Section A

DANGERS IMPACTING AGENTS

Masses of Marginal Agents Destroy Reputation A1

Commissions Spiral Downward A2

Agent Teams Threaten the Survival of Brokerages A3

IRS Forces Exodus of Independent Contractors A4

The Decline in the Relevancy of Agents A5

The Agent-Centric Era Ends A6

Housing Finance System Fails A7

Commoditization of Residential Real Estate A8

Commissions Concentrate into Fewer Hands A9

The Agent is Removed from the Transaction A10

DANGER A1

MASSES OF MARGINAL AGENTS DESTROY REPUTATION

The real estate industry is saddled with a large number of part-time, untrained, unethical, and/or incompetent agents. This knowledge gap threatens the credibility of the industry.

IN CONTEXT

The knowledge and competency gap from the most to the least is very large, due to the low barriers to entry, low continuing education requirements, and the lure of quickly making big dollars. For decades the industry has held the opinion that it's a profession, however the reality is that those outside the industry don't hold the same opinion. Most professions (doctors, lawyers, accountants, and engineers) require thousands of hours of study, beginning with a bachelor's degree. Even becoming an earth driller requires an average of 704 hours of instruction, and becoming a cosmetologist requires an average of a 372 hours. But to become a licensed real estate agent requires an average of only 70 hours with the lowest state requirement being 13 hours.

The delta between great real estate service and poor real estate service has simply become too large, due to the unacceptably low entry requirements to become a real estate agent. Professional, hardworking agents increasingly understand that the "not so good" agents are bringing the entire industry down.

Danger Index

100.0

Probability

5.0

Timing

4.0

Impact

5.0

INDEX
Danger evaluated in terms of PTI to provide comparison between the dangers/sections of the report. Danger Index, represents a composite, overall score.

"I don't like lawyers, but I rarely work with an incompetent one. I like real estate agents more, but there are a large number of incompetent ones."

AUTHOR'S PERSPECTIVE

There are too many real estate agents that are simply not qualified to the level they should be. Furthermore, there are no meaningful educational initiatives on the table to raise the national bar for real estate agents across the board. And while this lack of agent knowledge is a significant danger in itself, when combined with a lack of basic competency it could be destructive and harmful to both the industry and the consumer.

DANGER A2

COMMISSIONS SPIRAL DOWNWARD

A variety of powerful forces exert significant downward pressure on real estate commissions.

IN CONTEXT

The continued rise in home prices has facilitated the elevation of real estate earnings based on commissions. Those earnings have not gone unnoticed by consumers, who are responding by placing increased pressure on real estate agents to reduce their commission rates. As a result, many fear a gradual downward slide or a realignment of fees as charged in other countries in the world.

REAL ESTATE BROKERAGE FEES

According to a report by the *International Real Estate Review*, real estate brokerage fees around the world are:

1 - 2% United Kingdom

1.5 - 2% Singapore

1.5 - 2% Netherlands

2 - 3% Australia

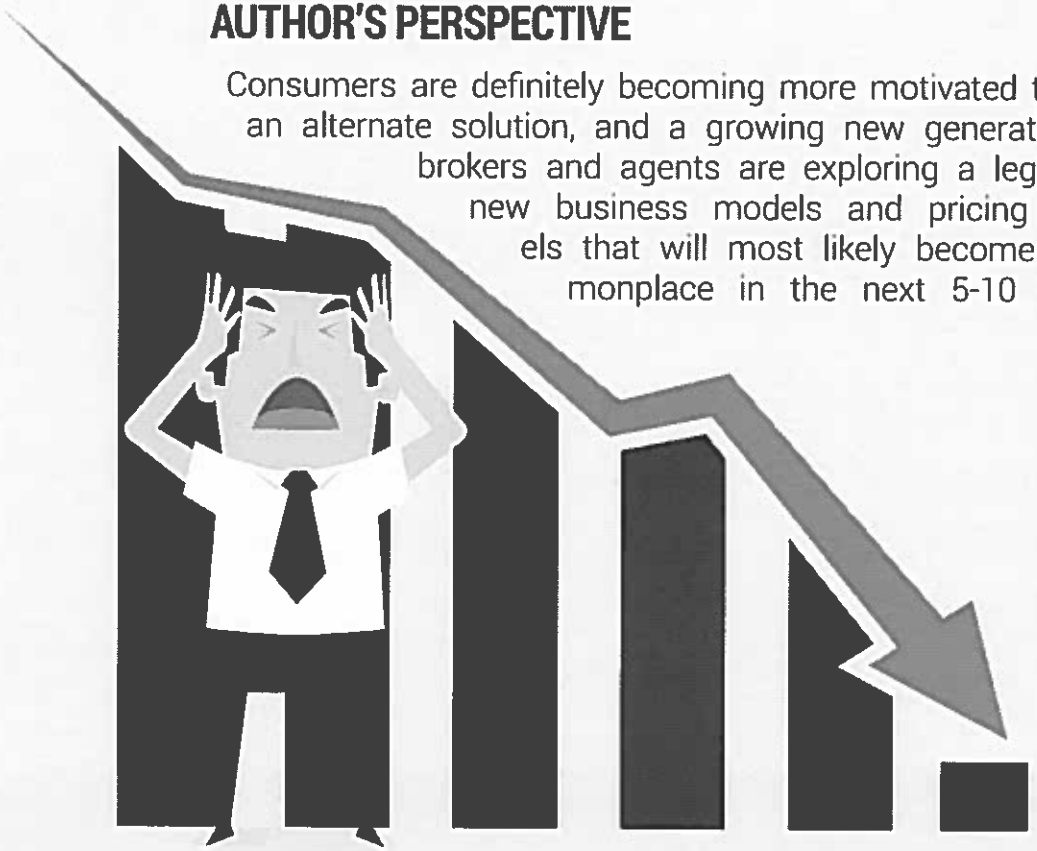
3% Belgium

3 - 6% Germany

"Home buyers might not always want to use a real estate agent, but most think they have to. What happens if their perspective changes?"

AUTHOR'S PERSPECTIVE

Consumers are definitely becoming more motivated to find an alternate solution, and a growing new generation of brokers and agents are exploring a legion of new business models and pricing models that will most likely become commonplace in the next 5-10 years.



Danger Index

87.5

Probability

5.0

Timing

3.5

Impact

5.0

INDEX
Danger evaluated in terms of PTI to provide comparison between the dangers/sections of the report. Danger Index, represents a composite, overall score.

AGENT TEAMS THREATEN THE SURVIVAL OF BROKERAGES

Teams cannibalize brokerage companies by siphoning off their profits, leaving them exposed to all the risk.

IN CONTEXT

The team concept has been around for a long time, but in recent history it has emerged as a much larger factor in the brokerage industry. Most companies have endorsed or at least tolerated the concept in light of the revenue it generates. However, there are issues that need to be addressed when teams function as an autonomous brokerage unit. From a marketing perspective they often develop their own brands, which in some instances become more powerful than the brokerage brand. Their self-directed status is enhanced by their ability to obtain their own technology and operate more efficiently and effectively for their own benefit. All of which presents the opportunity for the emergence of the "lead agent-centric" model, the company within the company.

Agent teams greatly expand the broker's potential legal liability as the master agent imposes standards and best practices on the team that have not been approved by either the brokerage or the broker's legal counsel.

Economics also come into play here. Master agents with teams tend to make more money than traditional office managers. So here again the industry's economic profile is being distorted when funds that arguably should be distributed as dividends are being expended for management or labor.

Danger Index

70.0

Probability

5.0

Timing

4.0

Impact

3.5

INDEX
Danger evaluated in terms of PTI to provide comparison between the dangers/sections of the report. Danger Index, represents a composite, overall score.

AUTHOR'S PERSPECTIVE

Teams dominate and make it harder for solo agents to succeed and for companies to act as entrepreneurial as they may wish. There is a strong tendency for teams, as part of their business plan and their own identity/brand, to establish their own operating guidelines, standards, and procedures. Some of these independent decisions and actions may run afoul of Real Estate Settlement Procedures Act (RESPA) compliance or the Consumer Financial Protection Bureau, especially decisions involving Affiliated Business arrangements.

On the other hand, with good management and oversight, teams can become a strong growth opportunity as demonstrated by some large national franchises.

IRS FORCES EXODUS OF INDEPENDENT CONTRACTORS

An IRS ruling is handed down that reclassifies the legal status of real estate agents from independent contractors to employees.

IN CONTEXT

Real estate law, which in most states requires brokers to supervise their agents, often conflicts with labor laws governing independent contractors. Furthermore, there are issues concerning the involvement of the IRS and the National Labor Relations Board that present challenges. These conflicts have opened the door for attorneys to bring suit against Boston Pads, Coldwell Banker, Redfin, and ZipRealty, claiming these organizations have misclassified their agents as independent contractors rather than employees.

The lawsuits assert that the labor laws controlling independent contractor status should take precedence over real estate law.

Employment law defines independent contractors in such a way that broker supervision can appear to undermine a contractor's independence. One of the widely adopted tests to determine a person's status is the Economic Reality Test (used by the U.S. Supreme Court) that examines the degree of employer control, the relative investment of both the employee and the employer, the opportunity for profit, the skill required, and the permanency of the relationship.

ECONOMIC REALITY TEST
Criteria used by the U.S. Supreme Court to determine if an individual is an independent contractor.

1. The degree of control exercised by the alleged employer;
2. The extent of the relative investments of the (alleged) employee and employer;
3. The degree to which the employee's opportunity for profit and loss is determined by the employer;
4. The skill and initiative required in performing the job;
5. The permanency of the relationship.

"Part-time agents are a huge risk to our future."

AUTHOR'S PERSPECTIVE

A decision by the Supreme Court going against the status quo, although unlikely, could have a far-reaching, industry-wide impact, including the transformation of the brokerage revenue model and a significant shift in the operational model.

A scenario in which agents are considered employees would initiate a complete reorganization of the existing revenue model. Most brokerage companies would be unwilling to hire agents that will not generate enough business to cover their costs. Employee status also does not necessarily include top wages and benefits for everyone. Consider the case of restaurant workers who exchange access to tips for an additional $2.13 minimum wage. Agents would thus have three primary options: work as an employee for a large company under its operational guidelines, become a broker and work as a sole practitioner, or leave the industry altogether.

Danger Index
63.0

Probability
3.5

Timing
4.0

Impact
4.5

INDEX
Danger evaluated in terms of PTI to provide comparison between the dangers/sections of the report. Danger Index, represents a composite, overall score.

DANGER A5

THE DECLINE IN THE RELEVANCY OF AGENTS

The role, function, and perceived value of agents deteriorates as agents fail to properly assess and respond to changing consumer demands and expectations.

IN CONTEXT

The real estate industry has long served the consumer at a local level, but in the opinion of many leaders it has never really had a firm understanding of consumers as a collective, let alone understood that consumers are constantly evolving and changing. The industry's most frequently cited weakness is its inability to understand what the consumer wants. The problem is that consumers don't care about agents—as much as agents would like to think consumers do—and the role of the agent not only can be, but is being redefined.

Furthermore, numerous participants in the industry are guilty of violating key parts of The Consumer Bill of Rights, especially the consumers' rights to be informed (of all the facts), to choose (from among competing services), and to be heard (to have all their questions understood and answered). The root cause is often the failure to listen, or worse, appearing to listen but failing to respond by focusing on the transaction and not the consumer.

AUTHOR'S PERSPECTIVE

Agent photos and self-branding are omnipresent in home sales. In many cases the promotion of the real estate sales person surpasses the importance of the house being sold. That's uniquely different to most other sales industries where the role of the sales person is secondary. Too many real estate agents believe their role is critical and their relationship with home buyers and sellers is beyond reproach. It's that kind of overconfidence that often results in failure.

"Time to clearly define the value proposition for REALTORS®."

Danger Index

60.0

Probability

5.0

Timing

3.0

Impact

4.0

INDEX
Danger evaluated in terms of PTI to provide comparison between the dangers/sections of the report. Danger Index, represents a composite, overall score.

THE AGENT-CENTRIC ERA ENDS

The disproportionate power that independent contractors have enjoyed over the past three decades goes out of vogue as capital or economies of scale change the rules and the Wall Street reign begins.

IN CONTEXT

Unlike brokers, the majority of agents do not have the same level of financial investment in the industry. Many agents have been unable and/or unwilling to effect the changes the brokers need to build effective and profitable businesses. It remains a numbers game and brokers frequently don't make decisions that are in the best interests of the brokerage, they make decisions to appease their top-producing agents.

With the growing impact of technology, consumers are now wielding newfound power and imposing increased demands on the brokers through their agents, which further complicates the existing model and favors change.

> *"Technology is constantly evolving and agents aren't. The difference is noticeable and it's getting larger."*

AUTHOR'S PERSPECTIVE

As real estate brokerage companies and franchise organizations continue to consolidate and expand in size, head count, and profitability, the obvious need for increased standardization of best practices and the implementation of best systems has become critical.

Going forward in the evolution of the brokerage business, there is danger in failing to address the legacy of fragmentation that was brought about in large part by agent-centricity, which has become a multilevel handicap to the brokerage business and the ability of brokers to adapt and move forward.

To realign from an agent-centric model, significant time and money will need to be invested in realigning company assets to ensure that the organization's foundation will be able to sustain, or carry, the scalability of size required to change the paradigm. And in many cases that scalability will need to be added on top of an existing, fragile, and in some cases inadequate structure. In the process, the importance of the sales associate and a strong and powerful sales team should never be underestimated or underappreciated.

Danger Index

52.5

Probability

3.5

Timing

3.0

Impact

5.0

INDEX
Danger evaluated in terms of PTI to provide comparison between the dangers/sections of the report. Danger index, represents a composite, overall score.

HOUSING FINANCE SYSTEM FAILS

Mortgage-backed securities as a method of financing is discontinued because it's too risky and the related fines imposed on banks too severe.

IN CONTEXT

The U.S. has $9 trillion in outstanding home mortgages, not including $1 trillion in seconds and home equity loans. In response to the financial crisis, the Fed began quantitative easing (QE) to stimulate the economy, including purchases of mortgage-backed securities (MBS) issued by Fannie Mae and Freddie Mac.

One of the most significant effects was a decline in mortgage rates to generational lows, which supported the housing market and the economy during one of its most vulnerable periods.

The financial crisis highlighted the importance of the secondary mortgage market and the vulnerability of financing for homebuyers in times of crisis. Should lenders decide to move away from mortgage lending because of onerous regulations or increased risks in the secondary market, home buyers' ability to access affordable mortgage financing would be severely limited.

Danger Index

48.0

Probability

3.0

Timing

4.0

Impact

4.0

INDEX
Danger evaluated in terms of PTI to provide comparison between the dangers/sections of the report. Danger index, represents a composite, overall score.

AUTHOR'S PERSPECTIVE

When and to what extent Fannie Mae and Freddie Mac are revamped or replaced remains unknown. A secondary market that is not available in all economic climates and that does not preserve access to affordable mortgage financing for qualified home buyers would place agents and the entire industry in jeopardy.

DANGER A8

COMMODITIZATION OF RESIDENTIAL REAL ESTATE

The concentration of residential ownership into the hands of a few large investors commoditizes residential real estate and impacts market dynamics and liquidity.

IN CONTEXT

The significant increase in the liquidity of residential real estate brought on by the slow down starting in 2006, the emerging foreclosure crisis of 2007, and the recession of 2008, created the peril that institutional investors would acquire and control major housing resources as a sound long-term investment asset. Over the past few years Residential Real Estate Investment Trusts (RREIT) have grown and publicly traded companies like Blackstone and Colony Financial currently own one and a half percent of the approximately 14 million rental homes in the U.S. RREITs have expended $20 billion to acquire somewhere near 200,000 single-family rentals in just the last two years.

The type of single-family rentals desired by RREITs and their location is remarkably consistent: the ideal asset is a three-bedroom, two-bathroom house in a good school district and close to jobs. Like individual homebuyers, these institutional investors prefer long-term appreciation and therefore their target markets are infill neighborhoods over the new "exurban" communities.

Largest RREIT companies and the total number of homes they own

43,000	Invitation Homes (Blackstone)
27,000	American Homes 4 Rent
16,000	Colony American Homes (Colony Financial)
11,400	Starwood Waypoint
8,200	Altisource Portfolio Solutions
6,000	American Residential Properties
5,600	Silver Bay

Source: nasdaq.com, Seeking Alpha, CoStar Group, 2014

"Wall Street has discovered constant housing income streams."

AUTHOR'S PERSPECTIVE

When a small number of RREIT companies own a large number of homes, they have the ability to place a large number of homes on the market at the same time, possibly depressing values. Some are even exploring partial ownership or the right to use the home for a certain time period without becoming the owner. It has been estimated that this represents a $1.5 trillion opportunity.

The single-family market could follow in the footsteps of the multifamily market, with a large percentage of all rental homes eventually being owned and managed institutionally. This could, over time, change the market dynamics of neighborhoods and subsequently the neighborhood agent.

Danger Index

42.0

Probability

3.0

Timing

3.5

Impact

4.0

INDEX
Danger evaluated in terms of PTI to provide comparison between the dangers/sections of the report. Danger Index, represents a composite, overall score.

DANGER A9

COMMISSIONS CONCENTRATE INTO FEWER HANDS

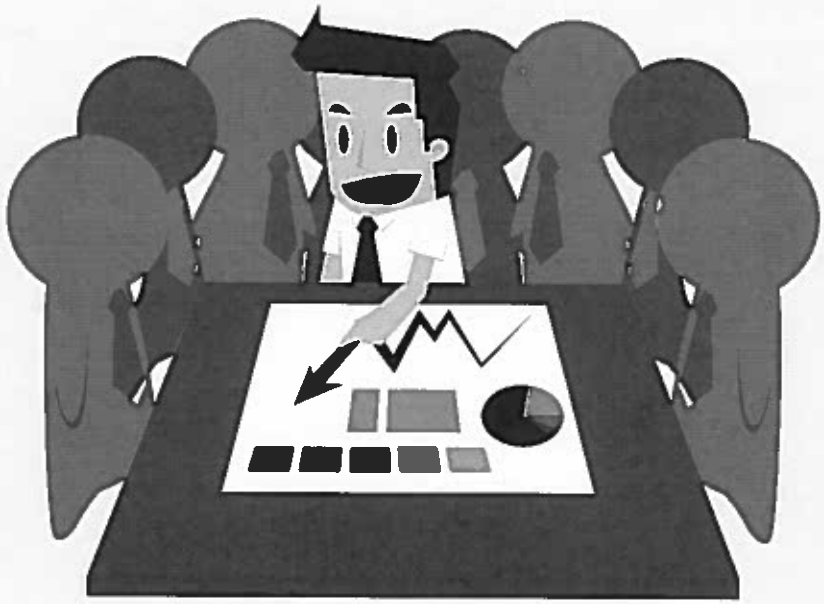
A very small group of very efficient and effective agents discover the winning formula and secure a disproportionate market share.

IN CONTEXT

The 80/20 rule (Pareto Principle), or some variation thereof, most certainly applies to real estate sales. Few agents are responsible for a large portion of all real estate sales.

In a recent book titled *80/20 Sales and Marketing*, author Perry Marshall takes the Pareto Principle to the next level. This can also be expanded such that the 80/20 rule also exists within the top 20 percent. Meaning that the top 20 percent of the top 20 percent (or the top 4 percent overall) represent 64 percent of sales.

"We don't need more agents. Just better ones."



AUTHOR'S PERSPECTIVE

As the industry successfully adapts to an ever increasing amount of technology, there are agents that have learned to create systems that leverage themselves to even higher levels, with a number of closed transactions not previously achieved. And there are a rapidly growing number of rookies that are also finding success much quicker and at a higher level than has previously been the case.

Danger Index
40.0

Probability
4.0

Timing
2.5

Impact
4.0

INDEX
Danger evaluated in terms of PTI to provide comparison between the dangers/ sections of the report. Danger Index, represents a composite, overall score.

DANGER

A10 THE AGENT IS REMOVED FROM THE TRANSACTION

A tech company cracks the code and connects enough of the dots to conduct real estate transactions without the need of an agent.

IN CONTEXT

The industry has always had a group of homeowners that have attempted to conclude the sale of their home without the help of a licensed real estate professional, thereby attempting to save all or a part of the commission. Commonly referred to as FSBO (For Sale By Owner), this market segment has historically remained constant at around 10 percent of the total market. While certain lower economic profiles may be the central focus of today's growing consumer cash consciousness, it isn't the only driving force. There are consumers who consider independence from institutional norms to be a symbol of successful lives. Self-healing, doing your own taxes, growing your own food, and involvement in all aspects of life are positive personal goals for many.

With the Millennial Generation drawing closer to its natural home buying juncture, it's obvious that their "first time" will not be as easy as it was for the Civic or Boomer generations. To start with, the opening economic profile for the Millennials is not what it was for their predecessors. It's generally believed that the younger generations will have less cash to work with and more challenging financial thresholds to meet. As a result, Millennials will be looking for ways to shave costs from their real estate transaction. At the other end of the spectrum are the Boomers who are seeking to downsize from large homes to more affordable, "sized right," and accessible housing options. Their primary objective will be to convert as much of their equity into cash as possible. Shaving costs from their real estate transaction may also become increasingly important.

Examples of New Models

- Uber
- AirBnB
- TurboTax
- LegalZoom
- ScottTrade

"The 'UBERIZATION' of real estate threatens agents the same way it did cab drivers."

"Agent-centricity may be our downfall."

AUTHOR'S PERSPECTIVE

Some consumers may be dissatisfied with how complex the home buying process is, but most of them can't do anything to change that. There is one element that can change all of that: Money. Keep in mind that FSBO doesn't necessarily mean without assistance—it means without an agent as we know it today. Consumers are availing themselves of alternative options regarding search and research.

Furthermore, business models constantly change. Portals that may never have had the intention of being brokers may believe they have to, and an e-commerce or online auction company providing consumer to consumer services via the Internet may decide to expand their channel into residential sales.

The bottom line is that change is certain. It is the approach that's an unknown.

Danger Index

31.5

Probability

3.5

Timing

3.0

Impact

3.0

INDEX
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DANGER CHECKLIST: DANGERS IMPACTING AGENTS

DATA CLASSIFICATION

In order to best evaluate and present each danger, an Index was created based on the probability (P) of each danger occurring, the future timing (T) of the potential danger, and the possible impact (I) of each danger. The combined scoring of these factors results in the PTI Index. The index is not scientific but rather a combined and weighted representation of the research, surveys, and interviews that enable the dangers to be placed in order of significance as to the level of danger they present.

INDEX

In evaluating each danger, the overall result is presented in the PTI index (Probability, Timing and Impact), which ranks the danger in order to provide a level of comparison between the dangers/sections of the report. The Danger Index represents a composite, overall score.

#	Probability	Timing	Impact	Danger Index	
5.0	100% Chance	1 Year	Game Changer	81-100	Critical
4.0	80% Chance	1 - 3 Years	Major Impact	61-80	Severe
3.0	60% Chance	3 - 5 Years	Moderate Impact	41-60	High
2.0	40% Chance	5 - 10 Years	Some Impact	21-40	Moderate
1.0	20% Chance	10 + Years	No Impact	0-20	Low

		Danger	Probability	Timing	Impact	Index
☐	A1	Masses of Marginal Agents Destroy Reputation	5.0	4.0	5.0	100.0
☐	A2	Commissions Spiral Downward	5.0	3.5	5.0	87.5
☐	A3	Agent Teams Threaten the Survival of Brokerages	5.0	4.0	3.5	70.0
☐	A4	IRS Forces Exodus of Independent Contractors	3.5	4.0	4.5	63.0
☐	A5	The Decline in the Relevancy of Agents	5.0	3.0	4.0	60.0
☐	A6	The Agent-Centric Era Ends	3.5	3.0	5.0	52.5
☐	A7	Housing Finance System Fails	3.0	4.0	4.0	48.0
☐	A8	Commoditization of Residential Real Estate	3.0	3.5	4.0	42.0
☐	A9	Commissions Concentrate into Fewer Hands	4.0	2.5	4.0	40.0
☐	A10	The Agent is Removed from the Transaction	3.5	3.0	3.0	31.5

Dangers Impacting Brokers

Section B | Second of Five Sections

Realtor.org/**DANGER**Report

DANGERReport.com

Section B

DANGERS IMPACTING BROKERS

Regulatory Tsunami Hits B1

Paper Brokerages Cause Disruption B2

Brokers Lose Control of Data B3

A Consumer Brand Crashes the Party B4

New Business Models Go Mainstream B5

Brokers Simply Go Broke B6

Technology Becomes a Runaway Train B7

FSBO Develops into a Do-It-Yourself Model B8

Sales Tax Threatens Margins B9

Portals Leverage Lead Gen Dominance B10

REGULATORY TSUNAMI HITS

Regulatory creep and large financial penalties increase compliance costs.

IN CONTEXT

The CFPB was established as a new bureau through the authorization of the Dodd-Frank Wall Street Reform and Consumer Financial Protection Act of 2010. It has overwhelmed each of the industries it has entered (Student loans, Automobile loans, Credit cards, and Mortgages) and, given its short but impressive history, there is every indication it will have a significant impact on national, large, and/or diversified real estate groups. The intent behind its creation is to:

- Give consumers a vehicle to enforce the provisions of the Dodd-Frank Act and other consumer financial protections laws.
- Educate the public about financial transactions.
- Utilize research to prevent future financial crises, such as another housing bubble.

In its mission to rebuild the mortgage banking landscape, the CFPB has attempted to examine every aspect of the home buying transaction and the roles of the various participants facilitating the transaction. Its investigations haven't been limited to the lenders whose practices were a large contributor to these recent changes; the investigations have extended to real estate brokerages. Important to note here is that the CFPB was also granted responsibility to oversee the Real Estate Settlement Procedures Act (RESPA), which was formerly overseen by the U.S. Department of Housing and Urban Development (HUD).

"Dodd-Frank is a train wreck."

AUTHOR'S PERSPECTIVE

Only time will tell how much of an impact the CFPB will have on real estate brokers, resulting in increased costs due to compliance, increased risk for small brokers with limited capital, increased scrutiny on marketing agreements, and the increased risk of agents moving to firms with strict compliance in place. What we do know is that the failure to comply at any level is not an option, and the penalties for failure will be costly. Those who suggest that real estate service providers are not vulnerable under the Financial Services provisions need to remember that there has been little or no effective RESPA enforcement by HUD over the past decade. Most brokerage companies are either ignorant of the fact or believe they are in compliance with CFPB/RESPA regulations, however most are likely in violation already.

Danger Index

100.0

Probability

5.0

Timing

4.0

Impact

5.0

INDEX
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DANGER B2

PAPER BROKERAGES CAUSE DISRUPTION

With no walls and little operating costs, Paper Brokerages proliferate and become a major force overnight.

IN CONTEXT

Paper Brokerages are companies that join multiple listing services (MLSs) in order to gain access to listing data and subsequently display it online. They do not, however, provide traditional brokerage services to consumers; they are created to generate leads for other brokerages. Paper Brokerages that obtain a brokerage license, or partner with a licensee who can be their "broker of record," are able to display Internet Data Exchange (IDX) listing feeds compiled by MLSs.

As Paper Brokerages don't have the same operating and cost structures as traditional brokerage companies, the concern is that they are "misusing" the MLS system and that the widespread adoption of the Paper Brokerage business model will undermine participation in IDX and the MLS system itself.

Danger Index

80.0

Probability

5.0

Timing

4.0

Impact

4.0

INDEX
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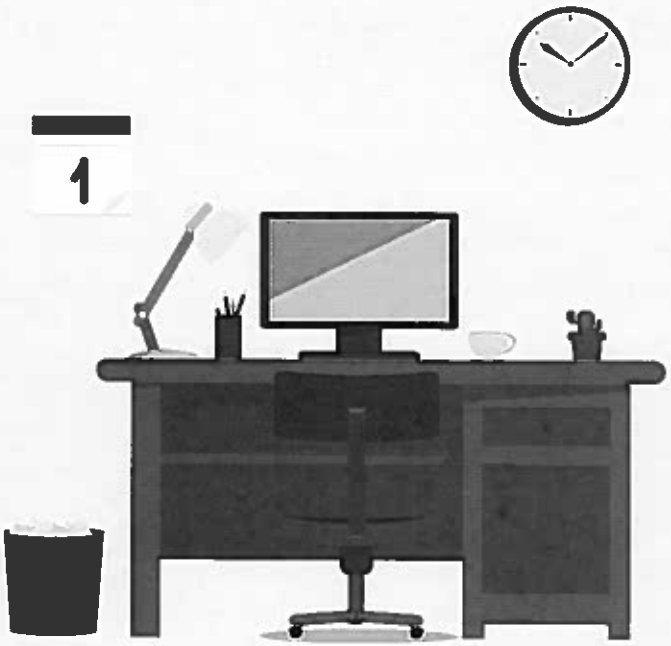
“IDX is in a fragile state. We are fighting on the front patio with the back door open.”

1



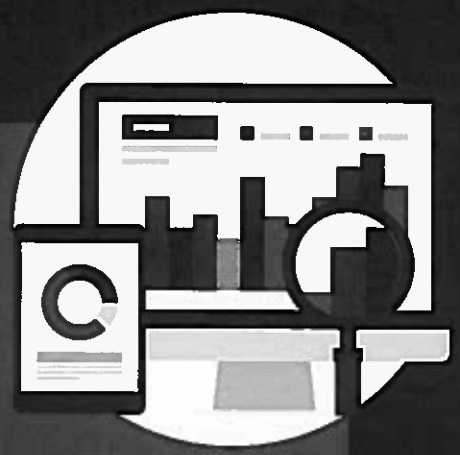
AUTHOR'S PERSPECTIVE

As the real estate industry evolves and increasingly experiments with different business models, IDX opens a new variation of models not originally contemplated. Existing big brokers have become vulnerable because some MLS services have enabled non-traditional entrants (basically non full-time brokers) to utilize their information in a variety of ways. In some cases the owner does the negotiating and sale with the buyers agent and uses the cooperating brokerage company to facilitate the closing.

This shift has marginalized large brokers, causing many to consider withdrawing from the MLS, and others to question the viability of MLS going forward.

B3 BROKERS LOSE CONTROL OF DATA

Consumer confidence in industry data erodes due to the multiplicity of conflicting data sources.



IN CONTEXT

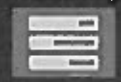
Traditionally, data was aggregated on a local level with an excess of terms, conditions, and criteria, all of which was deemed to be accurate. With the advent of the portals there is a movement toward the aggregation and syndication of data that has resulted in data collection from multiple sources that are not always kept updated, and is therefore compromised. The battle over the ownership of the data has resulted in certain data sources being disallowed, which in turn has further compromised the accuracy of the data.

Furthermore, the data mentioned really only refers to the listing data and, while it is a key piece, it is just part of the overall real estate data portfolio—tax records, insurance info, demographic records, mortgage loans, credit reports, drive times, lifestyle information, school performance, criminal activity, etc. So now the entire industry is focused on and concerned with controlling the consumer search process, which incorporates the creation, compilation, and distribution of all data.

Danger Index

72.0

Probability



4.0

Timing

4.0

Impact

4.5

INDEX
Danger evaluated in terms of PTI to provide comparison between the dangers/sections of the report. Danger Index, represents a composite, overall score.

> *"Mindsets have to change.*
>
> *Margins have to change.*
>
> *Management has to change."*

AUTHOR'S PERSPECTIVE

Innovation pushes the boundaries of existing paradigms and mindsets with new opportunities that test both current and new players.

The struggle facing brokers is that decisions regarding the management of real estate data—with regard to the release, withholding, and application of data—are made by a fragmented industry and are very diverse and inconsistently implemented. Inaccuracy of data and ownership of such data has become a major issue in our industry.

As a result, there are numerous models that are constantly evolving, creating voids and roadblocks that many outside the industry view as opportunities. The industry finds itself at the early, challenging stage of laying down new rules and guidelines for managing real estate data with the delivery of unique content that is unavailable elsewhere.

A CONSUMER BRAND CRASHES THE PARTY

A well-established consumer brand is introduced into the marketplace and a new multi-billion dollar residential real estate brokerage brand is created.

IN CONTEXT

Historically, introducing a new brand from outside the residential real estate brokerage marketplace has been difficult, and considered by many as very unlikely due to the fragmented, hyper local, and highly personal nature of the industry. With growing consolidation in the industry and the increased addition of systems and technology, the previously held limitations on building a brand no longer apply.

Over the past decade, Realogy has proven that it is feasible to take certain "outside" brands such as BH&G and Sotheby's and successfully introduce them into residential real estate franchising. Warren Buffett has proven that a completely unknown brand in the residential real estate industry such as Berkshire Hathaway can be introduced and built into a new powerhouse.

AUTHOR'S PERSPECTIVE

It would not be a stretch for home improvement giants Home Depot ($133 billion market cap; $79 billion in annual sales) and Lowe's ($70 billion market cap; $55 billion in sales), to expand into the residential real estate brokerage business.

One example would be to take the model that Lowe's has, assisting REALTORS® in providing marketing benefits and finding savings for their clients, and expand it into an online lead generation service model. A second example would be to take Lowe's existing partnership program with construction and repair vendors and expand it into a type of DIY real estate model, while a third option could be to acquire a successful existing global real estate brand such as RE/MAX.

Other interesting possibilities could include banks or HGTV. They already have a recognizable brand in the financial or home lifestyle markets and can expand into, partner with an existing company to create, or leverage a new real estate brokerage brand. However, while the dollars are always enticing, the fragmented and byzantine structure of the industry goes against the nature of these organizations.

> *"New leadership at a large company often causes a change in the direction of that company."*

Danger Index

64.0

Probability

4.0

Timing

4.0

Impact

4.0

INDEX
Danger evaluated in terms of PTI to provide comparison between the dangers/sections of the report. Danger Index, represents a composite, overall score.

DANGER B5

NEW BUSINESS MODELS GO MAINSTREAM

The existing compensation structure gets eclipsed as new business models gain rapid traction.

IN CONTEXT

The relationship between brokers and agents has been redefined a number of times during the last 50 years. Each time the redefinition of the relationship resulted in the formation of a new company and/or group of companies. The innovations brought to the industry by those new companies caused a disruption in the industry that resulted in an increase in the number of agents jumping between companies.

In the 1960s and 1970s the franchise model created new national entities, in the late 1970s and 1980s the 100 percent model exploded, and in the 1990s and 2000s the interdependent and team model gained significant traction.

Each new business model led to new global companies that dominated the industry for decades. The next winning model could be a technology-powered, agent-centric, flat fee, transaction-based fee, salaried, or auctioneering model.

Danger Index

63.0

Probability

4.5

Timing

4.0

Impact

3.5

INDEX
Danger evaluated in terms of PTI to provide comparison between the dangers/sections of the report. Danger Index, represents a composite, overall score.

> *"The residential real estate business is in turmoil. Everyone—brokers, agents, the MLS, associations—are all up for grabs... and brokers seem to be extremely vulnerable."*

AUTHOR'S PERSPECTIVE

It is interesting to note that over 40 percent of Fortune 500 companies in 2000 were no longer around in 2010, yet at the same time those top companies that were in the real estate industry in 2000 are all still here.

Two of the successful models, RE/MAX and Keller Williams International Realty, both took a decade (or more) to gain significant national critical mass. Interesting companies such as Redfin (in its fifth round of funding and in 48 metros), HomeSmart (a technology-offering already in place), and eXp Realty (a cloud-based virtual real estate brokerage) are still in early enough stages that in time they may become dominant national models.

The entrepreneurial spirit in residential brokerage is strong. Innovation of the broker/agent relationship, whether initiated by internal or external forces, is just around the corner.

BROKERS SIMPLY GO BROKE

Brokers are undercut by outsiders offering the same support and services at a fraction of the cost.

IN CONTEXT

Over the past couple of decades, brokers' control over their agents and the services they offered has shifted. This is changing the financial viability of the brokerage model. Many say it is being eroded by technology, and especially in recent times by portals. Portals capitalized on the slow responsiveness by brokerage companies that for a long time were either not able to, or chose not to, generate online leads for their agents.

Historically, lead generation hasn't been the responsibility of the broker as agents have generated their own leads from a variety of sources. Previously, no one single source could generate enough leads and therefore agents' relationships were not dependent on one entity. This is, however, changing as portals grow and become more powerful. For example, the largest portals have millions of homes viewed daily, and this in turn generates significant enquiries. Zillow has so many leads every day that they have been able to sign up over 60,000 agents to pay them for those leads. And many agents in turn have built a strong business from this source.

> *"Something is always displaced when something new is created.*
>
> *That's Capitalism."*

AUTHOR'S PERSPECTIVE

Not only are all leads not equal, not all leads are really leads. But maybe that doesn't matter. With the explosion in online leads the portals created a new category of lifestyle and home searching that previously did not exist at this level. Now there are not only more home sales, there is more interest. And it's the entities that control the interest that, diluted or not, gain access to the consumers.

It's not that portals will put brokers out of business, it's just one example of a service being offered to agents by third parties. And it is uncertain to what extent this relationship will undermine the relationship between brokers and their agents. The proliferation of the web has however most certainly triggered the transformation of the existing brokerage business model—for better or worse.

Danger Index

56.0

Probability

4.0

Timing

4.0

Impact

3.5

INDEX
Danger evaluated in terms of PTI to provide comparison between the dangers/sections of the report. Danger index, represents a composite, overall score.

TECHNOLOGY BECOMES A RUNAWAY TRAIN

The financial resources necessary to build the technology solutions required exceed the average broker's ability to remain competitive.

IN CONTEXT

There is a widely held assumption that technology will make everyone and everything better. That's simply not true. But at the same time, technology has changed the world.

Around 40 percent of the world's population has an Internet connection today. In the early days of 1995 it was less than one percent. Within a decade the number of individuals connected to the Internet reached its first billion in 2005; a second billion in 2010, and a third billion in 2014. By the end of 2016 it is estimated that it will eclipse half of the world's population. As for connected devices, it is expected that the number will exceed 4.9 billion in 2015, up 30 percent from 2014, and will reach 25 billion by 2020. But the number of Internet users and connected devices drive many other consumer trends. Digital disruption is now felt on all levels of business. This huge wave of innovation makes it very hard for small real estate entrepreneurs to remain competitive and relevant.

AUTHOR'S PERSPECTIVE

Technology innovation has taken place at an alarmingly rapid rate, but brokerage companies aren't technology companies, nor are they structured to grow at this rate. Even many of the large brokerage companies and national franchises, with more capital than most in the industry, are unable or unwilling to invest the financial and human resources needed to compete with publicly funded technology companies. It never was a level playing field, but the gap is becoming wider and wider, and it will become increasingly harder for real estate brokerages to create or deliver the latest state of the art technology in any specific area. Things are just moving too fast.

> *"Beware of digital overload and technology fatigue."*

Danger Index

48.0

Probability

4.0

Timing

4.0

Impact

3.0

INDEX
Danger evaluated in terms of PTI to provide comparison between the dangers/sections of the report. Danger Index, represents a composite, overall score.

DANGER B8 FSBO DEVELOPS INTO A DO-IT-YOURSELF MODEL

With so much real estate information and so many apps at their fingertips, it has never been easier for consumers to buy and sell real estate.

IN CONTEXT

The For Sale By Owner (FSBO) option has been available in the industry for many decades, and has been used primarily on an individual basis (local level) by consumers that want to take control of the transaction in order to save money. The FSBO share of the real estate market in 2014 amounted to nine percent of the 5.1 million houses sold. Should this method be packaged in a more dynamic and formal offering—bundled together with a portfolio of technology and mobile applications—and be aggressively marketed and sold to consumers, the model could gain rapid adoption by a new generation.

Today's consumer is demanding choice in every aspect of the real estate process from search to closing, and there are numerous companies offering new tools in the DIY arena that are steadily empowering this "digital consumer." The question facing the industry is whether or not the DIY movement will become a major disruption to the way the industry currently operates, or will it just continue to bump along as it has in the past. There are numerous factors impacting that outcome, like FSBO sites that are using technology to reach out to the consumer at the outset of the process, providing them with a flexible DIY structure and an easy process to follow.

EXAMPLES OF DIY WEBSITES

FSBO.com

Owners.com

ListByOwnerInMls.com

BuyerCurious.com

10Realty.com

SalebyOwnerRealty.com

AUTHOR'S PERSPECTIVE

Community marketing opportunities can be found in many colleges, universities, hospitals, and other professional environments that experience high levels of employee relocation. These environments have in essence created and facilitated private property listing operations that enabled homeowners to sell their properties directly to new arrivals in their communities.

In a similar vein, more and more neighborhoods have undertaken to create websites that provide hyper-local information regarding a wide range of lifestyle related subjects. By enhancing the FSBO concept with an automatic value model, global portal exposure, access to standard forms, and with the emergence of 'RealtyZoom', an Enabled FBSO is increasingly being explored.

If this Do-It-Yourself variation of the traditional FBSO was to gradually double the existing FSBO niche, it could result in billions of dollars in real estate commissions being saved by the consumer and lost by the real estate industry.

Danger Index

42.0

Probability

4.0

Timing

3.0

Impact

3.5

INDEX
Danger evaluated in terms of PTI to provide comparison between the dangers/sections of the report. Danger index, represents a composite, overall score.

SALES TAX THREATENS MARGINS

Sales tax on real estate commissions impacts already thin profit margins and forces fundamental change to the already strained broker/agent relationships.

IN CONTEXT

States are scrambling for income in the face of declining tax revenues and increasing demands for services. Advocates have indicated that the taxing of services is simply a matter of fairness and good sense, and that there should be a "spreading out the tax burden" as widely as imaginable. According to the Federation of Tax Administrators, a majority of states apply their sales tax to less than one-third of 168 potentially taxable services.

For real estate, the touch point of taxes on "services" is the sale from the employer (broker) to the ultimate purchaser (consumer). To the extent that the tax is passed on, or built into the commission, it is owed by the broker, and thus increases the cost of the sale. In South Dakota for example, commissions received by a real estate broker under any type of agency agreement, or any fee originating from the sale of real property sold in the state—regardless of the broker's or agent's residence—are subject to state and applicable municipal sales tax based on where the property is located. The sales tax is due during the reporting period in which the broker receives the commission, determined by the time of closing.

STATES THAT TAX REAL ESTATE COMMISSIONS

Examples of states that have already introduced the taxing of real estate commissions.

AUTHOR'S PERSPECTIVE

At the present time, sales tax on real estate commissions is not a widespread practice, but the danger of it gaining more traction is real and will increase as more state taxing authorities explore options for enlarging their tax base.

A service tax on commissions would have a direct impact on the sales price and the entire real estate industry as fees (and taxes) are—and have historically been—passed on to the consumer.

Danger Index

40.0

Probability

4.0

Timing

2.5

Impact

4.0

INDEX
Danger evaluated in terms of PTI to provide comparison between the dangers/sections of the report. Danger Index, represents a composite, overall score.

PORTALS LEVERAGE LEAD GEN DOMINANCE

Portals leverage online dominance and morph their business model into a more aggressive transaction-based revenue sharing concept.

IN CONTEXT

It's estimated that the real estate brokerage industry annually spends between $6 to $10 billion on advertising and promotion. Historically this has been spread across multiple media sources, including printing, magazines, newspaper, and online advertising and promotional items. As the online portal channel continues to grow, a handful of companies now offer—for the first time—advertising options on a national basis, thereby consolidating the advertising revenue. At the present time the leading portal's revenue from that pool is approximately $200 million, which accounts for only about two to three percent of the total while their online traffic garners between 30 to 50 percent of the eyeballs browsing for houses. With portals' publicly stated goal to capture more of the agent ad dollar market revenue, it is not improbable that they may in the future capture 30 to 50 percent of the advertising dollars.

"Agents expect portals to act in their best interests...Why? Portals have no higher responsibility to the industry. They are a business, like everyone else, out to make a buck."

AUTHOR'S PERSPECTIVE

The re-directing of the industry's ad dollars spent on new sources is significant, but it does not threaten the industry per se. It is, in essence, a consolidation and reallocation of existing advertising and marketing dollars.

The brokers' fear is that once a national company obtains a dominant share, it may enable that company to change its revenue model to one based on transactions, resulting in a higher fee.

With a growing number of agents becoming increasingly dependent on portals to provide them leads, it will be interesting to see if this new source of lead generation becomes the dominant choice and thereby dramatically impacts other existing sources. Agents will most likely continue to work for brokers but may be less dependent on them as the result of their receiving a large number of leads via the portals.

Danger Index
36.0

Probability
3.0

Timing
4.0

Impact
3.0

INDEX
Danger evaluated in terms of PTI to provide comparison between the dangers/sections of the report. Danger Index, represents a composite, overall score.

DANGER CHECKLIST: DANGERS IMPACTING BROKERS

DATA CLASSIFICATION

In order to best evaluate and present each danger, an Index was created based on the probability (P) of each danger occurring, the future timing (T) of the potential danger, and the possible impact (I) of each danger. The combined scoring of these factors results in the PTI Index. The index is not scientific but rather a combined and weighted representation of the research, surveys, and interviews that enable the dangers to be placed in order of significance as to the level of danger they present.

INDEX

In evaluating each danger, the overall result is presented in the PTI index (Probability, Timing and Impact), which ranks the danger in order to provide a level of comparison between the dangers/sections of the report. The Danger Index represents a composite, overall score.

#	Probability	Timing	Impact
5.0	100% Chance	1 Year	Game Changer
4.0	80% Chance	1 - 3 Years	Major Impact
3.0	60% Chance	3 - 5 Years	Moderate Impact
2.0	40% Chance	5 - 10 Years	Some Impact
1.0	20% Chance	10 + Years	No Impact

Danger Index	
81-100	Critical
61-80	Severe
41-60	High
21-40	Moderate
0-20	Low

	Danger	Probability	Timing	Impact	Index
☐	B1 Regulatory Tsunami Hits	5.0	4.0	5.0	100.0
☐	B2 Paper Brokerages Cause Disruption	5.0	4.0	4.0	80.0
☐	B3 Brokers Lose Control of Data	4.0	4.0	4.5	72.0
☐	B4 A Consumer Brand Crashes the Party	4.0	4.0	4.0	64.0
☐	B5 New Business Models Go Mainstream	4.5	4.0	3.5	63.0
☐	B6 Brokers Simply Go Broke	4.0	4.0	3.5	56.0
☐	B7 Technology Becomes a Runaway Train	4.0	4.0	3.0	48.0
☐	B8 FSBO Develops into a Do-It-Yourself Model	4.0	3.0	3.5	42.0
☐	B9 Sales Tax Threatens Margins	4.0	2.5	4.0	40.0
☐	B10 Portals Leverage Lead Gen Dominance	3.0	4.0	3.0	36.0