

Freddie Mac Confirms Heightened Appraisal Gaps in Minority Areas

By: Jann Swanson | Tue, Sep 21 2021, 11:34 AM

A cluster of stories about appraised values of homes in minority areas hit the national news earlier this summer and now Freddie Mac has released an analysis of the smoke/fire variety. The company says it found appraised values are more likely to fall below the contracted sale price of a home in census tracts with a higher share of Black and Latino households, **resulting in what is known as an appraisal gap**. This is precisely what was alleged in news reports. Further, the extent of that gap increases as the percentage of persons of color living in the census tract grows. Freddie Mac based its analysis on 12 million appraisals it received as part of the home purchase process between 2015 and 2020.

"An appraisal falling below the contracted sale price may allow a buyer to renegotiate with a seller, but it could also mean families might miss out on the full wealth-building benefits of homeownership or maybe unable to get the financing needed to achieve the American Dream in the first place. This is a persistent problem that **disproportionately impacts hundreds of thousands of Black and Latino applicants**," said Michael Bradley, senior vice president of modeling, econometrics, data science and analytics in Freddie Mac's Single-Family division.

"Our research marks the beginning of a comprehensive effort to better understand the key drivers contributing to the appraisal gap. Our goal is to develop solutions to this persistent problem, including appraisal best practices, uniform standards for automated valuation models, enhanced consumer disclosures, improved value processes, and revised fair lending exam procedures and risk assessments."

The company said that properties located in predominately Black or Latino tracts received appraised values that were below the contracted sales price 12.5 percent of the time while the lower values came in only 7.4 percent of transactions in largely White tracts. This leads to a **5.2 percent gap**. As the minority population grows so does the gap. As an example, as the Latino population increases, the gap moves from 7.7 percent to 9.4 percent.

Only single-family on-unit homes were included in the analysis and the company conducted numerous robustness checks on the data. It was viewed by appraisal and occupancy type, property condition, and housing trend as noted in the report. Differences in comparable sale distances, reconciliation, and sale prices explained only a modest amount of the observed gaps. Possible systematic overpayment for properties by minorities was discounted as well.

The gaps were not limited to a subset of appraisers but were observed in the product from a large portion of those who conducted appraisals in both minority and non-minority neighborhood. The work contained what the analysis called "statistically significant gaps."

"Equity in housing is a critical issue and one Freddie Mac takes very seriously," said Pamela Perry, single-family vice president of equitable housing at Freddie Mac. "We're uniquely positioned to investigate potential gaps and provide data-driven research like this to advance solutions that promote equity across the valuation process. In addition, we are committed to engaging with the Appraisal Institute to **review the analysis in depth so that we can work together in identifying causes and solutions**."

Freddie Mac said it will explore opportunities to leverage data collection methods, analytics and to develop tools to create new approaches to valuation. It is also testing whether alternatives to traditional appraisals offer a more objective analysis of property value.

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