

The NAR Settlement, and What It Means to the Title Industry

Description

In March, the National Association of Realtors (NAR) agreed to a \$418-million settlement to settle several pending lawsuits alleging that NAR members used business practices that kept commissions artificially high, and drew compensation from the seller for services given to the buyer. Many news outlets, including the *New York Times*, *Washington Post*, *USA Today*, *Richmond Times-Dispatch*, *Housing News*, and NAR itself have published articles predicting various changes in the homebuying process. Those predictions range from the extreme end, in which 50% of the real estate agents in the United States will find new careers, and commissions will drop from an average 5 to 6% to an average 2 to 3%, to the “not much will change” camp that describes the changes as inconsequential to the industry.

What has been absent from the news coverage is how the changes will affect other aspects of the real estate industry, including mortgage and title. To fully understand those impacts, we must first understand the core changes from the NAR settlement. The settlement has two key provisions:

- The advertisement of cooperative compensation agreements on MLS systems is to be eliminated, and the option to pay any part of a buyer’s agent commission is negotiable.
- Any agent who is not the listing agent, must have a buyer-broker agreement to provide services to a potential buyer. Buyer-broker agreements are now required.

When it comes to the advertisement of cooperative compensation agreements on MLS systems, this could mean that sellers may choose to list their property for a flat fee, or 2 to 3% commission paid entirely to the listing agent. On the other hand, sellers can still choose to pay 5 to 6% commission, and pay half of that commission to the buyer’s agent. A third option may be that the seller signs a listing agreement with a 2 to 3% commission to the listing agent, and offer a flat-fee dollar amount as a seller concession to the buyer. The buyer could then negotiate to pay some or all of that to a buyer’s agent at closing.

The requirement to have a buyer-broker agreement in place on behalf of the buyer, prior to any work being done, is expected to limit the work done by buyer’s agents. Furthermore, it may make working as a buyer’s agent harder and provide less compensation. This could drive some buyers to only contact listing agents directly (remember, they can show their own listing without a buyer-broker agreement) and forego working with a buyer’s agent. On the other hand, a new sub-specialty of real estate agent could emerge, one who only works with buyers. How this will affect the market is still unknown.

These developments have caused most industry experts to conclude that the real estate industry will change in three specific ways:

1. There will be fewer part-time and small brokerages. Fewer real estate agents overall will result in a greater concentration of the “80-20 rule.” If 20% of the agents in the United States sell 80% of the properties, a large portion of that 80% may opt to leave the industry.

2. Revenue for real estate brokerages will be reduced. If there are fewer buyers willing to sign buyer-brokerage agreements, or if commissions for listings are reduced, the overall effect is there will be less revenue going to real estate brokerages.
3. If there are fewer buyer's agents, and less representation on the buyer's side, this will likely mean less cooperative brokerage compensation. Translation: This could result in more deals where the listing agent is the only real estate agent involved, and there is no buyer's side agent.

So how will these potential changes affect the mortgage and title industry? Fewer real estate agents and fewer real estate brokers will mean a higher concentration of control over real estate transactions. If an average town of 50,000 people had 10 real estate brokerages and 50 agents, imagine the impact if that was cut to 7 brokerages and 35 agents. It wouldn't mean there would be fewer transactions – it would mean that those fewer brokers and agents control the deals. For title and mortgage companies, this will require them to become more highly specialized and increase levels and quality of service to capture referrals of business.

I will give you a past example. Back in the early 1990s, my title agency was against providing mobile closings. We did not want to sign customers at their house, place of work, or after hours. As the market became much more competitive with fewer transactions during the recession of 1994, we changed our stance, and began offering flexibility in our services. We accommodated after-hours closings, mobile closings, and other customer requests. Our business did not decline as much as other market players. This was not a huge innovation back then; we were simply meeting market demand. But it is a good example that when fewer industry players control more transactions, title and mortgage companies are pushed to become even more innovative and service-focused to capture and maintain business.

Some have suggested that this will cause a shift, incentivizing buyers and sellers to better shop for title and mortgage services. This would mean that title and mortgage companies will need to advertise to consumers more. We may see in some markets that when a listing pops up in the market, title companies contact the seller *directly* and offer their services. While this may turn off some real estate agents who have their favorite title resource, it may actually be the only way to break the cycle of fewer real estate agents controlling more of the transactions that happen.

Pressure on revenue is another area to watch. Real estate brokers already earn between 40- to 60% less profit than they did 25 years ago. With the advent of the 100% commission model – where a broker pays the agent 100% of the commission earned, but then bills the agent back for fees (like MLS membership, advertising, etc.) – these models could fail. One model that has been suggested is the merging of title, mortgage and real estate brokerage. In some markets, this would be called a joint venture, in which the real estate broker owns a piece of the title and mortgage business. In other markets, be prepared for the possible merging of the three businesses into one – we handle everything for you – business. If a real estate broker also owns the title and mortgage company, and the only way to achieve profit on a deal is capture the title and mortgage business, it will cause some brokers not to hire agents who do not support the affiliated title and mortgage company.

Maybe the most lasting impact of the NAR settlement will be a return to the "old way" of the real estate brokerage. Long before the Internet, a real estate broker would list a property, and spend time and money marketing it for sale. The agent would hold open houses, advertise the property for sale and complete showings to prospective buyers. Back then, a much larger percentage of deals were "same side," referring to a listing agent who sold their own listing to a buyer. Real estate agents craved this

type of deal, as it meant they kept the entire cooperative compensation (both sides) commission.

Many articles are suggesting that buyers will have to do more work now to buy a house. This will include researching neighborhoods, viewing properties online, taking virtual 3D tours, prequalifying for a mortgage and determining their price range. Buyers may forego representation by a real estate agent entirely. Only when a buyer is ready to buy would they contact the listing agent for a showing and to make an offer. The listing agent will draft the purchase agreement and do minimal work for the buyer. For the title and mortgage companies who rely on referrals from buyer sides, this could be devastating. Listing agents will gain much more control over transactions. Mortgage companies will have to find new ways to lend to unrepresented buyers, and title companies will need to invent new ways to stand out to listing agents.

One good possible outcome from this shift may be fewer requests for “split closings”. A split closing refers to a buy-sell transaction where two title and escrow companies are hired to process the transaction, one for the seller (referred by the listing broker) and one for the buyer (referred by the buyer’s agent broker). While any reduction in split closings would be welcome and save consumers money, the sober fact remains that if more listing agents control the referral of the transaction, title companies will need to become more competitive to capture those deals.

The changes contemplated for the real estate industry range from very significant to just incremental. Depending on the market, the way boards of REALTORS® adapt and how Multiple Listing Services change will determine how much these predicted changes happen. Regardless, you can expect some level of fewer real estate agents, shrinking margins for real estate brokers and less buyer representation. How you adapt for these changes will determine how your title or mortgage company survives in the new environment. Be ready for the changes, and be prepared to provide an even higher level of service to real estate professionals moving forward to receive referrals.

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