, 1999, his opinion on the value of the land was \$103,400,000. *Id.* at 102.

39. The reliability and credibility of this opinion, however, is diminished for several reasons. First, the Oetzel Appraisal relies on exceptionally small sales in comparison to the subject tract of 3,154.6 acres. Sales 1 – 6, for example, are 5.01 to 75 acres, which according to this appraisal require a minus 20 percent adjustment. USS Ex. No. 2, p. 15. The land value Mr. Oetzel actually used did not make an effective adjustment for this significant difference in the size of the properties.

40. Additionally, the adjustment for water usage is inappropriate because the Solo Cup sale was not a reliable, arm's length sale and the figures used by Mr. Oetzel were incorrect. Mr. Oetzel's water adjustment of 30 percent was based upon the Solo Cup transaction (Sale #7). LC Ex. No. 18, p. 51-52. In cross-examination, Mr. Oetzel admitted that his water adjustment would be "flawed" if the sales price were wrong or if the sale were not an arms-length sale. Tr. Vol. II, p. 15. Based on the unrefuted testimony of Mr. Michael Prendergast, Property Tax Manager for U.S. Steel, the Board finds that Mr. Oetzel's water access adjustment was not justified for several reasons.

- a. The Oetzel Appraisal report states that the Solo Cup sale was a "cash" sale, involving the transfer of 117 acres of land from U.S. Steel to Solo Cup in 2001. LC Ex. No. 18, p. 50.

b. The sale was not a cash (or even a cash equivalent) sale. Mr. Oetzel reported that Solo Cup paid U.S. Steel \$8.9 million for 117 acres of land. LC Ex. No. 18, p. 50. In fact, U.S. Steel received only \$4.7 million in cash, with the remaining \$4.2 million to be paid out of proceeds of two Tax Increment Financing bonds, if and when the Solo Cup site was developed. To date, the site has not been developed and U.S. Steel has received none of the \$4.2 million. Moreover, Oetzel failed to report that immediately upon closing U.S. Steel was required to pay Solo Cup \$1.2 million in connection with the transaction, thus reducing the \$4.7 million cash to \$3.5 million. Additionally, U.S. Steel was obligated to move certain railroad tracks and power lines on the property at an estimated cost of \$\*\*  
\*\*\*\*\*.

c. The Solo Cup transaction involved the sale or transfer of approximately 249 acres of land in a three-party transaction, not simply 117 acres in a two-party transaction. The remaining 132 acres were donated to the City of Chicago for right-of-ways (32 acres) and to make a waterfront park (100 acres).

d. The sale price of the land sold to Solo Cup was inaccurately presented in the Oetzel Appraisal. Furthermore, the sale could not be considered an arms' length transaction.

e. Accordingly, there was no factual basis for Mr. Oetzel's 30 percent adjustment for water access.

41. If the Board took the unadjusted average of the first six sales (i.e., \$25,000 - \$26,000/acre) and reduced that by the 20 percent size adjustment explained (but not applied) by Mr. Oetzel, it would produce a \$20,500/acre value, which is very close to the per acre value concluded by U.S. Steel's appraisers and the Department. This similarity corroborates the land value determined by the Department.

42. Additionally, Lake County has taken the position in filings and in testimony that U.S. Steel should have been assessed according to the same methodology applied to other industrial taxpayers in Lake County. *See Lake County Assessor's Final Statement of Contentions and Defenses ("Lake County Contentions & Defenses")*, ¶ 7. Two witnesses for Lake County, Frank Kelly of Nexus Group, and Ms. Sherry Stone, the Director of Real Estate for Lake County, testified that Cole Layer Trumble ("CLT") assessed other industrial taxpayers in Lake County pursuant to the GUIDELINES. Mr. Kelly testified, "If CLT had valued this land, I believe that – if done correctly, they would have arrived at a value per acre of approximately \$11,312 per acre." Tr. Vol. I, p. 118.

43. The Board declines to adopt the \$11,312/acre value because the weight of the evidence suggests that the proper value is \$19,000 per acre. It is significant, however, that the testimony of Lake County's own witnesses conflicts and strongly undermines the credibility of their position on land value at the Gary Works.

44. Lake County's representative, Ms. Sherry Stone, testified that the real property at Gary Works should have been assessed pursuant to the GUIDELINES applied to other taxpayers in Lake County.

45. Lake County's appraiser, however, did not apply the GUIDELINES to determine the value of the improvements at Gary Works under the cost approach. LC Ex. No. 18, p. 52-69. Instead, Mr. Grzybowski and Mr. Oetzel derived a replacement cost that ultimately tied back to the 2001 cost tables from Marshall Valuation Services, a well known and frequently used cost estimating service. The cost tables in the GUIDELINES are also based on the Marshall Valuation Services, but from 1999.

46. Mr. Grzybowski was primarily responsible for Lake County's replacement cost analysis. His report was incorporated into, and adopted in, the Oetzel Appraisal.

47. Mr. Grzybowski and Mr. Oetzel were provided with a prior appraisal of Gary Works' real property, conducted by the appraisal firm Marshall & Stevens, for assessment year 2001 and updated by Marshall & Stevens for 2002 ("Marshall & Stevens Appraisal"). They were provided with the same property record cards provided to Ernst & Young. Although the appraisers for Lake County had property record cards for Gary Works, they did not rely on these cards because they could not correlate the building numbers and measurements.

48. Mr. Grzybowski began his analysis by adopting the reproduction cost analysis from the Marshall & Stevens Appraisal in its entirety. LC Ex. No. 18, p. 63 ("The costing process involved the utilization of the Marshall and Stevens valuation report"). Specifically, Mr. Grzybowski incorporated into his analysis the "building-by-building reproduction cost estimate of the Gary Works" from the Marshall & Stevens Appraisal. LC Ex. No. 18, p. 57.

49. Mr. Grzybowski's adoption and Mr. Oetzel's incorporation of the reproduction costs from the Marshall & Stevens Appraisal was severely flawed for several reasons:

a. Mr. Grzybowski's sampling of the Marshall & Stevens' measurements was too small to be reliable and demonstrated substantial errors in Marshall & Stevens' data.

b. Mr. Grzybowski sampled measurements totaling a very small percentage of the building space. USS Ex. A. In a few instances, his own measurements showed as much as a 50 percent difference in square footage and a cumulative difference of approximately 20 percent as compared to the building measurements from the Marshall & Stevens Appraisal.

c. In light of the limited sampling and high error rate, it was inappropriate for Mr. Grzybowski and, by extension, Mr. Oetzel, to adopt the reproduction cost analysis from the Marshall & Stevens Appraisal.

50. The measurement errors described above were corroborated by the testimony of Mr. Prendergast, who testified that U.S. Steel did not rely on the Marshall & Stevens Appraisal because it was “deeply flawed.” U.S. Steel checked 25 buildings that had been measured by Marshall & Stevens and found errors in the measurements of 22 buildings, some as much as 50 percent. Marshall & Stevens was asked to re-measure the buildings, but after re-measuring the appraisal still had errors. Tr. Vol. II, p. 204 (“At that point, we lost faith in the basic data of the report and felt it was unreliable.”).

51. Mr. Grzybowski conceded that for the buildings he sampled, his measurements were actually closer to the measurements contained in the U.S. Steel property record cards.

52. Given the errors described, the Board finds that Mr. Grzybowski’s adoption of Marshall & Steven’s reproduction costs was not reasonable, especially in light of the fact that his own sample measurements were more consistent with the measurements on the property record cards produced by U.S. Steel.

53. Based on the Marshall & Stevens Appraisal, Mr. Grzybowski arrived at a reproduction cost of \$911,031,905 for the Gary Works’ buildings, as of March 1, 2002. LC Ex. No. 18, p. 59. From the reproduction cost of \$911,031,905, he and Mr. Oetzel made additional adjustments to arrive at an “adjusted reproduction cost” and, ultimately, the replacement cost for the Gary Works’ buildings (excluding yard improvements) of \$798,617,068. Then he added \$155,562,322 for yard improvements, to arrive at a total adjusted replacement cost of \$954,179,390 for all improvements.

54. Mr. Oetzel made deductions from the reproduction cost to account for “superadequacy” (*i.e.*, abandoned buildings, abandoned basements and changes in construction materials), and he made adjustments for “functional obsolescence” based on “change in building function” (*i.e.*, adjustment for ceiling heights, manufacturing to warehouse uses), as well as “underused building space.” LC Ex. No. 18, pp. 97, 99, 103 (see adjustments in Summary of Cost Approach). He quantified the amount of functional obsolescence from the foregoing causes, as of March 1, 2002, as follows: (i) deductions for “superadequacy” totaled \$25,076,144 (or \$10,281,219 on a depreciated basis), (ii) deductions for change in building function totaled \$64,970,746 (or \$26,638,006 on a depreciated basis), and (iii) deductions for underused building space” totaled \$24,391,413 (or \$10,000,480 on a depreciated basis). LC Ex. No. 18, pp. 97, 99, 103 (summary of cost approach).

55. Although his deductions for these items (\$46,919,705) were greater than Ernst & Young’s deductions (\$10,337,091), the Board finds that Oetzel’s deductions for the foregoing items were insufficiently supported in his appraisal. Specifically:

- a. In order to make proper deductions from reproduction cost, or to make proper calculations of functional obsolescence due to changes in building use and function, the base-line starting point (reproduction cost) must first be validly

determined. As noted above, Mr. Grzybowski and Mr. Oetzel relied on the Marshall & Stevens Appraisal in determining reproduction cost, but that calculation was not reliable.

b. Unlike the Ernst & Young appraisal that contained addenda specifically detailing the approach and supporting information for each obsolescence adjustment, the Oetzel Appraisal did not contain supporting detail or information. Instead, the Oetzel Appraisal contained an addendum comprised of approximately 108 pages of photographs of interior and exterior views of the buildings that Oetzel visited at Gary Works. These pictures were not specifically explained or tied to Oetzel's adjustments. As such, they are of no probative value. *Quality Farm & Fleet, Inc. v. State Bd. of Tax Comm'rs*, 747 N.E.2d 88, 93 (Ind. Tax Ct. 2001); *Heart City Chrysler v. State Bd. of Tax Comm'rs*, 714 N.E.2d 329, 333 (Ind. Tax Ct. 1999).

56. Lake County dismissed the possibility of abnormal economic obsolescence because the steel industry is cyclical. "External obsolescence has been considered in subject property; however, as of the date of value, it is considered to be non-existent. Subject property is part of a cyclical industry." LC Ex. No. 18, p. 99; Tr. Vol. I, p. 299. To this argument, Lake County added a chart purporting to "illustrate the cyclic nature of the steel industry." LC Ex. No. 18, pp. 100-01. While it is undeniably true that the steel industry is part of a cyclical industry, "[e]xternal obsolescence can either be *temporary or permanent*." GUIDELINES, App. F, p. 13 (emphasis added). Market data must be used in estimating external obsolescence. *Id.* Lake County's observation of the cyclicity of the market does not undermine U.S. Steel's claims for abnormal external obsolescence. Furthermore, it does not constitute probative evidence that would rebut U.S. Steel's quantification evidence.

57. Lake County's appraisers did not conduct a sales comparison approach to determine the value of the improvements. LC Ex. No. 18, pp. 46-48. Therefore, Lake County presented no contrary evidence suggesting a *different* value under the sales comparison approach. Instead, Lake County argued that it was not possible to do a reliable sales comparison approach. LC Ex. No. 18, p. 48 ("I have concluded that there is insufficient reliable market data to complete a sales comparison approach; therefore, I have not completed a sales comparison approach as part of this appraisal assignment.")

58. For reasons explained later in this determination, the Board finds that sufficient, reliable market data did exist to establish the value of the Gary Works improvements under the sales comparison approach. That approach was largely corroborated by both U.S. Steel's and the Department's analysis. For all these reasons, the Board disagrees with Mr. Oetzel's conclusion of value.

59. Nevertheless, the Board will consider each of Lake County's contentions to determine whether they rebut or undermine the Department's Assessment.

60. Mr. Oetzel first argued that “[t]he problem with using the sales comparison approach in this appraisal is that there was a lack of sales in the marketplace.” The Board disagrees. There was an unprecedented abundance of sales of comparable steel mill properties. Given the “remarkable” occurrence of integrated steel mill sales in the midwest, particularly Indiana and Lake County, Mr. Oetzel’s failure to analyze and consider those sales was unreasonable.

61. Mr. Oetzel’s next argued that the sales that did occur were “measured against a market value definition and not [a] market value-in-use definition.” This argument misses an essential point. The comparable sales were of steel mills (including integrated steel mills) and the buyers continued the steel making use of the property. Those sales were not cases where the steel mills were purchased and then converted to a different use, which might reflect different motivations. The Board agrees with Mr. Barrow that a sale may be used as evidence in Indiana’s market value-in-use system where the property sold was going to be put to the same use as the subject property. This is consistent with the definitions of market value-in-use and with the requirements of the MANUAL and the GUIDELINES. Therefore, the Board rejects Lake County’s contention.

62. Mr. Oetzel also argued that only the Inland sale occurred prior to the assessment date. In essence, he makes two arguments. First, any sales occurring after the assessment date could not be used to indicate value as of the assessment date. Second, the information on the Inland sale was derived from the Deloitte & Touche Appraisal that was not completed for purposes of determining true tax value. Therefore, it should not be used in this case. The Board disagrees with both contentions. The assessment of Gary Works did not occur until January of 2004, when the Department sent U.S. Steel and Lake County its preliminary determination. Then in late February the Department sent its final determination. The Department had within its possession information from the comparable sales, which have already been described. There is nothing in the MANUAL or the GUIDELINES that precluded the use of the data. The Board recognizes that sales occurring too far past the assessment date might, under certain circumstances, be entitled to less (or no) weight. But sales occurring after the assessment date may be used as long as they are adjusted for time. Additionally, it is appropriate to use sales that have occurred after the appraisal date if the market conditions at the time of the sale were generally the same as those that existed on the appraisal date. The Board rejects Mr. Oetzel’s criticism that the Inland sale was not a good sale because the Deloitte & Touche (“D&T”) appraisal was based on a different standard of value than is used to determine true tax value. The Board agrees with Mr. Barrow that the D&T Appraisal was performed consistent with USPAP and took into account “use value” sufficient to make it a reliable source of information.

63. Mr. Oetzel’s final reason for not using a sales comparison approach was that all sales (except for the Inland sale) were bankruptcy sales, which generally are not considered arm’s length transactions in the market value definition. LC Ex. No. 18, p. 47. The Board rejects this argument. Unlike the general rule where bankruptcy sales represent exceptional circumstances, in the steel industry as of the assessment date, bankruptcy was the rule. Approximately 67 percent of the integrated steel making

capacity was in bankruptcy, and over 40 steel making companies, including 5 of 7 integrated manufacturers, had gone into bankruptcy. Moreover, there are a number of countervailing reasons that the price obtained in bankruptcy represents the most consideration the property could obtain in the market. Mr. Oetzel criticized the use of bankruptcy sales because the companies sold out of bankruptcy were relieved of their “legacy costs” (pension costs, contracts, etc). Although Lake County and Mr. Oetzel presented no evidence or quantification of this effect, the Board finds that, even if certain companies were relieved of their legacy costs, such an occurrence would *increase* not decrease the value of the company sold. In other words, given the choice between buying Company A *with* legacy costs or Company B *without* legacy costs (all other things being equal), a knowledgeable buyer would pay more (not less) for the company without the legacy costs. Lake County’s own expert, Mr. Regelbrugge, agreed with this principle.

## V. DISCUSSION OF U.S. STEEL’S CASE

64. U.S. Steel submitted a Complete Summary Appraisal Report of the Gary Works real property by Ernst & Young, LLP (“E&Y Appraisal”). *See* USS Ex. No. 1.<sup>2</sup> As with the D&T Appraisal, E&Y utilized a sales comparison approach. USS Ex. No. 1-A, p. 32.

65. Ernst & Young relied on 8 sales of industrial tracts, ranging in size from 25 acres to 386 acres, located in Indiana or nearby in Illinois. USS Ex. No. 1-A, p. 34-48. Each of the sales relied on by E&Y required some adjustment to account for the different tract size, different location, different access and different use when compared to the land at Gary Works. USS Ex. No. 1-A, p.44-47. The adjusted sales prices per acre for the sold tracts of land ranged from approximately \$8,000 per acre to \$69,000 per acre. USS Ex. No. 1-A, p. 48. E&Y derived a weighted average of the eight sales based on their comparability to the land at Gary Works, and arrived at a range of \$20,000 to \$28,000. USS Ex. No. 1-A, p. 48.

66. E&Y initially concluded that the value most appropriate to apply to the land at Gary Works was \$21,000 per acre for the 2,842 acres under the operating plant and land considered vacant usable. USS Ex. No. 1-A, p. 48. E&Y excluded 312 acres of unusable land based on the principle that “any portion of the facility not in use ... as of the assessment date” should be deducted under the value-in-use estimate. *See* GUIDELINES, APP. F, p. 19; USS Ex. No. 1-A, p. 48.

67. At the hearing, Mr. Perry explained that only 232 acres (instead of 312) was “unusable,” consisting of capped landfills, \*\*\*\*\*, or land subject to legal restrictions prohibiting its use. USS Ex. No. 1-A, p. 48. Accordingly, it is appropriate to apply the \$21,000 per acre value to the additional 80 usable acres. The revised value (\$21,000 x 2,922) would be \$61,362,000 for the total land at Gary Works, or \$19,449 per acre. Adjusted to January 1, 1999, based on the trending factor, the value of the land would be \$57,385,742, or approximately \$18,188 per acre.

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<sup>2</sup> The E&Y Appraisal is comprised of 3 documents: USS Ex. No. 1-A (Volume I), Ex. No. 1-B (Errata to Volume I), and Ex. No. 1-C (Volume II).

68. Rather than proving that the Department's land value is wrong, the per-acre value conclusions of E&Y corroborated the per-acre value conclusions of the Department. Therefore, USS failed to establish a prima facie case for any relief regarding land value.

69. The appraisal submitted by U.S. Steel's appraisers, E&Y, included both a Cost Approach analysis and a Sales Comparison Analysis. *See* USS Ex. No. 1-A (Volume I) and 1-B (Errata to Volume I).

70. Within its cost approach analysis, E&Y applied the GUIDELINES to develop the replacement cost new, physical depreciation and remainder values. *See* USS Ex. No. 1-A, pp. 50-53. E&Y developed a replacement cost new of \$751,931,541 for the buildings and site improvements at Gary Works as of March 1, 2002.

71. As stated in its appraisal report and described in the testimony of U.S. Steel's appraiser, E&Y undertook the following steps in developing the replacement cost of the improvements at Gary Works:

- a. Members of the team visited Gary Works, spending at a minimum, 100 hours inspecting the property, taking note of the construction materials, physical condition, and deterioration of the buildings.
- b. E&Y reviewed detailed property record cards for the Gary Works that were provided by U.S. Steel. The property record cards were developed by members of the Gary Works property tax department, together with an experienced steel mill cost consultant (Tammy Harnish) who was hired to assist in the project.
- c. E&Y independently verified the accuracy of the property record cards. When necessary, E&Y corrected items on the property record cards such as building dimensions, use, square footages, perimeter area ratios (PARs), wall construction type, grade, condition and date of construction.
- d. E&Y then compiled all of the foregoing information on a building-by-building basis to produce a True Tax Value ("TTV") for each building, utilizing the appropriate tables in the GUIDELINES. E&Y determined the replacement cost new (prior to obsolescence) for each of the buildings at Gary Works. USS Ex. No. 1-A, p. 50.
- e. E&Y followed steps similar to those identified above, including application of the appropriate tables in the GUIDELINES, to develop the TTV for the site improvements (e.g., roads, fencing, slips) at Gary Works. USS Ex. No. 1-A, p. 50.



72. According to U.S. Steel's evidence, the replacement cost new of the buildings and site improvements at Gary Works was \$751,931,541 as of March 1, 2002, pursuant to the GUIDELINES. USS Ex. No. 1-A, p. 50, 53.

73. Though Lake County disputed the accuracy of the replacement cost developed by E&Y in using the GUIDELINES, Lake County did not offer any substantial evidence tending to show that the replacement cost new developed by E&Y – or any of the component pieces upon which the replacement cost was based – was incorrect. Instead, Lake County argued that the replacement cost developed by its appraiser was more credible, but the Board does not find the opinion of Lake County's appraiser to be more credible.

74. E&Y applied the GUIDELINES to determine the value of the Gary Works' improvements under the cost approach. USS Ex. No. 1-A, p. 50. As part of that process, E&Y applied the depreciation schedules in Appendix F to determine normal depreciation. See USS Ex. No. 1-A, p. 51-53 (describing application of the GUIDELINES in determination of normal depreciation).

75. By applying the depreciation schedules, E&Y determined that the buildings and site improvements at Gary Works were entitled to normal depreciation of approximately 71 percent, or \$535,300,533. USS Ex. No. 1-A, p. 53; Tr. Vol. IV, p. 122-23. When subtracted from the replacement cost figure of \$751,931,451, E&Y concluded that the replacement cost, less normal depreciation for the improvements at Gary Works was \$216,631,008, which is almost identical to the parties' stipulated value of \$216,515,600.

77. "Normal depreciation" accounts for the loss of value due to "physical deterioration and typical obsolescence." GUIDELINES, APP. F, p. 8. Property may experience additional losses in value that are not accounted for in normal depreciation: "Any additional loss in value from atypical forms of obsolescence will be referred to as **abnormal obsolescence** and will be estimated separately from the normal depreciation." GUIDELINES, APP. F, p. 4 (emphasis in original). There are two general categories of abnormal obsolescence, functional obsolescence and external (or economic) obsolescence. GUIDELINES, App. F, p. 4. "Any abnormal or excessive functional and external obsolescence that affect the structure[s] must be considered separately since they have not been accounted for in the normal depreciation table." GUIDELINES, APP. F, p. 8. There are a variety of ways to calculate abnormal obsolescence. "Abnormal obsolescence is calculated using different methodologies depending upon the type of inutility it represents. There are numerous methodologies and as a general rule, common appraisal concepts and methods may be used to determine obsolescence under true tax value." *Id.* (citing *Canal Square*, 694 N.E.2d 801).

78. All witnesses who testified at the hearing agreed that it is appropriate to make deductions for abnormal functional and external obsolescence if they exist.

79. “Functional obsolescence is either a physical element that buyers are unwilling to pay for or a deficiency that impairs the utility of a property when compared to a more modern replacement, leading to a loss in value.” *Inland Steel Co. v. State Bd. of Tax Comm’rs*, 739 N.E.2d 201, 210 (Ind. Tax Ct. 2000) (footnote in original), (citing Michael D. Larson, *Identifying, Measuring, and Treating Functional Obsolescence in an Appraisal*, 10 J. PROP. TAX MGMT. 42, 44 (1999)).

80. “[F]unctional obsolescence is a ‘form of depreciation resulting in loss of value due to lack of utility or desirability inherent in the design of the property.’” *Inland Steel Co.*, 739 N.E.2d at 210 n.3 (citing INSTITUTE OF PROPERTY TAXATION, PROPERTY TAXATION 114 (Jerrold F. Janata ed., 2d ed. 1993)).

81. Functional obsolescence is “caused by factors internal to the property and is evidenced by conditions within the property.” *Pedcor Invs. v. State Bd. of Tax Comm’rs*, 715 N.E.2d 432, 435 (Ind. Tax Ct. 1999) (citations omitted). Functional obsolescence works as a penalty against the property’s value. See *Inland Steel Co.*, 739 N.E.2d at 210 (citing Larson, *supra* at 44).

82. The appraisers for U.S. Steel and Lake County each recognized the need to make deductions to account for several forms of “atypical” functional obsolescence. Specifically, E&Y and Mr. Oetzel both made deductions to account for (i) excess construction costs (e.g., adjustment for metal construction in lieu of masonry), (ii) change in building use (comparing original use with present use), and (iii) under-utilized space (e.g., prior manufacturing space with high clearances, now used for storage of spare parts). The Department also recognized the existence of functional obsolescence. DLGF Ex. No. 1, p. 9 (“upon inspection, DLGF staff observed that many of the buildings on these properties are abandoned. The mill owners maintain, and the DLGF agrees, that these buildings are overbuilt, outdated, and serve no use in modern integrated steel producing operations. . . . Hence, they are obsolete in today’s market and have little or no value-in-use to their owners.”).

83. E&Y first identified the abnormal functional obsolescence for “excess construction costs” due to the use of brick and block construction materials where steel or different construction materials would be used today. After determining the depreciated cost of the existing brick and block construction, E&Y compared these amounts to the depreciated cost of construction with modern materials (e.g., steel). The difference – \$\*\*\*\*\* – represented the abnormal functional obsolescence and was deducted from the replacement cost new less normal depreciation (RCNLD) to account for the functional obsolescence due to excess construction costs. USS Ex. No. 1-A, p. 54. Additionally, E&Y made an adjustment of \$\*\*\*\*\* for excess construction costs associated with site improvements (bulkhead pilings). GUIDELINES, APP. G, Schedule G, p. 30. E&Y’s appraisal included two addenda containing the supporting information for these adjustments. USS Ex. No. 1, Addenda D, E.

84. E&Y applied a similar methodology in calculating abnormal functional obsolescence due to changes in building use (e.g., change from former use as “heavy

utility” structure to present use as “light utility”) and under-utilized space (*e.g.*, changes to account for actual present use as opposed to former use of buildings). USS Ex. No. 1-A, p. 55-56, Addendum F (supporting detail for change in building use), and Addendum G (supporting detail for under-utilized space). E&Y calculated the depreciated abnormal functional obsolescence due to change in building use at \$\*\*\*\*\*. E&Y calculated the depreciated abnormal functional obsolescence due to under-utilized space at \$\*\*\*\*\*.

85. In addition to the foregoing items of abnormal functional obsolescence, U.S. Steel claimed an adjustment for abnormal functional obsolescence caused by inefficient layout of buildings and processes at Gary Works that caused the property to incur excess operating costs. Such abnormal functional obsolescence adjustments are permitted for excess operating costs:

**Excess operating costs** are often incurred by a property that suffers functional obsolescence. This means the inutility within the structure causes the owner to have to pay more to operate the property than he/she would if the inutility did not exist. An example of this would be an industrial property that has had a warehouse addition made to the main plant. Because of the site size ..., the warehouse addition was constructed in a manner that makes movement of materials between the main plant and the warehouse less than efficient, thereby causing inutility. In order to overcome this inutility, the owner of the plant has had to purchase a forklift and hire an operator that would not have been needed had the warehouse been an integral part of the main plant.

GUIDELINES, APP. F, p. 10. Adjustments for excess operating costs are not included within “normal depreciation” because they are plant-specific and are not accounted for within the depreciation tables. Moreover, adjustments to account for functional obsolescence due to excess operating costs apply to all properties assessed under the GUIDELINES, including special purpose properties.

86. U.S. Steel claims that Gary Works suffers abnormal functional obsolescence due to excess operating costs associated with plant layout and design inefficiencies caused by changes in technology and accepted production methods.

87. Gary Works first broke ground in 1906, and the first heat of steel was poured in 1909. When originally constructed in 1906, the plant was laid out as a direct flow process to promote smooth and efficient steel making in accordance with the existing technology on unimproved land. To keep up with changes in technology, eventually new facilities needed to be constructed and others expanded. The existing layout of Gary Works’ buildings evolved over time with the addition of new processes. The distances between existing process areas cause substantial costs associated with the movement of raw materials, semi-finished and finished product through the plant.

88. The process of making steel has changed substantially from the days when Gary Works was first built. Until the 1960's, the prevailing steel making technology involved open-hearth furnaces; since that time, steel has been made in BOP (basic oxygen process) shops. Until the 1970s and 1980's, steel was poured into ingots. More recently, steel has been continuously cast in slab casters. Additionally, the process of thinning and rolling slabs into sheets of steel has changed with technological advances and accepted production methods, with the introduction of Hot Strip Mills in the late 1960's. As technologies and accepted production methods have changed, the buildings, improvements and processes at Gary Works have developed and changed substantially to keep up with the market.

89. Using the Existing Layout schematic (US Steel Ex. No. 5), and beginning with the coke production, Mr. Anderson described to the Board each area of the steel making process at Gary Works, how raw and semi-finished materials are handled and transported between process areas (*e.g.*, by rail, by "slab haulers," by conveyor), what products are ultimately produced (*e.g.*, flat sheet, plate, tin) and what markets these products serve (*e.g.*, automotive, appliance, construction, rail). He described how changes in steel making processes affected the layout of plant facilities. For example, at one time, the coke plant had 16 batteries that were used to make coke. Today, Gary Works only uses four batteries due to changes in technology, although the coke plant occupies the same total area (roughly 15 million square feet). Due to the excess space between coke batteries and between the coke plant and the next operation (the blast furnaces, which receives/uses coke), Gary Works incurs materials handling penalties that would not exist if the coke plant were designed to operate with only 4 batteries in a much smaller area. Mr. Anderson similarly described the evolution of, and inefficiencies associated with, the blast furnaces (in the past, there were twelve, today there are four), the #1 and #2 BOP shops, the casters, the plate mill, the hot strip mill, the pickle lines, the electro-galvanized lines and other downstream lines where steel slabs or coils are finished for the customers.

90. As new facilities were added, they could not be placed in locations that appear vacant on the Existing Layout (USS Ex. No. 5). Because new facilities take between 2 and 3 years to construct, they had to be installed in locations outside the then-existing (direct flow) processes in order to maintain ongoing production operations. For example, the 84-inch hot strip mill, which receives steel slabs from the casters, is located approximately \*\*\*\*\* away from the casters. The hot strip mill was constructed in the late 1960's, at a time when the new 84" technology was developed. The 84" hot strip mill could not be placed adjacent to the casters (south of the plate mill) because that area was completely occupied with merchant mills that were then in operation and producing products being sold at the time. Additionally, the 84-inch hot strip mill took approximately two years to construct. It would have been economically infeasible to close production of existing facilities for that period of time, in order to construct a new facility in a more efficient location. Each new facility, and the building that houses it, was built in the most efficient location possible given operating constraints.

91. Mr. Anderson similarly described each process of the plant where facilities/buildings were constructed outside the direct flow and how the location of such process created transportation and materials handling problems and costs. This information was also provided to U.S. Steel's appraisers, E&Y. USS Ex. No. 1-A, pp. 56-58.

92. U.S. Steel introduced an engineering schematic, drawn to scale, showing the existing buildings and processes configured in a direct flow layout as would be found in a modern replacement plant. USS Ex. No. 6. The Modern Replacement plant was developed by a team comprised of (i) an engineering firm with extensive experience in the steel industry (Eichleay Engineering), (ii) an employee of the Gary Works engineering department, (iii) operations managers from throughout the Gary Works plant, and (iv) Mr. Anderson, who oversaw the project and checked the work.

93. Using the Modern Replacement Layout (USS Ex. No. 6) and another layout/schematic showing the locations of buildings in the Existing and Replacement Layouts (USS Ex. No. 7), Mr. Anderson detailed how the raw materials and product would flow through the plant. (a) The coke plant would be reconfigured in a much more compact fashion and closer to the blast furnaces. (b) The coke plant would be reduced in size from its 16-battery layout to 4 batteries, eliminating miles of extra pipelines and utilities. (c) Blast furnaces would be pivoted to facilitate a railroad track layout to run through the furnace. (d) The #1 BOP shop would be located adjacent to the # 2 Q-BOP shop. (e) The liquid steelmaking capabilities would be in closer proximity to the casters. (f) The distance in transporting the slabs would be cut by about \*\*\*\*\* round trip. (g) Rather than taking \*\*\* percent of the slabs to the closest facility (the plate mill), \*\*\* percent of the slabs would now be taken to the closest facility (the hot strip mill). (h) Most of the double-handling of slabs would be eliminated. (i) Miles of conveyors with numerous turnarounds would be eliminated and replaced with a short conveyor that runs about \*\*\*\*\* feet from the discharge end of the strip mill to the coil storage yard for the pickle lines. Both pickle lines would be in the same building. (j) The galvanized facility would be relocated to the exit end of the cold mill facility, rather than being \*\*\*\*\* from the cold mill. (k) The overall plant area would be reduced by approximately \*\*\* percent, which would minimize the amount of product handling and excess transportation, energy lines, maintenance and damage to the product. USS Ex. Nos. 5, 6 and 7 (showing existing and replacement layout on same page); USS Ex. No. 14, pp. 2-4.

94. To quantify the excess operating costs associated with the Existing Layout as compared to the Modern Replacement, Mr. Anderson and his department assisted in the preparation of a report titled, "Plant Layout – Excess Handling Costs." USS Ex. No. 14 (Plant Layout – Excess Handling Costs), pp. 2-4.<sup>3</sup> The Plant Layout – Excess Handling Costs report incorporated information on the differences in areas, in linear feet, and materials flow/traffic patterns between the Existing Layout and the Modern Replacement plant.

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<sup>3</sup> USS Ex. No. 14 is essentially the same as Addendum H to USS Ex. No. 1-A (E&Y Appraisal), but reflects certain minor corrections that were made by Mr. Anderson and Mr. Sloan and detailed at the hearing.

95. Based on (i) the information on distances and materials and product flow provided by Mr. Anderson's engineering department and operations managers throughout Gary Works, and (ii) actual production costs for 2001 from the financial data and accounting systems of Gary Works, Mr. Ronald Sloan, the Controller for Gary Works, calculated the amount of excess operating costs attributable to the plant layout problems/inutility. With respect to production cost data, Mr. Sloan explained that each manufacturing/process area of the plant has a "cost center" where production costs are tracked, on a monthly and annual basis, so that U.S. Steel can track the efficiency of the Gary Works operations. Mr. Sloan and members of his department segregated all costs associated with each separate "cost center" (e.g., coke, Steel Products, Hot Strip Mill, Pickle Lines, Sheet Products, Hot Roll Finishing, Plate Products and Tin Products). Once segregated by cost center, the variable costs of operations associated with materials handling, product flow, etc., were "unitized" (i.e., reduced to a unit of measurement, such as dollars per ton or dollars per linear foot) allowing U.S. Steel to compare materials handling costs under the Existing Layout with the costs of materials' handling under the Modern Replacement. Tr. Vol. III, p. 219-21 (describing process in context of "Central Shops" example in Steel Producing page); USS Ex. No. 14, pp. 1-15.<sup>4</sup>

96. In addition to production costs, which are segregated by cost center, U.S. Steel also tracks plant-wide costs that are not limited to any individual production area or cost center. Tr. Vol. III, pp. 215-16; USS Ex. No. 14 (Excess Handling Cost report), p. 1. To identify and account for these costs in the Excess Handling Cost report, Mr. Sloan and his department identified a number of "Miscellaneous Impacts" separate and apart from the particular manufacturing areas. The miscellaneous items included plant-wide truck hauling, energy/line maintenance, lost profits due to damaged coils, labor savings from "operations services," sucker trucks (that remove sludge and waste), etc. Any costs identified within the "miscellaneous impacts" category were specifically removed from the calculation of costs associated with particular manufacturing areas or cost centers.

97. Using the Excess Handling Cost report (USS Ex. No. 14), Mr. Sloan described in detail the process by which he and members of his department calculated variable costs of operations for 2001 (the last full year before the assessment year) and derived "excess operating costs" by comparing actual production under the Existing Layout (USS Ex. No. 5) with the production costs as they would exist under the Modern Replacement Plant (USS Ex. No. 6). The total annual "excess operating cost" penalty associated with the current configuration/layout of the buildings and improvements at Gary Works is \$\*\*\*\*\*. USS Ex. No. 14, p. 1. These production costs are very stable and do not change significantly from year to year.

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<sup>4</sup> In most cases, the costs associated with materials handling under the Replacement layout were less than the costs associated with the Existing Layout. In one instance, however, the costs were greater under the Modern Replacement – i.e., with the Plate Mill, which was moved further away from the casters. In that instance, Mr. Sloan recorded the cost increase (and thereby reduced cost savings) associated with the Modern Replacement. Tr. Vol. III, pp. 234-35 (Sloan); U.S. Steel Ex. No. 14 (Excess Operating Cost report), p. 1, 14 (describing Plate Products).

98. Based on the \$\*\*\*\*\* annual excess operating costs, U.S. Steel's appraisers, E&Y, next depreciated the annual penalty over the remaining useful life, as directed in the GUIDELINES. *See* Appendix F, pp. 10-11. Specifically, E&Y first determined the number of years of remaining economic life for the buildings at Gary Works (*i.e.*, 15 years) taking into account historical maintenance and capital expenditures. USS Ex. No. 1-A, pp. 58-59. To avoid double counting of tax benefits, E&Y reduced the annual excess operating costs by the applicable tax rates. Tr. Vol. IV, p.20; USS Ex. No. 1-A, p. 59. E&Y then developed a 15 percent discount rate by determining the Weighted Average Cost of Capital for participants in the steel industry as of the assessment valuation date. Mr. Stall explained the steps in developing the discount rate, and provided additional supporting detail for its weighted average cost of capital in Addenda J and K to its report. USS Ex. No. 1-A at Addenda J, K. Thus, E&Y calculated that the total penalty due to excess operating costs associated with the existing layout of the buildings was \$\*\*\*\*\* as of the assessment date.<sup>5</sup>

99. "The existence of one or more environmental conditions can reduce the value of a property or even create a negative value." APPRAISAL INSTITUTE, *THE APPRAISAL OF REAL ESTATE* 209 (12 Ed. 2001). The Department agrees that environmental factors at Gary Works have "a negative effect upon the marketability of the land." DLGF Ex. No. 1, p. 8. A potential buyer would be liable for environmental contamination present at the property unless the buyer was an "innocent purchaser" and that potential liability would affect the price paid by the potential buyer.

100. Therefore, U.S. Steel claimed a deduction from value for the costs associated with cleanup of environmental contamination directly related to the operation of Gary Works. USS Ex. No. 1-A, p. 72. As described in the E&Y Appraisal and explained by Mr. Perry of E&Y, U.S. Steel spent over \$\*\*\*\*\* related to the environmental clean up of the Grand Calumet River. As explained by Mr. Perry, the known and quantified costs of remediation would affect the price demanded by the seller and the price to be paid by a buyer in a sale of the subject for continued use in steel making. "To calculate the impaired value, one begins with the unimpaired value and deducts the cost to remediate the site and impact of stigma. The same phenomenon is witnessed in the analysis of contaminated property. The property sells to a knowledgeable buyer at an impaired price. This price generally consists of two elements: First, the buyer's estimate of the cost to remediate[;] Second, a discount due to uncertainty (stigma)." APPRAISAL INSTITUTE, *THE APPRAISAL OF REAL ESTATE* 216 (12 Ed. 2001). E&Y did not take any deductions for generalized environmental contamination or conditional liability for clean up in the future.

101. Lake County counters that this was not an appropriate deduction because U.S. Steel was required to pay these expenses associated with clean up of the Grand Calumet, and they would not have been "passed on" to a subsequent buyer of the property due to existing governmental orders making this a liability of U.S. Steel alone. Tr. Vol. I, p. 274, 275; LC Ex. No. 19, p. 10 (Corrective Action Order dated Feb. 1998). Lake County's analysis on this

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<sup>5</sup> The E&Y report originally quantified abnormal functional obsolescence due to excess operating costs at \$\*\*\*\*\* USS Ex. No. 1-A (E&Y Appraisal), pp. 56-59, 72. This number was adjusted at the hearing based on certain minor corrections to the annual excess operating cost figures provided by Mr. Sloan.

issue is inconsistent with its own theory and it is incorrect. Lake County has claimed that the market value-in-use standard requires the Board to focus on the value to the owner (*i.e.*, focus on “ask price”) and not the value to a similar user (*i.e.*, bid price). LC Ex. No. 18, pp. 5-6. If that were the proper focus, then the deduction for the known costs associated with clean up of environmental contamination would not be flawed because U.S. Steel had to pay those costs. But that is not the proper focus. The Board has explained that *value-in-use considers the utility received by the current owner or a similar user*. As such, the deduction of known costs is appropriate because it has negative impact on what a buyer would be willing to pay for the property and what a seller would expect to receive for it. Notwithstanding any consent decree, a prospective purchaser would still take into account the potential liability associated with environmental contamination. If U.S. Steel were unable to pay those costs due to bankruptcy or some other reason, the government would still look to a purchaser, who could not escape liability on the basis that U.S. Steel was also liable. The prospective purchaser would make a deduction from the purchase price for these known costs.

102. Dr. Kaplan agreed with Mr. Regelbrugge (Lake County’s witness) that the steel industry is a cyclical industry. Nevertheless, Dr. Kaplan opined that, unlike other cyclical industries, the steel industry’s historical performance indicates that it is cyclical around a “downward trend.” In other words, through the early 1990’s, the domestic steel industry generally followed the demand cycle, but the trend line for the steel industry was a downward trend caused by the increase in excess world steel capacity over time, depressing real (*i.e.*, inflation adjusted) prices. With respect to the actual market conditions around the assessment date, Dr. Kaplan opined that the conditions in the steel industry varied widely from the traditional business cycle in the sense that the steel industry was suffering unprecedented turmoil due to a series of world events. In particular, Asia and Russia suffered economic crises that caused domestic demand for steel to drop substantially, which in turn forced domestic steel producers in those countries to export their product to other countries, including the United States. Furthermore, at the time of the assessment, the steel industry experienced “a financial collapse not seen ... since post World War II.” Between 1997 and 2003, approximately 40 steel companies entered bankruptcy, including 5 of the 7 (domestic) integrated steel companies. Between 2001 and 2004, approximately 67 percent of the domestic integrated steel making capacity was in bankruptcy.

103. Lake County points to a recent upturn in market conditions as evidence that the market conditions in 2002 did not cause economic obsolescence. The Board, however, rejects Lake County’s argument. Deductions for external obsolescence for “temporary” losses in value are expressly sanctioned. GUIDELINES, Appendix F, p. 13 (“Temporary external obsolescence is caused by factors in the market such as an oversupply of the type of space [*i.e.*, products] [the company] provides.”). As of 2002, the market participants in the steel industry were anticipating flat to minor increases in prices. The best indicator of the market’s anticipation of the steel industry is reflected in the sales of steel companies between 2002 and 2003, where the prices were still greatly reduced (*i.e.*, the future anticipated return on investment was low as reflected in the prices paid for the companies). Furthermore, the 2004 prices for steel are simply too



remote from the March 2002 assessment date to be relevant and those prices were unforeseen on the assessment date.

104. Even today's relatively high prices for steel may be the result of phenomena widely believed to be temporary, and are expected to decline. Dr. Kaplan opined, the price spikes of 2004 were unanticipated and based on China's recent growth and demand for steel. Two factors are expected to reduce or eliminate China's positive impact on steel prices. First, China has been building substantial steel making capacity of its own over the past few years and as those facilities come on line, they will add to the excess capacity problem. Second, China's economic growth has already slowed, such that China has already started to become a net exporter of steel. The steel prices in late 2004 and early 2005 are too remote to be used as a basis to deny the unprecedented market conditions or rebut their effects on the steel industry and the value of Gary Works as of the assessment date. Lake County failed to establish that 2002 and 2005 steel prices have probative value for the January 1, 1999, valuation date for the 2002 assessment.

105. Lake County offered the testimony of Mr. Roger Regelbrugge to support their argument that the Steel Industry is cyclical and that Gary Works would not be entitled to adjustments for external obsolescence due to market conditions. While the Board agrees (as did U.S. Steel's witnesses) that the steel industry is cyclical, this fact does not resolve the inquiry or indicate that Gary Works did not suffer external obsolescence. External obsolescence may affect properties in a cyclical industry. Moreover, under the value-in-use concept, if an industry comprised of special purpose properties is in difficult economic times, individual plants within that industry will almost certainly experience economic obsolescence because they are not readily adapted to alternate uses. Mr. Regelbrugge did not refute any of the testimony as to the severity of the turmoil in the steel market or its affect on the steel industry. He did not dispute the existence of the downturn in market conditions in Asia or Russia. Nor did he dispute that the drop in demand for steel in these countries, in conjunction with excess global capacity, affected prices for steel. He did not dispute *any* of the statistics on which Mr. Kaplan's testimony was based – including the number of bankruptcies, the impact on employment levels, or the drops in steel prices.

106. Mr. Stall of E&Y reinforced many of Dr. Kaplan's observations and explained how the unprecedented market conditions negatively affected the value of Gary Works as of the assessment date. Tr. Vol. III, pp. 259-60 (Economic conditions "were about as bad as [they have] ever been in the industry"). In addition, Mr. Stall explained how E&Y quantified the external obsolescence affecting Gary Works' real property as of the assessment date at \$\*\*\*\*\* (rounded). USS Ex. No. 1-A, pp. 59-72. The external obsolescence was applied only to the improvements (not land) based on the generally accepted appraisal theory that land does not suffer from any form of depreciation.

107. E&Y's quantification of external obsolescence was based on the economic reality that an investor or purchaser wanting to enter the integrated steel making business has two options, build a facility or buy an existing facility. If an equally desirable

substitute plant can be purchased for less than it would cost to construct, the investor would make that purchase. One way to account for external obsolescence is to compare the build-or-buy options, which is the approach E&Y followed: “We know from the Cost Approach what it would cost to replace the land, buildings and site improvements at Gary Works. As explained ..., we also know that steel making companies were on the market and being sold for *less* than it would cost to build (i.e., replace) those assets. In general terms, the difference between the market value of those existing real property assets and the cost to build or ‘replace’ those assets under the Cost Approach (less physical and functional obsolescence) represents the *economic obsolescence*.”<sup>6</sup> USS Ex. No. 1-A p. 59.

108. To determine the difference between the market value of existing real property assets and the cost to build/replace those assets, E&Y applied the following conceptual steps:

a. First, E&Y determined the total value of all assets (i.e., the Business Enterprise Value, or “BEV”) of the Gary Works. At the hearing and in its Appraisal, E&Y detailed two methodologies – a Guideline Company Method and a Sales Transaction Method – that were used to determine the business enterprise value for Gary Works. Tr. Vol. IV, p. 33; USS Ex. No. 1-A, pp. 61-67. E&Y concluded that the value for the total assets of the Gary Works would be \$\*\*\*\*\* as of March 1, 2002. USS Ex. No. 1-A, p. 67.

b. E&Y then calculated the net current assets (e.g., cash and items readily converted to cash, such as inventory and accounts receivable), based on balance sheets/financial data from Gary Works. Because the net current assets are not being valued for tax purposes, their value must be deducted. E&Y determined that the inventory had a market value of \$\*\*\*\*\*, the accounts receivable had a value of \$\*\*\*\*\*. From these current assets, E&Y deducted current liabilities of \$\*\*\*\*\*, which was necessary to derive the “net” current assets. USS Ex. No. 1-A, pp. 67-70. The net current assets of \$\*\*\*\*\* was then deducted from the total Business Enterprise Value (\$\*\*\*\*\*) to arrive at the total value attributable to underlying tangible and intangible property (i.e., \$\*\*\*\*).

c. E&Y applied no value to the intangible assets; thus the total \$\*\*\*\*\* was attributed to the underlying tangible property (i.e., real property and tangible personal property).

d. E&Y next deducted the land value (i.e., \$\*\*\*\*\*) from the \$\*\*\*\*\* attributable to all tangible assets, because it is generally accepted appraisal theory that land does not suffer from any form of depreciation, including external obsolescence. USS Ex. No. 1-A, p. 71. Thus, E&Y determined that, under the market approach, a total of \$\*\*\*\*\* was attributable to taxable personal property, exempt property and buildings.

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<sup>6</sup> E&Y use the term “economic obsolescence” rather than “external obsolescence.” Both terms are synonymous.

e. E&Y next compiled the pre-economic obsolescence values for the taxable personal property, exempt property and buildings: taxable personal property was reported at \$\*\*\*\*\* (which is the value, prior to abnormal obsolescence adjustments, that U.S. Steel reported on its 2002 personal property returns); exempt property was reported at \$\*\*\*\*\* (which is the value it would have if taxed); and buildings were reported at \$\*\*\*\*\* (which is the replacement cost less all forms of depreciation except external obsolescence). Thus, the total indicated value for all tangible assets other than land before any economic obsolescence was \$\*\*\*\*\*.

f. E&Y next compared (i) the value attributable to the tangible assets developed under the BEV, to (ii) the pre-economic obsolescence values assigned to the tangible assets (excluding land). Mathematically, this comparison was made by dividing the adjusted BEV (\$\*\*\*\*\*) by the total value (pre-economic obsolescence) for the tangible assets (\$\*\*\*\*\*):  $[\$*****] \div [\$*****] = \text{*** percent}$ , indicating that the tangible personal property, exempt property *and* the buildings each suffered a 37 percent external obsolescence penalty (*i.e.*, \*\*\*\*\*). Tr. Vol. IV, p. 45, 46; USS Ex. No. 1-A, p. 71.

g. Finally, E&Y applied the 37 percent penalty pro rata to all of the tangible assets, except the land.

109. U.S. Steel's witnesses testified that minor corrections in the calculation of excess operating costs reduced the abnormal functional obsolescence penalty from \$\*\*\*\*\* to \$\*\*\*\*\*. This change increased the pre-economic obsolescence value of the improvements from \$\*\*\*\*\* to approximately \$\*\*\*\*\*. E&Y then applied the external obsolescence penalty of 37 percent to the revised value of \$\*\*\*\*\* for the improvements. That percentage translates into a dollar penalty of approximately \$\*\*\*\*\* for external obsolescence that was not accounted for in the depreciation tables of the GUIDELINES. Tr. Vol. IV, pp. 48-49 (describing application of percentage penalty to original \$\*\*\*\*\* figure); USS Ex. No. 1-A, pp. 71-72. U. S. Steel's application of the abnormal external obsolescence penalty resulted in a final value for the improvements of approximately \$\*\*\*\*\* (\$\*\*\*\*\* minus \$\*\*\*\*\*) under the cost approach.

110. Mr. Barrow criticized one aspect of E&Y's calculation based on the valuation of inventory within the BEV analysis. Rather than using the inventory value (\$\*\*\*\*\*) reported on U.S. Steel's personal property return, E&Y valued the inventory pursuant to Revenue Procedure 2003-51 and paragraph 37 of FAS 141. By contrast, in compiling values for the tangible personal property, E&Y relied upon the pre-obsolescence value U.S. Steel reported on its personal property tax return (*i.e.*, \$\*\*\*\*\*). USS Ex. No. 1-A, p. 71. Mr. Barrow argues that, if E&Y had used the \$\*\*\*\*\* inventory figure instead of the \$\*\*\*\*\* figure, it would have reduced the total external obsolescence penalty, in percentage terms, from 37 percent to approximately 5 percent. He did not have problems with E&Y's remaining calculations.

111. As with the Department, E&Y performed the following steps in conducting the sales comparison approach: (1) Research the market for sales information involving properties similar to the subject in type, date of sale, size, physical condition, location, and land use; (2) verify the data for accuracy and ensure that they are arms length transactions, (3) select relevant units of comparison; (4) analyze differences between the comparable sale of properties and the subject property; and (5) reconcile the various value indications produced from the analysis of comparables into a final value indication or range. *See* USS Ex. No. 1-B, p. 73.

112. E&Y began by identifying sales transactions involving operating steel mills that were acquired. Because it was a market value-in-use appraisal, E&Y selected transactions where (i) the acquirer was an integrated steel manufacturer producing flat rolled products (sheet/coiled products), (ii) the transaction date was within a reasonable range of the assessment date, and (iii) there was sufficient transaction data available. USS Ex. No. 1-B, p. 73. Tr. Vol. III, pp. 264-65. E&Y researched publicly available financial data, such as annual reports, SEC 10K and 10Q filings, the DLGF Valuation Report and IRON AND STEEL WORKS OF THE WORLD, 2002. E&Y also interviewed management of the companies involved in the transactions and toured the steel mills that were ultimately selected as comparables. USS Ex. No. 1-B, p. 74; Tr. Vol. III, p. 264-68.

113. Based on the foregoing research, E&Y selected five companies as most comparable to the Gary Works on the basis of steel products produced, capacity of raw steel production and timing of transaction:

- Ispat (Inland),
- ISG (LTV) – Indiana Harbor,
- ISG (LTV) – Cleveland,
- US Steel (National) – Great Lakes, MI, and
- ISG (Bethlehem) – Burns Harbor.

*See* USS Ex. No. 1-B, p. 74.

114. Based on the detailed information obtained through publicly available sources and interviews with management of the companies involved in the transactions, E&Y determined the total consideration paid in each transaction as well as the breakdown of total consideration attributable to the underlying land, buildings and site improvements for each of the identified steel mills/transactions. USS Ex. No. 1-B, p. 75 (Table 1 and discussion of methodology).

115. While an appraiser generally does not rely on or assign significant weight to bankruptcy sales in the sales comparison approach, in light of the conditions in the steel industry on the assessment date, the number of companies in bankruptcy and the fact that bankruptcy sales were in fact the market, it is under these circumstances appropriate to consider bankruptcy sales.

116. E&Y next selected units of comparison to be applied to the Gary Works. E&Y ultimately selected two units of comparison: (1) value of buildings and site

improvements per ton of capacity, and (2) value of building and site improvements per square foot.<sup>7</sup> If all five of the sales comparables identified by E&Y are considered, under the first unit of comparison, they would produce a range of value from \$\*\*\* to \$\*\*\* per ton of capacity. Under the second unit of comparison, they would produce a range of value from \$\*\*\* to \$\*\*\* per square foot of building.

117. E&Y analyzed the differences between the comparable sales and Gary Works. Ultimately, E&Y applied the units of comparison “per ton of capacity” and “per square foot of building” based on two sales transactions, the ISG (Bethlehem) – Burns Harbor transaction and the U.S. Steel (National) – Great Lakes transaction.<sup>8</sup> E&Y explained the reasons it relied on the Burns Harbor and Great Lakes transactions. Burns Harbor set the upper limit of value because it was the most modern facility, without the plant layout problems of Gary Works, having been built as an integrated steel mill in the 1960s. The Great Lakes transaction set the lower limit of value. Having originally been constructed in 1929, it is comparable to Gary Works in age, and the plant has similarly undergone significant upgrades over the years, creating excess operating cost issues similar to those of Gary Works. Both Burns Harbor and Great Lakes are integrated steel mills that produce similar products and serve the same markets as Gary Works.

118. Applying the Burns Harbor and Great Lakes data, E&Y explained that a knowledgeable buyer of Gary Works at the time of the assessment date would not have paid more than the price paid for Burns Harbor, at \$\*\*\* per ton of capacity or \$\*\*\* per building square foot, and would not have paid less than the price paid for Great Lakes, at \$\*\*\* per ton of capacity or \$\*\*\* per building square foot. E&Y gave equal weight to the upper and lower indications of value and arrived at \$\*\*\* per ton of capacity and \$\*\*\* per building square foot, which it then applied to the capacity and square foot of building space at Gary Works. Gary Works has 7.5 million tons of capacity and approximately 15 million square feet of buildings. USS Ex. No. 1-B, p. 80 (Table 5). Based on the foregoing units of comparison, the indicated range of value for the improvements was \$\*\*\*\*\* to \$\*\*\*\*\*. E&Y ultimately gave approximately equal weight to each indication of value by unit, producing a value of approximately \$\*\*\*\*\* for the improvements at Gary Works.

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<sup>7</sup> E&Y considered, but did not use, a third unit of comparison “value of total real property per ton of capacity” because the inclusion of land from the various transactions distorted the analysis due to the facts that (i) there were large differences in the size of parcels, which ranged from 800 acres to 3300 acres, and (ii) the land sites were dispersed throughout the Midwest, introducing variation due to local market conditions. USS Ex. No. 1-B, p. 77.

<sup>8</sup> The two properties with the lowest price per ton of capacity and per square foot of building, LTV-Indiana Harbor and LTV-Cleveland, were not relied upon because at the time they were sold their facilities were in “hot idle” condition. Therefore, they were not as comparable in circumstances to the Gary Works.

## **VI. DISCUSSION OF DEPARTMENT OF LOCAL GOVERNMENT FINANCE'S CASE**

119. In response to the *Town of St. John* litigation, the Department, as the agency charged with interpreting Ind. Code § 6-1.1-31-7(d), promulgated 50 IAC 2.3-1-2, which incorporates the 2002 REAL PROPERTY ASSESSMENT MANUAL (“MANUAL”) as the new rule of property tax assessments of Indiana. It defines true tax value as “[t]he market value in use of a property for its current use, as reflected by the utility received by the owner or a similar user, from the property.” Following this definition in the MANUAL is the Department’s interpretation of market value-in-use. Under the above definition, market value-in-use incorporates 1) the current use of the property, and 2) the value to the owner or similar user.

120. The “current use of the property” is clear. It is the use at the time of the assessment. Mr. Barrow testified that value-in-use as defined by the manual is the value of a property for a specified use. He further testified that market value-in-use reflects the value of the utility for which the property is currently being used.

121. Value-in-use cannot be judged solely by utility received by the current owner. The phrase “the value to the owner or similar user” suggests the value to the seller or buyer who would continue the use of the property in a like manner. In other words, value-in-use reflects the value to the owner that put the property to a specific use or a subsequent user or buyer who would continue to utilize the property in the same manner. Thus, the measure of value for the use of the property under Indiana’s market value is what similar users would pay for the specified current use; it does not relate to the quantity of use or the fact that it could be zoned for other purposes that would render a greater value. For example, a residential property’s value-in-use would not be affected by its homeowner living in a nursing home. Similarly, a home that sits on a highly valuable commercial lot and is currently being used as a residence would be valued as residential property. The fact that commercial users would pay substantially more for the residential property is irrelevant.

122. Because the measure of value is what similar users would pay, true tax value or market value-in-use may at times equal value in exchange. The MANUAL states, “[I]n markets where there are regular exchanges, so that ask and offer prices converge, true tax value will equal value in exchange.” Mr. Barrow testified that one example that could evidence true tax value equating to value in exchange is a sale of residential property as long as it was a valid transaction. He testified that a sale of a special purpose property could also be a situation where true tax value could also equal value in exchange which is consistent with the MANUAL. LC Ex. 12, p. 4.

123. Because true tax value may sometimes equal value in exchange, true tax value can be determined by looking at the bid price and the ask price. The bid price is what a buyer is willing to pay to purchase an asset. The ask price is what the seller is willing to take in exchange for an asset; it is generally set by an owner. It is the starting point for determining market value in use. The ask price is not limited to the initial ask

price. Usually the initial ask price is typically higher than the ultimate sales price of real estate. Ask price is not the only test of true tax value as it is not representative of any objectively verifiable data. Mr. Barrow testified that if ask price was the only test of true tax value, there would not be any objectively verifiable standard against which one could judge the accuracy of the assessments, unless the assessor had an ask price for every individual property.

124. Sales are objectively verifiable data. The measurement for accuracy of assessments in Indiana is not comparing assessments to ask prices; rather, the assessments are compared to sale prices for the continued use. The sale price would be considered the target that the assessor is trying to achieve. This applies to all classes of property except for the agricultural class. Therefore, the best evidence of market value-in-use is what the seller initially asks and revises for the utility of the property until a convergence of ask and bid price occur. Mr. Barrow testified that it would not be appropriate under Indiana's value-in-use standard to ignore sales.

125. The MANUAL specifically addresses bid price and ask price in relation to special purpose properties. It provides:

In the second instance, special-purpose properties often have very different property wealth estimates under a value-in-use scenario as opposed to value-in-exchange due to the motivations of the parties involved. This difference can be expressed as the difference between the bid and ask price for a special-purpose asset. The bid price is what a buyer is willing to pay to purchase an asset, the ask price is what the seller is willing to take in exchange for an asset. Typically, the bid price will initially be lower than the ask price, some negotiations will occur, and when the two are equal an exchange will take place.

In assessment, we are estimating how this negotiation will be resolved as of January 1, 1999. For property types that are frequently traded, the bid and ask price are likely to be fairly similar. For properties that are infrequently exchanged, or that are only exchanged under extraordinary circumstances, this difference between the bid and ask price is likely to be wider and more difficult to reconcile.

A seller of a special-purpose property would accept nothing less than a price equal to the utility being gained from the property. For properties currently in use, this amount would be termed the value-in-use (i.e. the ask price). A buyer of a special purpose property would initially bid no more than necessary to motivate the seller. A buyer would likely start with a low bid such as the liquidation value of the property. Assuming that the buyer intends to use the property for its current use, the buyer will likely adjust the bid price until a transaction is completed. Since the seller has no motivation to sell at anything less than the value in use for a special purpose property, the ask price becomes the benchmark for a likely

transaction under a value-in-use scenario. In the case in which the seller adjusts its opening price and actually consummates a transaction with the buyer at an agreed price, the bid and ask price coincide and reflect the value-in-use of the property.

LC Ex. 12, p. 4.

126. A special purpose property is a property whose unusual physical design makes it primarily useful for the use for which it was built, but of limited utility for other purposes. A steel mill is an example of such a property. The use for an integrated steel mill is as an integrated steel mill. Applying statutory construction principles to the Department's interpretation of market value-in-use for special properties, the result is that where the bid and ask price for a special purpose property converge, at that point market value-in-use would be established. Mr. Barrow testified that if a grain elevator sold and the buyer continued the use of the property that sale would represent market value-in-use. He testified that if one integrated steel mill was bought by another steel mill and that use was continued, the sale price would represent market value-in-use. Because, the seller would accept nothing less than a price equal to the utility being gained from the property, the negotiated price for the special purpose property represents the utility to the owner. Similarly, the price that the buyer pays for a special purpose property to continue the use of the property reflects the utility to a similar user. Thus, such a sale determines the market value-in-use of a property.

127. In 2001, the Legislature directed the Department to assess all industrial facilities with an estimated true tax value greater than twenty-five million dollars (\$25,000,000). Ind. Code § 6-1.1-8.5-8. The Department identified four properties in Lake County that met the requirements of the statute: 1) BP America Refinery in Whiting, Indiana; 2) International Steel Group Integrated Steel Mill in East Chicago, Indiana; 3) Ispat Inland Integrated Steel Mill in East Chicago, Indiana; and 4) United States Steel Corporation's Integrated Steel Mill in Gary, Indiana.

128. In July 2003, the Department sent letters to each of the tax departments of the facilities notifying them of its statutory responsibility to assess the property and requested certain assessment data. This assessment data consisted of maps, plats, construction data, any appraisals that had been conducted on the property, any sales of the comparable property, and any other information the taxpayer thought was relevant. Late in July 2003, the Department sent a follow-up letter again requesting assessment data from the tax departments. DLGF Ex. 1, p. 3. The Department also notified them that it would be contacting them regarding a time and a date to conduct an on-site meeting and tour of the facility.

129. U.S. Steel provided the requested information to the Department. It included sales information. The Department conducted the USS on-site meeting and tour of the facility in the summer of 2003. Based on these meetings and property data, the Department calculated a preliminary certification of the true tax value of the property. Notice of the preliminary certification of true tax value of U.S. Steel's property in Gary was mailed to U.S. Steel, its attorney of record, and the Lake County Assessor in



December 2003 pursuant to 50 IAC 19-2-3 (a). After sending the preliminary certification, the Department met with U.S. Steel and Lake County officials in January 2004 to explain the methodology used in arriving at the true tax value. DLGF Ex. 1, p. 4. The assessment date for the 2002 general reassessment was March 1, 2002. The guidelines for the pre-approved mass appraisal system used a valuation date of January 1, 1999. Therefore, to arrive at a value for the 2002 assessment date, the physical and market conditions that existed on March 1, 2002, should be trended to a January 1, 1999, value-in-use.

130. In determining the assessment for U.S. Steel, Mr. Kurt Barrow, the assessment director for the Department, researched steel trade publications and looked at the price per ton of steel domestically and globally. He concluded that the price of steel on March 1, 2002, was very similar to the price of steel in July 1998 when Inland Corporation sold to Ispat International. Mr. Barrow then explained to U.S. Steel and Lake County that he established the land value at \$19,000 per acre based on an appraisal of the sale of Inland Corporation to Ispat International provided by Ispat Inland, Inc. To arrive at an assessed value of improvements, the Department utilized the sales approach because two of the three integrated steel mills in Lake County sold between 1998 and 2002.

131. Mr. Barrow identified seven sales of integrated steel mills where both buyers and sellers were steel companies. These sales are as follows: 1) Ispat's purchase of Inland in Lake County, Indiana; 2) sale of LTV in Lake County, Indiana to International Steel Group ("ISG"); 3) ISG's purchase of the Bethlehem Steel facility in Burns Harbor, Indiana; 4) ISG's purchase of a LTV facility in Cleveland, Ohio; 5) USS's purchase of National Steel's Great Lakes, Michigan plant; 6) USS's purchase of the National Steel facility in Granite City, Illinois; and 7) U.S. Steel's purchase of National Steel's facility in Portage, Indiana. Mr. Barrow determined that the Ispat sale was the best comparable sale for U.S. Steel and placed all weight on this sale.

132. In July 2004, the Department released *The Valuation of the Lake County Industrial Facilities Greater than \$25M in value for the 2002 General Reassessment* ("The White Paper"), which explained how it arrived at the assessed valuation for U.S. Steel and three other industrial facilities. The Department stated seven reasons it relied on the Ispat Sale for assessing U.S. Steel.

- The sale represented the sale of one of the three subject properties.
- The sale was an arms length transaction.
- Inland was operating efficiently (approx. 90 percent of capacity) at the time Ispat made the purchase.
- The steel economy was in a "good" period. The effects of foreign steel dumping and overcapacity in the domestic market had not yet been reflected in the domestic steel prices.
- The Inland sale was the only sale not out of a bankruptcy.
- The sale price was supported by an appraisal conducted by Deloitte and Touche. The appraisal was completed for the sale of the property and not as part of a property tax appeal. The appraisal complied with the

standards and rules of the UNIFORM STANDARDS OF PROFESSIONAL APPRAISAL PRACTICE (“USPAP”).

- The Department further determined that similar to Inland, U.S. Steel had maintained its production and capacity as well as remained viable through the downturn of the steel economy.

DLGF Ex. 1, p. 13.

133. True tax value of real property can be reached using three methods of valuation used by the appraisal profession: 1) the sales-comparison approach, 2) the income approach, and 3) the cost approach. As an assessor, the Department is not required to use all three approaches of value to arrive at an assessment. The sales-comparison approach estimates the total value of the property directly by comparing it to similar, or comparable properties that have sold in the market.

134. The sales comparison approach is the best indication of value when there is valid sales data. The sales comparison approach quantifies many of the judgments that the appraiser would have had to make, such as obsolescence and environmental contamination. Essentially, the sales comparison approach limits the number of judgments the appraiser has to make because they have been made by the buyer and the seller when they agreed to a sale price.

135. A sale of an integrated steel mill owned by a steel company to another steel company constitutes a market value in use sale. As long as it is an arms length transaction and neither party are under duress, a sale of an integrated steel mill to another integrated steel mill constitutes a market value in use sale.

136. There is no rule of thumb as to the number of sales needed in the sales comparison approach to establish value of a real property. A single sale of real estate may be enough to establish value. “[A] single sale of real estate may or may not be indicative of the market at large.” THE APPRAISAL OF REAL ESTATE, 12<sup>th</sup> Edition p, 60. A single sale can be indicative of the market at large particularly if it is of a highly comparable property or the subject property itself. An appraiser does not need to find a specific number of sales to which he would be able to give equal weight.

137. To conduct a sales comparison approach, an appraiser should follow a systematic procedure. The steps in conducting the sales comparison approach are 1) identifying sales of comparable properties, 2) collecting and analyzing data on the subject and comparable sales, 3) selecting appropriate units of comparison, 4) making reasonable adjustments based upon the differences between the subject property and the comparable sales, and 5) applying the data to the subject property. THE APPRAISAL OF REAL ESTATE 11<sup>th</sup> Ed. p. 402; DLGF Ex. 1, p. 10.

138. In valuing U.S. Steel, the Department utilized the sales comparison approach. Mr. Barrow testified that because two out of three integrated steel mills sold between 1998 and 2002 and sales of other comparable mills in the Midwest existed, he felt that the sale prices would provide the best indication of true tax value.

139. The Department properly established the land value of \$19,000 per acre. “Land value ... was set based on the purchase price of the Inland Steel Mill by Ispat International. An allocation of the land value in the Ispat purchase was made by an appraisal using sales of comparable, large industrial tracts in Indiana and the Midwest.” DLGF Ex. 1, p. 2. Mr. Barrow testified that the land value was taken directly from the 1998 Deloitte and Touche appraisal of the sale of the Inland integrated steel to Ispat International. That the appraisal was relevant to establishing the value-in-use for U.S. Steel because the appraisal conformed to USPAP standards, it was a value-in-use appraisal, and it was completed as part of the sale of an integrated steel mill. There would have been no incentive for the Inland appraisal to allocate more, or less, value to the land versus any other property component. The Inland sale was best indication of value for a large tract of industrial land along Lake Michigan because no recent sales of large, comparable tracts of land had occurred in Lake County. Similar to the Gary Works, large portions of the land involved in the Inland sale have potential environmental contamination that would require remediation in order to make them useable to the market. Additionally, the demand for large tracts of industrial land in north Lake County is low as evidenced by the substantial amount of vacant land and abandoned industrial sites in that area. The sales the Department used are the best reference for land value.

140. The Department considered more than one sale of an integrated steel mill in arriving at a value-in-use. Mr. Barrow identified seven sales of integrated steel mills where both the buyers and sellers were steel companies. The Department reduced the sale prices of the real property totals of each of the comparable sales into economic units of comparison. First, Mr. Barrow divided the total sale price by the purchased mill’s capacity, and then he divided the total sale price by the purchased mill’s annual production. He divided only the real property sales price by the purchased company’s production and capacity.

141. After reducing the sales into economic units of comparison, the Department then compared the data to U.S. Steel. Mr. Barrow correlated the units of comparison to what he felt would be the best indication of value for the Gary Works based upon its production and capacity.

142. Upon comparing the economic units of comparison, the Department placed all its weight on the July 1998 sale of Inland to Ispat because it was a highly comparable sale and the best indication of value. It is common practice for appraisers to identify comparable sales and give more weight to one sale and not another sale. Mr. Barrow properly discounted the other sales because they occurred during the downturn of the steel market and because they involved bankruptcy.

143. In this case, Ispat is a highly comparable sale and the best indication of value. There are several reasons that support this comparability. 1) When this sale occurred in July 1998, the market conditions for steel were similar to the assessment date, March 1, 2002. 2) Ispat Inland is geographically located just west of Gary Works. 3) The sale was an arms-length transaction. 4) Inland was the only sale not out of a

bankruptcy. 5) Inland was operating efficiently, at approximately 90 percent of capacity at the time of the purchase. 6) The sale price was supported by a value-in-use appraisal conducted by Deloitte and Touche. Moreover, both Ispat International and U.S. Steel remained viable steel producers during the downturn of the steel economy and they maintained their customer base.

144. The Department trended its estimate of U.S. Steel's value back to January 1, 1999. To arrive at a value for the 2002 assessment date, the physical and market conditions that existed on the assessment date should be trended to a January 1, 1999, value-in-use. Mr. Barrow researched steel trade publications and looked at the price per ton of steel domestically and globally. He concluded that the price in March 2002 was very similar to the price level in 1998 when Ispat purchased the Inland mill. Mr. Reugelbrugge confirmed that the price of steel was similar in 1998 and in 2002. Tr. Vol. I, p. 242.

145. If the Department were to redo the assessment at this time, it would come to the same value it previously determined.

146. Ultimately, the Board agrees that the Ispat sale is the best comparable for determining the value of Gary Works.

## **VII. CONCLUSIONS**

147. The Board concludes that neither U.S. Steel nor Lake County refuted the Department's assessment of the Gary Works' land at \$59,945,000 (*i.e.*, \$19,000 x 3,155 acres). Expert testimony by U.S. Steel's appraisers largely corroborated this value, while Lake County failed to offer substantial evidence to rebut the Department's evidence.

148. The Board finds that Lake County failed to present a *prima facie* case as to the replacement cost of the buildings and site improvements at Gary Works. As discussed, above, the Oetzel Appraisal was so demonstrably flawed as to be of no probative value.

149. The Board further finds that U.S. Steel failed to show that the Department failed to properly follow and implement its own regulations and guidelines.

150. In the final analysis, the use of the sale of the Inland property was most indicative of the true tax value-in-use of the Gary Works. Because that sale was an arm's length sale that was not in bankruptcy and was of an integrated steel plant that closely resembled Gary Works, the theoretical concepts relied upon by U.S. Steel would have been included in the ultimate "ask" price of the plant.

151. Neither Lake County nor U.S. Steel presented sufficient evidence to convince the Board that the Department's evaluation of the true tax value of Gary Works was erroneous.

152. The Department provided sufficient evidence to support its assessment in light of the evidence presented by Lake County and U. S. Steel.

153. The law and the facts are with the Department and against Lake County and U. S. Steel.

IT IS THEREFORE ORDERED, that the Department's assessment of \$113,664,100 is affirmed.

March 29, 2005

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Terry G. Duga, Commissioner  
Indiana Board of Tax Review

### IMPORTANT NOTICE

- APPEAL RIGHTS -

You may petition for judicial review of this final determination pursuant to the provisions of Indiana Code § 6-1.1-15-5. The action shall be taken to the Indiana Tax Court under Indiana Code § 4-21.5-5. To initiate a proceeding for judicial review you must take the action required within forty-five (45) days of the date of this notice.