

D. RESIDENTIAL REAL ESTATE BROKERAGE FIRMS

1. Firm Size and Industry Concentration

a. Traditional Predominance
of Small Firms

The residential real estate brokerage industry traditionally has been dominated, in terms of numbers of firms and volume of sales, by small brokerage firms.^{390/} Surveys conducted by the NAR have found that more than 50 percent of all firms employ ten or fewer brokers and salespersons. Single-office firms predominate, with almost two-thirds of all firms having only one office.^{391/}

What little statistical evidence exists suggests that in recent years the typical office has not increased greatly in size, while the average number of employees per firm may have increased substantially. This can be taken to mean that there has been a growth in large, multi-office firms. The median numbers of full-time equivalent salespersons in firms for the years 1953 and 1977 were, according to these statistics, respectively, 6.3 and 10.0. However, the mean numbers were, respectively, 5.0 and 22.6.^{392/} The effect of the probable increase in the number of multi-office firms can be seen by comparing the relative numbers of full-time equivalent salespersons, as found by the 1977 NAR survey, for the average single-office and average multi-office firm. These figures were, respectively, 9.1 and 46.7.^{393/}

These statistics are among the best available. Nonetheless it should be pointed out that they must be used with caution and probably are overstated because of a heavy inclusion of large, multi-office, urban firms. The NAR survey sample from which the figures were calculated was drawn from members who participated in the Graduate Realtor Institute educational program for that year, and these brokers may not be typical of the entire universe of brokers and brokerage firms.

The FTC Consumer Survey found that 92 percent of homes sold through brokers were listed on the MLSs.^{394/} Statistics relating to MLS members and sales, therefore, can also be used to help obtain a more accurate picture of the entire residential brokerage industry, including average office and firm sizes.

The FTC MLS survey found that mean number of participating brokers and sales

^{390/} Case Report, supra, note 57, Part 1 at 15.

^{391/} NAR, Real Estate Brokerage 1978, at 37-38. This publication summarizes the findings of a 1977 NAR survey. Part-time agents are accounted for by converting their numbers into "full-time equivalents" (FTE's), based on hours worked relative to a 40-hour week.

^{392/} Case Report, supra, note 57, Part 3, at 14.

^{393/} Id., Part 4, at 3.

^{394/} FTC Consumer Survey Exhibit, Screener Question 13.

associates per multiple were, respectively, 122 and 573.^{395/} The mean number of firms and offices per multiple were respectively, 115 and 125.^{396/} This would indicate a mean number of total agents per firm of 6, and a mean number of total agents per office of 5.6.

The only consistent conclusion is that the average brokerage firm is very small.

Seventy-three percent of firms are now corporations. Almost all of these are closely held. Approximately 20 percent of firms are proprietorships and 6 percent are partnerships.^{397/}

The predominance of relatively small firms is generally explained by a combination of the few economies of scale available to firms, the cyclical nature of business, and the relatively easy entry into the industry.

Traditionally, there have been few economies of scale in the real estate brokerage business.^{398/} The one function that does involve enormous economies is the MLS.^{399/} However, this function generally is undertaken by the Association for the benefit of all of the member firms. Therefore, it is not an economy that one firm can use to gain an advantage over other firms.

There are some economies of scale in advertising and otherwise attracting buyers and sellers. Even here, however, our consumer survey indicates that referrals in one form or another are the principal means by which buyers and sellers become aware of brokers. Advertising by firms in the media, which may involve economies of scale, appears to account for less than 15 percent of listings and sales.^{400/}

The cyclical nature of the real estate brokerage market may also contribute to its fragmented structure. The smaller firms appear to have an advantage in

395/ FTC Multiple Listing Service Survey, Questions 13, 14.

396/ Id., Questions 11, 12.

397/ Case Report, supra, note 57, Part 4, at 9.

398/ See e.g., B. Becker, Economic Aspects of Real Estate Brokerage (1971), at 87-98. See also subsection c. below, relating to the growth of large corporations and franchises.

399/ See Ch. II, for a discussion of the theory of the market. See Ch. IV, Part C for a detailed discussion of the MLS.

400/ FTC Consumer Survey Exhibit, Seller Question 17 and Buyer Question 15 asked, "How did you become aware of the agent who handled the sale/purchase of your home?" The results were as follows:

	<u>Seller</u>	<u>Buyer</u>
From newspaper/magazine advertising:	5.2%	12%
"For Sale" signs/other homes for sale in area:	4%	12%
Other comments on advertising/TV:	2.6%	2.3%
Agent/firm recommended to us:	13%	23%
Previous experience with agent/firm:	21%	6%
Agent/Broker was friend/relative:	33%	27%
Other:	21%	18%

adjusting to market fluctuations. They are also characterized by lower overhead. This includes few fixed assets and relatively fewer salaried employees.^{401/}

Regardless of the size of the firm, the relatively small office appears to have an advantage. The geographic market in which salespersons conduct most of their business are local in nature. The salespersons' primary expertise consists of their knowledge of these local markets. A 1958 survey showed that 70 percent of transactions came from prospects living within a five-mile radius of the office.^{402/} The small office advantage is illustrated by the trend in franchise operations to grant exclusive territories with a radius of only about one mile. These territories are based on populations per franchise of approximately 30,000 to 50,000.^{403/} And the preferred radii may be getting smaller with time.

b. Entry

New residential real estate brokerage firms are formed continuously. In fact, the increase in the number of real estate firms appears to have kept pace with the substantial increase in average home prices. The number of firms, for example, appears to have increased during the recessionary year of 1974.^{404/}

Entry at the firm level generally involves an experienced broker leaving an established firm and starting his or her own firm. Perhaps because of the role that referrals play in obtaining business and the availability of MLS listings to the smallest brokerage firms, the owner of even a small firm may make a personal income very close to what he or she might earn in a larger operation.^{405/}

c. Growth and Entry of Large Corporations and Franchises

In recent years it has been fashionable to predict that eight to ten large national corporations and franchises will soon dominate the residential brokerage market.^{406/} These predictions have been caused by two relatively recent phenomena. First, the spectacular rise in home prices combined with a stable or rising commission rate has meant a corresponding rise in total industry revenues. These revenues have attracted the attention of large national corporations, several of which have investigated the field. A few, e.g., Coldwell Banker and Merrill Lynch, undertook the process of entry through purchases of local, traditional brokerage firms. Second, there has been very

^{401/} Case Report, supra, note 57, Part 1, at 15; Part 2, at 6.

^{402/} The Brokers Roundtable, Letter No. 7 (August 1958).

^{403/} Id., Part 4, at 53.

^{404/} Case Report, supra, note 57, Part 1, at 17-18; source: IRS data.

^{405/} Id., Part 3, at 6.

^{406/} Id., Part 4, at 55.

rapid growth in real estate franchising in recent years.

At present, the largest corporate chain of residential brokerage offices is Coldwell Banker. This national firm's total national market share of residential brokerage transactions, based on revenues generated from residential brokerage, was, however, estimated at less than .5 percent in 1977.^{407/}

Coldwell Banker, Merrill Lynch, and other large corporations attempting to enter or expand rapidly in the residential brokerage industry have generally done so by purchasing existing businesses. Acquisitions are preferred because entry at the local market level requires knowledge of the local market conditions. However, entry through such purchases has been quite difficult for at least two reasons. Because the primary assets of the firm are local management and a sales force with a knowledge of local conditions, it is very difficult to assign a dollar value to such corporations. If the talented people leave, the prospective corporate owner may have nothing left but an empty shell. Second, the tax and other consequences of an acquisition to the broker-owners of traditional firms appear to be such that they often prefer to remain independent.^{408/}

While the picture of rapidly escalating corporate growth through acquisition of existing firms may be somewhat exaggerated, the growth of the franchise systems has indeed been spectacular. From a very small market share in 1970, such systems may now account for as much as 38 percent of industry transactions.^{409/} In 1977 there were approximately 7,000 franchisees. In 1979 this number had increased to approximately 15,000 franchisees.^{410/}

Century 21 has been, at least in terms of number of franchisees, the most successful franchise system. This system was founded in 1972. By 1979 there were over 7,000 Century 21 franchisees. Their total industry market share for that year has been estimated at between 8 percent and 14 percent of total industry transactions.^{411/} It may now have reached 18 percent.^{412/}

^{407/} Id., Part 1, at 23; Part 3 at 9. In 1977 Coldwell Banker reported revenues of \$53.5 million from residential sales. Total industry commissions for the year have been estimated at \$14.6 billion. In local markets, a single firm seldom accounts for more than 10% of residential sales. Bruce Owen, supra, note 23, at 947-949.

^{408/} Report of Interview with Sol Rabin, Ph.D., First Vice-President and General Manager, Research and Consultation, Coldwell Banker (August 24, 1979).

^{409/} FTC Consumer Survey Exhibit, Seller Question 6. Other estimates for 1979 have been somewhat lower; e.g., F. Case estimates a 25% share. Case Report, supra, note 1, Part 4, at 42.

^{410/} Case Report, supra, note 57, Part 4, at 41.

^{411/} Id., Part 4, at 14.

^{412/} The FTC Consumer Survey, generally covering transactions during the second half of 1979, indicated that the total franchise market share was up to 38%. Of this 38%, Century 21 accounted for 48% of total franchise transactions. Id. indicates approximately an 18% market share of all industry transactions. The second largest franchise organization has less than 3% of the total national market for residential brokerage transactions. Seller Question 6.

Advertising, and the image identification it creates, appears to be the most important economy of scale available to large brokerage firms or franchises.^{413/} Sellers, in selecting a firm or broker with which to list their houses for sale, rate honesty and integrity as the most important attributes of such firm or broker.^{414/} In seeking these attributes, sellers traditionally have selected brokers and firms on the basis of personal contacts or referrals, or by community reputation.^{415/} Image identification established by mass advertising, however, may be making inroads into this consumer search process. Consumers may place trust in a familiar name with a presumed reputation to protect regardless of the source of that familiarity -- a pattern familiar in consumer goods marketing.

With a perceived increase in the importance of mass advertising, smaller local firms have felt some pressure to go beyond such symbols of presumed quality as the Realtors' service mark and associate themselves with organizations that can economically utilize modern marketing tools in establishing an image. Thus, the franchise systems create and also respond to the demands of small local brokers increasingly concerned about the potential advantages and economies available to the brokerage chains.

In addition to the economies of scale available in establishing image identification, there are economies available to both franchise organizations and corporations relating to recruiting and training of personnel. Large firms very often are affiliated with or operate pre-licensing schools for prospective real estate agents. These schools can return a net profit to the parent company, and serve as an aid in identifying and recruiting good sales personnel. Firms can sometimes even use salespersons of marginal quality recruited from their own schools, because sellers often list with a brokerage firm for which a friend or relative works.^{416/} (A common method of competing for listings is having a steady turnover of the largest number of salespersons manageable.) Because salespersons are generally paid only when they produce, i.e., on a commission basis, such a form of competition for listings can sometimes be successful.

^{413/} No firm has a sufficient market share to efficiently establish its own multiple listing service. Most attempts by local large firms to establish independent, closed multiple listing services have failed unless those firms have had approximately 50% of the total local market share. Report of Interview with Ira Griblin (October 30, 1979), at 2.

^{414/} FTC Consumer Survey Exhibit, Seller Question 20.

^{415/} See, e.g., FTC Consumer Survey Exhibit, Seller Questions 17 and 18.

^{416/} FTC Consumer Survey Exhibit, Seller Question 17. Up to 40-50% of these new people exit the industry within two years, however. Los Angeles Times (April 20, 1980) Part IX at 24.

2. Importance of the Individual Broker

a. Nature of the Firms

The brokerage business is very labor-intensive. Almost 60 percent of a brokerage firm's gross revenues typically are paid to brokers and salespersons in the form of fees and commissions.^{417/} Generally, a firm's principal assets are considered to be its sales personnel and their knowledge of the local market.^{418/} With each firm providing a customary range of brokerage services, job mobility of successful brokers and salespeople is fostered, and real estate firms become, in effect, flexible collections of independent, skilled, semi-autonomous contractors.^{419/}

Because of the relative unimportance of "the firm" when compared to either the MLS or the individual broker or salesperson, a perennial problem faced by a firm is finding and keeping successful brokers and salespersons.^{420/}

Firms compete in terms of the percentage of the total commission that the broker or salesperson will receive for acquiring a listing or completing a sale. These "internal splits" vary among firms, communities, and according to market conditions. Typically they range from 10 percent - 30 percent to the listing broker, 40 percent - 60 percent to the selling broker or cooperating firm, and the remainder to the firm. They are also frequently progressive — that is, as a broker produces more listings or more sales per year, the percentage he or she receives increases. A successful broker who sells his or her own listing can sometimes receive 70 percent of the total commission.^{421/}

The use of brokers and salespersons and their relative importance to the firm can be seen in the internal split structure. First, the ability of inexperienced salespersons to obtain the listings of friends and relatives usually is reflected in the relatively low split given for listing the first several properties. The relative importance and difficulty of converting a prospective buyer to an actual buyer is reflected in the larger split given for that function. Furthermore, the progressively higher splits for increasing numbers of transactions per year reflect the rewards reaped by those individual brokers and salespersons with the ability to quickly obtain listings from or make sales to people outside their circle of friends and relatives.

The fees and commission paid to brokers and salespersons by clients are almost always contingent in nature. The contingent form of payment is a major inducement for the broker or salesperson to persuade the buyer and seller to complete the transaction.^{422/} It also facilitates the use of marginally

^{417/} Id., Part 4, at 2-3; source: NAR, Real Estate Brokerage 1978.

^{418/} Case Report, supra, note 57, Part 3, at 6.

^{419/} Id., Part 5, at 1; Part 4, at 5.

^{420/} Case Report, supra, note 57, Part 3, at 10.

^{421/} Case Report, supra, note 57, Part 2, at 13. See also City Summaries.

^{422/} Potential conflicts of interest arising from the contingent nature of the broker's payment, and his agency and fiduciary duties to his or her principal, are discussed in Ch. IV, Part F, below.

productive salespersons and part-timers because their time is viewed by many as being "cheap" or even "free" to the firm.^{423/}

b. Profile of the Typical
Real Estate Broker

Profiles of representative real estate brokers have been compiled from surveys conducted by the Realtors' associations. The typical Realtor-broker is a man close to age 50 who has been associated with the real estate business for at least ten years, having worked for at least two different brokerage firms, who specializes in selling single-family homes, who works more than 40 hours per week. While this picture has remained somewhat constant over the years, there is a trend toward increasing education of the typical Realtor. By 1978, over 40 percent had completed four years of college.^{424/} While organized real estate and full-time real estate brokers generally believe part-time brokers are less able to give quality service to consumers, almost 45 percent of firms use them.^{425/}

c. Entry

The various state licensing requirements are not considered serious barriers to entry.^{426/} The numbers of licensees have been found to vary according to various indirect measures of demand when comparing different market areas,^{427/} and the numbers of licensees both in absolute numbers and as a percentage of population have generally increased.^{428/}

^{423/} Case Report, supra, note 57, Part 5, at 5.

^{424/} Id., Part 4, at 10.

^{425/} For a very tentative view holding to the contrary, see Sidney L. Carroll and Robert J. Gaston, "State Occupational Licensing Provisions and Quality of Service: The Real Estate Business," pp. 1-13 in Zerbe, ed., 1 Research in Law and Economics, JAI Press, 1979.

^{426/} Id., Part 4, at 9; NAR, Real Estate Brokerage 1978, at 37; See also California Real Estate (November 1978), at 13.

^{427/} Becker, supra, note 398, at 45; Case Report, supra note 1, Part 1, at 17.

^{428/} Case Report supra, note 57, Part 1, at 2, 8, 19. See also Ch. IV, Part B and Appendix B.

There are no accurate statistics on the number of brokers and salespersons actively involved in brokerage, as opposed to the total number of licensees registered with the states. Most observers believe the number of licensees greatly exceeds the number of people actually engaged in brokerage. Local surveys attempting to measure the actual percentage of licensees who are full-time practitioners, however, have produced results ranging from approximately 30 percent to 80 percent of licensees.^{429/}

E. ALTERNATIVE BROKERS

1. Market Segment

a. Alternative Brokers Defined

The FTC has, over time, received a number of complaints from brokers who characterize themselves as offering commission rates or services to consumers that differ from the norm in their communities. Many of these complaints allege what appear to be numerous possibly unfair practices by other brokers, by trade associations, and by state regulatory bodies. While a great variety of practices were alleged, there is a similarity in the patterns regardless of the local market in which a complaint arises.

The practices complained of by these alternative brokers may be important understanding why, overall, commission rates are so stable. These brokers are examples of individuals whose behavior as brokers deviates from the norm. problems they claim to face as a result could be examples of the mechanism for enforcing price stability at work.

We have defined "alternative" brokers for the purposes of this Report as those who charge and promote a commission rate or fee that is at least 2 percent lower than the fee prevailing in their geographic area, or who offer and promote services that differ significantly from those generally offered in their geographic area.

We conducted more than 25 in-depth interviews with such brokers, and then undertook a nationwide survey of all identifiable alternative brokers. Over 150 responded to the survey.^{430/}

This section will describe how alternative brokers operate and their experiences in the marketplace. We present our factual findings first and then

^{429/} Case Report, supra note 1, Part 4, at 15, 20.

^{430/} See Appendix D for a detailed description of the alternative broker survey. A total of 725 questionnaires was mailed to potential alternative brokers. This sample was generated from numerous leads, including an association of such brokers, franchise organizations of such brokers, newspaper articles and advertisements, and responses to requests for alternative brokers to supply the names of others. From the initial mailing, 81 were returned as not deliverable; 39 were returned because the broker was not an alternative broker. This left 605 delivered questionnaires. A total of 154 alternative brokers responded. This is a response rate of 25.4%.

analyze those findings primarily in the second part of this section.

b. Prevalence of Alternative Brokers

Alternative brokers exist in every state. Our consumer survey showed that while 35 percent of sellers were aware of the existence of a "discount" broker, only 12 percent contacted such brokers, and only 2.6 percent listed their homes with one.^{431/} Only 1.7 percent of buyers indicated that they purchased from discount brokers.^{432/} Our City Summaries of local markets found only a few alternative brokers in each community.^{433/}

2. Alternative Broker Firm Operations

a. In General

Most alternative broker firms are relatively new entrants. Of those responding to our 1979 survey, the mean year of commencing the firm was 1977. Only 10 percent had started before and survived the 1974 recession.^{434/}

While most of the firms were relatively new, the brokers operating them were experienced. The typical responding alternative broker had been licensed for eight years. Most had been traditional brokers before becoming alternative brokers.^{435/} But fewer than 50 percent of alternative brokers were members of the Realtors' associations.^{436/}

While alternative and traditional brokers use the same range of techniques to attract buyers and sellers, the percentage of customers and clients acquired by the various techniques differs considerably between the two types of brokers. Alternative brokers surveyed attracted 45 percent of their listings from media advertising. Only 29 percent resulted from referral and repeat business.^{437/} Our consumer survey, however, indicated that brokers as a group obtain approximately 67 percent of their listings from referrals and repeat

^{431/} FTC Consumer Survey Exhibit, Seller Questions 22, 23, and 24. Due to the problems of defining "alternative broker" in a consumer survey, the phrase "discount agents" was used.

^{432/} FTC Consumer Survey Exhibit, Buyer Question 25. While our definition of "alternative" broker may be somewhat different from consumers' of "discount" brokers, we believe that the consumer responses relating to discount brokers give a close estimate of the market share of alternative brokers.

^{433/} See City Summaries.

^{434/} FTC Alternative Broker Survey, II, 2.

^{435/} Id.

^{436/} Id.

^{437/} Id.

business. Only about 8 percent of all listings are produced from media advertising.^{438/}

The pattern with respect to attracting buyers is also different for alternative brokers. Among alternative brokers surveyed, 40 percent of buyers were obtained through advertising, 30 percent were produced from "for sale" signs, and 20 percent from referral and repeat business.^{439/} Our survey of buyers, however, indicated that most brokers obtain approximately 56 percent of their buyers from referrals and repeat business. Fourteen percent are produced from advertising, and from 5 percent to 20 percent from "for sale" signs.^{440/}

The higher response to advertising, which is at least in part price advertising, may indicate that there is price elasticity of demand for the individual listing broker or firm. That is, consumers are attracted by lower prices. Some alternative brokers have gotten extremely strong initial responses to price advertising. In fact, attracting listings is relatively easy. The problem is selling the listed homes.^{441/} The average alternative broker we surveyed sold fewer than 60 percent of his or her listings.^{442/}

The percentage of listings sold by all brokers seems to be substantially higher. The Federal Trade Commission consumer survey indicated that over 88 percent of responding sellers had not listed their home with a different broker before being successful.^{443/}

Alternative brokers we interviewed generally stressed the need for realistic appraisals in order to hold down selling expenses. Many alternative brokers feel that in order to survive at a lower commission rate, it was essential to avoid inflated listing prices and thus sell the homes in a reasonably short period of time. Alternative brokers often encourage sellers to split some of their commission savings with the buyer by offering the home for sale at a lower price in order to attract buyers more quickly.^{444/}

^{438/} FTC Consumer Survey Exhibit, Seller Question 17.

^{439/} FTC Alternative Broker Survey, IV, D. 9.

^{440/} FTC Consumer Survey Exhibit, Buyer Question 15. The two numbers for "for sale" signs indicate the range from direct answers relating to "for sale" signs to answers indicating the consumers probably learned of the brokers initially from such signs.

^{441/} See, e.g., Report of Interview with Gina Williams (January 31, 1979).

^{442/} FTC Alternative Broker Survey, IV, D. 2.

^{443/} FTC Consumer Survey Exhibit, Seller Question 16.

^{444/} See Appendix D, at 10. Some observers feel that "puffing" the listing price in order to acquire a listing has been an historic problem, especially associated with exclusive listings and MLSS. See, e.g., California Real Estate (December 1923), at 22, 42; (November 1925), at 23; (April 1928), at 21; NAR, Annals of Real Estate Practice, Volume II (1926), at 342. See also Brunner, President, Group 1 Realty, "Salespeople: Do They Inflate Home Prices?," California Real Estate (March 1978), at 9.

Our survey found that alternative brokers have been successful, to a certain extent, in their efforts to reduce selling times. They claimed an average of 47 days to sell a property as opposed to an average of 58 days for their market areas.^{445/} The average selling price of homes listed with the alternative brokers was \$58,000, compared with a \$62,000 average for their market areas, according to the alternative brokers.^{446/}

b. Non-MLS Alternatives

Alternative brokers can be classified into those who choose to operate without the MLS; and those who choose to participate in the MLS, as do the vast majority of traditional brokers.

Seventy-four percent of alternative brokers surveyed do not use the MLS in their primary marketing operations.^{447/} For these brokers, only 2.5 percent of their sales were cooperative sales.^{448/} They sold 54 percent of their listings.^{449/}

Seventy-five percent of non-MLS alternative brokers said they charge a flat fee instead of a percentage commission rate. The average flat fee for these brokers was \$932, which is equivalent to a commission rate of 1.6 percent, based on the average price of homes sold by these alternative brokers.^{450/} The 25 percent of non-MLS brokers who charge by percentage commission rate charged an average rate of 2.9 percent.^{451/}

Alternative brokers who charge a flat fee often require that at least some of it be paid in advance. Approximately 50 percent of non-MLS, flat-fee brokers surveyed charge an advance fee.^{452/}

Non-MLS alternative brokers typically offer to consumers a package of services which varies from the package provided by traditional brokers in two important ways. These alternative brokers do not list the home on the MLS, and 84 percent of them require that the seller show his own home.^{453/}

^{445/} Alternative Broker Survey, IV, D. 7; III, 8.

^{446/} Id., IV, D. 5; III, 1. We do not know whether homes sold by alternative brokers are comparable, on average, with homes sold by traditional brokers. Sellers should, of course, balance any commission savings against a reduced sale price.

^{447/} Some alternative brokers offer more than one plan to sellers. If the broker's most popular plan was a non-MLS plan, we classified that broker as "non-MLS," FTC Alternative broker Survey, IV, A. 2.

^{448/} Alternative Broker Survey, IV, D. 3; see also Appendix D, Table 4.

^{449/} Alternative Broker Survey, IV, D. 2.

^{450/} Alternative Broker Survey, IV, A. 1; Appendix D, Table 4.

^{451/} Id.

^{452/} Appendix D, at 13.

c. Multiple Listing Service Alternatives

Twenty-four percent of alternative brokers surveyed offered only MLS marketing plans and used the MLS in a manner similar to the traditional residential real estate broker. Another fifteen percent offered both MLS and non-MLS plans. The MLS alternative brokers typically charged a percentage commission rate averaging 4.2 percent. However, 25 percent instead charged a flat fee. Among those surveyed who charged a flat fee, the average amount was \$1,490. This is equivalent to approximately 454/ 2.6 percent of the average selling price reported by those alternative brokers.

The MLS alternative brokers typically split their commissions 50/50 with cooperating brokers who sell their properties. However, it was not uncommon for the alternatives to follow a plan whereby they receive 1 percent and the cooperating broker receives 3 percent. This was done to give cooperating brokers an incentive to sell the alternative broker's listings 455/

Obtaining listings was said to be relatively easy. There is considerable consumer response to price advertising. However, selling the houses was a problem. MLS alternative brokers surveyed did somewhat better than the non-MLS alternative brokers in this respect, selling 62 percent of their listings 456/. This is still well below the selling rate of traditional brokers. 457/

Much of the lower selling rate of the alternative brokers is attributable to their low percentage of cooperative sales. MLS alternative brokers surveyed averaged only 29 percent cooperative sales 458/. By comparison, our consumer survey of sellers found that for all brokers approximately 53 percent of sales involved two different firms and 66 percent of sales involved two different brokers. 459/

MLS alternative brokers tended to be full-service brokers, offering to consumers the same package of services as the traditional brokers. However, 47 percent did have plans whereby the seller could show his or her own home 460/

A minority of MLS alternative brokers had incorporated into their marketing plans significant variations to deal with the problems associated with the commission split. These plans varied the commission rate according to whether or not a cooperative broker was used, so that the seller did not have to pay a split if no cooperating broker were used. 461/

453/ Alternative Broker Survey, IV, A. 3; Appendix D, Table 4.

454/ Alternative Broker Survey, IV, A. 1; Appendix D, Table 4.

455/ Alternative Broker Survey, IV, A. 2.

456/ Alternative Broker Survey, IV, D. 2.

457/ FTC Consumer Survey Exhibit, Seller Question 16. The FTC Consumer Survey indicated that 88% of sellers accomplished the sale of their home through the broker with whom they had initially listed.

458/ Alternative Broker Survey, IV, D. 3.

459/ FTC Consumer Survey Exhibit, Seller Question 52.

460/ Alternative Broker Survey, IV, A. 3.

Some of the MLS alternative brokers were also competing in price for buyers. Because of the tradition of compensating cooperating brokers by a split of the listing broker's commission, competing in price (commission rates) for buyers is not extensively done by traditional brokers. However, a few alternative brokers have developed plans under which the buyer receives a rebate of a portion of the split to which cooperating broker is entitled (or a reduction in the price of the house) if the buyer purchases a home off the MLS through such cooperating alternative broker. For example, an alternative broker may qualify for a 3 percent split. He or she may attract buyers by rebating two-thirds of the normal 3 percent split — 2 percent of the purchase price — to the buyer. The cooperating broker, in other words, offers to aid the buyer for 1 percent instead of 3 percent and rebate the difference to the buyer.^{462/}

3. Problems Reported By Alternative Brokers ^{463/}

a. FTC Survey

In the initial series of in-depth interviews with alternative brokers, many of these brokers described a number of practices by brokers and others that they claimed to be unfair and injurious to their businesses. These problems were alleged to occur far more frequently by the alternative brokers than by the traditional brokers we interviewed. While not all of the alternative brokers had the same complaints, there was a pattern that emerged from these complaints and interviews.

The most frequently alleged problems described by the alternative brokers were included in our survey of alternative brokers. The surveyed brokers were asked whether they had experienced any of these problems, and to indicate only those problems that they believed occurred because they were alternative brokers. They were asked not to report problems that all brokers in their areas are likely to experience.

In our initial interviews some alternative brokers who had been in business for several years indicated that some of the problems that they had experienced frequently during their first year of operations subsided in subsequent years. Other problems did not. The survey, therefore, asked the alternative brokers to indicate a frequency of occurrence of the problems, where appropriate, allowing a response of "frequent," "occasional," or "never" for both the alternative broker's first year of operations and the year of the survey, 1979.

^{461/} In one case, the alternative broker's plan leaves compensation of the cooperating broker strictly up to the buyer. The broker explained that, "In our plan: Seller agrees to increase his price in direct proportion to buyers brokers fee, then to credit buyer in escrow -- so that buyer can compensate his agent whatever his agent has agreed to accept as fee." Survey Return No. 52, Bond, California.

^{462/} See, A. Maher, Virginia Survey Return; Report of Interview with Gina Williams (January 31, 1979). Such rebating practices may be illegal in a few states. See Appendix B.

^{463/} For a more detailed description of these problems than will appear in this section, see Appendix D.

Table IV.E.1. contains results from this part of the survey. The descriptions of the problems in the table use the exact language of the survey, which reflects the descriptions of the problems as alleged by the alternative brokers in the initial interviews.

We will first describe all of the primary problems and the survey results, and then analyze those results.

b. Most Frequent First Year Problems

(1) Disparagement

The problem alleged most frequently by alternative brokers is the general disparagement of their businesses to present or prospective clients by traditional brokers. During their first year of operation, over 93 percent of the alternative brokers experienced this disparagement. Almost 74 percent of alternative brokers reported that it occurred frequently.^{464/}

Disparagement of the alternative firms was alleged to take a great variety of forms. These include statements that the brokers were operating illegally, that they were unethical or unprofessional, or simply that the sellers will not succeed in selling their homes through the alternative brokers because no other brokers will deal with them.

While it is unusual for disparagement to be in writing, a written statement was apparently used against a Hollywood, Florida, alternative who participated in the MLS. A letter bearing the local Board of Realtors' letterhead was sent to clients who had listed their homes with the alternative broker. The letter was from "United Realtors" and contained the following language:

As a homeowner who has listed their home for sale with _____, please be advised that numerous Realtors, associated with the Multiple Listing System, have chosen not to show or sell your home, due to the unethical conduct of _____ towards their fellow Realtors.^{465/}

While general disparagement of the business is the most frequent problem alleged, its frequency was also often alleged to decrease after an alternative firm's first year in business. Comparing "frequent" survey responses during the first year with "frequent" responses during the "present" year (1979), "disparagement of your business" decreased 21 percent from the first year. However, even after the first year in business this problem allegedly continued to be the most frequent.

^{464/} Alternative Broker Survey, V. 4; see also Table IV.E.1.

^{465/} Palmview Realty materials. See also Appendix D, at 18.

TABLE IV.E.1.

Frequency of Occurrence

Description of Problem	First Year of Operation						Present year (1979)											
	Frequent			Occasional			Never			Frequent			Occasional			Never		
	Total # (#)	MLS	Non MLS	Total # (#)	MLS	Non MLS	Total # (#)	MLS	Non MLS	Total # (#)	MLS	Non MLS	Total # (#)	MLS	Non MLS	Total # (#)	MLS	Non MLS
1. Angry criticism or personal threats	42% (50)	55%	37%	45%	42%	47%	13%	3%	16%	30%	46%	24%	42%	36%	45%	28%	18%	31%
2. Vandalism (example: destruction of signs)	18% (21)	18%	16%	61%	57%	65%	21%	25%	19%	12%	14%	10%	58%	41%	66%	31%	46%	24%
3. Unfair grievance proceedings or legal action (threatened or actual)	9.6% (11)	18%	7%	33%	29%	34%	58%	53%	60%	6%	-38%	14%	33%	33%	33%	61%	52%	64%
4. Disparagement of your business (to clients or prospective clients)	74% (89)	77%	74%	20%	18%	21%	6.6%	5.9%	4.9%	58%	-21%	64%	57%	30%	27%	33%	11%	9%
5. Lost or cancelled listings resulting from disparagement in #	42% (49)	58%	37%	41%	27%	47%	17%	15%	17%	38%	-9%	55%	33%	41%	23%	21%	23%	18%
6. Lost listings resulting from other licensees soliciting your clients ("pirating")	40% (46)	45%	38%	41%	36%	44%	19%	19%	18%	40%	0%	46%	37%	39%	36%	21%	18%	20%
7. Refusals by other brokers to show homes listed by your business	53% (55)	59%	52%	31%	31%	31%	16%	9%	16%	49%	-9%	50%	48%	35%	41%	33%	17%	9%
8. Alteration by other brokers of your terms of cooperation (example: a broker writes an offer calling for him to receive a 3% commission, when you offered him only 1%)	19%	24%	17%	32%	36%	31%	49%	39%	53%	18%	-6%	18%	19%	30%	41%	25%	52%	41%

Description of Problem	First Year of Operation				Present Year (1979)								
	Frequent		Occasional		Never		Frequent		Occasional		Never		
	Total % (#)	Non MLS %	Total % (#)	Non MLS %	Total % (#)	Non MLS %	Total % (#)	Non MLS %	Total % (#)	Non MLS %	Total % (#)	Non MLS %	
9. "Discriminatory" splits from other brokers (example: a broker who normally splits 50/50 with cooperating brokers offers you only 10/90 splits because you charge reduced rates)	25% (24)	44% 16%	20% (19)	28% 16%	56% (54)	28% 68%	20% (14)	-20%	33% 14%	27% (19)	38% 22%	54% (38)	29% 63%
10. Refusals by Board of Realtors to enforce ethical standards	19% (18)	23% 15%	18% (17)	13% 21%	64% (62)	63% 65%	22% (16)	+19%	26% 18%	19% (14)	16% 22%	58% (42)	58% 60%
11. Refusals by state agencies to enforce state law standards to protect you	18% (20)	20% 16%	7.3% (8)	8.6% 7.1%	74% (81)	71% 77%	23% (18)	+28%	32% 17%	5.2% (4)	4.5% 5.8%	71% (55)	64% 77%
12. Discriminatory law enforcement by state agencies against you (including, if applicable, threats of or actual removal of your license)	11% (12)	11% 8%	8% (9)	9% 8%	81% (92)	80% 84%	12% (10)	+16%	14% 11%	6.2% (5)	9.1% 3.6%	82% (66)	77% 86%
13. Consumer belief that commission rates are fixed by law or are otherwise non-negotiable	62% (73)	68% 59%	31% (36)	27% 33%	7.6% (9)	5.9% 8.7%	51% (42)	-17%	62% 47%	42% (34)	29% 47%	7.3% (6)	9.5% 6.9%

(2) Negotiability of Commission Rates

The second most commonly mentioned problem among alternative brokers was a prevailing belief of consumers that commission rates are fixed by law or are otherwise non-negotiable. Over 90 percent of alternative brokers indicated experiencing such a belief as a problem in both their first year of operating and in subsequent years. However, the frequency with which the problem occurs appeared to decrease somewhat. Sixty-two percent indicated it was a "frequent" problem during their first year of operation; 51 percent indicated it was "frequent" during 1979.^{466/}

(3) Refusals to Show Homes

The third most common problem reported by alternative brokers was a refusal by other brokers to show homes listed by the alternative brokers. Eighty-five percent of alternative brokers surveyed said they experienced this during their first year of operation. Fifty-three percent indicated that it was "frequent."

This problem appears to decrease only slightly in subsequent years. Forty-nine percent of alternative brokers responding to this section indicated that the problem was "frequent" in 1979.^{467/}

Some clients of alternative brokers were reported to have alleged that they had called other local real estate brokers posing as interested buyers and requested information relating to their own unsold home. They are reported to have said they have been erroneously told that the house has been sold.^{468/}

(4) Lost and Cancelled Listings

Eighty-three percent of alternative brokers responding indicated that they had experienced lost or cancelled listings resulting from disparagement during their first year of operation. Forty-two percent reported that this was a "frequent" occurrence.^{469/}

This problem appears to decrease in frequency only slightly in subsequent years. Thirty-eight percent of responding alternative brokers indicated that this problem was still "frequent" in 1979.^{470/}

^{466/} Alternative Broker Survey, V. 13.

^{467/} Alternative Broker Survey, V, 7.

^{468/} See, e.g., Report of Interview with Bob Park (September 21, 1978).

^{469/} Alternative Broker Survey, V, 5.

^{470/} Id.

c. MLS and Non-MLS Alternatives Compared

(1) In General

According to our consumer survey, 92 percent of sellers who utilize a broker have their homes placed on the MLS.^{471/} Yet, 61 percent of alternative brokers surveyed did not use the MLS. Moreover, fully 76 percent of alternative brokers have at least one non-MLS marketing plan.^{472/} In an effort to understand why most alternative brokers do not use the MLS, we calculated the frequency with which the various problems were reported according to whether the responding broker used or did not use the MLS. These responses are contained in Table IV.E.1.

For virtually every problem described by the alternative brokers surveyed, the MLS brokers more often responded that the problem was "frequent" than did the non-MLS alternative brokers.^{473/} The four problems where the difference in reported frequency was the greatest between MLS and non-MLS alternative brokers are listed below.

(2) "Discriminatory" Splits

A "discriminatory" split involves a traditional broker giving a cooperating alternative broker a smaller commission split than is generally offered to other brokers. For example, a traditional listing broker who usually offers 3 percent to the cooperating broker who qualifies as procuring cause for a listing might offer a cooperating alternative broker only 1 percent.

Among MLS brokers responding to this issue, 44 percent indicated that this behavior occurred "frequently" during their first year of operation. Only 16 percent of non-MLS brokers reported this problem as occurring "frequently."^{474/}

(3) Unfair Grievance Proceedings

Alternative brokers complained that they sometimes have been the subject of what they felt to be unfair Board of Realtor grievance proceedings or unfair, or baseless legal actions. While only 9.6 percent of all alternative brokers responding to this section indicated that this occurred "frequently" during their first year of operations, it was much more frequent for MLS alternative brokers than for non-MLS brokers. Among MLS brokers, 18 percent responded that it was a "frequent" occurrence. Only 6.8 percent of non-MLS brokers responded that it was "frequent."^{475/}

^{471/} FTC Consumer Survey Exhibit, Screener Question 13.

^{472/} FTC Alternative Broker Survey, IV, A. 2.

^{473/} See Table IV.E.1.; compare "MLS" and "non-MLS" "frequent" first-year responses.

^{474/} Compare percentages of Table IV.E.1., Problem No. 9.

(4) Refusals by Board of Realtors to Enforce Ethical Standards

Some alternative brokers claimed that many of the practices that injured their businesses, including disparagement and solicitation of their listings by other brokers, were violations of the Realtor's Code of Ethics. As such, these alternative brokers would have liked their respective Boards of Realtors to take action against the offending brokers. However, some alternative brokers claimed that some Boards of Realtors would not enforce their standards when an alternative broker complained about a traditional broker. Of alternative brokers responding to this section of the survey, 19 percent said that it was "frequent" for the Boards of Realtors to refuse to enforce their ethical standards. Comparing MLS alternative brokers with non-MLS alternative brokers, the figures were, respectively, 23 percent and 15 percent.^{476/}

(5) Lost or Cancelled Listings

One of the relatively frequent complaints of alternative brokers was that they have lost listings or had sellers cancel their listings because of disparagement of their businesses by other brokers. While more than 80 percent of both MLS and non-MLS brokers said that this problem affected their businesses, it was more often mentioned as "frequent" by MLS brokers. Fifty-eight percent of MLS brokers responding to this section of the survey indicated that the problem was "frequent." Thirty-seven percent of non-MLS alternative brokers stated that the practice was "frequent."^{477/}

d. Change in Frequency After First Year of Operation

(1) In General

In an effort to distinguish among problems experienced primarily by new entrants as opposed to long-term structural problems, we asked responding alternative brokers to state the frequency of the occurrence of the problems for both their first year in operation and the year in which they responded to the survey, 1979. In comparing the results, we have calculated the change in the percentage of responding alternative brokers who felt the problem was "frequent." The percentage change is listed in Table IV.E.1. under the column "Change From First Year" for the "frequent" responses relating to the "present" year, 1979. The categories of responses, according to whether the "frequent" responses decreased, remained relatively stable, or increased, are discussed below.

^{475/} Id., Problem No. 3.

^{476/} Id., Problem No. 10.

^{477/} Id., Problem No. 5.

(2) Problems Decreasing Significantly
in Frequency

Most practices were reported as "frequent" more often in the first year of operation than in subsequent years of operation. The problem which appeared to decrease the most is "unfair grievance proceedings or legal action." The "frequent" responses by alternative brokers decreased 38 percent from the first to subsequent years of operation. The decrease in frequency of this problem was closely followed by the problems of "vandalism" and "angry criticism or personal threats."^{478/}

(3) Problems Showing Little or
No Decline in Frequency

Four of the problems listed on the alternative broker survey showed a decline in "frequent" responses of less than 10 percent between first and subsequent years. These were all of the problems dealing with loss of the alternative brokers' listings, refusing to show listings, and changing the terms of cooperation.^{479/}

(4) Problems Increasing
in Frequency

Three problems covered by the alternative broker survey showed an increase in the relative number of "frequent" responses from the first to subsequent years. These three problems were those which related to alleged institutional discriminatory behavior by state real estate commissions or by the Boards of Realtors.

The problem showing the largest relative increase in frequency was alleged "refusals by state agencies to enforce state law standards to protect [alternative brokers]." From a "first year" response of 18 percent, this problem increased 28 percent to a "present" year "frequent" response of 23 percent.^{480/}

The other two problems which increased in frequency were alleged "refusals by Board of Realtors to enforce ethical standards," and "discriminatory law enforcement by state agencies against [alternative brokers]." These showed increases of 19 percent and 16 percent, respectively, in the number of responding alternative brokers claiming that this was a frequent problem.^{481/}

^{478/} See Table IV.E.1., Nos. 1-3.

^{479/} Id., Problem Nos. 5-8.

^{480/} Id., Problem No. 11.

^{481/} Id., Problem Nos. 10, 12.

e. Problems Relating to Advertising

(1) Refusals by Media to Run Advertisements

Among alternative brokers responding to our survey, 34 percent indicated that they had experienced refusals by the media to run their advertisements or requirements by the media that they change their advertisements substantially.^{482/} Interviews with alternative brokers indicate that these problems were usually associated with advertisements that compared the alternative broker's commission rate with that charged by most of the brokers in the community. The alternative brokers often expressed the opinion that the media which were involved may have been concerned about boycotts by other brokers who also buy advertising space or time from such media.^{483/}

Threats by traditional brokers to boycott a publication or statements by a publication that it fears a boycott or has been threatened with one are usually not in a written form. However, the publisher of Homes magazine did state such fears in writing. After a Marlton, New Jersey alternative broker had advertised his \$950 flat fee brokerage services in Homes magazine, then published by R.L. White Company, he received the following letter from the publisher:

Homes magazine is produced for the exclusive use of local Realtors and Agents. Your ad . . . does not qualify.

Our publishing policy is not to accept any advertising that may result in loss of business. [Your] advertising is controversial and we are threatened by loss of revenue because of your advertising. I am sure you can find other media to advertise [your] property.

A subsequent telephone conversation with the publisher by the particular broker allegedly confirmed that the refusal to print the advertisement was due to a threat from the traditional brokerage community to boycott the publication.^{484/}

(2) Denial of Governmental Approval

Alternative brokers have also alleged problems relating to the approval of their advertisements by state real estate commissions. Such problems apparently sometimes are associated with licensing laws that require state clearance for advertising "advance fee" brokerage plans. Some feel that the clearances discourage comparative price advertising.^{485/} Among alternative brokers responding

^{482/} Alternative Broker Survey, V.15.

^{483/} See, e.g., Boston In-Depth Study.

^{484/} Dale Strack materials, November 20, 1979; see Appendix D, at 28.

to this section of the survey, 20 percent indicated that they had been denied approval by government agencies for their advertising, or that they had been required to change their advertisements substantially.^{486/}

f. Consumers' Views of
Discount Brokers

Because sellers are the ones who must make the decision to list with a traditional or an alternative broker, the reasons they do not list with alternative brokers are highly relevant to the success or failure of such brokers. Sellers surveyed by our consumer survey were asked to indicate the "single most important reason other people who are selling their home might not list with a discount agent."^{487/} The most common category of response, given by approximately 22 percent of sellers, made reference to lack of service(s) in selling the home. The second most common category of response, indicated by approximately 14 percent of sellers, made reference to problems of exposure of the property, including the availability of an MLS. The third most common category, indicated by approximately 13 percent of sellers, concerned unethical or unprofessional behavior suspected of such brokers.^{488/}

Comparing sellers who had actually contacted discount brokers with those who were aware of discount brokers but did not contact them, the survey indicates that those who had contacted discount brokers were less concerned with lack of service but were more concerned with the exposure of their properties. Significantly more sellers who had actually contacted discount brokers and presumably, more seriously considered the pros and cons of listing with such alternative broker felt that the ability of the agent to list on an MLS was very important.^{489/}

g. Analysis of Problems

(1) In General

Many experienced brokers believe that charging the prevailing commission

^{485/} See Appendix D at 28.

^{486/} Alternative Broker Survey, V.14.

^{487/} FTC Consumer Survey Exhibit, Seller Question 27. See also note 2, supra.

^{488/} Id.

^{489/} Seventy-five percent of the sellers who "contacted" a discount agent (Question 23) indicated that "Agent's ability to place home on multiple listing service" was "very important" (Question 20). Fifty-nine percent of sellers who had no "contact" with a discount agent indicated that the MLS was "very important." FTC Consumer Survey Exhibit, Seller cross-tabs of Question 23 by Question 20.

rate, usually 6 percent or 7 percent, is necessary to make a reasonable income. They maintain that the cyclical nature of the housing market may allow brokers charging less to survive during very active, rising markets, but that such brokers will generally not survive cyclical recessions.^{490/}

On the other hand, some who have studied the residential brokerage industry believe there is another reason for the failures of brokers who charge less than the prevailing commission rate:

The typical residential brokerage office is so dependent on other firms (largely because of its dependence on multiple listing service arrangements) that price competition in commissions would mean disaster. Relative commission levels have not been a major factor in determining the choice of broker by potential home sellers. Given the absence of price competition the general public finds it difficult to discover major differences between brokerage offices.^{491/}

Our evidence lends some strength to the latter hypothesis. The major theme of this report is that interdependence among brokers is the primary reason that price competition in commission rates can be a self-defeating business strategy. The problems reported by alternative brokers and the reasons consumers give for not listing with "discount" brokers are explained both as effects of interdependence and as the results of individual and institutional efforts to "deal with" perceived threats to the customary functioning of the industry.

The problems are discussed below by the categories in which they were arranged above.

(2) The Most Frequent Problems

General disparagement of their businesses was the most frequent problem alleged by alternative brokers. While this problem decreased after the first year, it allegedly still remained very frequent. That problem is closely associated with several other important problems. For example, the fourth most frequent problem alleged was lost or cancelled listings resulting from disparagement. This problem did not decrease significantly over time and was especially felt by MLS alternative brokers. It will be further discussed in section (3) below.

General disparagement of the business may also be associated with the third most important reason consumers gave for not listing with the discount broker. Many believe that such brokers are unethical or unprofessional. The disparagement, therefore, may affect the overall consumer response to price advertising. Less than "standard price" could possibly be a signal meaning "unethical behavior" to some consumers.

An example of possible disparagement given in Section 3.b(4), above, made

^{490/} See, e.g., C. Wallace, President, California Association of Realtors, California Real Estate (April 1979), at 27.

^{491/} N. Miller, "The Changing Structure of Residential Brokerage," California Real Estate (September 1979), at 22, 25.

reference both to allegedly unethical conduct by the alternative broker and the alleged decision of other brokers not to show or sell homes listed with the alternative broker. To the extent that disparagement consists of advising consumers that other brokers may not show the homes of the alternative broker the "disparagement" may, in part, consist of factually accurate statements. The third most frequent problem mentioned by alternative brokers in fact was the refusal by other brokers to show the homes listed by alternative brokers. Among consumers surveyed, the need for exposure of the home and the availability of the MLS were important reasons why many consumers would not list with discount brokers. Exposure of the home was of even more concern to those who had actually been contacted and, presumably, seriously considered using a discount broker. And this, of course, is a legitimate concern in light of the low percentage of cooperative sales and the relatively low percentage of listings sold reported by the alternative brokers.

General disparagement of the business, therefore, may be a serious concern but its long-term significance may lie in its relation to two more specific problems: possible refusals by other brokers to show the homes of the alternative brokers and listings lost or cancelled due to disparagement. These problems are discussed further in this section and in section (3), below.

The consumer belief that commission rates are fixed by law or are otherwise non-negotiable was the alternative brokers' second most frequently mentioned problem. Our consumer survey also demonstrated the extent of this consumer misperception. Because fee schedules historically existed in the real estate industry and because price competition among brokers generally has not been a successful competitive strategy, it is understandable that many consumers might believe that commission rates are in fact non-negotiable. Dispelling consumer beliefs that it is illegal or unethical to charge a lower commission rate might increase the response to price advertising, which, in turn, might make price advertising and price competition more attractive competitive strategies. The belief that charging a lower commission rate is illegal or unethical may be one reason many consumers express distrust of discount agents as a class.^{492/}

Refusals by other brokers to show the homes listed by the alternative brokers was the third most frequently mentioned problem. Unlike general disparagement of alternative brokerage, this problem allegedly did not decrease significantly after the first year. This problem also may be a primary factor contributing to the low cooperative sales rate and low overall sales rate of listings by alternative brokers.

In our hypothesis of the interdependence of brokerage competitors, brokers have an individual financial incentive to engage in this behavior. Brokers considering which homes to show buyers have an immediate interest in maximizing their return in terms of the commission split offered to them by the listing broker. These cooperating brokers also would appear to have a long-term interest in not dealing with brokers whom they believe pose a threat to their customary way of doing business.

^{492/} Thirteen percent of sellers surveyed indicated that possible unethical or unprofessional behavior might be the "single most important reason other people who are selling their homes might not list with a discount agent." FTC Consumer Survey Exhibit, Seller Question 27.

(3) Problems More Frequent for
MLS Alternative Brokers

In general, all problems reported by alternative brokers were more serious for alternative brokers who participated in the MLS than for those who did not. This may explain why alternative brokers are more often non-MLS brokers. Further, it is consistent with the hypothesis of interdependence through the MLS system.

"Discriminatory" splits was a problem alleged to be relatively common for MLS alternative brokers, but it decreased after their first year of business. The issue whether such conduct by traditional brokers constitutes price fixing in violation of the antitrust laws depends on the facts surrounding such conduct.^{493/}

Allegedly unfair grievance proceedings or legal actions were also reported by MLS alternative brokers much more than non-MLS alternative brokers. This probably is a statistical artifact resulting from the requirement that, in order to gain access to most MLSs, one must become a member of the Realtors' Association. In becoming Realtors, brokers agree to subject themselves to the grievance procedures of that group. Non-MLS alternative brokers can avoid this exposure simply by not becoming Realtors. Fewer than 50 percent of alternative brokers surveyed were Realtors.

Complaints by alternative brokers that Boards of Realtors refused to enforce their ethical standards were much more common for MLS alternative brokers. Again, the reason is probably because MLS access often is conditioned on Realtor membership. While this problem was considered a frequent one by only 19 percent of alternative brokers during their first year of operation, it allegedly increased in frequency in subsequent years. The importance of this problem may lie in its relationship to other problems. Specifically, many problems, such as disparagement, likely are violations of the Realtors' Code of Ethics.^{494/} If Boards enforce their ethical standards to protect both traditional and alternative brokers, the frequency of problems reported by alternative brokers should be reduced.

Failures of Boards to enforce their ethical standards uniformly, as well as unfair grievance proceedings and arbitrations, were often alleged by alternative brokers to relate to the composition of the Boards' arbitration and grievance committees. These committees, which are responsible for decisions in grievance proceedings and arbitrations, are composed of Board members. These Board members, being brokers in the local community, may have difficulty being "disinterested" parties. They are often direct competitors of the alternative brokers. Moreover, competing by lowering commission rates traditionally has been disfavored by most brokers.^{495/}

MLS alternative brokers also reported experiencing lost or cancelled

^{493/} See Penne v. Greater Minneapolis Area Board of Realtors, 604 F.2d 1143 (8th Cir. 1979).

^{494/} See NAR, Interpretations of the Code of Ethics (1976), Articles 21 and 23, at XII.

^{495/} See, e.g., D. Moore, "Commission Cutting Hurts Future Sales," reprint from NAREB, Brokers Roundtable, in California Real Estate (September 1965), at 32. See also Ch. IV, Part G below.

listings resulting from disparagement more often than non-MLS brokers. One likely reason this problem may affect MLS alternative brokers more is that distributed a convenient list of the alternative brokers' clients to the competing brokers in the community. Brokers in certain communities who are inclined to solicit the clients of others may feel there is a lower risk of a successful grievance proceeding or other group reaction against them for such conduct if they solicit clients of an alternative broker rather than those of a traditional broker.

(4) Change in the Frequency
of Problems After the
First Year of Operation

Many of the problems mentioned by alternative brokers were alleged to be most extreme during the brokers' first year of operations. Others, however, were alleged not to decrease; some even to increase in frequency.

The problems alleged by alternative brokers often involved conduct by other brokers. This conduct, if it does take place, must often take time from, or otherwise involve an expense to, the broker engaging in such conduct. As such, one might expect it to gradually be perceived as self-defeating unless the individual broker engaging in the conduct received a reward from such conduct which more than offset its cost.

"Angry criticism or personal threats," "vandalism," and "unfair grievance proceedings or legal action," the problems which were alleged to decrease the most in frequency, all involve substantial individual effort by another broker. Furthermore, there seems to be relatively little monetary reward to a specific broker for engaging in such conduct. While the community of traditional brokers as a whole may "benefit" if an alternative broker fails, the financial returns to any individual broker engaging in the alleged harassing conduct may be less than the costs of such conduct. Unless the costs of harassment can be equitably spread, there is a "free ride" problem which, in theory, should discourage individual effort.

While a community of traditional brokers might try to organize a group response to entry by an "alternative" firm, coordinating and policing such a group response might be difficult. The alleged problems of harassment, therefore, may be more akin to artificially erected barriers to entry than to permanent structural biases which work against alternative brokers who seek to introduce price competition. Once those barriers are hurdled, their importance may quickly recede.

The reported problems which showed a relatively stable frequency -- "lost listings resulting from other licensees soliciting your clients," "alteration by other brokers of your terms of cooperation," "lost or cancelled listings resulting from disparagement," and "refusals by other brokers to show homes listed by your business" -- all involve individual broker conduct for which there is a specific reward for the broker's efforts. The broker engaging in the conduct alleged is either attempting to acquire a listing or he is attempting to increase his or her income in the form of a commission split. Because these problems are self-rewarding, they may be much more important as long-run structural defects which prejudice price competition. All of these problems are closely associated with the MLS system. They involve the distribution of competitive information to potential cooperating brokers, and they involve the cooperating broker's compensation. These problems also are indirectly related to the alleged refusals by the Boards of Realtors to enforce ethical standards. Th

alleged problems relating to lost listings may be partially alleviated by the Boards' grievance procedures if these are available to alternative brokers on a non-discriminatory basis.

"Refusals by Board of Realtors to enforce ethical standards," "refusals by state agencies to enforce state law standards to protect [alternative brokers]," and "discriminatory law enforcement by state agencies against [alternative brokers]," problems which allegedly increased in frequency, are all institutional in nature. That is, these are problems with the Boards of Realtors and the states, and not problems directly involving individual broker conduct.^{496/} While these problems were not among the most frequently alleged, their institutional character could make them quite severe. Discriminatory law enforcement against alternative brokers could, of course, result in competitive disadvantages to alternative brokers, including, but not limited to, the suspension of the broker's license. Refusals by either the Boards or the states to enforce standards to protect alternative brokers could result in all of the other problems increasing markedly in frequency. Further, the threat of such problems could have a serious chilling effect on those forms of competition that brokers feel might lead to such problems.

(5) Advertising Problems

Alternative brokers receive a very large percentage of their business as a result of advertising. As we have defined alternative brokers, most of them charge a fee which is less than the prevailing commission rate. These brokers are attempting to attract clients by offering such lower fees. If they cannot advertise this fee to the public, their competitive strategy may be severely harmed. Generally, newspapers and other media should have no direct interest in refusing to carry the advertisements of alternative brokers. It is alleged, however, that they sometimes are reluctant to carry price competitive advertising for brokerage service because they fear they may be boycotted by the local community of traditional brokers. It appears that the media may over-estimate the threat of an effective boycott.

Traditional brokers regularly use the advertising media to compete against each other. The refusal by a single firm, or even by several firms, to advertise in a particular publication should be a detriment to those individuals and a benefit to the rest of the brokerage community. Furthermore, a few traditional brokers refusing to advertise should not result in any substantial loss of revenue to most publications. Thus, unorganized boycotts by individual brokers are not likely to last very long or be very effective.

On the other hand, an organized boycott by a substantial part of the brokerage community, which is a type that can injure a publication effectively, is legally dangerous to those participating in it. Such a boycott should be detected very easily by the publisher, the alternative brokers in the community, and by state and Federal antitrust authorities. The risks to the participating brokers ought, therefore, to seem unacceptably high to them.

^{496/} Institutional response to alternative brokers may be one way traditional brokers can avoid the "free ride" problems discussed above.

(6) Consumers' Reasons For Not Listing With Discount Brokers

The consumer survey found that those who actually contacted a discount broker, and, presumably, had seriously considered listing with such a broker, were much more concerned with the exposure of their property and the availability of the MLS than those who did not contact a discount broker.

4. The Survivors

a. In General

Only 10 percent of the alternative brokers surveyed in 1979 had begun business prior to the 1974 recession. No MLS alternative broker had been in operation since before the 1970 recession. The vast majority of all alternative brokers had begun within the two years previous to the survey.

MLS alternative brokers reported a higher frequency of all surveyed problems when compared to the non-MLS alternative brokers. Because they were trying to operate within the interdependent MLS system, they were subject to more pressure to conform than non-MLS brokers, who operated outside the system. Many of the non-MLS brokers were, in effect, almost in a separate market segment located between the for-sale-by-owner segment and the full-commission broker.

In light of the poor survival record and the relatively high frequency of problems reported by MLS alternative brokers, those eight alternative brokers responding to the FTC survey who did survive the 1974 recession were somewhat more carefully studied. Their operations appear to contain elements which helped to avoid some of the problems reported by other alternative brokers.

We will look first at pertinent summary statistics for those surviving MLS alternative brokers. We will then examine their individual businesses.^{497/}

b. Summary Statistics

The eight surviving alternative brokers sold an average of 74 percent of their listings. This is substantially higher than the 62 percent of listings sold for the total sample of MLS alternative brokers. The surviving alternative had a cooperative sales percentage of 49 percent, as compared with 29 percent for the sample as a whole. This could be a key difference, but it does not indicate how they induced the other brokers to sell their listings.

The surviving alternative brokers show a ratio of their average selling price to the community average selling price of 87 percent. The entire sample of MLS alternative brokers shows a ratio of 94 percent. This is a substantial

^{497/} The eight responding MLS alternative brokers beginning business before 1974 were as follows: D. Bond, Ca.; J. Clark, Ill.; Jefferson, Ill.; T. Abraham, Mich; C. Knudsen, Minn.; R. Cook, Ok.; B. Park, Tex.; and A. Maher, Va. The statistics in this section were manually derived from the survey returns of these brokers. Individual statistics are kept anonymous.

difference and could be a source of inducement to traditional cooperating brokers to sell the alternative brokers' listings. On the other hand, we do not know that the homes listed by alternative brokers are comparable to those listed by traditional brokers.

c. Individual Statistics

The surviving MLS alternative broker with the lowest commission fee charged a flat fee of \$700. He split this 50/50 with cooperating brokers. Yet, he achieved a 48 percent cooperative sales ratio. His average sales price was only 78 percent of his community average. Furthermore, 25 percent of his cooperative sales involved other brokers purchasing the homes listed with him for their own accounts.

The surviving MLS alternative broker with the highest percentage of cooperative sales, at 70 percent, offered cooperating brokers the going 3 percent split.

The surviving MLS alternative broker with the highest percentage of sales to listings, at 98 percent, lived in a relatively small community where the MLS may have been less important. In a small community with relatively few brokers, the chance of a prospective buyer contacting the broker directly is generally higher. Therefore, steering by cooperating brokers might have less effect on the alternative broker's business.

Two of the eight survivors operated under plans which varied the commission rate to the seller depending upon whether a cooperating broker was used. The sellers paid for the cooperating broker only if such broker was used; in those cases, they paid the going rates. Yet, the sellers had the possibility of a very low commission rate if theirs turned out to be an in-house, non-cooperative sale.

One of the above alternative brokers varied the commission rate not only according to whether a cooperating broker was used, but also according to whether the seller showed the home or the broker showed the home. This firm also offered a buyer's package. Buyers who purchased a home listed on the MLS through this firm received a 2 percent rebate if the home was originally listed at 6 percent. This alternative broker, therefore, price competed for both sellers and buyers.

This marketing plan appears to work well. This firm had the highest average home selling price of all alternative MLS brokers surviving the 1974 recession. The average selling price was claimed to be no different than that for the community as a whole. The firm had the highest percentage of cooperative sales, 70 percent, of any surviving MLS alternative broker. This alternative broker also claimed an 85 percent sales-to-listings ratio, which is quite comparable to most traditional brokers.

This firm not only survived, but is alleged by its principal to be highly profitable, more profitable than a traditional brokerage firm of comparable size.^{498/}

The listing and selling format of the above alternative broker is highly significant. While it is only a single sample, it may be a model of how price competition can take place within the MLS structure. This apparently successful business format not only competes in price for both sellers and buyers, but it also avoids many of the problems of "reverse competition" which generally

^{498/} See A. Maher, 4-3-2-1 Realty, Alternative Broker Survey return No. 39 (Va.).

characterize the MLS and split form of compensation to cooperating brokers. This firm's buyer's plan allows for the broker to simply pass any reduction in split from a listing broker along to the buyer in the form of a reduced rebate. Thus, this alternative broker has less incentive to steer away from listings providing lower splits.

5. Conclusion

The experiences of the alternative brokers are consistent with our hypothesis of broker interdependence through the MLS. Those alternative brokers who have survived the longest appear to have either avoided the MLS or found business formats which cope with the problems resulting from interdependence, especially steering.