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AI and Bias: What Everyone is Worried About

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We have all, no doubt, heard and read about the growing concern about AI, but what is the basis for that growing concern? Why are so many agencies at all levels of government worried about the impact of AI within the mortgage space? We know that one of the biggest concerns about the use of AI is its potential to make biased decisions. In mortgage lending, there is worry that AI bias could result in harm to lower-income or minority borrowers. Let's examine how the uncontrolled use of AI has resulted in bias outside of lending and why these stories of AI-gone-rogue may be influencing legislators, regulators and advocacy groups with regard to the mortgage space.

One of the most egregious examples of the potential negative impacts of AI bias occurred not in the U.S., but in the Netherlands: The Dutch childcare fee scandal. And while it received little news coverage in the U.S., it was big news in Europe, because it brought down the Dutch Government. Here's the background: Over a 14-year period, the Dutch government used an AI system to detect fraud within its childcare benefit program. The system apparently used dual nationality and poverty as major indicators of fraud, but beyond that, the system was a black box: It couldn't tell the user why someone had been flagged for fraud. In addition, it was a self-learning system, so it changed over time, without the original programmer's input or knowledge. The Dutch tax authorities targeted low income and immigrant parents flagged by the system and forced families to pay debts as high as 100,000 euros. Tens of thousands of families were falsely accused of fraud, leading to bankruptcies, divorces and even suicides. When it came to light, the entire Dutch government was forced to resign.

Closer to home, the Rite Aid Facial Recognition scandal is another example. Rite Aid reportedly used AI-based facial recognition technology to identify customers who may have been engaged in shoplifting or other problematic behavior. The data used by the AI system was fed from thousands of low-quality security cameras and employee cell phone images. As a result, false positives were frequent, causing employees to follow customers around stores, falsely accuse them of shoplifting in front of friends and family members, or in some cases to call the police. The AI falsely flagged Black or Asian customers as shoplifters far more frequently than White customers. In 2023, the scandal broke, resulting in significant negative publicity and an FTC ban from using any facial recognition software for five years.

What's in a name?

Earlier this spring, Stanford Law School and its Institute for Human Centered Artificial Intelligence (HAI) released a new study showing systemic bias within ChaptGPT and other Large Language Models in various retail situations. "Asking ChatGPT-4 for advice on how much one should pay for a used bicycle being sold by someone named Jamal Washington, for example, will yield a different—far lower—dollar amount than the same request using a seller's name, like Logan Becker, that would widely be seen as belonging to a white man. It's $150 for white-sounding names and $75 for black-sounding names," according to an associate director at the Stanford HAI. "Other scenarios, for example in the area of car sales, show less of a disparity, but a disparity nonetheless." Names associated with Black women receive the least advantageous outcomes, according to the study.

Advertising

Targeted advertising in the online world has long been a fair housing concern because the available tools can be used in ways that violate the Equal Credit Opportunity Act or the Fair Housing Act. As a result, targeting advertising to particular demographics, which is a staple of the online advertising world (as can be seen by the ads for yoga pants in my Facebook feed and Carhartt® clothing in my husband's feed) can be illegal if conducted in the context of mortgage lending or real estate.

This becomes even more complex when AI is used in marketing, as HUD points out in its recent Guidance on Advertising through digital platforms.

According to HUD's Guidance, "New technologies can be used to target advertising toward some consumers and away from others. This can be done deliberately—for example, when advertisers choose to have their ads directed in a particular way—but it also can occur through the operation of complex automated systems designed to make ad delivery more efficient in accomplishing an advertiser or ad platform's purpose….Importantly, this can happen without the advertiser's direction or knowledge, and can even frustrate an advertiser's intention that an ad be distributed more broadly."

Concerns influencing regulators

The issues that have arisen with AI bias in other sectors are one of the factors that is driving increased scrutiny and new regulation in the mortgage and real estate sectors.

California is considering Assembly Bill 2930, which regulates the use of automated underwriting decisioning tools by mortgage companies. It would require lenders to perform annual assessments of how the automated underwriting tool is using personal information, including protected characteristics, to make decisions, and to determine whether the user needs to put any safeguards in place to prevent discrimination. Mortgage companies would need to provide borrowers with a disclosure outlining the tool used and the way it is used, and borrowers would have the right to opt out of being evaluated using the tool. The opt-out provision in particular is of significant industry concern, as it could result in an increase in underwriting costs in an environment in which lenders are already struggling with high origination costs.

Meanwhile, Colorado just passed a comprehensive AI law (Senate Bill 24-205) that requires a developer of a high-risk artificial intelligence system to use reasonable care to avoid algorithmic discrimination. Automated underwriting and valuation tools would both be considered high-risk systems under the law.

At the national level, The National Institute of Standards and Technology (NIST) has been tasked with developing best practice approaches to testing, evaluation, verification, and validation of AI systems to eliminate bias. It has selected credit underwriting for its first phase in this standards-building exercise, which indicates both that this is an area of significant concern but also that credit underwriting is an area in which the AI experts at NIST think standards could prove particularly effective.

Appraisal bias has been a major topic in mainstream media coverage over the past few years, although most of the high-profile instances have involved appraisers, as opposed to automated valuation models (AVMs) and AI.

In response, thirteen federal agencies, including the CFPB, HUD, FHFA, USDA and the VA joined an Interagency Task Force on Property Appraisal and Valuation Equity, also known as the PAVE Task Force. Although much of the taskforce's initial work has focused on taking steps to combat appraiser bias and the under-representation of minority appraisers, PAVE has also looked at the broader issue of technology fostering bias in home valuations.

While in theory AVMs can help eliminate human bias, they could also perpetuate it if bias is baked into their creation. Last summer, a group of federal agencies including the CFPB proposed a rule on quality standards for AVMs. The rule added a fifth quality factor, nondiscrimination quality control, to the existing four factors. This will require users of AVMs to establish policies, practices, procedures and control systems to specifically address nondiscrimination in the use of AVMs.

As more and more mortgage lenders and servicers integrate AI into their workflows, they can't relegate AI bias to the bottom of a long list of things to think about. Both the EU AI Act and the U.S. copycat laws that are already being passed require the developers and deployers of AI tools used in credit underwriting and real estate valuation to take steps to ensure that the tools do not discriminate. But existing laws like the Fair Housing Act and the Equal Credit Opportunity Act mean that U.S. regulators don't have to wait on new laws or regulations to take firm action on AI discrimination. And every indication is that discrimination in lending is at the top of regulators' lists to think about.