

Notice of New Zoning Laws

On December 20, 2019, the Commerce Department sent notice to appraisers and appraisal management companies about new zoning laws in the City of Minneapolis. On January 1, 2020, these new zoning laws went into effect. In an effort to understand how the new zoning laws are being implemented, Commerce staff requested appraisals completed in Minneapolis after January 1, 2020. The Department received and reviewed 135 appraisal reports for Minneapolis properties. This letter summarizes the Department's findings.

Of these 135 appraisals,

1. 117 of them provided the correct Specific Zoning Classification (e.g. R1A, R2B);
2. 15 provided the correct Zoning Description, which was "Multiple-family District." The other 120 reports contained a mix of Zoning Descriptions, including: Single Family District (low density) (R1 & R1A) and Two-family District (low density) (R2 & R2B). After January 1, 2020, the R1, R1A, R2 and R2B classifications changed to the Zoning Description of "Multiple-family District."
3. Three files had a Highest and Best Use analysis that conformed to USPAP Rules 1-3 and 2-2(xii), as described below. The other 132 reports seemed to stop their analysis at single family residential, which is what their current use was, but did not account for the multiple family uses allowed by the new Minneapolis zoning law. If analysis was completed, it was not reported and USPAP requires appraisers to summarize and report their analysis.
4. Zero work files associated with these reports included data that would support either the appraisers' analysis or conclusion. The USPAP Record Keeping rule states that, among other things, a work file must contain "all other data, information, and documentation necessary to support the appraiser's opinions and conclusions and to show compliance with USPAP,

or references to the location(s) of such other data, information, and documentation.”

As described above, the vast majority of appraisal reports reviewed by the Department as part of this analysis did not take into account the new Minneapolis zoning laws. In addition, work files did not fully document the analysis of the appraisal performed.

Commerce shares this information to make appraisers and appraisal management companies aware of the results of the agency’s review. The Department will collaborate with the Real Estate Appraiser Advisory Board, trade organizations, and continuing education providers to ensure a common understanding of how available tools can be used to raise the overall awareness of the appraisal treatment of residential property in Minneapolis.

Highest and Best Use

The definition of highest and best use, as defined by, *The Appraisal of Real Estate*, 14th Edition, is as follows:

“The reasonably probable and legal use of vacant land or an improved property that is physically possible, appropriately supported, financially feasible, and that results in the highest value. The four criteria the highest and best use must meet are legal permissibility, physical possibility, financial feasibility, and maximum productivity. Alternatively, the probable use of land or improved property – specific with respect to the user and timing of the use – that is adequately supported and results in the highest present value.”

Under USPAP Standards Rule 1-3,

“When necessary for credible assignment results in developing a market value opinion, an appraiser must:

- Identify and analyze the effect on use and value of: (i) existing land use regulations; (ii) reasonably probable modifications of such land use regulations; (iii) economic supply and demand; (iv) the physical adaptability of the real estate; and (v) market area trends; and
- develop an opinion of highest and best use of the real estate.”

In addition, under USPAP Standards Rule 2-2(xii), when an opinion of highest and best use is developed by the appraiser, the appraiser must state that opinion and summarize the support and rationale for that opinion.

The comments to USPAP Standards Rule 1-3(b) notes that an appraiser “must analyze the relevant legal, physical, and economic factors to the extent necessary to support the appraiser’s highest and best use conclusion(s).” For example, when running through these factors, local zoning restricts potential uses (e.g. single family residential being the only use permitted), so the highest and best use analysis would be restricted to what is legally permissible as of the effective date of the appraisal.

However, there may be instances when multiple uses are legally permissible. In those instances, an appraiser must consider the site’s physical possibilities, financial feasibility of the permissible uses, and which use will result in the highest monetary return. It further provides that when a site contains improvements, the highest and best use may be different from the existing use. Implied in the definition of highest and best use is that the determination of highest and best use takes into account the contribution of a specific use to the community and community development goals, as well as the benefits of that use to individual property owners. Regardless of the result of the highest and best analysis, whether its the same as its current use or differs from its current use, an appraiser must summarize the analysis that led to their conclusion.

In all appraisal reports, an appraiser should report the correct zoning designation, zoning description, and include in their analysis of all uses that are legally permissible. Of the uses that are legally permissible, an appraiser must identify which of those uses is the highest and best use and their rationale for selecting that particular highest and best use pursuant to USPAP Standards Rule 1-3. In addition, the work file must contain support for the appraiser’s conclusion as required by USPAP Standards Rule 2-2(xii).

If an appraiser would like more information on where to obtain additional education on this topic, education providers can be found [here](#) or by contacting the Minnesota Department of Commerce.