

## **ANGRY OVER THE ACCUSTIONS OF APPRAISAL RACIAL BIAS? LET'S TALK!**

How should you, an appraiser, respond to accusations of widespread racial bias? To the typical appraiser these sorts of accusations make little sense. After all, appraisers have been fired, laughed at, threatened, and lost friends when their values were perceived as too low or sometimes too high. They endured all of this ridicule because they view the appraisal profession as sacrosanct, meaning they consider their work to be essential to shield those who own real estate from jeopardy. I personally feel outrage, maybe you do too. But let's get back to my original question, "How should appraiser's respond?"

The lawsuit brought by Connolly and Mott (homeowners) against Lanham (appraiser) is a strong catalyst to widespread accusations of appraiser bias. Two appraisals were performed on their house, during the first the appraiser would have been aware that the owner/borrowers were black. The house was "whitewashed", and a second appraisal was made. The second appraisal came in MUCH higher than the first. I have not seen the two appraisals, nor do I know of anyone who has performed a forensic review of them. I do know that correlation does not prove causation. What are the odds that the second appraiser valued the property much higher than the first appraiser based on appraisal error only (no bias)? As wild as it sounds these types of errors can and do happen. However, the odds of these sorts of errors occurring at this magnitude where the first appraisal was the low one and the second appraisal was the high one have a very

low probability of happening. Consider that if the probability is one quarter of one percent (0.0025) of this scenario occurring where there were 14 million loans applied for in a year. Then this disparity in appraisal values where the first was far below the intrinsic value and the second was far above the intrinsic value (creating a monstrous gap), could have happened 35,000 times in one year. I am not blindly defending these specific appraisers. I have only demonstrated how this could happen without racial bias being involved. However, if this could happen thousands of times in a year, I would not blindly accuse the appraisers of racial bias either. This scenario is not factual (based reasonable parameters only) and may not be realistic. It is simply presented to add context to the complicated subject of probability. Did I mention that Conolly and Mott are not the only whitewashing incidents on record?

A second issue is that Freddie Mac formed a conclusion that appraisal values missed the contract price a higher percentage of times for minority borrowers than for white borrowers. After that, several entities claimed to see pattern of appraisal bias when analyzing lending data. Not surprisingly many of these organizations have a history of promoting the cause of minority groups. There is more circumstantial evidence of appraisal racial bias circulating out there. All-in-all the result is that most articles on the matter are written in a tone that implies racial bias is running rampant in the appraisal profession. This sort of sensationalism is what sells newspapers and magazines. I have been asking the question, how should appraisers respond to this? The first thing I would say is without emotion and by focusing on the facts.

## A FEW FACTS:

1. Bigotry still exists in the USA- believe it. Black people have been lynched within my lifetime.
2. The rate per capita of minority home ownership is a smidgeon compared to the rate of white home ownership.
3. On average, whites earn more and have more than minorities.
4. As with all professions some appraisers could be bigots occasionally carrying out explicit bias and intentional discrimination. Even so, it would not be on a “widespread” basis.
5. A year ago, most appraisers did not fully understand the meaning of implicit or unconscious bias.
6. There is a low percentage of minorities in the appraisal profession.

Is there anything positive to say about appraisers in context of these accusations? Consider the following: As of the date of this writing I was unable to find where an appraiser has been convicted or admitted to violating fair housing laws when acting as an appraiser. In addition, no one seems to be able to get access to the appraisals related to any of the “Whitewashing” cases for forensic review. Without this forensic analysis all the negative conclusions implied by this case are speculation. In addition, the American Enterprise Institute (AEI) has performed at least one study on the matter. The following is taken from the paper, “Confirming alternative explanations for appraisal under-valuations: New evidence from appraisal-level data” by Tobia Peters and Edward Pinto:

*We find that seemingly large differences in the share of under-valuations-- appraisals where the appraised value is below the contract price-- received by people of color are almost entirely or entirely due to differences in geographies where people, regardless of race or ethnicity, reside. When comparing appraisals for people of color to those for non-Hispanic white people within the same census tract, we find that there are no or minimal differences.*

As far as the general comparison of economic and financial status of whites versus minorities, it simply is not possible for appraisers to have caused it. Yet, instead of statements like, “As we continue to investigate the accusations of racial bias in appraisals...” the public reads this, “We are working hard to eradicate racial bias in the appraisal profession”. This is really important as the second statement implies that racial bias by appraisers is now “conventional wisdom”, i.e. a fact. What we now have is a study of true lies and false truths. John Kenneth Galbraith an economist and social behaviorist stated, “Conventional wisdom must be simple, convenient, comfortable, and comforting- though not necessarily true”. (Freakonomics, Chapter 3, Levitt and Dubner)

What about statistical data that the appraiser often relies on when performing the appraisal?

In 1977, one year after I became an appraiser, the United States (U.S.) brought an action against many of the appraisal organizations that existed at that time. The complaint alleged that the defendants violated the Fair Housing Act (42 U.S.C. §3601 et seq.). A lot of the concern was the common practice of appraisers reporting statistics which often shed a bad light on minority neighborhoods. In response to this lawsuit the defendants began to modify various teaching material and standards to restrict the reporting of certain information. However, a group of 72 individuals spearheaded by F. Gregory Opelka intervened (with what I would call a quasi-legal action) to prevent the defendants from modifying appraisal practices. The concern of this group was the crippling effect these changes would have on the appraiser's ability to perform analyses in an objective manner if they could not identify, analyze, and report certain demographic information. It appears that this intervention was in a losing position and would not be able to stop the appraisal organizations from modifying appraisal practices much longer. At this point an important case was concluded by the Supreme Court of the United States. The case was **Linmark Associates, Inc. v Willingboro, 431 U.S. 85 (1977)**. This was a landmark case concerning housing laws and race. In fact, this case led to the Government's (DOJ) motion to dismiss the original case against the appraisal organizations in 1978 (with prejudice). This case has been cited approximately 370 times. I am not going to try to summarize the case, but I will make a simple statement: *This case considered the impact of the*

*dangers of suppressing information to the public versus the dangers of misuse of information regarding the promotion of stable integrated housing. Society is always walking this invisible tightrope where housing and minorities are concerned, requiring that each step be carefully considered. Certainly, the appraiser is torn by their duty to inform versus their duty not to interfere with fair housing practices. Quite a tight rope! (Note: I am not an attorney. I have tried to only present the facts of these cases which should not be considered legal advice.)*

We are getting closer to answering the question, “How should you, an appraiser, respond to accusations of widespread racial bias?” There are a couple of things we should address first. Consider that when a ship builder is accused of building ships that leak the first response would be, “No I don’t- I have been building structurally sound ships for 30 years”. However, as soon as he is alone, he will search his ships for leaks. Appraisers should do the same especially where unconscious racial bias is concerned.

The following hypothetical story should be considered:

*Appraiser Jill, a white person, has an assignment that is more complex than initially believed. It has an auxiliary unit, large site, and a suspicious crack in the foundation. Jill has maintained her license and taken the mandatory (but minimum) continuing education classes. She is on an AMC's rotation list and doesn't want to turn down the assignment based on "Incompetency" fearing being removed from the list. Over the years Jill has stayed out of trouble by being just a little slyer than her competitors. She has figured out if the value meets the contract price and the borrowers are financially strong her incompetent appraisal skills are not noticed. Alternatively, if the borrowers are not financially strong, she keeps the value as low as possible. During the inspection Jill realizes that borrower May is an older black woman. Jill has watched a lot of old television shows where back in the 1960's and 1970's most black women were portrayed as maids, and they had to support their husbands who were apparently lazy. Because May is black Jill believes there is a high chance this loan might be foreclosed upon. To protect herself she decides to keep the value as low as possible. During the inspection she noticed the borrower, being older, needed some help around the house. Jill stayed an extra hour helping her and was delighted to spend time with May. The low appraisal value resulted in May being turned down for the refinance loan. May needed the money to help her granddaughter complete her law degree. May went to her loan officer for help. The loan officer called Jill who assured him the value was "Spot-on" and she felt the loan officer was pressuring her for a higher value. The loan officer took Jill's word as he didn't want to be guilty of pressuring her for a higher value. Anyway, he was ready to move on to the next project.*

## What issues can we identify?

1. Jill is an incompetent appraiser.
2. Jill is not ethical.
3. Jill does not dislike black people.
4. This act of unconscious racial bias has huge implications in terms of May's family's ability to build generational wealth.
5. May did not receive the reconsideration of value she deserved.
6. Something is very wrong with the lending process, as the appraisal management company and lender who are responsible for overseeing the appraisal remained in the dark.

In this example, Jill is both unethical and incompetent. Appraiser incompetence is an unintended consequence of Dodd-Frank law where appraisers are selected from a list on a rotation basis, not on merit. Over the past 14 years many appraisers have found that having an appraisal license and being on the right lists is all that is necessary to earn a living.

*I profess that neither the comparison analysis nor using comparables from the subject neighborhood is the problem. The real problem is that the incompetent appraiser would apply adjustment rates extracted from other markets they are more familiar with, instead of studying the subject market and applying the adjustment rates that are appropriate for that particular minority market. These inappropriate adjustment rates would likely cause the value opinion to be incorrect. The problem is not bad appraisal principles, but rather bad appraisers who do not conform to those principles.*



## Finally, how should appraisers respond?

1. We should support the goals and objectives of the Property Appraisal and Valuation Equity (PAVE) plan. However, it should be titled “the Mortgage Industry and Housing Equality Plan (MIHE)”. After all, if minorities are not receiving a fair shake in lending, then the problem is with the entire lending community and its regulators, not just appraisers.
2. Ask any appraisal organization to which you pay dues to initiate and participate in a joint taskforce. This taskforce would:
  - a. Quantify the big picture.
  - b. Separate fact from fiction.
  - c. Develop a plan of action.
  - d. Initiate and carry through with the plan.
  - e. Appraisers should convey their side of the story to the public.
3. We should applaud those who demanded more minorities be brought into the appraisal profession and associated organizations. As we all know, sometimes it is hard to see the forest for the trees.
4. We should express that a root cause of racial wealth inequity lies in the unfair distribution of educational resources available to minority children. Recall the findings of the study performed by the American Enterprise Institute: “We find that seemingly large differences in the share of under-valuations--appraisals where the appraised value is below the contract price-- received by people of color are almost entirely or entirely due to differences in geographies where people, regardless of race or ethnicity, reside.”

5. We must search our ship for leaks. Every appraiser must be aware of how unconscious bias could occur and be sure it doesn't. Take a seminar on Fair Housing Laws, this was the point of presenting the Jill and May story.
6. Do away with the automatic rotation of appraisal assignments, allowing lenders to engage competent appraisers they know and trust. This will take congressional action.
7. Prevent the secondary market from using third party inspectors. This must be done by appraisers and trainees. The appraisers need to send in their people, as they cannot control any potential racial bias by third party inspectors.
8. There must be a sovereign and quick reconsideration of the valuation process put in place. The Tidewater plan is too slow and does not communicate enough information to the borrowers.
9. Most importantly we should never have a negative thought or feeling about a group or individual that is diligently working to improve the position of minorities. In the worst-case scenario (which we may well be in), I have nothing but admiration and compassion for these dedicated individuals who are doing a hell of a lot more than most of us to correct the injustices of society. They should consider that when they intentionally or unintentionally infer that a group of innocent people are racially bias, then they have become the people they have been trying to fight.

Conclusion:

Most appraisers are very professional and skilled. Very few would consciously conspire to lowball the appraisal value of a minority borrower or owner. As the competent appraisers address the problem of the incompetent appraisers, it should be noted that all Partners in the lending process are susceptible to unconscious bias and must be aware of how it might present itself anywhere in the lending process.

With Highest Regards,



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