

What's the Use?—Most Probable Use Versus Highest and Best Use

Steven Thair

In this article, the evolution of the term "highest and best use" to its present wide variety of confusing meanings is examined. The term "most probable use" is also discussed, including an explanation of its superiority over highest and best use stemming from its unambiguous nature and relation to the actual marketplace. The concepts of most fitting use and most probable selling price are discussed as well.

"Most probable use" as a term and as a concept is replacing "highest and best use" for several reasons. Some relate to the name itself and others to changes in the concept, which has outgrown its original label. This article explains these changes and what they mean for lenders, clients, and serious students of appraisal.

BACKGROUND

The beginnings of the term highest and best use can be traced to economics—the study of defining value and what creates value.

It is only in this century that the field of property appraisal has experienced rapid development because lenders, governments, and the public have demanded some method to insure that loans made against property are secure. In its earliest days, appraisal was concerned primarily with the cost approach. Highest and best use was a term that related to land as though vacant. Improvements were handled by estimating reproduction cost less deterioration.

The role of the courts in establishing highest and best use as fundamental to their determination of property value should not be overlooked. This has contributed to the

concept's widespread use of appraisal. Appraisers have been less anxious than other professionals to lay down the definitions of their practice in a formal and legally responsible way. For instance, both the American Institute of Real Estate Appraisers (AIREA) and the Appraisal Institute of Canada (AIC) print disclaimers in their basic textbooks absolving them of responsibility for theories or practices advanced therein.¹

In its earliest days, appraisal was concerned primarily with the cost approach.

In contrast, other professions publish official positions on matters relating to appraisal, such as the Financial Accounting Standards Board's paper on income property. James A. Graaskamp has explained why the appraisal profession is falling behind in this regard.² He points out that the development of appraisal practices and the use of the term highest and best use have basically been carried out by nonappraisers, which partially explains the impediment to growth and change in appraisal theory.

The concept of highest and best use is nonetheless well established in the report writing of many Canadian appraisers. What follows is a realistic examination of the names, definitions, and concepts of highest and best use and most probable use.

LABELS

Names or labels and our reactions to them profoundly influence our thinking and actions. The label highest and best use suggests a superlative degree of use. In fact, highest and best use is neither high nor best. Early use of this term in less sophisticated analyses gave rise to an inaccurate name for what is actually a



A.R.E.A. SERVICES, INC.

ACQUISITION/RELOCATION/
ENGINEERING/APPRaisal

15 Years Experience in Turnkey Right-Of-Way

Acquisition Projects Inclusive of:

- R/W Engineering ■ Acquisitions ■ Damage Claims
- Appraising ■ Review Appraising ■ Relocation Assistance
- Property Management ■ Environmental Impact Studies
- Project Cost Estimates ■ Feasibility Studies

Serving:

- Federal, State, County & Municipal Governments
- Gas & Electric Utilities
- Pipe Line Companies
- Communication Companies
- Airports

INQUIRIES ARE WELCOMED

Home Office

A.R.E.A. Services, Inc.
4810 North Black Canyon Hwy.
Suite 401
Phoenix, Arizona 85017
(602) 242-8952

In Affiliation With:

D.E. McGillem & Assoc., Inc.
77 South Girls School Road
Indianapolis, Indiana 46231
(317) 241-8336

complex situation. This situation involves nothing less than the interaction of all factors that affect how individuals and groups decide to utilize a parcel of land either vacant or developed.

In contrast, the meaning of the term most probable use is more precise. The word probable clearly indicates that a particular use is not a certainty—experience confirms that plans for property are often uncertain. Most probable use, then, means just what it says—that a particular use is most probable among alternatives. Probable does not mean that a shoddy or incomplete study has been done, but that a situation is not fully predictable and that there are other possible uses.

In contrast, highest and best use suggests finality; that there is nothing else. In the courts this nuance of meaning is acceptable, even desirable. In the real estate field, use is a continuous and dynamic process. The concept of most probable use better and more realistically suits this process. Therefore, it is the more appropriate term because it allows both appraiser and client, or instructor and student, to get off on the right foot.³

DEFINITIONS

Three current definitions of highest and best use follow:

That reasonable and probable use that will support the highest present value, as defined, as of the effective date of the appraisal.

Alternatively, that use, from among reasonably probable legal alternative uses, found to be physically possible, appropriately supported, financially feasible, and which results in highest land value.⁴

A third definition is found in Lincoln W. North's monograph

published by the AIC and now part of its introductory appraisal text.

The only explicit definition which the author considers self-standing without elaboration is the one which states that highest and best use represents the most probable use of a given property at a particular moment in time.⁵

These definitions of highest and best use necessarily incorporate the words probable or probable use. The definition of most probable use, however, is not contingent on highest and best use. Therefore, most probable use is more parsimonious; it covers the same or more phenomena with a simpler definition.

In response to a changing world, the term highest and best use has

The word probable clearly indicates that a particular use is not a certainty—experience confirms that plans for property are often uncertain.

been continually redefined from that use which is most profitable or results in the highest present value to other various definitions. The original definition barely relates to the present one. Frequently, readers of reports, appraisal students, and sometimes even appraisers do not understand what is meant by highest and best use. Many report readers believe that most profitable use is a good definition of highest and best use. Nothing could be further from the truth.

The adjectives "highest" and "best" suggest only one use. In fact, in what is probably an effort to simplify a complex situation, the AIC's introductory text states:

Fundamental to any appraisal is the selection by the appraiser of that single use that develops the highest value in the subject property.

Highest and Best Use is defined as "that use which, at the

time of the appraisal, is most likely to produce the greatest net return in money or amenities over a given period of time."⁶

While the intent of this statement may reinforce the principle of consistent use, which states that building and land must be valued according to the same use, it suggests that there is no possibility that one of two or three different uses are equally likely to be selected, even though they do not yield an equivalent net return. Nor does it suggest that one use is more probable than others, while other uses are clearly possible. Nonetheless, users of the term highest and best use continue to expand the concept to the point where most probable use is employed as a

definition of highest and best use.⁷ If anything, the reverse is true: highest and best use is a specific and highly theoretical kind of most probable use.

In the frequently quoted Real Estate Appraisal Terminology, most probable use is defined, but under the heading highest and best use.

In the context of most probable selling price (market value) another appropriate term to reflect highest and best use would be most probable use.⁸

It is time that most probable use has its own definition. Efforts to categorize everything under the umbrella of highest and best use are producing confusion among students, lenders, and others. The term has finally worked itself out of a job—it suffers from functional obsolescence.

Continued on Page 30