

Federal Trade Commission
A Staff Report by the Los Angeles Regional Office

The Residential Real Estate Brokerage Industry

Volume II

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1. Introduction

The Real Estate Brokerage Investigation (File No. 762-3052, Unnamed Real Estate Brokers and Others) is a nationwide investigation of the residential real estate brokerage industry. The Los Angeles Regional Office of the Federal Trade Commission, working in conjunction with the Seattle Regional Office, conducted the investigation, which was jointly sponsored by the Bureaus of Consumer Protection and Competition. The project responsibility was assigned to the Los Angeles Regional Office on February 17, 1978.¹ The assignment was announced in an FTC news release, dated March 31, 1978.²

The purpose of the investigation was to determine how competition is working and how the consumer is served in the brokerage process. Several initial decisions as to the scope of the project were made at the outset. First, we determined to focus on residential brokerage practice, as opposed to commercial real estate, property management, and other activities of real estate brokers. This emphasis is consistent with the consumer protection mission of the agency, and allowed us to focus on the practices of the majority of members of the brokerage community.³

Second, we determined to focus the investigation on patterns of structures and practices throughout the nationwide industry, as opposed to individual practices or anecdotal problems. Our investigation has borne out our initial hypothesis that common structures and practices exist throughout the entire industry. Since no project of this scope could canvass all the practices or problems of the more than two million brokers and agents in the nation, we focused the study on these macro-patterns.

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- 1 Commission examination of real estate brokerage actually preceded that date; See "FTC to Investigate the Residential Real Estate Brokerage Industry." FTC news release (December 27, 1975). It was in February, 1978, however, that what were then several separate staff proposals were consolidated into a single investigation and assigned to the Los Angeles Office.
 - 2 "FTC Los Angeles Regional Office to Coordinate Real Estate Brokerage Investigation," FTC news release (March 31, 1978).
 - 3 The National Association of Realtors has determined that "85% of NAR members are in residential real estate." NAR, 1978 Annual Report, at 2.

Third, we determined to direct our efforts to identifying, and then investigating, the issues of greatest impact and significance. It became clear in the early stages that scores of issues could be addressed by the investigation. We chose to focus upon what we believe to be the key issues facing the industry.

We planned the investigation to take place in two broad phases. Phase One extended through approximately the first year of the project. Phase Two began in the spring of 1979 and culminated with this Staff Report. The remainder of this section will described these two phases.

2. Phase One

Phase One began with a comprehensive effort at stating the issues and questions for the project and planning its course. During this phase, we undertook a wide range of background research in order to familiarize ourselves with a complex industry. The staff surveyed the relevant legal, economic, and industry literature. Meetings and interviews were conducted with numerous industry experts, including government officials, trade association representatives of all three levels, traditional and alternative brokers, attorneys, consumers and consumer groups, and members of the academic community.

FTC headquarters staff helped organized two efforts to suggest directions and issues for the larger project. A consultant, Wayne I. Boucher, was hired to interview a wide range of industry experts, using the Delphi interviewing technique, in order to identify key issues in real estate brokerage. Accompanied by FTC staff, Boucher conducted extensive structured interviews with 18 industry figures, representing all factions of the industry.

Also, in May of 1978, the FTC and the Department of Housing and Urban Development jointly sponsored a conference on important issues in the real estate brokerage industry. Academic experts from throughout the country participated. Several were asked to prepare papers to focus the conference on the key issues. Those papers, and the transcripts of the conference, have been released publicly by the Federal Trade Commission.⁴

Also during this phase the staff initiated several long-term data-gathering efforts, including four contracts with consultants, inter-agency cooperation with federal and state officials, and contacts in selected local communities believed to be typical of brokerage practices throughout the nation.

⁴ See Commission Minutes of October 31, 1979, "In Re: FTC-HUD Seminar on Real Estate Brokers Practices."

This phase yielded a number of theories as to how the industry functions. These related to the five primary issue areas we identified as of highest priority: (1) the nature and role of private trade associations of brokers; (2) the structure and operations of multiple listing services; (3) problems facing brokers who offer innovative packages of prices and services; (4) the role of the broker in residential brokerage transactions, including issues of potentially conflicting duties and interests which may make difficult the adequate representation of consumers; and (5) the nature and role of state law and of state agencies which regulate the industry.

3. Phase Two

Phase Two of the investigation was intended to test the theories developed in Phase One. To do this, two levels of industry analysis were employed. First, in-depth studies were conducted in several local real estate markets in order to understand the degree of variation which might occur among markets. Second, information was gathered using nationwide surveys in order to provide a national overview of the industry.

Five representative sites were selected for the in-depth studies of local brokerage markets: Los Angeles, Seattle, Boston, Minneapolis-St. Paul, and Jacksonville, Florida. The criteria for selection included geographical diversity (sites in the south, the northeast, the midwest, the northwest, and the southwest were selected); diversity of brokerage structures and practices, such as prevalence of MLSs, levels of trade association activity, and the presence of alternative brokers; and proximity to FTC staff and to resources such as academic experts.

FTC attorneys and investigators traveled to each of the five study sites to conduct at least a portion of the investigative work first-hand. The investigational strategy involved interviewing carefully selected representatives from every segment of local brokerage markets. Meetings were held with government officials, including those from state departments of real estate, state attorneys general, and local officials or prosecutors who were active in the industry; trade association officials, generally including representatives from each state Association of Realtors and representatives from local Boards of Realtors in each area; traditional brokers, including representatives from large firms, small firms, and franchise firms; alternative brokers, including every active alternative broker we could locate in each area; academic experts; real estate attorneys; and other experts. In each site, staff attempted to gain a balanced overall impression and specific insights useful for the project as a whole.

The capstones of the investigative fieldwork were three major national surveys conducted by the staff.

MLS Survey -- The staff tried to survey all functioning MLSs in the nation. The survey was designed to obtain basic information about MLS structure and operations, and to test hypotheses about MLSs as they relate to the brokerage industry as a whole.

Since 90% to 95% of all MLSs are controlled by Realtor organizations, the staff determined that cooperation with the National Association of Realtors would facilitate the survey. We worked closely with NAR staff on drafts of the survey instrument, adopting many of the changes suggested by the NAR, while retaining complete control over content. After extensive cooperative efforts, we completed a satisfactory draft. The NAR distributed a special notice to its members, encouraging them to respond to the questionnaire.

The questionnaire was sent to a total of 986 multiple listing services, consisting of 931 Board-affiliated MLSs and 55 unaffiliated or independent MLSs. Participation in the survey was entirely voluntary. More than one-third of the questionnaires were completed and returned to the staff. The results were computer tabulated and analyzed, preparatory to their use in the Staff Report.

Alternative Brokers Survey -- The staff attempted to survey all active alternative brokers in the nation. An alternative broker was defined as a broker whose price or service practices varied significantly from the norm in his/her community. With regard to price variance, we determined that a variance of two percentage points or more would be necessary to be considered significant. For example, in a community where 6% was the prevailing commission rate, a broker had to charge 4% or less in order to qualify as "alternative" under our definition.

The alternative brokers survey was designed to gather information on the structure and operations of these firms, with particular emphasis on the patterns of problems and successes the brokers experienced. General market data was also sought.

FTC investigators made an extensive effort to identify active alternative brokers throughout the country. Sources included a mailing list compiled by NARESA, the loosely-organized trade association of alternative brokers; written inquiries from alternative brokers accumulated over the course of the investigation; referrals by brokers to other alternative brokers; newspaper and magazine articles and advertising; and other sources. After conducting more than 25 in-depth interviews with alternative

brokers to identify key issues, the staff drafted a questionnaire. This was mailed to more than 650 alternative brokerage firms throughout the country. Nearly 150 of the questionnaires were returned to the staff as either undeliverable or as addressed to brokers not active in alternative practice. Of the remaining group of approximately 500, a total of more than 150 questionnaires were completed and returned to the staff by alternative brokers. The results from this survey were computer tabulated and analyzed, prior to their use in our Staff Report.

Consumer Survey -- The staff conducted a nationwide survey of home buyers and sellers. The consumer survey was designed to measure the knowledge, behavior (especially home and broker search behavior), and experiences of home sellers and buyers. Basic demographic data on these consumers was also gathered to assure that the sample was demographically representative of the United States population of home sellers and buyers.

Staff contracted with the market research firm of National Family Opinion, Inc., to conduct the actual survey, using a sample of consumers participating in the NFO consumer mail panel system. Extensive collaborations between the investigative staff, economists, marketing experts, and the NFO staff produced survey instruments for buyers and sellers. The NFO contractors then surveyed more than 350 buyers and 350 sellers, and turned the results of these surveys over to FTC staff for computer analysis.

The four contractor studies set in motion in Phase One were also completed during this period. These studies included a survey of state agency law and analysis of its effect on brokerage practice (conducted by Barry Brown and Eric Green, professors at the Suffolk University and Boston University Schools of Law, respectively); a compilation of general industry data and profile of traditional brokerage practices prepared by the UCLA Real Estate Research Center, under the direction of Professor Fred I. Case; and two studies of commission rate data and other information derived from HUD-1 forms, the forms for disclosure of settlement costs mandated by the Real Estate Settlement Procedures Act of 1975.

We also sent formal notice of our investigation and invitations to comment on issues raised by the investigation to hundreds of state and local government officials throughout the nation. These officials included the chiefs of all the state departments of real estate, the state governors, the state legislatures, the state attorneys general, state consumer or consumer protection agencies, local prosecutors and other active local officials, and others. The staff received 79 responses from the notice, 55 of which contained written comments and suggestions. Five governors,

26 real estate regulatory agencies, 14 attorneys general, five district attorneys, and six state and local consumer agencies provided written remarks. These were incorporated into the staff's findings and recommendations, and are summarized in Appendix B.

The staff also continued and broadened its contacts with the trade associations, especially with representatives of the National Association of Realtors and of the California Association of Realtors, whose membership represents about one-fifth of all the nation's Realtors. A series of meetings and telephone conferences with spokespersons for both organizations was spaced over a period of more than one year. The discussions were wide-ranging and thorough, and provided information not only about the trade associations but about most of the major issues facing the industry, as well.

In addition to the Realtors' leaders, the staff met with representatives of three other trade groups of significance in the industry. We met with spokespersons for the National Association of Real Estate Service Agencies (NARESA), the informal group of alternative brokers mentioned above; with the chief staff person for the National Association of Real Estate License Law Officials (NARELLO), which is the trade group for real estate regulatory officials; and with leaders of the National Association of Real Estate Brokers (NAREB or "Realtists"), the trade association of minority real estate brokers. Each group's specialized viewpoint was thus added to our perspective.

Also during this period the staff completed its review of legal, economic, and industry literature. The staff performed a comprehensive review of trade association journals, primarily those of the California Association of Realtors, since that organization's magazine is the oldest industry journal in continuous publication. This research provided particularly useful insights into the history of the industry.