Fallout from the National Association of Realtors' settlement

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Most people interested in real estate have heard about the recent settlement involving claims of price-fixing by the National Association of Realtors. By the terms of that settlement, broad changes were implemented in the way that realtors will do business with respect to the purchase and sale of single-family homes. Of note: The rules regarding commissions for seller's and buyer's agents have changed.

The settlement has yet to be formally approved, but that approval seems likely. There has already been at least one court decision against a local realtors' association on the same anti-trust grounds, and many more such lawsuits have been filed at the local level throughout the country.

On the assumption that the changes that have been agreed upon by the National Association of Realtors will be implemented, this article discusses the new rules and provides some insights on the impact on the residential real estate market.

New rules for how realtors do business

There are fundamental elements of the new rules about how realtors will do business. A listing that is put forth by a seller's agent cannot specify the amount of the commission to be paid to the buyer's agent and cannot require that the commission of the buyer's agent be paid by the seller. The seller's listing agreement will thus specify only the amount of the commission to be paid to the seller's agent.

The buyer will enter into a separate agreement with the buyer's agent, regarding the commission to be paid to the buyer's agent. The buyer's agent may (but cannot be required to) receive, as their compensation, a portion of the commission paid by the seller to the seller's agent. However, the buyer's agent may do so only if that arrangement is freely negotiated on the basis of one individual transaction, and with the agreement of the buyer.

No longer will access to the MLS listing service be limited to agents who agree in advance to a structure whereby the commission of the buyer's agent is stated in the listing as a portion of the total commission to be paid to the seller's agent.

Commissions for the seller's agent

An agent representing a seller will likely confine their discussion about compensation to a single figure representing the commission to be paid to the seller's agent only, with no mention of the commission to be paid to the buyer's agent. It is still permissible, on a transaction-by-transaction basis, for the listing agreement to specify a larger commission and to require that a portion of it be paid to the buyer's agent.

Some agents for sellers may convince their clients that this is still the best way to handle things. That may be easier to do at the beginning, but if major changes start to occur in the marketplace, sellers may want to leave the issue of the commission to the buyer's agent to be resolved by the buyer.

The rules regarding commissions for seller's and buyer's agents have changed.

In the short run, established, successful agents will likely argue that "you get what you pay for" and that a commission on the order of 2% or 3% is appropriate for a good seller's agent. Newer and more aggressive agents may offer to do the job for less, arguing that technology enables them to do just as good a job, for a smaller commission.

In addition, entirely new business models can be expected to enter the scene, now that the same MLS data is available independent of the compensation structure for the agents. An entrepreneur may well devise a system that presents a seller's property and answers many of the relevant questions about it digitally in a manner that is less costly and thus allows for a reduced commission.

Commissions for the buyer's agent

The disruption is likely to be even more extensive on the buyer's side. At a minimum, the buyer's agent will have to secure a written agreement with their client — the buyer — regarding the amount of the compensation to be received by the buyer's agent and the manner of payment of that commission.

Regarding the amount of the buyer's agent's commission, the question would appear to be whether the compensation would be 1%, 2%, or 3% of the purchase price. But other pricing mechanisms may be developed. The commission could be based on an hourly rate, or the amount of the compensation could be a fixed fee

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that could have various levels, depending upon the services to be provided.

An enterprising buyer's agent could develop a program whereby they offer various suites of services, with different pricing for each level.

The manner of payment of that compensation will also have to be determined. The initial question is whether the commission will be paid by the buyer or whether the agent is instructed to negotiate with the seller's agent. That is still permissible, if it occurs on a transaction-by-transaction basis, freely negotiated.

Will a price reduction materialize for a seller?

A major impetus behind the settlement was the theory that by removing the burden of the total commission from the seller, the price to be received by the seller would be reduced. No longer would the price be automatically increased by, in most cases, 6%, in order for the seller to pay a commission of 3% to the seller's agent and 3% to the buyer's agent.

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It remains to be seen whether the anticipated price reduction does materialize. Buyers and their agents will have to be vigilant to try to make sure that prices do decline accordingly. It is possible that new data-driven, tech-driven mechanisms will be developed to evaluate the pricing of properties in order to determine if prices are being lowered in a manner that is commensurate with the changes in the commission structure.

Data companies could easily enter the market, presenting new methods to determine the prices of homes in order to present some "objective" standard to help buyers determine whether they are paying a price that has been sufficiently reduced because of the change in the commission structure.

Will buyers of lower-priced homes be adversely affected?

The conventional wisdom is that buyers of lower-priced homes will be most adversely affected by any change in the way that the buyer's agent's commission is currently handled. Agents may be less inclined to reduce commissions for low-priced homes because of the amount of work that is required.

Further, homebuyers in the lower price range are less likely to be able to pay the commission of the buyer's agent from their own pocket. The old system essentially allowed buyers to roll the cost of the buyer's agent into the purchase price, and thus to finance most of that cost by means of their mortgage loan.

It seems likely that the old structure will continue in effect for low-priced homes. Buyer's agents will, on a transaction-by-transaction basis, likely enter into agreements with their clients that the buyer's agent's commission will be paid by the seller, thus increasing the purchase price but allowing the buyer to finance that extra cost rather than paying it upfront.

Again, however, entrepreneurship and technology may allow for disruption at the lower end of the scale, where the buyer does not need as much hand-holding or as many sophisticated services as the buyer of a high-priced home.

Business as usual?

In the end, disruption seems inevitable and innovative approaches seem likely. However, there also seems to be a continued role for traditional agents who offer in-depth services that technology alone cannot provide. Those agents are likely to be able to continue to command commissions based upon a percentage of the purchase price, in the range of 2% or 3%. The traditional model will likely continue strongly in the short run, and its continued dominance will likely depend upon the degree of disruption that occurs later.

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