
Testimony of

Geoffrey D. Lewis

On Behalf of

RE/MAX International, Inc.

Before the

Subcommittee on Housing and Community Opportunity

Committee on Financial Services

United States House of Representatives

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Mr. Chairman, my name is Geoff Lewis. I am Senior Vice President/Chief Legal Officer of RE/MAX International, Inc. Thank you for allowing me to testify today on behalf of RE/MAX. More than 90,000 independent RE/MAX real estate agents in the United States sell more homes in this country than agents affiliated with any other brand. There are 4,100 RE/MAX brokerage offices in the United States. Notwithstanding this, RE/MAX International, Inc. is not engaged in the brokerage business. We are in the business of selling franchises, just like other national real estate brokerage franchising companies such as Coldwell Banker, Century 21, Prudential Real Estate and Help-U-Sell, to name a few.

All but two of the 4,100 RE/MAX franchises are independently owned and operated. I have come to speak on behalf of RE/MAX International. RE/MAX International considers itself to be extremely knowledgeable about the residential real estate brokerage business, but neither RE/MAX International nor I claim to speak on behalf of our independent brokers or agents.

Those who decry the lack of competition in the real estate industry would be prudent to follow the common sense advice applicable to every weather man. Before you broadcast current weather conditions, stick your head out the window to make sure you see what is really going on. In today's real estate market, consumers are bombarded with choices via the Internet and in the physical world. Home sellers and buyers can choose between full service, limited service, discount commissions, flat fees, rebates and other incentives.

RE/MAX knows about competition in the industry. When Dave and Gail Liniger started RE/MAX 33 years ago, they had a revolutionary new business model: let the agent keep all of his or her commissions and give them the freedom to run their business as they see fit. This came at a time when the traditional industry kept up to 50 percent of the agents' commissions and exercised tight control over how they operated.

RE/MAX knows about breaking into an industry. We know about the difficulty of overcoming an established business model. But today, more real estate is sold under the RE/MAX name than any other brand. How did RE/MAX overcome our competition and reach the pinnacle of our industry? We did it because we had a better business model

and we made it successful the old-fashioned American way, through hard work and customer service.

The marketplace recognized the value of the RE/MAX system and rewarded it. It took over ten years for RE/MAX to establish its business model. RE/MAX recognizes that the Internet has accelerated the pace of change, but new business models still take time to succeed. Those businesses who complain their success has been improperly hindered because they have not achieved instant success suffer more from impatience than they do from any alleged unfair efforts to thwart them.

Today, as always, RE/MAX welcomes competition from any legitimate business that can stand on its own merits and its own resources. RE/MAX believes there is no need for Federal Government legal or regulatory intervention in the residential real estate brokerage industry. There are virtually no barriers to entry into our industry, the Internet is enabling new business models and there is no evidence that free market forces are being impeded in any way.

COMMISSION RATES

It is often overlooked that full service agents work on a success basis. If a seller does not sell his house, he pays nothing and the agent gets a 0% commission despite the time and money invested. If a buyer does not buy a house, the agent gets a 0% commission. When an agent does earn a commission, it often comes several months after he has expended his time and money with no guarantee of closing the sale. Realtors drill a lot of dry wells.

In cases where successful transactions are completed, full-service commission rates have been trending down over the past decade. They have gone from 6.1 percent in 1991 to the current average rate of 5.1 percent. That is not a one percent decrease, it is a 16% decrease. How many other industries have experienced that level of decrease in pricing over the same period of time?

With the rapid rise in housing prices recently, many have questioned why commission rates have not come down further. The answer is that agent income has not increased correspondingly. The median gross income for real estate professionals in 2004, as reported by the National Association of Realtors (NAR) was \$49,000.¹ That is without healthcare and retirement benefits which are paid for by the agent. That is also before the agent pays for advertising, website hosting, gasoline and other expenses. Over the past two years, agent gross income is down 6 percent.² On a net basis, average

¹ The median gross income for sales agents was \$37,600 and for brokers it was \$52,800. National Association of Realtors. 17 August 2005, Press Release. "NAR Member Survey Shows Income Disparity With Rising Ranks."

² National Association of Realtors. 17 August 2005, Press Release. "NAR Member Survey Shows Income Disparity With Rising Ranks."

income is lower than average school teachers' salaries.³ School teachers receive healthcare and retirement benefits. Agents do not. School teachers get a three month summer vacation. Agents work 24/7, 365 days per year.

The lack of increase in agent income despite rising housing prices is due to the large increase in the number of agents entering the industry. NAR reported a 26% increase in membership over the past two years and a 40% increase over the past five years.⁴ In 1995, NAR reported having 1.2 million members. The Association of Real Estate License Law Officials (ARELLO) reported that there are 2.6 million licensed agents in the U.S. (that is one for every 115 people). These agents are being drawn in by the increase in housing prices. Many of these agents are coming from the downsizing that has occurred in corporate America over the past decade. Many of these agents are homemakers working part-time.

As a result of the increase in the number of agents searching for transactions, the average number of transactions per agent is decreasing. That puts resistance on the ability of commissions to continue to come down further. Nonetheless, as noted above, commission rates have decreased significantly.

INTERNET COMPANIES AND NEW BUSINESS MODELS

There is little difference between traditional companies and online companies in terms of Internet use. Traditional companies all embraced the Internet years ago and have a significant online presence. Virtually every broker and most agents have a web site that allows consumers to search all MLS listings in their market.

It is easy to say the Internet has brought down costs in other industries so it should do the same for real estate, but not all industries are the same. The Internet has not decreased prices for doctors, accountants or attorney services, newspaper subscription rates, landscaping contractors or a myriad of other businesses. Nor has it done so for government services. Not every business is going to be impacted by the Internet the same as airline ticket vendors, stockbrokers or book sellers. After all, these industries are selling commodities. Real estate agents are selling unique properties and providing individualized services.

One of the most heralded Internet start-ups in our industry is Zillow.com, a web site that provides a free home valuation service. Zillow was founded by Rich Barton who earlier revolutionized the travel industry with Expedia.com. Mr. Barton raised \$32 million in start-up capital for Zillow. This indicates there is plenty of financing available for new business models that wish to challenge the established industry. Nonetheless, Mr. Barton was quoted in *The Wall Street Journal* as saying: "Zillow faces the risk of unrealistically high expectations, as change will come much more slowly in real estate

³ American Federation of Teachers. 15 July 2004, Press Release. "Teacher Salaries Remain Stagnant but Health Insurance Costs Soar AFT Releases Annual State-by-State Teacher Salary Survey."

⁴ National Association of Realtors. 17 August 2005, Press Release.

than it did in travel and other businesses such as stock trading. That is largely because home sales typically involve lots of personalized service from agents who know their local markets and how to solve the many problems that can crop up before a transaction is completed. It isn't simply an order-taking business."⁵

The Internet has enabled hundreds of real estate companies with new business models. These companies offer rebates, flat fee services and discounted commissions. A quick search will reveal any number of national and regional companies in virtually every market. New companies appear on a daily basis. Internet giants Google, Yahoo and eBay have all jumped into the business of allowing home sellers to list their homes in online classified ads. Media titans including Tribune Company, The Washington Post Company, Belo Corporation and Gannett Company recently formed an online classified service that has a primary focus on real estate. In addition, Tribune Company recently bought HomeGain, an Internet start-up that displays property listings and locates agents. Another media heavyweight, Barry Diller's Interactive Corp., owns LendingTree, a popular web site that offers significant rebates to home buyers and sellers who locate a realtor by using the site.

It should be noted that in the last few years, we have seen one of the "hottest" real estate markets in history. In parts of the country, sellers have been able to attract multiple offers the instant their home goes on the market. Some sellers receive offers above their asking price. It is not surprising in these markets that many sellers have been tempted to avoid full service brokers in favor of limited service providers or discount brokers. It is these same conditions that have caused the explosion in these new business models. Since the beginning of this year, the market has returned to normal levels: inventories and time-on-market have increased considerably over last year.

MULTIPLE LISTING SERVICES (MLS)

The MLS was designed as a B2B vehicle, not a business-to-consumer vehicle. It was designed as a mutual sharing of information by industry peers to facilitate the sale of and search for properties. The idea was that cooperating brokers and agents would work to earn their own customers using their own assets and then share listings via the MLS. The concept is simple: you earn a customer, you get to use the MLS with the customer. The concept is not: you get free access to the MLS and then you use it to advertise the properties of your competitors in order to attract customers.

The MLS is a cooperative among brokers. A broker is licensed under state law. A broker, by law, takes on agency and fiduciary duties towards a client to represent the client's best interests through every aspect of the home sale transaction. A business that merely seeks to sell a client a yard sign and enter a property into the MLS is not acting as a broker. A business that merely seeks to attract prospective home buyers and sellers to its Internet site in order to sell the prospect's name to a real broker in exchange for a

⁵ The Wall Street Journal, Jan. 13, 2006.

referral fee is not itself acting as a broker. Businesses that are not truly providing brokerage services do not have a right to participate in the MLS which is established by and for brokers.

Third parties who are not acting as brokers do not have an absolute right to display the listings of legitimate brokers in order to advertise them in an effort to attract customers. The MLS is not a public utility. Dave Liniger, Founder and Chairman of RE/MAX, likens these companies to the guy who shows up at a potluck dinner bringing only a fork. These interlopers are essentially asking for a free ride or subsidy from the established industry in order to jump start their dot com business models overnight.

For comparison purposes, look at the automotive industry. When you sell a car, you have a number of options. One is to simply trade it in to the dealer when you buy a new car. Another is to try to achieve a better price by selling it yourself using the newspaper. Another tactic is to park the vehicle in a high-traffic area with a for sale sign in the window. But no one should presume to have the right to park the vehicle on the lot of one of the dealers on auto row with a for-sale-by-owner sign in the window. That lot is proprietary to the dealer, just as the MLS is proprietary to brokers.

Economic theory explains that the result of allowing free riders is that members of a system who are making legitimate contributions may decide to withdraw if they perceive they are not receiving their fair share of benefit. To require the MLS to open up to anybody could jeopardize the viability of a system that has been very beneficial to consumers.

In any event, the MLS no longer has the exclusivity it once did as the source for real estate listings. The Internet has enabled many new websites that allow brokers or individual home sellers to upload property information for free. These are essentially alternatives to the MLS. Since almost 80% of new home buyers use the internet (an increase from two percent in 1995!)⁶, home sellers and new business model real estate companies now have a tremendous number of avenues through which they can reach consumers.

LIMITED SERVICE REQUIREMENTS

All 50 states require real estate professionals to be licensed. In order to obtain a license, would-be professionals must become knowledgeable about the intricacies of real estate transactions, including agency, fiduciary obligations, sales contracts, escrow, title, appraisal, survey, property disclosure, environmental hazards, Megan's Law, mortgages, deeds of trust and a number of other subjects.

RE/MAX International has never lobbied for or against minimum service requirements. We feel this is a matter that should be left to the state legislature. Since the purchase or sale of a home is a transaction involving the most valuable asset most

⁶ National Association of Realtors. 17 January 2006, Press Release

people own, a state legislature may legitimately determine that the fiduciary duty and agency responsibility of a broker or agent requires a minimum level of representation of the client.

An alternative to minimum service requirements would be to require limited service providers to make a thorough disclosure to their client of all the steps involved in a real estate transaction and identify the aspects of the transaction where the client will be left on their own. Mr. Aaron Farmer of Texas Discount Realty has been a vocal critic of minimum service requirements. At an FTC/DOJ workshop last Fall, Mr. Farmer stated that a disclosure requirement was an acceptable solution.⁷ While some consumers may be sophisticated enough to represent themselves in some or all of the steps of a transaction, most are not. Mr. Farmer of Texas Discount Realty stated in that same workshop that because of the importance and complexity of the home sale process, not more than 10 to 15 percent of consumers should use a limited service company.⁸

RESTRICTIONS ON REBATES

Some states have had laws restricting the ability of a broker to provide a customer with a rebate. RE/MAX believes that brokers and agents should be allowed the ability to freely negotiate transaction service pricing with their clients. The RE/MAX business model empowers the agent to do this.

BANKS AND REAL ESTATE BROKERAGE

Given the increased competition in our industry, the new Internet business models and declining commission rates, RE/MAX wonders why banks would want to get into real estate brokerage? Residential real estate brokerage requires a high level of individual service. It has not been our experience that banks are good at this. When RE/MAX entered the Canadian market in 1980, all of the Canadian banks had real estate brokerage operations and dominated with 60% of the market. Today, RE/MAX agents are involved in 50% of the home sales in Canada and the banks are no longer major players in the market. This provides good reason to question whether it is in the best interest of the U.S. banking system to allow banks to expand into real estate services. Nonetheless, RE/MAX knows it can compete against banks and neither opposes nor supports changes to federal laws on this subject.

⁷ Competition Policy and the Real Estate Industry – A Public Workshop hosted by the Federal Trade Commission and the Department of Justice, Oct. 25, 2005. Official Transcript, p. 115.

⁸ *Id.* at p. 109.