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American property

The great realtor rip-off

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Why is it so expensive to buy or sell a house in America?

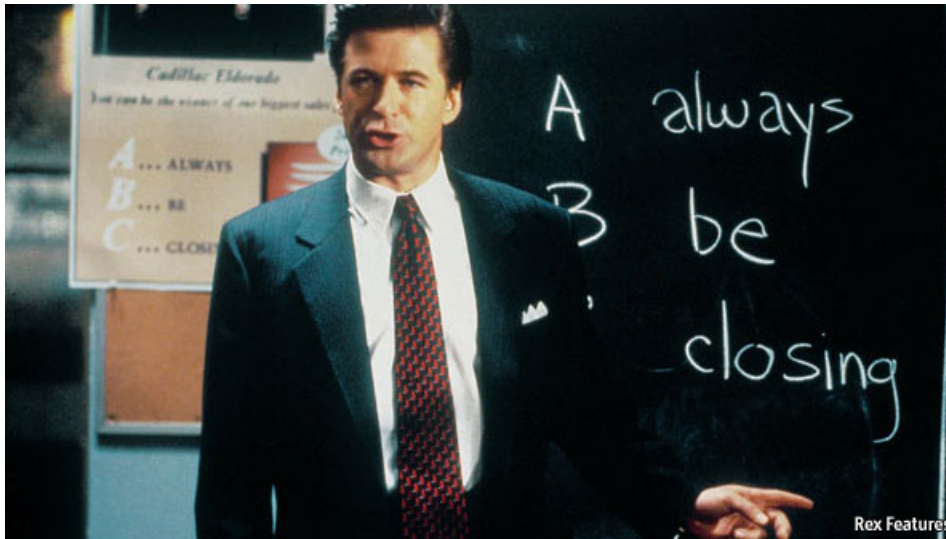
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IN BRITAIN, if you want to sell your home, an estate agent will list the property, find a buyer, help you negotiate a deal and guide you through the transaction, all for a commission of 2-3% of the sale price. In America, realtors provide the same services for roughly double the fee.

Are they worth it? The shouty realtors in David Mamet's film *Glengarry Glen Ross* (pictured) certainly think so. ("[My] watch costs more than your car...that's who I am.") Others disagree. Chang-Tai Hsieh of the University of Chicago finds that American property brokers cause "social waste" of \$8 billion a year via overcharging and inefficiency.

Economists are baffled. The internet has squelched inefficient middlemen in other industries, from insurance brokers to travel agents. Why not American realtors? Although scores of discount brokers and for-sale-by-owner websites have sprouted up, traditional full-service realtors have somehow maintained their market share of 80% without reducing fees.

The business used to operate like a series of local cartels. In a typical area, a handful of brokers controlled a shared

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database of available homes, and limited their cheaper rivals' access to those listings. In 2008 in the United States and 2010 in Canada, regulators struck deals with realtors to open up these databases. Yet since then the average commission has actually risen, from 5.0% in 2005 to 5.4% in 2011, according to REAL Trends, a research firm.

Why are high fees so persistent? One counterintuitive theory is that America's housing bust has buoyed them. Selling a home is easy when prices are rising. But when financing dries up and volumes dip, sellers may need an agent's expertise and energetic marketing to find a buyer.

Never give a sucker an even break

Another theory is that clients are suckers. Agents routinely tell buyers not to worry about the fat commission because "the seller pays it." Meanwhile, they tell sellers not to worry because they will jack up the price of the home to cover it. According to Steve Murray of REAL Trends, two-thirds of clients choose an agent because of a prior personal relationship or referral. They may be reluctant to haggle with realtors to whom they have social ties.

A third theory is that the industry is less competitive than it looks. In most areas a few big brokers handle most transactions. They set high fees, which lure ever more people into the profession: between 1998 and 2005 the number of members of America's National Association of Realtors grew by 67%. These agents waste time competing with each other for the exclusive right to sell each home, sapping productivity. According to Norm Miller of the University of San Diego, an average agent in Britain closes 40-50 deals a year, compared with just seven in America.

Cynics say the industry has captured its regulators. The property commissions of American states are usually made up of brokers. Perhaps this is why many states have banned commission rebates—a form of discounting—or set up "minimum-service" standards that stop brokers offering fewer services for less money.

The biggest cause, however, is probably the interdependent nature of the business. Since both the buyer and seller are represented by agents in most transactions, brokers must collaborate to close deals at the same time as they compete for listings. Buyers' agents have an incentive only to show their clients homes whose sellers offer them a standard 3% commission.

To solve this problem, many sellers' agents offer to cut their own fee while still offering the full price to the buyer's agent. Alas, word soon spreads that they are giving rebates. That makes many buyers' agents steer their clients elsewhere—either in solidarity with full-service brokers or because they fear a discounter will leave them with the lion's share of the work.

Such stealth discrimination is hard to prove: buyers' agents can always say they ignored a listing because it did not meet their client's needs. But Colby Sambrotto, the founder of ForSaleByOwner.com and USRealty.com, a discount broker, says that after trying to sell his own home in New York by himself, he was forced to hire an agent to get it shown to potential buyers.

Such retaliation is hardly universal: Mr Sambrotto says it was a "regular exception rather than the rule" for his firm's clients in most markets. But because discounters need to make up for lower commissions with higher volumes, even a small amount of discrimination is often enough to drive them out of business. The demise of the 6%

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commission may still be inevitable. But for now, it seems a long way off.

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