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Comments of the
American Homeowners Grassroots Alliance

Submitted to the

U.S. Federal Trade Commission

and the

U.S. Department of Justice

For the Public Workshop on

Competition Policy and the Real Estate Industry

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Background:

The American Homeowners Grassroots Alliance (AHGA) is a national consumer advocacy organization serving the nation's 75 million homeowners. AHGA engages in policy issues that significantly impact homeowners and home ownership. Among those issues is competition within the real estate services industry.

AHGA has long had an interest in competition policy within the real estate services industry. Real estate commissions appear to be about 1.5% higher in the U.S. than in other developed countries, suggesting our system needs scrutiny. In more expensive markets such as Washington DC, where the median sales price recently passed $500,000, the predominant real estate sales commissions remain in the 5 - 6% range (i.e. $25,000 - $30,000 on a $500,000 home), in a "seller's market" that until recently saw few homes go unsold in their first month of listing.

Summary

Brokerage industries in the U.S. have changed dramatically in recent decades. Prior to that time the securities, travel, and real estate brokerage industries competed mainly on the basis of service, most offering homeowners and other consumers a full range of services within a narrow range of fees.

New business models in each of these brokerage industries have resulted in an unbundling of services. Today consumers can trade in stocks and bonds on the Internet for a fraction of the cost of full service brokers. However those low-cost companies do not always offer the full range of services of a traditional stock broker, allowing the consumer to choose the service right for him or her. Large Internet travel brokers have helped reduce the costs of airline travel, hotels, and car rentals dramatically. Again, the Internet companies do not offer the range of services of a traditional travel agency, allowing the consumer to choose among low cost providers if price is their priority or among full service providers if service is their priority.

In real estate brokerage, new Internet-based business models have provided home sellers and buyers many new choices. In the most dramatic case, a consumer might use a broker to only list their home in their local Multiple Listing Service (MLS) for as little as $300. As in other brokerage sectors, these low cost companies do not provide the full range of services of other brokers. The consumer should have choice.

Many other new business models have evolved in the real estate service sector. Some are based in part on benefiting from potential economies of the Internet. Others, such as the evolution of exclusive buyer agency, where the real estate broker's business model and fiduciary duty is exclusively to the buyer, have resulted from the migration of an existing business model into residential real estate brokerage.

In the securities and travel industries these new business models have evolved naturally. Most have gained substantial market share, and consumers have their choice of working with full service travel agents or stockbrokers who compete mainly on the basis of the quality of their services, or selecting companies that perform only a limited core service and who compete mainly on price. The real estate service sector is an exception. Traditional full service real estate companies have created industry rules and have promoted federal, state, and local laws and regulations that have created barriers or undermined new real estate services business models. Unlike the travel and securities brokerage sectors, barriers to new business models in the real estate services sector has limited the market penetration and thus consumer access to new business models. The result is that some home buyers and sellers are forced to pay for full services that they might not want or need. In addition, other consumers would be surprised to learn their broker is withholding information from free and easy distribution on the Internet, while others find themselves deprived of services that they had expected.

These barriers to new business models in the real estate sector appear to be growing and efforts to slow them have had limited success. Powerful state real estate lobbying groups have engineered regulations and legislation in 20 states that prohibit competitors with new business models from offering specialized services and consumer rebates. Their counterparts in other states appear poised for similar efforts next year. Absent intervention by the federal government, it is entirely possible that the right of consumers to purchase unbundled services from real estate brokerage companies and the right to receive a discount through a consumer rebate in real estate transactions will no longer exist in this country.

At the federal level, the insistence of the National Association of Realtors to implement anticompetitive rules that enable real estate brokers to restrict the dissemination of homeowners listings against their fiduciary's best interest, threaten to further erode broker's fiduciary duty to American homeowners. NAR continues to battle for the ability of brokers to protect their own interests at the expense of the consumer – the exact opposite of what a consumer hires an agent to do. Even as the DOJ highlights the obvious antitrust problems with the brokers' conspiracy, NAR battles on.

These barriers and changes cannot be explained by consumer interests. Consumers have not supported the regulation of new business models in any these brokerage industries. AHGA has not received complaints from its members about problems associated with new business models in the real estate brokerage sector. Even states that have passed new regulations are widely reported to have done so in the face of practically zero consumer complaints. Although disputes between consumers and real estate service providers are quite common, we have not been able to substantiate any real level of consumer discontent over new business models in real estate services.

Organizations representing traditional full service real estate brokers assert consumer protection in support of these laws and regulations. However, it is surprising that consumers would bring their complaints to full service brokers to the exclusion of consumer advocacy organizations and government consumer protection organizations that are traditionally the first resort for consumer complaints. Furthermore, the solution to a problem of where consumers might make an unwise choice is disclosure – fully inform the consumer of the nature of the services offered. These facts raise profound doubts about the underlying motives of traditional real estate service brokerage companies and organizations that are the authors of and driving forces behind the restrictive rules, laws and regulations.

On behalf of the nation's 75 million homeowners AHGA commends President Bush and the leaders of the Federal Trade Commission and the Department of Justice for hosting this workshop and for their ongoing efforts to prevent antirust violations and anticompetitive behavior that is limiting consumer choice and artificially propping up real estate transaction costs. AHGA also urges federal and state legislators to review the record of this workshop with a view towards determining what legislative measures are needed to remove existing barriers to new competitors in the real estate services sector.

Overview of the Real Estate Transaction

Unlike many traditional brokerage industries, where brokers are merely intermediaries or facilitators, real estate brokers and agents owe a fiduciary duty to their clients. This is a responsibility to put the best interests of the client, be it a home buyer or home seller, above their own interests. Appropriately, real estate industry professional and trade associations have developed extensive training programs and certifications to assure that industry professionals understand their responsibilities and help consumers differentiate the educational qualifications of industry professionals.

The fiduciary responsibility and these educational programs and certifications are very important. Consumers who choose a full service real estate brokerage to represent them as a seller or buyer have a right to expect those brokerages and their agents to put the buyers or sellers best interest ahead of their own both in all cases in individual transactions and in their conduct in determining internal and external policy for their trade and professional organizations.

Some real estate transactions, such as inheritances, family subdivisions, and gifts or sales between families or friends do not require real estate marketing services. For the overwhelming majority of the balance the local Multiple Listing Service (MLS) is an essential facility for the real estate transaction. The MLS is an electronic database of information about the homes of the fiduciaries of participating brokers. Most are owned and governed by those brokers. Traditionally MLS's disseminated data and other intellectual property owned or created by the homeowner, along with public information, and in many cases additional contributions by the real estate agent, to other MLS members. With the growth of the Internet most MLS's now also feed partial MLS listing information to the consumer-facing websites of participating brokers. With the Internet now used in the home search by 70% of buyers, maximum and unrestricted dissemination of listing information over the Internet is of critical importance and benefit to both home buyers and sellers.

The Internet has also facilitated consumer education on the real estate transaction, Home buyers and sellers can access a wide array of helpful information on marketing techniques, applicable laws and regulations, and other unbiased information from the websites of government agencies or consumer educational organization. This has enabled more consumers those who wish to take the effort of assuming some of the responsibilities themselves to do so or to purchase real estate services in an unbundled fashion from multiple sources.

New business models offering unbundled real estate services have been created to fill this demand. In areas where barriers to this business model have not been created consumers who are experienced in real estate transactions, such as former real estate agents and experienced investors, as well as other consumers who take the time to understand the process, have saved substantial amounts on real estate sales transactions. AHGA believes that the existence of these new lower cost business models is very like contributing to increased home sales, because they enable home sellers who require specific net proceeds to sell in cases where they could not achieve their net after a traditional 5-6% commission.

Many home sellers prefer to use traditional full service real estate brokers. For example a dual income couple with small children may not have the time to conduct all of the requisite real estate marketing activities, which can vary tremendously depending on market conditions. For this reason they rely on the broker to exercise the same fiduciary duty and care that the broker and agent would use in selling their own home.

The rules affecting real estate transactions are developed by the trade associations representing the profession, promulgated by federal, state or local regulators, or enacted by federal or state legislators. Homeowners have traditionally been under-represented in policy deliberations affecting the real estate transactions.

While there are some exceptions, most state real estate commissions, which are charged with representing consumers, are dominated by traditional real estate service providers. State real estate trade associations also dominate state and federal lobbying on real estate issues. A review of state lobbying reports in almost any state will list state and local real estate associations among the major spenders on lobbying and consumer advocacy organizations, who have much broader issue agendas, among the smallest. The practice of appointing independent consumer advisory committees, common in some industries, has not taken hold in the real estate services sector. Those factors help explain why state laws affecting such issues as dual agency have reduced the fiduciary responsibilities and potential liabilities of real estate service providers in recent years, and why those changes have not been reflected in reduced commission rates.

The real estate transaction remains overly complex. Simplification will help reduce the complexity. Disclosure, in plain English terms that consumers will understand, will also help. Allowing consumers to obtain the level of service they desire from a multiple array of service providers to fit each consumer’s unique requirements will also help.

Issues Affecting Competition among Sellers Brokers

Numerous issues affect competition between sellers’ brokers. One is the cost of services provided. A full service real estate broker, like his counterparts in the securities and travel agency fields must make a significant investment in a variety of areas in order to be able to provide a full range of services. There are numerous full service competitors in all three markets, and competition in the full services segment of each imposes some upper limits on the transaction pricing on their segment of the market. This explains why transaction pricing for full service in all areas is essentially the same today as it was before new business models were introduced in all three industries.

In the real estate sector net real estate commissions, adjusted for inflation, are probably slightly higher that they were in past decades. The unusually rapid appreciation of U.S. homes in recent years (far faster than inflation and more than 50% in many areas), have enabled the average national real estate commission rate to drop from just below 6% to just above 5% while yielding more actual dollars for traditional broker transactions. For example a 6% commission on a $200,000 home several years ago would have yielded $12,000 while a more recent 5% commission on the same home now worth $300,000 is $15,000. That $3,000 difference represents a 25% increase in actual dollars, and is probably a net increase for a traditional broker and agent even after inflation. AHGA believes that were there no barriers to new business models their penetration would be much greater and the average commission today would be much lower.

AHGA believes the ability of traditional real estate brokers to maintain, if not increase commission proceeds is explained by the numerous current barriers to competition in the U.S. real estate services industry. The barriers include overt efforts by organizations at the federal and state level to promulgate industry rules as well as enact state legislation and regulations that are anticompetitive. They have had the effect of both limiting the participation of non-traditional real estate service providers and undermining the fiduciary responsibility of real estate brokers to home buyers and sellers. It is difficult to understand how organizations that represent businesses who owe a fiduciary duty to homeowners can advocate policies that undermine that duty.

Also limiting competition are flawed notions of intellectual property ownership that have not been sufficiently challenged. These include the assertion, widely voiced by organizations representing traditional real estate brokers, that the information contained in a home seller's real estate listing is the property of the real estate broker rather than the homeowner. In fact some of the data is always either provided by the homeowner and/or is a matter of public record. In many cases sophisticated homeowners provide most or all the listing information and data, including descriptions, photos, room measurements and other data. In such cases all the intellectual property contained in the listing obviously belongs to the homeowner. The MLS itself is an information conveyance, much like railroads that carry the farmers' grain to market. While the MLS owns the information railroads and the tracks, antitrust laws dating back to the 19^{th} century must be applied to these information railroads.

Since real estate brokers and agents owe a fiduciary duty to home sellers who also own or share the ownership the intellectual property contained in a home listing, real estate brokers have no right to make decisions that would limit the dissemination of that data without the home sellers permission. AHGA believes that duty extends to their collective actions in setting the policies of the multiple listing services, which are generally controlled by those same real estate brokers. Sadly all too often real estate brokers appear to be setting MLS practices that limit competition and work against the best interests of their clients. It was only recently, and then after intense pressure from the U.S. Dept. of Justice, that the National Association of Realtors withdrew an earlier version of their proposed "opt out" rules that would allow a broker to limit the dissemination of a homeowners listing without first getting the homeowners permission.

At the state level legislative and regulatory efforts supported by real estate industry associations have reduced real estate broker fiduciary responsibilities in some cases, and limited their unbundling in others. The common thread in both cases is that traditional companies are benefited and home sellers home buyers, and companies offering alternative business models to them are hurt. In the former regard state laws passed over the last several decades allowing for dual agency (the inherently conflict of interest practice of one real estate service provider representing both the buyer and seller in the same transaction) undermine independent advocacy services that are a key fiduciary responsibility to the client.

Prior to the passage of those laws it would have been a breach of fiduciary duty for a real estate broker representing a seller to subsequently agree to represent a buyer in that same transaction. While state laws may have made dual agency legal, they still remain unethical. They lessen competition because the broker has neither the undivided best interest of the buyer or the seller in mind during competitive aspects of the transactions, such as the negotiation of prices and terms.

Today local real estate associations typically bury provisions in the fine print of listing agreements language that allows the listing broker or agent the option of soliciting visitors to their client's open house to represent them as buyers agents, thereby undermining the services expected in the listing agreement. Those dual agency provisions do not provide for a commensurate reduction in commission rates to offset the reduced level of service. Dual agency laws hurt buyers and sellers alike and have hindered the growth exclusive buyer agency, a recent development in representation that provides a full and equal level of fiduciary representation to a home buyer. State real estate agencies are also hindering the clear disclosure to consumers of the services they forgo in a dual agency relationship. Economies coming out of dual agency and some real estate brokerages entrance into mortgage lending have apparently as yet not been reflected in lower transaction costs for home buyers and sellers despite their potential for doing so.

Currently state real estate associations are campaigning to limit the unbundling of real estate services and prohibit rebates. Unbundled real estate services enable home sellers, for example, to pay a real estate broker as little $300 to list their home in the multiple listing service, hold the open house themselves, and hire a real estate attorney to help with the legal requirements. Growing numbers of homeowners in the metropolitan Washington DC area where the median sale price is $500,000 are opting to list their home only for $300 and buy other needed services a la carte in lieu of paying a $25,000 - 30,000 commission to sell their $500,000 home.

However real estate professional associations in some 20 states outside the metropolitan Washington DC area have passed legislation requiring every broker to provide "minimum level of services" and/or prohibiting rebates. The former would require all real estate services companies to provide a full range of real estate services, which would undermine the business models of Internet based companies that offer list only services.

Issues Affecting Competition Among Buyers Brokers

Many of the same issues that affect sellers also affect buyers. State dual agency laws have enabled traditional real estate companies to fool unsophisticated buyers into believing that they are getting the same exclusive representation the buyer might receive from an exclusive buyers agent. When a buyer who is not represented attends an open house it creates a powerful incentive for the sellers agent to abrogate his or her fiduciary responsibility to the seller and sign the prospective buyer to a buyers representation agreement. At that instant the broker has created a conflict of interest.

Anti-rebate laws also limit the ability of brokers to, in effect, offer a discount to home buyers.

Empirical Evidence on Competition in the Real Estate Industry

U.S. real estate sales commissions average 1.5% higher in the U.S. than in other countries. Thanks to home appreciation net proceeds continue to increase. To put that in perspective, in the Washington DC market, median home sales recently passed $500,000, yielding a $25,000 - $30,000 commission to a traditional real estate broker charging a 5-6% commission. What is to explain this discrepancy between sales commissions in the U.S. and other countries, and the fact that a transaction whose major efforts are still concluded in less than a month in sellers markets costs $25,000 - $30,000?

According to a recent study by Dr. Steven D. Levitt, professor of economics at the University of Chicago, real estate agents yield more on the sale of their own homes than they do on the sale of their fiduciary's homes. In his new book, Freakonomics Dr. Levitt determined from a sample of 100,000 home sales that real estate agents yielded 3-4% more on average from the sale of their own home as compared to the proceeds of their clients home. This is evidence that that the current real estate model is somewhat dysfunctional. Most real estate agents and brokers are compensated completely by commission. The risk of not getting any commission at all (when a sale is not made) has a much greater economic impact for agents representing either buyers than does getting a little more money for the seller or saving a little more money for the buyer. A commission compensation arrangement inherently makes those compensated by the commission more in favor of a deal that they themselves might not take, as evidenced by the aforementioned study.

This also consistent with the efforts of real estate brokers and agents who are collectively abrogating their fiduciary duty in their advocacy of laws and regulations that are, on their face, contrary to the best interests of home buyers and sellers.

Recommendations

We commend the U.S. Department of Justice and the Federal Trade Commission for their ongoing and persistent efforts to increase competition in real estate services. The challenges are many, and the resources of those opposed to more competition in real estate services are deep. We hope Members of Congress will appreciate the vital work these two agencies are doing in this area, and will increase the agency's budget to better enable them to address the immense task at hand.

Many of the challenges will need to be addressed at the legislative level. AHGA has already made suggestions for increasing competition in real estate services. On September 30, 2004 AHGA submitted comments to the U.S. Antitrust Modernization Commission. Many of our recommendations were focused in this area. The Commission, whose work is still in progress, is charged with making recommendations to Congress on specific needed changes in U.S. antitrust laws.

AHGA recommended that the antitrust commission review the impact of dual agency laws on competition. Tie-in arrangements between real estate trade associations and multiple listing service (MLS) organizations would also appear to undermine real estate agency. Those arrangements require membership in the local real estate trade association as a precondition for the use of the MLS, which is generally recognized as the most powerful real estate marketing tool. There are pending lawsuits and contradictory prior court decisions on this issue, and a bright line prohibition of anti-competitive tie-in practices would be timely.

There are several potential antitrust issues related to real estate financing. There appears to be insufficient competition in title insurance reissue market. Consumers in many cases are charged the full retail price or near the full retail price for reissued title insurances on homes that are refinanced fairly soon after their purchase. It would seem unnecessary to repeat the entire research process for the history of the property in such cases, and relatively simple and inexpensive to determine if any new threats to the marketability of the title had occurred in very recent years.

As multiple factors, including consumer demand, are driving increased overlap between real estate lending and real estate marketing, antitrust laws should be adjusted to both protect consumer interests and encourage greater competition. For example, real estate agents or brokers who arrange home financing should be subject to all Truth-In-Lending-Act (TILA) requirements.

The most pressing need may be to address the rapid growth in state laws and regulations that limit consumer choices and force home buyers and sellers to pay for services they neither want nor need. This issue is particularly pressing because these laws are growing rapidly. Twenty states now have them on the books and traditional real estate brokers are expected to press for more during the next state legislative session.

Congress should consider federal legislation that would preempt law or regulation that forces consumers to pay for real estate services that they might not want or need. This includes laws that prohibit consumer rebates and laws that restrict the ability of real estate brokers to offer minimum services with full disclosure.

It is clear the real estate services sector needs to be pulled into the twenty-first century. To do that, anachronistic practices and barriers to competition need to be broken down and violations of current antirust laws need to be enforced. Laws that have no justification except to protect the traditional real estate brokerage from new competition must be stopped or preempted by federal law to protect the interests of American homeowners.

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