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Title of proposal: Reassessing Value: Towards A Racially Equitable Appraisal Industry

Researchers have repeatedly shown that homes in Black, Latinx, and Indigenous communities are appraised at lower values than their counterparts in White neighborhoods (Anacker 2010; Hipp and Singh 2014; Moye 2014; Howell and Korver-Glenn 2018; Perry, Rothwell and Harshbarger 2018; Howell and Korver-Glenn 2020). In fact, even when neighborhood real estate demand, crime rates, school quality, local amenities, and socioeconomic status are held constant, homes in White neighborhoods are appraised at three times the value of comparably sized and constructed homes in communities of color (Howell and Korver-Glenn 2018). Even more striking, this inequality is increasing. Between 1980 and 2015, homes in White neighborhoods saw unprecedented appreciation rates, increasing on average $200,000 more than comparable communities of color (Howell and Korver-Glenn 2020). As a result, racial wealth gaps have continued to expand, creating cascading inequities in education, health, and housing stability.

In what follows, we begin by providing the historical context that has shaped contemporary inequality in the appraisal process. We then discuss how current appraisal and lending policies, practices, and processes contribute to the observed inequality and what steps federal agencies and the Federal Reserve System can take to create a more equitable and just housing market. Given the importance of housing in the economy as well as families' economic and physical wellbeing, taking these steps towards a more just and equitable appraisal industry are critical in the broader struggle for racial and economic justice.

## The Federal Government's Role in Creating the Racialized Appraisal Industry

Contemporary racial inequality in appraisal values has been created by both historical and contemporary governmental actions. To understand these actions, it is helpful to understand the roots of racialized property evaluation. Racialized property evaluation is when property is valued based on how useful it is to White populations and their ways of life. In the United States, the practice of racialized property evaluation traces back to the nation's origins.

Starting in the early 1600s, European settler colonists in North America used racialized property evaluation to justify the displacement of Indigenous nations and the enslavement of African peoples (Banner 2005). White Europeans' religious and scientific beliefs asserted that they should rule over all creation, including "subhuman" Black and Indigenous peoples (Smedley and Smedley 2011). As a result, they assessed the value of "property," both land and enslaved humans, based on its usefulness to White settlers' resource extraction and wealth accumulation. Land inhabited by Indigenous peoples was deemed virtually worthless because White settlers did not have dominion over it. This provided legal justification for treaties and land exchanges that displaced Indigenous nations with limited or no compensation. However, as soon as colonial powers displaced Indigenous communities and allotted the land to White settlers, the property appreciated in value because it was now inhabited by and thus useful to Europeans (Marchiel 2020). Likewise, enslaved Africans were literally appraised and exchanged based on their usefulness to White Europeans' businesses. Evaluating property based on its usefulness to White people allowed settler colonists to acquire resources at limited cost while extracting vast economic wealth and political domination from these resources.

Through the powerful resistance and uprisings of enslaved and freed Black and Indigenous activists, Whites' acceptance of enslavement, genocide, and displacement began to wane. However, racialized property evaluation persisted. In rural areas, sharecropping enabled the exploitation of Black people and labor to continue. In urban areas, local zoning ordinances were enacted to segregate and formally devalue communities of color (Rice 1968). Once again, spaces that White residents inhabited were deemed more valuable simply because of White residents were using them. These localized zoning processes were further institutionalized with President Franklin D. Roosevelt's National Housing Act.

Elected during the nation's largest economic depression and its subsequent housing crisis, President Roosevelt's administration sought to address the widespread economic and housing catastrophes by transforming property financing (Jackson 1985; Stuart 2003; Rothstein 2017). At the time, property was either purchased in cash or with 2-5 year non-amortizing mortgages that required large down payments, typically 50 percent of the property value (Marchiel 2020). President Roosevelt contended that 15-year fixed-rate mortgages with small down payments would allow working- and middle-class Americans to purchase homes *and* accumulate wealth as their properties appreciated. To incentivize banks to provide these longer, fixed rate loans, the National Housing Act promised to insure mortgages through the newly created Federal Housing Administration (FHA). Additionally, the federal government created a secondary market for residential mortgages, Fannie Mae, increasing banks' lending capacity (Marchiel 2020). Combined, these changes provided millions of families with capital to purchase homes. Yet, these same changes also institutionalized a national system of racialized property evaluation.

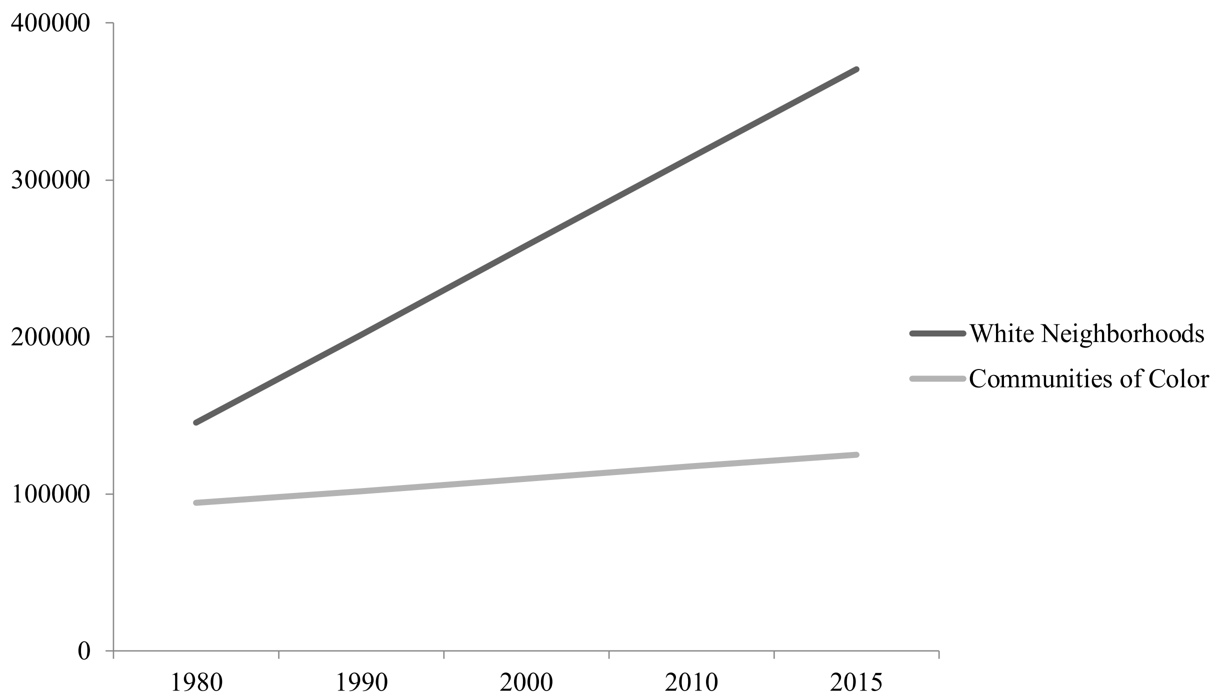
On the pretext that economic stability required federally insured mortgages to reflect the "true" value of property, the federal government partnered with the newly emerging appraisal industry to create a uniform appraising system. Central to this new system was the idea that properties should be evaluated based on their usefulness to the White population. This idea was formalized through two mechanisms: the appraising Underwriting Manual of 1936 and the Home Owners' Loan Corporation neighborhood rankings. Both of these mechanisms centralized neighborhood racial and class composition as the ***key*** factor driving value. White and middle- and upper-class neighborhoods were deemed most valuable where as Black, Indigenous, and Latinx communities were classified as "undesirable" and "unstable." Additionally, the Underwriting Manual recommended a new way of determining value. Instead of using the most common approach at the time, which evaluated properties based on the amount it would take to rebuild them in their current condition, the Underwriting Manual elevated the sales comparison approach. This approach relies on past sales within the neighborhood to determine the value of property. Consequently, the racialized evaluation of the neighborhood became a larger factor in determining home values than the quality of the structure itself.

Noting the devasting implications that these policies had on Black, Indigenous, and Latinx communities, activists and Civil Rights organizations began documenting and litigating the racially discriminatory practices within the housing market industry (Taylor 2019; Marchiel 2020). Their diligent efforts led to a series of legislative acts and lawsuits from 1968 to 1977 that outlawed the explicit use of racial demographics as a justification for value and provided new avenues for borrowers and communities of color to receive credit. However, these legal changes did not include any alterations to the appraising approach. Thus, appraisers continued to use past racialized property evaluations as justifications for current sales alongside their subjective evaluations of neighborhood demographics and appeal. Consequently, racialized property evaluations persisted as communities of color were offered predatory mortgages to gain ownership of devalued and dilapidated housing (Taylor 2019). This predatory inclusion combined with the ongoing racialized appraisal system fostered growing devaluation and disrepair in communities of color.

## Contemporary Racialized Appraisal and Lending Practices

After the Fair Housing legislation increased Black, Indigenous, and Latinx individuals' access to housing, home values in White communities began to skyrocket. Property in White neighborhoods accelerated seven times faster than comparably sized, aged, and quality property in communities of color with the same socioeconomic status, amenities, and homeownership rates (see Figure 1). In other words, even when we set aside the historical racialized processes that created the socioeconomic and geographic inequalities, the mere presence of White people still elevates appraisers' perceptions of a property's value.

**Figure 1.** Appraisal Values in 2015 Dollars for Comparable Homes in Comparable Neighborhoods in an Average Metropolitan Area, 1980 and 2015.

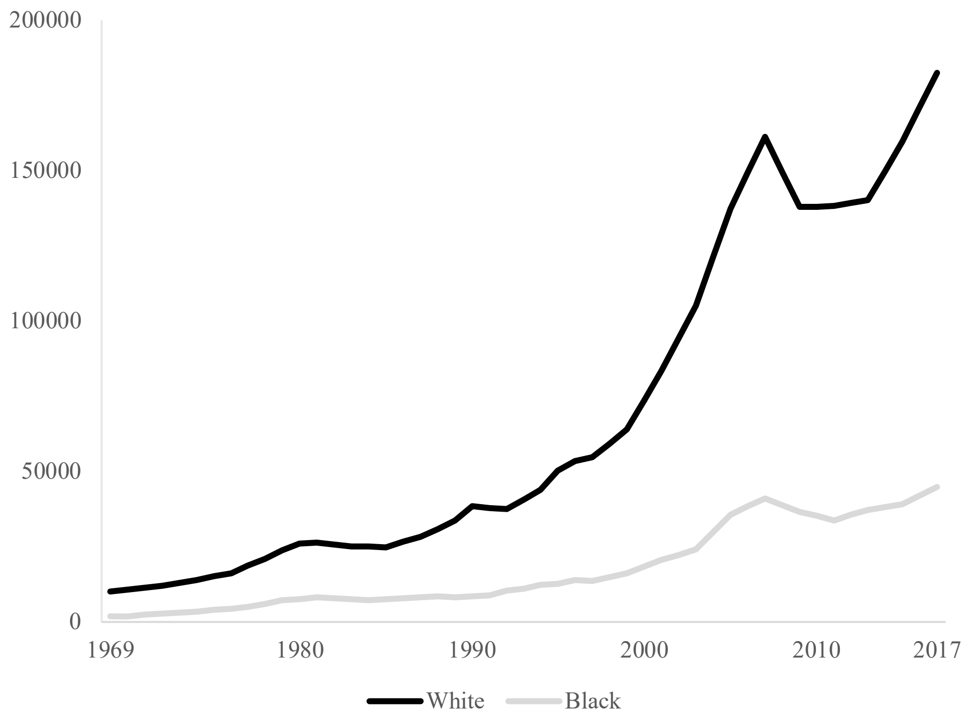



Source—Howell and Korver-Glenn 2020: Figure 2, page 15. Communities of color defined as Black and/or Latinx

The acceleration of home values in White neighborhoods has had a cascading effect on racial inequality in housing quality, household wealth, educational attainment, and physical wellbeing. Most directly, it has affected housing wealth accumulation. Housing wealth is the amount of capital a homeowner would have if they sold their property. Put another way, housing wealth is the value of a house minus any principle still owed on the property. For those who own homes, appreciating home values means they generate more wealth. This increased wealth can be used to buy a larger or more expensive home or as collateral for other investments. For everyone else, when home values appreciate faster than wages and other customer goods, the entry point to homeownership becomes more unattainable. When the appreciation of home values is racialized, this process increases racial wealth gaps and places economic constraints on Black, Indigenous, and Latinx families trying to secure housing.

As visualized in Figure 2, the accelerating home values in White neighborhoods lead to White families' average housing wealth increasing $170,000 in real dollars. Black families, on the other hand, have only seen their average home wealth increase by $40,000 in real dollars. This has resulted in the racial home wealth gap increasing 17-fold since 1969.

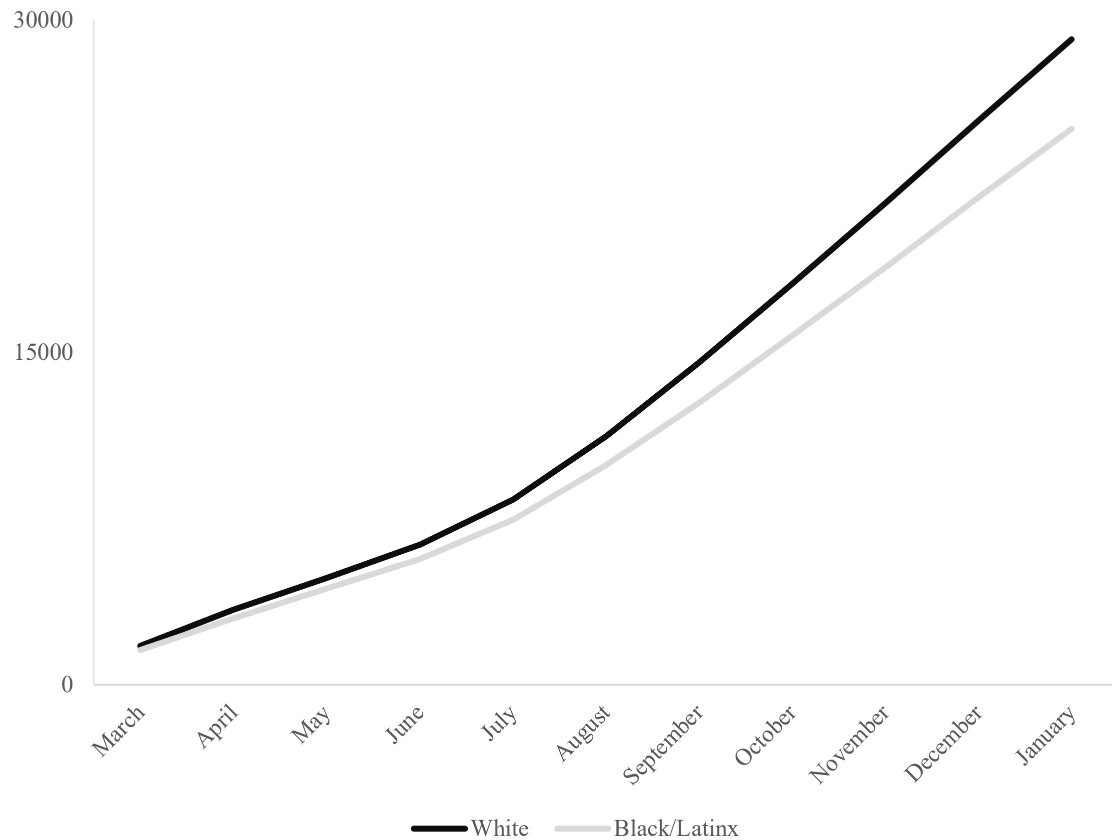
**Figure 2.** Housing Wealth (Housing Value Minus Mortgaged Principle) by Family Race




Source—Panel Student of Income Dynamics Core Family Sample

The growing inequality has accelerated in the last decade and even more dramatically since the beginning of the coronavirus pandemic. Since March 2020, home prices in the majority of the United States have seen unprecedented monthly appreciation rates. These quickly accelerated prices are growing faster in Whiter zip codes than Black and Latinx zip codes (see Figure 3). The increasing bifurcation as well as the overall increases in home prices are further concentrating the wealth into the hands of those who owned property before the pandemic. As a result, the economic policies in the last year are further exacerbating the nation's growing socioeconomic and racial inequalities.

**Figure 3.** Increase Since February 2020 in Home Prices by Zip Code Race




Source—Zillow Home Price Sales for all zip codes in metropolitan areas with over 400,000 in population

The persistent use of racialized property evaluation that has led to the growing inequality in racial home wealth is due to three interlocking mechanisms: appraisers' individual racialized evaluations, racialized assumptions built into appraising practices, and federally created economic incentives that perpetuate inequality.

*Appraisers' Racialized Evaluations*. Like any governmentally regulated industry, appraisers have general guidelines regarding how they should determine property value. Since the release of the 1936 Underwriting Manual, these standards have included using the sales comparison approach to assess the value of a property based on recently sold comparable properties within the neighborhood. Yet, within these general guidelines, appraisers have a large amount of discretionary power to define neighborhood boundaries and characteristics. They also can choose how they measure and evaluate the property's characteristics, condition, and construction and how closely these characteristics match the recent sales they select for their comparison properties.

Across the board, this discretion creates wide variation in appraisers' assessments. Studies examining how different appraisers evaluate the very same house show that nearly all property and neighborhood characteristics very from one appraiser to the next. This is even true for seemingly objective characteristics like square footage, land acreage, and number of rooms. In a recent quantitative analysis, Clear Capital found estimates of square footage vary across appraisers on average 8 percent for the same property (Allen 2021). Inconsistencies in square footage alone alter appraised values by tens of thousands of dollars.

Ethnographic observations, interviews, and quantitative analyses demonstrate that appraisers' discretion results in many appraisers pulling on racialized assumptions to define the worth of properties. That is, even though appraisers do not formally report racial demographics, these demographics still play a central role in how appraisers define neighborhood boundaries, evaluate neighborhood characteristics, perceive neighborhood trends, select comparable sales, measure property characteristics, assess property "appeal" and "marketability," and create adjusted sale values (Howell and Korver-Glenn 2018; Korver-Glenn 2021). As a result, in the aggregate, individual appraisers' decisions and biases create racialized property evaluations that continue to evaluate White homes in White neighborhoods as more valuable.

*Racialized Assumptions within Appraising Practices*. As discussed above, the sales comparison approach is the primary appraisal method for federally insured mortgages. By using 3-5 nearby recently sold comparable homes, this method centralizes the importance of location to appraisers' value and relies on historical patterns to justify contemporary prices. Using historical sales without adjusting for their racialized determinations has resulted in contemporary appraisals that are also racialized. Additionally, the majority of appraisers continue to view "appropriate" comparable sales as those in racially similar neighborhoods, even when these communities have distinct socioeconomic statuses, physical locations, amenities, or real estate demand (Howell and Korver-Glenn 2018). Thus, as neighborhoods undergo demographic changes, appraisers pull comparable sales from neighborhoods that reflect the changing racial demographics, ensuring that the racial hierarchy in home values persists (Howell and Korver-Glenn 2020). For appraisers who are trying to subvert these racialized patterns, they are constrained by the fact that they are still required to use comparable sales that are based on the assumption that White communities are more desirable and valuable.

*Federally Created Economic Incentives*. Before the National Housing Act of 1934, the appraisal industry's primary method of evaluating homes—the cost approach—appraised homes based on the "supply and demand" of housing itself. That is, appraisers' assessments of a structure's value fluctuated with the cost getting the material and labor to reconstruct homes in their exact condition. In this way, housing was primarily conceptualized as akin to other utilities like water or electricity, which are critical for flourishing within society. Yet, President Roosevelt's emphasis on housing being a generator of wealth creation required homes to be appraised based on their potential to accumulate wealth. This, of course, motivated the emphasis on racialized property evaluations discussed above, which relied on the speculative assumption that White space was at the time more valuable and would continue to be so in the future.

Instead of addressing these foundational assumptions within the appraisal industry, the legislative changes of the late 1960s and 1970s further entrenched the idea that the value of a home should be tied to speculative financing and investing, not its public utility. In 1968, the same year the first Fair Housing legislation past, congressed privatized Fannie Mae and authorized them to purchase conventional or non-FHA mortgages. Subsequently, Freddie Mac was created to increase competition within the secondary mortgage market. These changes alongside changes to saving and loan associations increased the capital available for mortgages while delocalizing the distribution of these mortgages. Numerous scholars have documented how these changes further racial inequality by increasing the availability of low-rate mortgages to White homeowners in White communities while creating a predatory market for communities of color (Baradaran 2015; Baradaran 2017; Taylor 2019; Marchiel 2020). Yet, what has not been discussed thoroughly is how these changes alongside the appraisal industry and the Federal Reserve's actions have contributed to increasing racial inequality in home values.

Given that appraised values are set based on previous sales in the neighborhood, values do not correlate with the "demand" for housing or the number of people needing housing. Instead, they fluctuate with sales. Since most U.S. homes are bought with credit, the "demand" captured by appraised values is driven by the availability of credit, not the number of people desiring to live in an area. Thus, it is not surprising that the macroeconomic policies that increase the availability of credit drive up home prices. For White families who had the privilege of owning homes before the financing changes, these changes have increased their wealth and enabled them to purchase larger and more elaborate homes. Yet, for everyone else who has experienced racial and socioeconomic discriminatory practices in accessing credit, these policies have further excluded them from the market and made a necessity, shelter, increasingly unaffordable.

During the coronavirus pandemic, the Federal Reserve has attempted to stabilize the housing market by minimizing short-term interest rates and purchasing mortgage-backed securities. Currently, it is impossible to fully understand the extent to which these decisions have affected the economy or racial inequality. Yet, what is clear is the influx of mortgage credit has once again driven up overall housing costs and racial inequality in home values. Ongoing finance policies that do not consider the racialized structure of appraisals and mortgages further exacerbate inequality.

## Cultivating Equity: Steps Towards Racially Just Appraising Practices

To cultivate a more racially just appraisal industry, the Federal Reserve, the Federal Housing Finance Agency, the Federal Housing Administration, the Department of Housing and Urban Development, and congressional lawmakers need to work collectively to create new standards, policies, and procedures that address these ongoing inequities. Below we propose interventions that will address the three primary mechanisms outlined above.

*Decreasing Racial Bias in Appraisers' Evaluations*. To help decrease the racial bias in appraising, the appraisal industry and the federal agencies that oversee the industry should adapt new processes and technologies that will further standardize appraisals. Specifically, the following adaptations should be considered:

1. *Automated Floor Plan Technology*. Noting the inconsistencies in appraisers' gross living area estimates, technology companies have created smart phone applications that use the phone's camera to measure depth and create automated floor plans. An analysis by Clear Capital showed that when untrained homeowners and other users employed CubiCasa's application they produced more accurate and consistent measurements than trained

appraisers using traditional methods (Allen 2021). Technologies like this should be phased in and eventually required to ensure more consistent measurements of gross living area, floorplans, number of rooms, and assessments of amenities.

2. *Automate Neighborhood Evaluations*. Instead of appraisers determining neighborhood boundaries—a process that often results in appraisers grouping areas by racial composition (Korver-Glenn 2021)—the uniform appraisal report should automatically generate standardized neighborhood characteristics based on the uploaded property address. GIS technologies and existing data sets (e.g. American Community Survey, Uniform Appraisal Dataset, National Establishment Time Series, and CoreLogic) could be used to create precise estimates of community amenities and trends. Additionally, each of the relevant neighborhood characteristics should be associated with standardized evaluation criteria to decrease implicit and explicit biases. However, it should be noted such algorithms need to be created with attention to historical and contemporary racialized processes to ensure they do not reproduce existing inequalities.

3. *Automate the Sales Comparison Approach*. When appraisers use the sales comparison approach, the selection of recent sales and their corresponding adjusted values should be derived automatically. Using the Uniform Appraisal Dataset, algorithms would select the most comparable recent sales based on the comparability of the information provided by appraisers on each property. The software would then use the information in the system on both the subject property and the comparable sales to create adjusted values. To account for historical discrimination, the algorithms should select comparable sales from racially diverse areas that have similar amenities.

*De-racializing Property Evaluations*. Although standardizing the appraisal process will decrease the influence of appraisers' racial biases in the assessment process, fully addressing racialized property evaluation will require creating new methods and regulatory measures. These new methods and measures should deliberately de-racialize property evaluations by valuing communities of all racial backgrounds equitably. To this end, we propose the following:

1. *Institutionalize a New Appraisal Method*. Like publicly owned and regulated utilities, housing costs should vary based on the amount of resources consumed, not speculative trading, credit availability or the perceived superiority of Whiteness. Larger homes with luxury features should be more expensive than smaller, more basic dwellings. Yet, the difference in value should be directly proportionate to the amount of natural materials, human labor, and public resources (e.g., electricity and road infrastructure) required to construct and maintain them. This standardization would eliminate speculation and enable residents to make informed decisions regarding the cost of purchasing or upgrading property and whether they want to pay for the property's amenities. To enact such a method, the appraisal industry should work with developers, technological companies, and computer scientists to create new applications and algorithms that can approximate the cost associated with a property's characteristics and location. Appraisers

would then upload multiple pictures and detailed information about the make and condition of the property's features and amenities. These technological applications would then evaluate the cost of construction as well as an approximant amount of the public resources used to build and maintain property in the specific physical location. This approach would directly connect the supply and demand of housing. In turn, this would ensure that the market incentivizes the needed development of affordable housing. Appraisal applications and algorithms should be open source so that homeowners or landlords making repairs can accurately determine the financial benefits of their investments. Moreover, any new method needs to be created in collaboration with tribal nations and representation from a wide range of communities to ensure diverse perspectives on the cost of resources are taken into consideration.

2. *Regulatory Processes that Track Equity*. Tracking racial and class inequality in appraisals over time would assist government officials and the public to recognize what interventions and practices are fostering equity and how we can collectively ensure we are implementing changes that uphold fair housing legislation. Moreover, individual homeowners and communities need tools to be able to determine whether they are observing or experiencing racialized property evaluations. To this end, federal agencies should create mechanisms to measure equity and legal mechanisms to discipline appraisal companies or individuals that violate Fair Housing legislation. Additionally, the Uniform Appraisal Data should be made public with tools for communities to be able to evaluate whether home prices have been racialized.

*Financially Incentivizing Racial Equity*. For nine decades, federal agencies and the federal reserve system has enabled White Americans to accumulate wealth by institutionalizing mechanisms that led to the hypervaluing and accelerating appreciation of White spaces. Over this time, we have increasingly made housing a speculative investment rather than a basic need. Moving towards racial equity will require addressing the inequalities created by past housing policies, restructuring insured mortgages, and rethinking the secondary mortgage market.

1. *Housing Policy Reparations*. As we have discussed, the tribal land treaties, the 1930s housing policies, and the World War II G.I. Bill enabled millions of White middle-class families to purchase property at federally subsidized prices and benefit from its racialized appreciation. No comparable opportunities have existed for Black, Indigenous, or Latinx Americans. Quite the opposite, their land and labor has been stolen, devalued, and degraded. Creating a de-racialized housing market requires adjudicating these injustices. Thousands of activists and scholars have derived detailed plans for how federal policy can provide housing reparations for these historical and ongoing unjust policies. These proposals need to be taken seriously and enacted.

2. *Restructuring Interest Rates for Federally Insured Mortgages.* The National Housing Act introduced federally insured mortgages to provide housing for working- and middle-class families. However, the privatization of the secondary housing market increased banks'

capacity to provide low-rate mortgages to more affluent people borrowing larger amounts. This system rewards wealthy borrowers instead of providing publicly subsidized avenues for new homeowners and working-class residents. Governmental agencies should incentivize banks to use progressive interest rates. That is, provide lower interest rates to borrowers with less accumulated wealth. These borrowers would still need to establish their income and ability to cover monthly payments. Conversely, wealthier borrowers would pay higher interest rates given that they have already benefited from federally subsidized policies that enabled them to accumulate their wealth.

3. *Rethinking the Secondary Mortgage Market.* In direct and indirect ways, the privatization and expansion of the secondary mortgage market has contributed to the racial appraisal gap and the affordable housing crisis. Theoretically, it is possible that changes to the appraisal industry alone can reverse these disturbing trends. Yet, the secondary mortgage market's unique contributions to these trends needs to also be further explored. Specifically, the Federal Reserve should conduct additional research on any unintended consequences of the Fed's purchase of mortgage-backed securities and whether new interventions could be adapted that would help stabilize the market without furthering socioeconomic and racial inequality.

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