
HOW DO U.S. RESIDENTIAL BROKERAGE TRENDS & FEES COMPARE TO THE REST OF THE WORLD?

by Natalya V. Delcours & Norm G. Miller

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INTRODUCTION: PRESSURES FROM THE INTERNET

There are many sweeping changes in the way business is conducted in all industries as a result of the Internet. The real estate industry is no exception. According to the 2000 National Association of REALTORS® Profile of Home Buyers and Sellers, in 1999, 37 percent of homebuyers used the Internet as a key source of information in their home purchase process, a 19 percent increase from 1998. It appears that in 1999 the U.S. real estate industry has become more Web-based despite the fact that four out of five customers used real estate agents in their home purchase process. If this trend continues, and more consumers use the Internet as the primary source in their real estate information search and purchase, real estate professionals may face a decrease in commission fees and a reduced demand for their services.

Technological innovation (voice mail, e-mail, cell phones, pagers, Web presence, etc.), has empowered consumers in their real estate information search and purchase decisions, and prompted the development of virtual real estate brokerages offering "ala carte" services to their customers. Cyber brokers, (*i.e.*, www.4Sale-ByOwners.com, www.FSBOFreedom.com, www.FISBODepot.com), provide customer services such as:

- free 24-hour-a-day access to property listings;
- different property listing fee alternatives, including promotional packages;
- a FSBO site index;

- blank pre-formatted real estate contracts and forms;
- virtual sale negotiations including instant contract formulation; and
- many other resources for homeowners.

For a traditional real estate firm to compete with cyber brokers, it has to perceive that the Internet expands capabilities and is a vital tool for achieving greater service, cost efficiency, and profitability, thus turning the technology into a source of new empowerment rather than threat to its existence. One tactic often exercised by traditional real estate firms to defend against the cyber brokers is to buy the more successful private MLS style networks. The consolidation process among traditional and newer real estate companies with a Web-presence can be already observed. For example, the www.cyberhomes.com Web site links to www.homeadvisor.com, which is owned by Microsoft Corporation. Also, Cendant Corporation owns www.homebytes.com, and www.coldwellbanker.com, and they recently acquired www.owners.com.

Successful real estate companies may gain several advantages if they efficiently use automated communication and information technology to attract and serve customers. Web-based programs like www.valueyourhome.com can estimate prices or market price trends and provide neighborhood information. Other online programs can set up appointments, transmit contract offers and counteroffers, provide mortgage assistance, and much more. Ancillary and complementary services including relocation, title insurance, landscaping, property insurance, and more can produce referral fees or new profit centers that many large traditional brokerage firms already attempt to capture, but the Web makes it easier to track the flow of information requested and to instantly offer potential services. Traditional firms that will survive have no choice but to embrace all the possibilities for new services and efficiency gains in order to compete in the future.

Investment in technological innovations requires cash outlays. There are economies of scale to such investments and small firms with no affiliations may have to look for assistance to support this investment. Thus, there is a potential for further consolidation trends in the real estate brokerage industry as smaller real estate companies look for a potential acquirer that will allow them to stay in business.

Another possibility for traditional real estate companies to survive the increasing competitive pressure from “lean and mean” cyber brokers is to mix traditional and non-traditional listings. For years U.S. real estate brokerage companies successfully operated through strong local, state, and national trade association representation (the National Association of REALTORS) and provided the core of the Multiple Listing Service (MLS) system. Most real estate agents belong to more than one MLS. Over the years, the access to MLS and strong interdependency among industry participants ensured high real estate commission fees in the U.S. compared to other countries and promoted a stable rise in the U.S. real estate agents’ compensation.¹ However, open listing MLS services and the development of cyber brokerages challenge the market information monopoly once held by traditional real estate companies and encourage commission price competition within the industry.

Until recently the majority of traditional real estate firms with a Web presence prohibited For Sale By Owner (FSBO) listings. However, there are exceptions. For example, www.owners.com, which was acquired by www.homebytes.com in October 2000, is the biggest FSBO database in the U.S. Also, open MLS vendors are starting to encourage commission price competition in residential real estate. Several Internet-based real estate companies charge fees of 3 percent to 5 percent instead of the 6 percent or 7 percent traditionally charged by real estate firms. Some cyber brokers charge a home seller 4.5 percent, the homebuyer agent receives 3 percent, and the company keeps 1.5 percent. Technological innovations allow real estate brokers to speed up Comparative Market Analysis (CMA) report generation, the contract negotiation process, thus making the real estate professional more efficient and productive.

BROKERAGE FEES AROUND THE WORLD

The evaluation of the commission rates in foreign countries (*Exhibit 1*) indicates that the real estate commission rates are lower when the information within the market is more efficient, open, and reliable. Less developed countries, like Russia, with costly information dissemination processes hampered by high bureaucracy and/or no MLS system, exhibit the highest commission rates (10 percent or even 15 percent). The economic efficiency is proxied by GDP per capita and compared to the median commission fees among 30 countries (*Exhibit 2*). The graphical representation of the relationship between $GDP/capita = f(\text{Real estate commission})$

International Commission Rate Comparisons

Country	License	Real Estate Transaction Characteristics	Compensation	Typical Sales Per Agent	Internet Impact
Argentina**	yes	6%, where 3% paid by the buyer, and 3% paid by the seller; does not require buyer broker.	commission	n/a	n/a
Australia	yes	5% on the first \$18,000, 2.5%-thereafter; also properties are sold through auction system; advertising is provided by real estate agent.	commission & auction	30	no significant impact
Belarus	n/a	6%-15% commission, averaging near 10%. Public information is scarce.	commission	n/a	n/a
Brazil	yes	5% commission, less on a higher priced units.	commission	n/a	n/a
Canada	yes	3-6% commission rate.	commission	30-50	no significant impact
Caribbean**	yes	5% - Jamaica, 3-5% - Trinidad & Tobago.	commission	n/a	n/a
China**	yes	No set regulations and standards for real estate transactions.	n/a	n/a	n/a
Denmark**	yes	2-4%, buyer pays 25% of sales price transfer tax; advertising is provided by real estate agent.	commission	n/a	Large impact on MLS
Finland	n/a	Fees run about 5% of the sale price on condos and 3%-4% - on a single family home. Higher priced houses have lower commission fees. Also, government collects value added tax (22% of the selling price).	commission	n/a	n/a
France**	yes	Only 50% of property listed with real estate agents; real estate transactions are kept very private; 50% of real estate is sold FSBO.	commission	n/a	MLS is encouraged
Indonesia**	no	5% paid by either buyer or seller, but not both; buyer broker is required for real estate transaction.	commission	n/a	n/a
Ireland**	yes	In cities - 1.5-2%, small towns - 2-3%; also properties can be sold through auction system.	commission & auction	n/a	n/a
Israel	yes	4% commission rate equally split between buyer and seller agents.	commission	n/a	growing impact
Italy**	yes	Paid by both buyer and seller; each party pays 2-3%.	commission	n/a	n/a
Japan**	yes	3% commission rate.	commission	n/a	n/a
Malaysia**	yes	3% on the first \$100,000 and then 2% of the remaining amount of the sale, commission is paid either by buyer or seller, not both.	commission	n/a	n/a
Mexico**	Varies	5-10% commission rate.	commission	n/a	Large impact on MLS
Netherlands**	yes	1.5-2%, broker represents either the buyer or the seller but not both.	commission	n/a	n/a
Norway**	yes	2-3%, broker represents both parties in the transaction.	commission	n/a	n/a
Philippines**	yes	5%, broker represents either the buyer or the seller but not both.	commission	n/a	n/a
Russia	yes	5% to 10% but "net listings" common; advertising is provided by real estate broker/agent; FSBO very common; buyer broker representation is not required.	fee above net	n/a	absolutely none
Singapore	yes	1.5-2.0%, FSBO very rare; buyer broker representation is not required.	commission	20-40	slight - for marketing
Spain	yes	Commission rate depends on the property location, averaging 5% of total estate price.	commission	n/a	n/a
Sweden**	yes	5%, commission is paid by seller, 10% commission is charged for lower priced units.	commission	n/a	n/a
United Kingdom	yes	1%-2%; in very competitive areas - 0.5-0.75%; in low priced areas - 3.5%; advertising is provided by real estate broker/agent; buyer broker representation is not required.	commission & auction	60-100	no significant impact
United States	yes	6%-7%; advertising is provided by real estate broker/agent; in 1999 - 6% of the residential real estate transactions were "FSBO" - excluding builder sales but the FSBO success rate appears to be climbing rapidly in 2000 and 2001.	Most commission; Some charges flat fees or 2% to 4%	4, 3* while top agents do 20 or more.	Rapidly increasing.

* This number is calculated as Total home sales in 1999 (according to NAR Profile) is 6.5 million. According to NARELLO, in 1999, there were 515,225 active real estate brokers and 980,083 active real estate agents. ** Information is obtained from <http://onerealtorplace.com>. *** Jamaica, Trinidad and Tobago

Exhibit 2

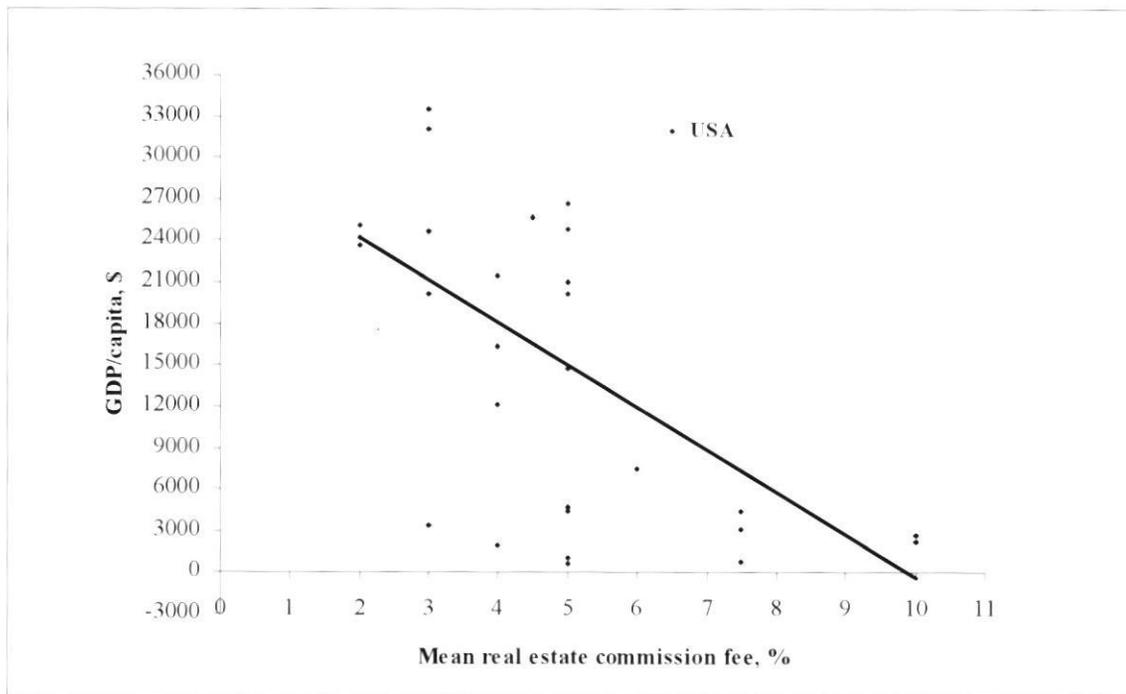
List of Countries, Average Real Estate Commission Fee, &
Per Capita GDP, 1999

Country	Mode Real Estate Commission Fee, %	1999 GDP/per Capita, \$
Argentina	6.00	7,550.00
Australia	5.00	20,950.00
Belarus	10.00	2,620.00
Belgium	3.00	24,650.00
Brazil	5.00	4,350.00
Canada	5.00	20,140.00
Caribbean	5.00	4,750.00
China	7.50	780.00
Denmark	3.00	32,050.00
Finland	5.00	24,730.00
Germany	4.50	25,620.00
Greece	4.00	12,110.00
Indonesia	5.00	600.00
Ireland	4.00	21,470.00
Israel	4.00	16,310.00
Italy	3.00	20,170.00
Japan	3.00	32,030.00
Malaysia	3.00	3,390.00
Mexico	7.50	4,440.00
Netherlands	2.00	25,140.00
Norway	3.00	33,470.00
Philippines	5.00	1,050.00
Russia	10.00	2,250.00
Singapore	2.00	24,150.00
South Africa	7.50	3,170.00
Spain	5.00	14,800.00
Sweden	5.00	26,750.00
Thailand	4.00	2,010.00
United Kingdom	2.00	23,590.00
United States	6.50	31,910.00

Note: The data was obtained from the World Bank Group Web site
(<http://www.worldbank.org>)

Exhibit 3

Average Real Estate Commission Fee vs. Per Capita GDP



Note: The data was obtained from the World Bank Group Web site (<http://www.worldbank.org>)

Statistical results:

Regression F statistic 12.918

R-squared = .316 Adjusted R-squared = .291

Beta Coefficient on Fee -.562 t = -3.594 significance = .001

Note the beta coefficient in this case is also the correlation between GDP and Fee.

K-S test 1.067 on GDP 1.269 on Fee Chi-Square test = 17.400

fee) is presented in *Exhibit 3*. The model exhibits good explanatory power (R-squared equals to approximately 32 percent). As it has been anticipated, the estimated beta coefficient is negative and statistically significant ($b = -.562$, P-value is .001, $t = -3.544$). The statistical results provide the evidence that in the foreign countries, commission rates are lower as information dissemination within the market becomes more efficient.

Also, there are other implications of price competition in the real estate industry. For example, lower price homes should see higher commission rates relative to higher priced homes. Such pricing approach is employed in Sweden, Finland, Ireland, Mexico, and Belarus. We should also see more marketable and higher priced homes listed at lower percentage commission rates, similar to those in the

United Kingdom, Singapore, and other developed countries. More developed markets rely upon a regulatory environment to facilitate the accuracy of the real estate transfer price and protect both parties involved in the transactions.

An alternative to the MLS system exists in UK, Ireland, and Australia: MLS brokered sales and auction sales. In these markets, the public auction system is not viewed as a reserve for the selling of distressed properties. Rather a public auction system is viewed as a positive alternative to the MLS.

CONCLUSIONS

The real estate industry seems to be undergoing an evolution of great significance. Consumers have become a driving force behind the real estate search process when they gather preliminary information

on property via the Web. More information is available than ever before and virtual touring is becoming the standard expectation, not only among cyber real estate companies, but also among traditional real estate firms as well.

As traditional brokerage firms use more automated services and expert systems to serve both consumers and agents offering a range of service packages they will become more efficient, enabling successful agents to serve more clients. The cost of the full service agent should decline to 5 percent or so within the next decade and possibly to as low as 2 percent or 3 percent within the next two decades — provided the fees in other countries are a reliable comparison. Agents in those countries where fees are lower make as much or more income than agents in the U.S., but there are certainly fewer real estate agents in those countries. A drop in the commission rates to a 3 percent range will likely drive more than half of the existing marginal producers out of the industry. This “weeding-out” process is likely to result in a more professional and experienced agent becoming the norm. For consumers, this is the greatest benefit from price competition.^{REI}

NOTES

1. This is a result of home prices rising faster than inflation over the past 30 years.

REFERENCES

- Delcours, N. and N. Miller, “The Future of the U.S. Residential Real Estate Brokerage Industry in Light of the Internet and International Indications,” working paper.
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