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IMPACT ON CONSUMERS OF BANK AND FINANCIAL HOLDING COMPANIES' ENGAGEMENT IN REAL ESTATE BROKERAGE AND PROPERTY MANAGEMENT

HEARING

BEFORE THE

SUBCOMMITTEE ON FINANCIAL INSTITUTIONS

OF THE

COMMITTEE ON
BANKING, HOUSING, AND URBAN AFFAIRS
UNITED STATES SENATE

ONE HUNDRED SEVENTH CONGRESS

SECOND SESSION

ON

THE EXAMINATION OF BANKING AND FINANCIAL HOLDING COMPANIES' ENGAGEMENT IN REAL ESTATE BROKERAGE AND PROPERTY MANAGEMENT

MAY 23, 2002

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IMPACT ON CONSUMERS OF BANK AND FINANCIAL HOLDING COMPANIES' ENGAGEMENT IN REAL ESTATE BROKERAGE AND PROPERTY MANAGEMENT

THURSDAY, MAY 23, 2002

U.S. SENATE,
COMMITTEE ON BANKING, HOUSING, AND URBAN AFFAIRS,
SUBCOMMITTEE ON FINANCIAL INSTITUTIONS
Washington, DC.

The Subcommittee met at 10:05 a.m. in room SD–538 of the Dirksen Senate Office Building, Senator Tim Johnson (Chairman of the Subcommittee) presiding.

OPENING STATEMENT OF SENATOR TIM JOHNSON

Senator JOHNSON. The Subcommittee on Financial Institutions will come to order.

I want to thank you for joining us for today's oversight hearing to discuss the impact on consumers of national bank and financial holding companies' engagement in real estate brokerage and property management.

Welcome, Ranking Member Bennett, who I am advised will be with us very soon, and my colleagues, and thank our distinguished panel of witnesses for taking the time to help the Financial Institutions Subcommittee consider this important issue.

Over the past several months, the consumer real estate market has served as an anchor in stormy economic seas, and I have been impressed by the resilience of the marketplace. It has been clear for some time the critical role that homeownership plays in creating strong communities, strong families, and helping individuals achieve the American Dream. We have come to understand, though, the additional role that consumer real estate plays in our economy.

For these reasons, it is critical that we proceed with caution with any changes in the real estate market. At the same time, however, under Gramm-Leach-Bliley, Congress did intend to create flexibility for the financial services industry to innovate. We should be mindful of the manner with which we proceed because the potential change provides an early test of the Gramm-Leach-Bliley regulatory process.

Today, it is not our job to discuss any particular proposal, but, rather, to step back to discuss the general issue of what impact financial holding company and national bank affiliate entry into the real estate brokerage and property management businesses might

have on American consumers. It is far too easy to lose sight of why this debate is important. We need to keep in mind that our objective is to keep America strong through a strong economy, strong communities, and continued opportunity for all of our citizens to achieve the dream of homeownership.

With that, it is an honor to introduce our panel of excellent witnesses, who have clearly spent considerable time and energy producing some very thoughtful testimony. We appreciate their willingness to appear before us today, and I will introduce three of the four guests, and then yield to Senator Santorum, when he comes in shortly, to introduce Mr. Hanna, who hails from the State of Pennsylvania.

First, I am pleased to introduce a fellow South Dakotan, Mr. Tom Murphy, of Sioux Falls. Tom, who is here today on behalf of the National Association of REALTORS®, is the President of the South Dakota Association of REALTORS®, which has been serving my home State for over 50 years.

Tom is affiliated with Chell REALTORS® of Sioux Falls, and is a graduate of the REALTORS® Institute. Tom has been, and is very active at the national, State and local REALTOR® levels. He is a past State Governmental Affairs Chairman of the South Dakota Association of REALTORS® and is serving on the grievance committee of the Sioux Falls Board of REALTORS® and has served in numerous task forces and work groups at the State and local levels.

We appreciate Tom taking time from both his job as a REALTOR® and the father of three to join us here today. Tom and his wife, Dr. Carla Murphy, of Physicians Laboratory of Sioux Falls, are widely recognized community leaders, and Tom's willingness to travel to Washington bears out his commitment to his community and to his colleagues.

Next, we welcome Mr. James Smith, President of the American Bankers Association. Mr. Smith is Chairman and Chief Executive Officer of Citizens Union State Bank and Trust in Clinton, Missouri. Mr. Smith has a long and distinguished career in banking, having entered that profession in 1967. I would also note that there appears to be a link between baseball and banking. Like the distinguished Senator from Kentucky, Mr. Smith played professional baseball in his past life, was part of the New York Yankees from 1963 to 1966, and we have no doubt that he has been practicing his pitch for today's hearing.

[Laughter.]

During his service with the ABA, Mr. Smith has chaired the communications council, the government relations council, the bankers electronic network, and task force on government relations grassroots.

Mr. Smith, thank you for being with us today.

Mr. SMITH. Thank you.

Senator JOHNSON. Our next guest and witness is John Taylor, President and Chief Executive Officer of the National Community Reinvestment Coalition, whose stated mission is to promote economic justice.

With over 820 national, regional, and local organizations, the NCRC has led the effort to increase low-income and minority access to credit and capital.

I would like to thank you, Mr. Taylor, for your organization's hard work on behalf of so many Americans. Mr. Taylor has worked in the community development and reinvestment industry for over 24 years, and in 2001, ran for the U.S. Congress to fill a vacancy in the 9th Congressional District of Massachusetts.

Mr. Taylor has been widely recognized for his commitment to community service and in 1996, received a presidential appointment to the community development financial institutions advisory board. He also serves on a number of boards and has received numerous awards and citations over the years for this work in economic justice efforts, including the Martin Luther King, Jr. Peace Award, two Congressional citations awards from the Congress, and many others.

Mr. Taylor, thank you for taking time to appear with us today.

Our final witness is Mr. Howard Hanna, from Pittsburgh, Pennsylvania. And I will defer to Senator Santorum to introduce Mr. Hanna.

But before I yield, I would ask that a written statement prepared by the Financial Services Roundtable and the American Homeowners Grassroots Alliance be included in the record. And we will proceed from there.

We will await Senator Santorum's arrival for the introduction of Mr. Hanna, and I would recognize my Ranking Member, Senator Bennett, for any introductory comments that he might choose to make.

STATEMENT OF SENATOR ROBERT E. BENNETT

Senator BENNETT. Thank you very much, Mr. Chairman. I appreciate it, and I apologize for being a minute or two late.

The Gramm-Leach-Bliley Act was a culmination of, I guess, 20 years of effort in the Congress to try to resolve the question of how banks and other financial institutions would operate in a non-depression atmosphere.

The Glass-Steagle was drawn up in a very different economic circumstance. I remember as a Member of this Subcommittee when Don Riegle was the Chairman, they were talking about it. When Al D'Amato was the Chairman, we made a number of runs at trying to deal with it.

It was not until Phil Gramm became the Chairman that we finally got a resolution, at least momentarily, of many of the issues of banking and commerce.

Now we are seeing the first test of regulations that have been proposed under Gramm-Leach-Bliley. I think it is very timely that we have the opportunity before the Congress to examine all the implications of what has been proposed.

So, I congratulate you on holding the hearing. I look forward to hearing from the witnesses and appreciate their willingness to come and share with us their views and attitudes on this very important subject, as I say, the first real test of revisiting, the possibility of revisiting, Gramm-Leach-Bliley that we have had since that landmark legislation was passed.

Thank you, Mr. Chairman.

Senator JOHNSON. Thank you, Senator Bennett.

Senator Reed.

COMMENTS OF SENATOR JACK REED

Senator REED. Mr. Chairman, I just want to commend you for holding this hearing. It is a very important topic for both the banking industry and the real estate industry. And I would like to submit my formal statement to the record.

Thank you, Mr. Chairman.

Senator JOHNSON. Very well.

Senator Allard.

STATEMENT OF SENATOR WAYNE ALLARD

Senator ALLARD. Mr. Chairman, I would like to thank you for convening this hearing.

As my colleagues know, this is an issue that I have followed very carefully. I appreciate the opportunity to gather more information.

Last year, I introduced Senate bill 1839, the Consumer Choice in Real Estate Act of 2001. This bill would clarify Congressional intent that real estate brokerage and management are not financial activities and would therefore retain the separation of commerce and banking that we intended during the consideration of the Gramm-Leach-Bliley Act in 1998.

The Gramm-Leach-Bliley Act closed the unitary thrift loophole that allowed a single savings and loan to be owned by a commercial entity. This clearly established that banking and commerce were not to mix.

Congress explicitly defined several functions to be financial in nature or incidental to finance to clarify the separation. Real estate management and brokerage services were not defined as financial services.

Congress already established a clear position regarding banks' involvement in real estate management and brokerage activities. My bill would reiterate that prohibition. I believe that we should not permit Federal regulators to preempt the intent of Congress.

The real estate and banking industries have served America well, and I believe that the current system provides consumers with many important options. I know that the regulators received many letters during the comment period and I commend them for taking the time to allow all interested parties to comment and for their pledge to carefully review all comments.

I believe that this hearing is a good opportunity to continue the dialogue on the matter of banks' involvement in real estate management and brokerage. I know that our witnesses will have very strong viewpoints and I look forward to their testimony.

Thank you, Mr. Chairman.

Senator JOHNSON. Thank you, Senator Allard.

Senator Crapo.

STATEMENT OF SENATOR MIKE CRAPO

Senator CRAPO. Thank you very much, Mr. Chairman. I too appreciate your holding this hearing. In fact, I think it was more than a year ago that I asked the Subcommittee to hold a hearing,

and I appreciate the fact that we are holding one, and it is interesting that it is still timely.

The Treasury and Federal Reserve have seen fit to delay their rulemaking on this matter. I do not know whether that is a good thing or a bad thing. But at least it gives this Subcommittee time to hold this hearing and to evaluate the issues.

When I served in the House, I was a part of the effort to review these issues. As I was elected to the Senate and on the Banking Committee, I was a part of the Gramm-Leach-Bliley effort.

As a part of that, I feel that we should let the law work, but also, oversee the law to make sure that it does work. And if this hearing can give us, as well as the Treasury and the Federal Reserve, guidance on what Congress intended and what we think is the appropriate direction which the regulations should take, then so be it.

But, for me, this is going to be an informational hearing. I want to hear the arguments on both sides laid out. I want to be able to compare those arguments to what we should achieve in the legislation, and then determine whether it is appropriate for Congress to take any further action at that point.

So, again, I thank you for this hearing.

Senator JOHNSON. Thank you, Senator.

Senator Santorum—and I would note that we withheld introductions of Mr. Hanna pending your arrival. We are pleased to have you here.

Senator SANTORUM. Thank you, Mr. Chairman.

Senator JOHNSON. Any opening remarks?

STATEMENT OF SENATOR RICK SANTORUM

Senator SANTORUM. Let me apologize to my constituent for having his introduction being withheld. But I appreciate you doing so, so I would have an opportunity to introduce someone who has been a friend of mine for a long time, from my hometown of Pittsburgh, someone who has been just a great citizen of southwestern Pennsylvania, who owns the largest real estate company in southwestern Pennsylvania.

They are tremendous corporate citizens and assets to our region and Howard Hanna, in particular, is someone who I have a tremendous amount of respect for.

My respect has been increased in that here he is as a REALTOR® coming and testifying on this issue, which is not in conformity with many in the real estate profession. I asked him whether he was bringing security to this hearing.

[Laughter.]

But he assured me that, other than Chip Roach, he was not going to bring security.

[Laughter.]

I do commend him for his articulation on this issue. I think he does provide a thoughtful perspective on this very important issue. I want to say that Senator Crapo's remarks are very close to mine. I think that this is an issue that we need to look at.

I have not come down firmly in stone on one side or the other, but I think it is important to weigh all the evidence. I think Mr. Hanna's perspective is a very thoughtful one and one that I think that this Subcommittee can benefit greatly from, and I appreciate

his willingness to come forward and share that with the Subcommittee.

Thank you, Mr. Chairman.

Senator JOHNSON. Well, thank you, Senator.

We will operate on a 10-minute clock during the course of this hearing. And so, we will begin testimony with the first witness, affording 10 minutes for each of the witnesses.

We will withhold Subcommittee questioning until after all four witnesses have had an opportunity to either read or to summarize their comments before the Subcommittee.

The first witness is Mr. Tom Murphy.

Tom.

STATEMENT OF TOM MURPHY
PRESIDENT, ASSOCIATION OF REALTORS®
SIOUX FALLS, SOUTH DAKOTA
REALTOR, CHELL REALTORS®
REPRESENTING
THE NATIONAL ASSOCIATION OF REALTORS®

Mr. MURPHY. Good morning, Chairman Johnson, Senator Bennett, and Members of the Subcommittee. My name is Tom Murphy. I am a REALTOR® with Chell REALTORS®, a small residential real estate firm in Sioux Falls, South Dakota. I am also President of the South Dakota Association of REALTORS®. Our State Association membership of over 1,400 REALTORS® are engaged in helping people buy, sell, and manage real estate every day.

I am here on behalf of the National Association of REALTORS®, which represents more than 800,000 members engaged in all aspects of commercial and residential real estate. I want to thank you for the opportunity to testify today on this critical issue.

It is important for *all* of us to take a good look at how the economy and consumers would fare if banks are allowed into the real estate business. That is one reason why I am glad we have the views of consumer groups represented on this panel.

Mr. Chairman, you and your Subcommittee Members are to be commended for examining all perspectives on this proposed regulation—those of the little guy, as well as those of the big guy.

As I mentioned, my business is a small, one-office real estate firm, just like nearly 80 percent of REALTOR® firms. My colleague from Pennsylvania here represents a large regional, multioffice firm. Obviously, we come here today to present different perspectives of this Nation's dynamic and diverse real estate market.

The fact that some of our members can differ on an issue, while respecting and supporting each other on most, is a great example of the vitality of the National Association of REALTORS®. It is a sign of the hearty competition of the real estate business today.

My comments today represent the overwhelming majority of NAR's members. Ninety-six percent of our members support the position of the National Association of REALTORS® to oppose this rule. Eighty-two percent of large broker/owners support this position, while 81 percent of our members believe we should be doing even more to stop the banks from unfairly entering our business.

We firmly believe that redefining real estate brokerage, leasing, and property management as financial in nature is totally unac-

ceptable because it mixes banking and commerce. If the Nation's most aggressive megabanks are allowed to add real estate to their long list of approved activities, you can be sure that consumer choices in real estate services will shrink.

The Nation's bankers, who petitioned the Federal Reserve and Treasury for this proposed rule, should not gain by regulation what they failed to gain by legislation. In 1999, Congress clearly went on record supporting the separation of banking and commerce.

Oddly enough, the American Bankers Association strongly supported an amendment you offered, Mr. Chairman, during the Gramm-Leach-Bliley debate to bar unitary thrift holding companies from engaging in commercial activities like real estate brokerage. It now appears that members of the ABA would like to corner the market on commercial businesses like real estate brokerage, leasing, and management.

Currently, we have a balanced marketplace for commerce, banking, and financial services. Let me direct your attention to the two charts enclosed in my statement.

The first chart shows how the commercial and banking industries compete in the "financial services" arena. REALTORS®do not engage in banking. They do not take deposits or run ATM's.

Again, REALTORS® are not engaged in banking. Banks do not sell real estate. Banking and commerce are separate. It is that simple. Otherwise, why shouldn't banks sell cars or appliances?

The second chart shows that in the arena where banks and REALTORS® do compete on mortgage originations, banks are already the winners. REALTOR®-affiliated mortgage lending companies only originate about 5 percent of mortgages, while the large banks handle 44 percent.

Today's competition occurs in the financial services arena where it belongs. Consumers benefit from this arrangement because the direct competition for financial services between commercial companies and banks results in greater consumer choice and consumer service. When banks say they want "one-stop shopping," what they are really saying is they want "one-bank shopping."

The reality is that the entry of Federally chartered banks into the real estate brokerage business would tilt this balanced marketplace toward the Nation's megabanks. It would pit Government subsidized banking companies against privately funded real estate enterprises. It would put taxpayer money at risk.

Mr. Chairman, the National Association of REALTORS® believes this issue is just too big to be decided by the regulators. The decision belongs with the Nation's lawmakers. That is why we have called on Congress to enact The Community Choice in Real Estate Act, S. 1839, and H.R. 3424, a companion bill in the House, to clarify Congressional intent.

REALTORS® from all over the country have sent more than 100,000 letters to their Congressional representatives urging support for this bill. We have sent more than 40,000 letters to the Federal Reserve and the Treasury expressing our opposition to the proposed regulation. And we have sent more than 50,000 letters to President Bush urging his support.

So far, H.R. 3424 has generated tremendous support in the House, with more than 230 cosponsors. So far, a dozen Senators

have cosponsored S. 1839. Last month, Treasury Secretary O'Neill announced that he plans to postpone making a decision on this issue until next year. The ball is back in your court. It is time for Congress to resolve this issue.

Mr. Chairman, REALTORS® are not alone on this issue. A diverse group of trade associations and consumer groups stand with us on this one.

Passage of the Community Choice in Real Estate Act will set the record straight. At the same time, it will ensure more balanced competition and more consumer choice.

This legislation will help to keep local entrepreneurs and businesses operating in our communities. It will help to keep some of our best community leaders and volunteers in place.

REALTORS® are more than business people. We are community leaders. Look in countless cities and townships across America and you will find it is a REALTOR® serving as a den mother, a REALTOR® who is leading the city-wide cleanup, a REALTOR® who is hosting the candidate meet-and-greet, and a REALTOR® who is coaching Little League. REALTORS® are linked to their communities in more ways than simply through their businesses. REALTORS® have a stake in the same neighborhoods where their clients live or want to live.

Finally, this proposal just doesn't make sense. Banks have it backward. Real estate brokerage is not incidental to a financial activity. It is the mortgage that is, in fact, incidental to buying a home. Twenty percent of all the homes in America involve no lender financing at all.

America's system of homeownership is the envy of the world. Homeownership is at an all-time high. Five out of six homebuyers and home sellers are satisfied with their real estate agent and they would use him or her again. Let's not destabilize this pillar of our economy and relationship that works in communities throughout America.

Thank you.

Senator JOHNSON. Thank you, Mr. Murphy.

Mr. Smith.

STATEMENT OF JAMES E. SMITH
PRESIDENT, AMERICAN BANKERS ASSOCIATION
CHAIRMAN AND CHIEF EXECUTIVE OFFICER
CITIZENS UNION STATE BANK AND TRUST COMPANY
CLINTON, MISSOURI

Mr. SMITH. I want to thank you, Mr. Chairman, for holding this hearing.

I believe that bankers and REALTORS® have more in common on this issue than the rhetoric suggests. Many agents and bankers already work closely with one another. We both believe that customers deserve to have the best possible service. We both want customers to have many choices of whom to deal with so they can seek out that agent or company that they trust most. And we both believe that any financial service should be provided in a safe and sound manner—including adhering to all licensing, sales practices, and continuing education requirements.

If banks could offer real estate services, consumers would have more choices of real estate firms when buying or selling a home. Real estate brokers would have more choices of potential employers. And real estate companies would have more choices of companies to partner with, providing new sources of capital and technology. By prohibiting bank involvement, S. 1839 results in fewer choices for everyone.

As we begin our discussion, it is important to note that combining real estate mortgage and banking services is not a new or unusual activity. Real estate firms do it. Insurance companies do it. Securities firms do it. And well over half of the depository institutions in this country, including many of the largest banks, can do it. In fact, my community bank in Clinton, Missouri, already has the authority to do it. The packages many real estate firms offer provide valuable cost, convenience, and service options. This is good for consumers. The ABA believe that all banks should have the same opportunity to meet the needs of our customers.

This issue of open and fair competition is not new—it has been debated in this body for years. What is new is that in 1999, Congress enacted the Gramm-Leach-Bliley Act. In the 20 years of debate on the Gramm-Leach-Bliley Act, Congress often found itself in the middle of arguments between financial services industries about who should do what. The result was an out-of-date financial system.

In light of these marketplace realities, and the pervasive changes due to technology, the need for regulatory flexibility is vital. Congress recognized this and expressly left it to the Fed and the Treasury to determine what additional services could be offered by banks. The proposal on real estate follows exactly the process Congress set forth.

It should be allowed to work, and Congress should not be put back in as referee for future competitive disputes. After so many years of effort to enact the Gramm-Leach-Bliley Act, it would be sad indeed to see Congress undermine its key provision the very first time it is used.

Let me assure you that this issue is important to banks of all sizes. In fact, the ability to offer real estate services may be more important for smaller banks in rural areas like mine. In these communities, the bank is perceived as having the best information on properties for sale, including farmland. I believe, as do my fellow community bankers, that these services would significantly benefit our customers and our communities.

In my small community, I am losing customers. The local real estate firm is offering mortgages and insurance. Since the customer often goes to the real estate firm first, I lose out on the ability to offer those products. And quite frankly, the customer misses out on the opportunity to have a choice. I may need to partner with a local firm to compete.

Furthermore, as national chains take over local real estate firms, any remaining local firms may have trouble competing. One of them may want to partner with me. This is exactly the kind of scenario Gramm-Leach-Bliley was designed to take into account. That law knocked down the walls between financial players and it gave the Federal agencies flexibility to decide what new powers would

be appropriate for banks as markets change. So let's look ahead, not backward.

We want to work with REALTORS® to realize advantages for both our industries. We want to cooperate, not compete. To prosper, not pull down. To make the most of the skills and advantages each side brings to a common goal—thriving in a marketplace of rapid change. Above all, we want to be able to partner with REALTORS® to provide good, honest real estate services to America's homeowners and homebuyers.

I would like to add for the record, that the market origination number that the NAR has just provided is 1 percent. We would like to add for the record information that the market share of just three firms alone—Cendant Mortgage, GMAC, and Weickert Mortgage—is 10 percent in today's market, not 1 percent as proposed.

Thank you, Mr. Chairman.

Senator JOHNSON. Thank you, Mr. Smith.

Mr. Taylor.

STATEMENT OF JOHN TAYLOR
PRESIDENT AND CHIEF EXECUTIVE OFFICER
NATIONAL COMMUNITY REINVESTMENT COALITION
WASHINGTON, DC

Mr. TAYLOR. Good morning, Chairman Johnson, Senator Bennett, and other distinguished Members of the Subcommittee and staff representing other Members.

My name is John Taylor and I am President and CEO of the National Community Reinvestment Coalition, and I am here representing 820 community-based organizations and local public agencies who work daily to promote economic justice in America and to increase fair and equal access to credit, capital, and basic banking services to traditionally underserved populations in both urban and rural areas.

Mr. Chairman, I ask that my written statement be entered into the record.

Senator JOHNSON. It is so ordered.

Mr. TAYLOR. Thank you. On behalf of NCRC, I thank you for the opportunity to testify before you today on this important issue that will impact our Nation's progress in extending the American Dream of homeownership to minority and low- and moderate-income families—banks becoming real estate brokers. NCRC's community organizations are at the helm of driving the reinvestment movement. Today, as a result of the fair lending laws like the Community Reinvestment Act, which turns 25 this year, poor neighborhoods have been empowered by bank partnerships with community organizations to address credit needs and missed market opportunities. As a result, the number of loans to minority and working class borrowers over the last decade has increased faster than the number of loans to the more affluent borrowers. Bank CRA commitments have grown from a few million dollars a year to over $50 billion annually. Without these loans and commitments, the economic flow of private capital and credit into our communities would be extinct and hence, certain death for disinvested neighborhoods.

The arena of competition has dramatically shifted in the wake of Gramm-Leach-Bliley, in our opinion, which we believe actually

blurred the distinction among financial industries. In March 2000, the Federal Reserve Board issued a list of the first 117 bank holding companies that elected to become financial holding companies to take advantage of the opportunities of entering into the insurance and securities markets. As of April 2002, over 600 bank holding companies have elected to become financial holding companies in order to diversify their businesses. Conversely, less than a dozen nonbank companies have converted to financial holding companies for the purpose of seeking a banking charter.

NCRC supports competition in its truest sense—when parties act independently and offer the most favorable terms to secure business. But one must wonder if today's financial market upholds the true meaning of competition when it seems like Gramm-Leach-Bliley has allowed all roads to lead back to the bank. While nonbank lenders own real estate companies, they have not utilized Gramm-Leach-Bliley to amass the market power that banks now enjoy after their mad rush to become financial holding companies. Would adding real estate to the menu of businesses that banks can own level the playing field between banks and nonbanks, or only serve to make banks more powerful to the detriment of real competition in the financial industry?

NCRC maintains that the addition of real estate to the already dizzying array of products now offered by "financial supermarkets" will lead to an even greater consolidation of bank market power and result in fewer choices for consumers. Our worst nightmare is a consolidated financial market that includes real estate brokerage is: A bank offers favorable terms to its real estate affiliate, giving it significant advantage over a competing real estate business that does not have an affiliate; The bank with the real estate affiliate stops offering loans to customers of nonaffiliated real estate competitors; The number of product choices offered to customers of nonaffiliated real estate businesses decreases, resulting in higher cost loans for consumers.

When considering banks in real estate, policymakers have not adequately addressed the negative impacts on small real estate businesses of further industry consolidation. And I think you heard Mr. Murphy allude to that. The over 375,000 women- and minority-owned small businesses in our country have played a significant role in community revitalization. Many of these real estate entrepreneurs have established themselves in working class communities and dedicated their business to helping rebuild formerly redlined neighborhoods through partnerships with affordable homeownership programs.

NCRC strongly takes the position that by allowing banks into the real estate business, small real estate businesses will be forced out of the marketplace by the monopolized "financial supermarkets."

Finally, on this point, the banking industry holds a special status, different from any other industry. They are the stewards of the American public's wealth. To encourage people to do business with these stewards, we taxpayers guarantee that investors cannot lose if they do business with these banking institutions.

With FDIC insurance, we guarantee the viability of these institutions. Was it the intent of Congress in doing that, that we were ensuring that these banks would be managed safely and soundly and

making sure that credit and capital was made available to consumers, or was Congress really thinking that banks should become real estate brokers and enter other forms of businesses and possibly lose the public's money and cut off the spigot to credit and capital?

The next area I would like to address in regards to today's subject matter is the consumer protection issues. In testifying before you today, I must be honest to NCRC's mission of economic justice and state emphatically that injustice exists in the banking, insurance, and real estate industries. Until those problems are solved to protect borrowers and consumers, these markets should not be commingled.

According to the Department of Housing and Urban Development, a report just released entitled, *Black And White Disparities in Subprime Mortgage Refinance Lending,* borrowers in upper-income African-American neighborhoods were 2.9 times more likely to refinance with a subprime lender than borrowers in upper-income neighborhoods overall.

Our own research at NCRC has found similar disparities. For example, major subprime and manufactured home lenders made 47 percent of the refinance loans in predominantly African-American and Hispanic neighborhoods in the District of Columbia in the year 2000, a significant increase from the 39 percent of the loans in 1999, and 25 percent of the loans in 1994. In contrast, subprime and manufactured home lenders made less than 4 percent of the loans in predominantly white neighborhoods in the 3 years of the study.

The major secondary market institutions have found pricing inefficiencies in the subprime loans. Freddie Mac states that up to 30 percent of subprime borrowers which they securitized were in fact qualified for prime loans. Fannie Mae's Franklin Raines is quoted as saying almost half of the subprime loans they see should have received prime loans.

The issue of insurance redlining is also a problem, but unlike home mortgage lending, insurance data is limited only to a handful of States. In California, for example, the Center for Economic Justice found that the average insurer wrote only about 5.57 percent of its private passenger automobile liability policies and only 6.62 percent of its homeowner policies in low-income and minority neighborhoods.

As I mentioned, the real estate market is not without its unscrupulous actors. Property flipping involves buying a home at a low price and then reselling it at a fraudulently inflated price within a short timeframe, often after making only cosmetic improvements to the property. NCRC has seen the following practices employed in property flipping schemes: Real estate investors continuing buying neglected properties at sheriff sales and reselling homes at escalated prices to unsophisticated first-time homebuyers; Targeting immigrant communities, particularly non-English-speaking individuals; Colluding with property appraisers to inflate property value; Tricking homeowners into thinking they are dealing with legitimate real estate companies; and Defrauding the Government by steering people to FHA financing, knowing the property is either inflated or has been frequently flipped.

In the year 2000, the Department of Housing and Urban Development's Inspector General testified about the rampant flipping rings the agency was combatting. One investigation alone uncovered over 1,200 flipped loans, totalling approximately $160 million. Twenty-five percent of the loans were in default. The IG indicated that approximately one hundred representatives of lending and real estate industries colluded on this scheme. If Congress allows banks and real estate firms to combine without strengthening the consumer protection laws, our communities are more likely to be the victims of these scams than beneficiaries of greater product choice and lower prices.

A couple of years ago, I and several others testified before different committees in Congress to not undo the 70-year-old Glass-Steagle law that allowed commercial banks to merge with securities firms and insurance companies. We argued that it would injure the banking industry and, more importantly, consumers' interests.

Not even 2 full years have passed before we see the perfect example of why Congress of 70 years ago argued against the merging of the banking industry with other industries—the fear of scandal, self-dealing, and swindling of investors. Need more proof of the need for the separation of finance from other industries than the biggest bankruptcy and business failure in the history of the American economy, the Enron swindle.

Mr. Chairman, I see that I am out of time. I just want to close by adding that we strongly oppose, from a consumers' perspective, the allowance of the banking industry into the real estate industry.

Should that occur, and we hope that it wouldn't, we would also hope that, along with that would be some very strong language about the real estate industry being able to provide data and be obligated to not ignore the interests of working-class and working-poor consumers and minorities and women who have difficulties often accessing credit and capital and homeownership.

I thank you for the opportunity to comment.

Senator JOHNSON. Well, thank you, Mr. Taylor.

Mr. Hanna.

STATEMENT OF HOWARD W. HANNA, III
VICE CHAIRMAN, REAL ESTATE SERVICES PROVIDERS COUNCIL, INC. (RESPRO®)
PRINCIPAL AND FORMER CHAIRMAN
THE REALTY ALLIANCE
PRESIDENT AND CHIEF EXECUTIVE OFFICER
HOWARD HANNA REAL ESTATE SERVICES
PITTSBURGH, PENNSYLVANIA

Mr. HANNA. Thank you and good morning, Mr. Chairman, and Members of the Subcommittee. And thank you, Senator Santorum, for the overly kind introduction.

My name is Howard Hanna and I am President of Howard Hanna Real Estate Services, a family owned and operated real estate brokerage company headquartered in Pittsburgh, Pennsylvania, and founded by my parents in 1957.

Howard Hanna Real Estate Service has 66 neighborhood and community offices, serving Pennsylvania, Ohio, West Virginia, and New York State. We also own a mortgage company that was estab-

lished in 1982, Hanna Financial Services, which is licensed in those States, plus an additional nine States in the United States.

Our firm has 1,500 sales associates and employees, of which 1,128, as of Monday, are members of the National Association of REALTORS®. I am proud and honored to be a 32-year member of the REALTORS® Association of Metropolitan Pittsburgh, the Pennsylvania Association of REALTORS®, and the National Association of REALTORS®.

I currently serve as Vice Chairman of the Real Estate Service Providers Council—known as RESPRO®—and I am a member of the Realty Alliance, as well as a past Director and Chairman. I represent both organizations today.

RESPRO® is a national association of approximately 200 residential real estate brokerage, mortgage, homebuilding, title, and other settlement service companies who promote an environment that enables providers across industry lines to offer one-stop shopping for homebuyers.

The Realty Alliance is a national organization of 45 regional residential real estate brokerage firms that provide us with idea sharing venues, industry forecasts and analysis, financial benchmarking, and technology information.

Mr. Chairman, I would like to ask that my written testimony be included in the record, and additionally, the written testimony from Murray Consulting, who performed a one-stop shopping survey that I will be discussing during my comments, be included in the record.

Senator JOHNSON. They will be placed into the record.

Mr. HANNA. Thank you, sir. Together in the year 2001, RESPRO®'s real estate broker members and Realty Alliance members closed over 2.6 million of the total 6 million home sales in the United States, utilizing over 315,000 sales associates who also are National Association of REALTOR® members, and 78,000 employees in our over 57,000 offices.

Like the majority of the Nation's top 350 residential real estate brokerage firms, most RESPRO® real estate broker members and Realty Alliance members also offer mortgage, title, closing and other settlement services.

In fact, according to a 1999 study conducted by the independent consulting firm of Weston Edwards & Associates, the top 350 real estate brokerage firms closed $22 billion in mortgage loans in 1998, and the realty-based and builder-based lending accounted for about 10 percent of the purchased money mortgages in that same year. Edwards also estimated that this amount would double within 3 years.

In fact, senior management from four real estate brokerage firms that own or partially own mortgage companies, who all are RESPRO® and Realty Alliance members, are here with me today: myself from Howard Hanna Real Estate Services in Pittsburgh, Pennsylvania; Dick Christopher, CEO of Patterson Schwartz in Wilmington, Delaware; George Eastment, Executive Vice President of Long and Foster Real Estate in the Washington, DC metropolitan area; and Chip Roach, Vice Chairman of Prudential Fox and Roach REALTORS® in Philadelphia, Pennsylvania.

We believe that the combined purchase money mortgage originations of our four mortgage companies equaled approximately 3 percent of all purchase money mortgage in the country in 2001. So the 5 percent that NAR referred to in its testimony, we have some question about.

Edwards also found in his study that 72 percent of the Nation's 350 largest real estate brokerage firms offered mortgage services in 1998, that 45 percent of those firms offered title insurance, closing, or escrow services, and that 36 percent offered personal insurance.

Mr. Chairman, RESPRO® and Realty Alliance favor the American free enterprise system and open competition. Any bank should be able to compete with us in providing homebuyers with one-stop shopping programs. All available evidence shows that the homebuyers prefer one-stop shopping and that realty-based one-stop-shopping programs offer those homebuyers potential benefits.

The most recent consumer survey in this area was performed in March of this year by Harris Interactive, the parent of the Harris Poll. Harris surveyed over 2,000 recent and future homebuyers and found that 82 percent of the homebuyers prefer using a one-stop-shopping service for their home purchase. The survey also found that 64 percent of the homebuyers who recently used a realty-based one-stop-shopping program had a much better overall home-purchase experience.

Other studies, some of which are described in my written statement, have found that the services offered through realty-based one-stop-shopping programs are not only competitive, but are even lower in cost in many cases, than those offered by independent firms.

RESPRO® and Realty Alliance do not believe the entry of financial holding companies and national banks would change the potential customer benefits of realty-based one-stop-shopping programs.

Over the last two decades, a number of financial conglomerates have entered the residential real estate brokerage business—Sears Roebuck, Metropolitan Life, Merrill Lynch, GMAC, Prudential Insurance Company, Cendant Corporation, and Warren Buffet's Berkshire Hathaway, which now owns the number two largest residential real estate brokerage company in the country.

On the surface, these companies appeared to have significant competitive advantages over traditional real estate brokerage companies, such as national distribution outlets, consumer marketing lists that made it easy to reach everyone, valuable data about buying habits, and name recognition. In fact, Sears even had access to Federally insured deposits through its affiliate, Sears Savings Bank.

Sears, Merrill Lynch, and Metropolitan Life have since left the real estate brokerage business, while Prudential, GMAC, Cendant, and Berkshire Hathaway remain good competitors. Their presence has not changed the basic character of the real estate brokerage marketplace; in fact, many of us believe that their entry has contributed to the development of a wider range of services and products and has caused traditional real estate brokerages, to be more efficient, more consumer-focused, than we ever were before.

Federally-insured financial institutions also have entered residential real estate markets recently, such as Great Western Bank

in California, Metropolitan Financial Corporation in Minneapolis, First Place Bank in Ohio, Empire Savings Bank in Wilmington, Delaware, and Pennsylvania, and Dollar Drydock in Connecticut. However, in a short period of time, most of these financial institutions have either sold their real estate brokerage businesses and entered new markets in which they feel that they can compete more favorably.

Finally, I believe it is important to remember that this would be a two-way street, in that real estate brokerages also would have the ability to own banks.

For example, my company had a close working relationship with a bank that was recently sold in our region. And Howard Hanna Real Estate Services, quite frankly, would have been very interested in purchasing this bank if Federal law had allowed it.

Mr. Chairman, I thank you for the opportunity to testify and I would be glad to answer any and all questions.

Thank you very much.

Senator JOHNSON. Thank you, Mr. Hanna, and thank you, members of the panel.

The Subcommittee will abide by a 10-minute question rule. That doesn't mean that it is mandatory that you consume 10 minutes each on questioning, but we will try to place some limits to make sure that everyone has an opportunity to ask their questions.

Let me begin by asking, with particular reference to Mr. Murphy and Mr. Taylor, I am sympathetic to the desire to maintain a variety of small independent businesses throughout our country. In my home State of South Dakota, we rely on small businesses to serve our small communities, and while large corporations play an important role in the economy, market economics do not always provide incentives to serve those small towns. But there have been concerns raised that bank entry into real estate brokerage could spell the demise of small local REALTORS®.

And yet, it seems that some of the largest corporate conglomerates are real estate brokerages with lending and insurance affiliates which operate today under existing authority. Would you elaborate a bit more on why bank entry into real estate brokerage is different than broker entry into the mortgage and insurance business?

Either one of the two of you can choose to elaborate a bit on that.

Mr. MURPHY. Thank you, Mr. Chairman. First of all, in a State like South Dakota, it would be no different than any other State.

What we have is a situation where, in a community where there is 10 or 20 real estate firms, if one banking institution starts its own real estate firm, the other two will follow in line.

With that, automatically, the smaller businessman cannot compete. They do not have the dollars to compete with the advertising. They cannot afford to lose the money or spend the money that is really stockholders' money.

When that deteriorates, we have fewer people in the business because if you are not working for the bank, we need people to keep generated into our industry. You have put a chokehold on that because if you cannot work for a bank, you cannot get started, then, into this business.

Now that is in a small State. So we will say in 10 of 12 communities in South Dakota, instead of having 150 real estate firms, you would be down to about 25, maybe 20. And with that, you would lose a minimum of 25 percent of the ages that we would look at. And with that also, these people are not going to have jobs in their area. They are all independent contractors. They are all small businessmen. They are being choked out of this.

But if we look at it as national, if you went to a State like California, instead of a thousand offices, you would be down to 6 or 10 megabanks who control the whole market. You have not only controlled the number of independent contractors, they also have the ability to choke out all their competition.

When that happens, it not only takes the number of independent contractors out of the business, but they are also in a situation where they can control the valuation of a property, because if you do not have thousands of REALTORS® involved in this, from many markets, the only comps they are going to have are within their own association. It is a chokehold.

Senator JOHNSON. Mr. Hanna.

Mr. HANNA. Senator, I mentioned Metropolitan Financial, which once owned Edina Real Estate Company in Minnesota. I believe they also had offices in South Dakota. I have not noticed that when they owned Edina Real Estate Company, they took a stranglehold in that market.

Senator JOHNSON. Mr. Smith, since brokers receive compensation on a commission basis, they have a strong incentive to make sure that property sales go through.

There have been instances where appraisers have been pressures by brokers to make sure that the appraised value met underwriting requirements. Is it conceivable that a bank-affiliated broker would have an incentive to pressure the lender in the same way, especially if the two worked in the same organization?

And would you comment just briefly on whether banks have appropriate internal controls to address that kind of concern? Could these pressures lead to substandard underwriting by insured depositories, especially during times when the property sales are slow?

Mr. SMITH. Well, we do have safeguards in place and our appraisers have to be registered and certified and go to school and have the State qualifications in order to be an appraiser for us. And that is required by the FDIC and our regulatory bodies that examine us because they do check the appraiser's qualifications.

It behooves every banking organization to make loans in a very safe and sound manner and to pressure an appraiser to make an appraisal that doesn't fit the qualifications of the real estate would be backward in making a safe and sound loan. And as the CEO of a bank, I want to be sure that my collateral is in place in order for that loan to be repaid properly. So that definitely would not be something that we would want to see.

Mr. TAYLOR. Mr. Chairman.

Senator JOHNSON. Yes.

Mr. TAYLOR. Currently, a broker has a main objective to get you to purchase that home. They get their fee for that. And so, it is in their interest to be able to draw upon an array of financing in-

stitutions that can satisfy whoever the borrower is, whoever the buyer is.

When that person is then employed by a specific financial institution, I would think that it is reasonable to think, in addition to the compensation they get from being a broker, that they will also be compensated for the amount of business that they steer into the mortgage segment of that financial institution, whether that is the best deal for the borrower or not. And I do not think that that gives consumers more choice. I think it actually narrows the choices.

Mr. HANNA. Wouldn't the same rules apply under RESPA for a bank's sales associates as they would for sales associates at Howard Hanna Company or Long & Foster today?

The RESPA rules wouldn't change. They prohibit a mortgage company from giving compensation to a real estate sales associate for referral of a mortgage.

Senator JOHNSON. Let me, in my remaining few minutes before we go on here, ask a question to the panel here. And this alludes somewhat to observations made by Mr. Hanna.

Based on the information available through the Conference of State Bank Supervisors, 25 States currently allow banks to engage at some level in real estate brokerage and property management. It would appear from available data that, in spite of this authority, only a small number of banks have actually taken advantage of the authority.

Also, it is my understanding that credit unions have had the authority to engage in real estate brokerage and property management through the credit union service organizations. Yet, data indicate that only two or three have engaged in any type of brokerage. None have engaged in property management.

Given how few banks, thrifts, and credit unions have taken advantage of the existing authority, I wonder if, first, Mr. Taylor and Mr. Murphy would elaborate a bit on the justification for the REALTOR® opposition to the entry of financial holding company national bank affiliates into the business, and for the rest of you, any brief observation on that as well.

Mr. Murphy.

Mr. MURPHY. Yes, Mr. Chairman. If you add up all the assets of these companies, it is not enough to do what one megabank does in a day.

Most of these places have one licensee sitting in a lobby. That is not their main course of business. They are in places where, to provide a service for their community, they cannot even make a living doing this in most of those communities.

So they are providing a service for their community that no one else can do for them. But at the same time, they are not in this to do real estate brokerage on a level that we are talking about here today.

Mr. TAYLOR. One of my major concerns would be that a major subprime lender gets in the business of becoming a real estate broker and I think creates further challenges, particularly for the population that we are concerned with, low income and minority. I have not heard an argument yet as to why the merging of this kind of financial services would at all serve consumers better.

Right now, we have an extremely competitive real estate brokerage industry. We have an extremely competitive financial services industry. And what is being proposed essentially would, in our opinion, lessen that competition and lessen the choices for consumers.

And when we hear about the large real estate firms that are already in the mortgage industry, we have not done this, but perhaps we should, is take a look at, to the extent that they are in the mortgage industry, who are they really serving?

Unlike financial institutions that have a CRA obligation, they have an obligation to make sure that the person at the bottom rung of the ladder working their way up to their version of the American Dream, has access to credit and capital.

Real estate brokerage firms do not have that obligation, neither do mortgage companies. And that is why, when you take a look at the difference in industries and who is serving people of color and who is serving working-class, working-poor people, disproportionately, you will see banks doing a much better job at that, because that is who the law applies to. Then you look at mortgage companies and real estate firms that are independent, I think you will see great disparities in terms of who they are really serving. And that should be of concern to everybody on this Subcommittee.

Senator JOHNSON. Any brief response?

Mr. Smith.

Mr. Hanna.

Mr. SMITH. I would just like to add that the banking industry is under the CRA and the REALTORS® are not under CRA.

I think if the banks are permitted to partner with the local real estate firms, that both of us could do a much better job of providing mortgages, products, and services to the low-income people in our communities.

Mr. TAYLOR. Well, if Mr. Smith is agreeing, and I would agree with him that having the real estate or even insurance industry come into the banking industry, that they would agree to be obligated to produce data on who they are serving and to have an affirmative obligation to make sure that they are not ignoring the needs of underserved populations, we may reconsider our position on this if that is the position of the ABA.

[Laughter.]

Senator JOHNSON. Mr. Hanna.

Mr. TAYLOR. And I am a Red Sox fan, anyway.

[Laughter.]

Mr. SMITH. I would just like to respond, that I do go through CRA examinations every year. I would welcome my colleague here to come and sit through the CRA examination so that he could understand what we are doing in our community.

Senator JOHNSON. Mr. Hanna.

Mr. HANNA. We would recommend the distinguished gentleman to my right visit Howard Hanna Company because we are a very open shop, and we would be happy to go over those numbers with you.

Mr. TAYLOR. I am going to take you up on those invitations.

Senator JOHNSON. My time is expired.

Senator Allard.

Senator ALLARD. Thank you, Mr. Chairman.

I am interested in trying to get the exact number of State-chartered banks, credit unions, and thrifts who engage in real estate brokerage. Do we have any idea how many financial institutions actually engage in real estate brokerage activity, and how many are involved in real estate management?

Does anybody have those facts?

Mr. Murphy.

Mr. MURPHY. Yes, Senator Allard. Only six States have banks in residential real estate brokerage operations. In these States, 18 banks have residential real estate brokerage operations.

These banks represent 0.2 percent of all banks and serve areas with 0.57 percent of the U.S. population. And it looks to me like there are about 18 banks, anyway, that are involved in this.

Mr. HANNA. I believe 26 States currently allow State-chartered banks to engage in real estate brokerage.

Senator ALLARD. I picked that up in the 26 States. I was just wondering how many institutions in those 26.

Mr. MURPHY. I have 18 down here, Senator.

Senator ALLARD. Okay. Currently, if a national bank wished to become involved in real estate in any of those 26 States, they could switch their charter, could they not?

Mr. SMITH. That is correct.

Senator ALLARD. They could switch that charter.

Mr. SMITH. That is correct.

Senator ALLARD. Okay. Now, if national banks are allowed to engage in real estate management brokerage, what percentage of banks do you estimate would enter the industry within 5 years?

Mr. Smith or Mr. Murphy, do you have any suggestions?

Mr. SMITH. I can only relate that to my personal experience.

I have had real estate powers since 1984. So 18 years.

Senator ALLARD. And you are a State bank. Is that right?

Mr. SMITH. I am a trust company. And Missouri trust companies have agency powers. I have had that ability since 1984.

But only recently has it become apparent that I may need to try to partner with one of the local real estate firms in order to continue to offer the products and services that I would like to offer.

In our community of 8,500 people, we have three or four real estate firms. But the largest one is a Re/Max firm. And at that office, a person drives to town, getting ready to move to town, goes in, finds a house, signs a contract to purchase the house. They walk into the next office of that firm, sign the papers to the mortgage. They walk into the next office of that firm and sign the papers for the title insurance.

I never have a chance to see that customer or offer that customer a product unless he or she happen to walk in the door of my bank to open a checking account. I would submit to you that is a Re/Max firm, which is the second largest real estate firm in the United States.

The question I would have is what are the other smaller real estate firms doing to compete with that? If I cannot compete with that, how are they going to compete with that? And I suggest to you that they may want to partner with the bank to have the capital and technology to compete with that. And likewise, I want to

partner with them to have the ability to compete with those products and services.

I would submit to you that it is very important to the smaller real estate firms to have that opportunity to partner with the bank, so they can continue to survive in that same marketplace.

Senator ALLARD. Does anybody else on the panel want to comment on that question?

Mr. Murphy.

Mr. MURPHY. Yes. Senator, the problem with the one-stop shopping is, in our marketplace now, we have buyer brokerage, we have leases and we protect each other. So if I represent the buyer, and he does not like me, he can fire me.

The problem with the setup that we are talking about today is, if you have inducements that are keeping you with an organization, and we have all seen negative closings in our State, it is kind of hard for you to feel like you can break your relationship with that organization.

With me, the way it is set up, you can break that because there is nothing that is bound together besides the contract. We do not have inducements—we cannot offer inducements that would keep them there for the whole term—title insurance, the mortgage, the appraisal, the closing fees. It puts the consumer at risk in the future.

Senator ALLARD. Mr. Hanna, did you have something?

Mr. HANNA. Are you talking about the consumer or the REALTOR®?

Mr. MURPHY. The consumer, sir.

Mr. HANNA. I find that the consumer is looking for the best service at the lowest possible cost and wants to make the process simpler and easier for them to buy homes. I think that is what our role is as REALTORS® in the market, to make it simpler and easier and less expensive for people to buy homes.

Senator ALLARD. Go ahead, Mr. Smith.

Mr. SMITH. I would just like to add that the banks are under the Bank Holding-Company Act is antitying provisions, which specifically says, we cannot force a product onto the customer in order to sell another product. We have to file disclosures in that respect. So we cannot tie those products together.

Mr. TAYLOR. Senator Allard.

Senator ALLARD. Mr. Taylor.

Mr. TAYLOR. If I may. This is a piece of my testimony—it is short—that I did not get to, that relates. I think it gets to your point.

It is a real story about someone in this city, an elderly couple who were victims of a real estate problem. They owned a house in the Mt. Pleasant neighborhood in DC, for over 43 years. And in order to pay their medical expenses, an independent mortgage company convinced them to take out an adjustable-rate mortgage with a prepayment penalty and a loan payment that exceeded the couple's monthly income.

The victims retained an independent REALTOR® to facilitate the short sale of their home, who quickly identified the appraisal conducted by the mortgage company was substantially inflated. It was

only after the victims' REALTOR® requested NCRC to intervene, that the sale took place instead of a foreclosure.

Now imagine if that real estate agent had been affiliated with that lender. They would have had no incentive to even catch anything or do anything other than to continue to take advantage of that person.

I am not suggesting that Mr. Hanna personally, that he conducts business this way. But that is the kind of problem we have, and people act funny when there is the opportunity to make a buck. And let's not allow that situation to occur by simply making it illegal to have those kinds of incestuous relationships between REALTORS® and bankers.

Mr. HANNA. The real estate agents that work for us, and most of the REALTORS® that I know, are pretty independent contractors I do not think that example you gave is typical of a REALTOR®, whether it works for Long & Foster, Howard Hanna, or Mr. Murphy's firm.

Mr. TAYLOR. I am just saying, if that REALTOR® had a relationship with the mortgage lender, in which they actually were their employee, because the Federal Reserve, without this law, allowed that to happen, why would an employee turn on their employer and say, hey, gee, this is an inflated appraisal value. This is not in the interest of the consumer. They'd be silent. They wouldn't do it.

Senator ALLARD. Mr. Smith brings up an interesting issue on the antitying provisions that we have now.

The question I have for you, Mr. Smith, is regarding the concern that is raised about whether homebuyers might feel pressure to use a bank's entire range of services. In other words, if you are going to get a loan from us, then you have to use us for real estate and everything else.

Do current antitying provisions offer consumers sufficient protection against such a possibility? How are these antitying provisions enforced?

Mr. SMITH. Well, we have to disclose to our customers any arrangements we have on any products and services. We have to disclose that. They have to sign it to say that it was disclosed properly to them. And then the regulatory body that comes in to examine us makes sure that we have those documents in the file and that the customer in fact did sign that, saying that they are aware of any tying arrangements. That is checked. I can tell you explicitly and by all the regulatory bodies, whether it be the OCC, the FDIC, or our State banking center.

Senator ALLARD. Do people even sign this provision when they are not granted a loan, for example?

Mr. SMITH. Yes, they sign the documents, and then the loan goes to the loan committee to see if the loan is going to be approved.

Senator ALLARD. But you are a customer. You come in and you talk to the bank and you say, "look, I would like to have a loan." And the bank says, "well, where is your savings account?" I have it over, some place else over here. But I have a checking account.

Then the bank could say, "well, before we give you a loan, we want to have the savings account moved over into our bank. And if you happen to have real estate, which is a concern raised, we would like to have you deal with our real estate agent to do that."

Now if the person who is applying for the loan says, "forget it, I am not going to deal with you on that," then do you ask him to sign that form that there was no antitying provisions? My question is, how is it enforced?

Mr. SMITH. Well, obviously, if you make the loan or you would sell the real estate, then you have to disclose that.

Senator ALLARD. That there were no antitying.

Mr. SMITH. That there was no tying. And that is how it would be enforced.

Senator ALLARD. Yes, sir.

Mr. Taylor.

Mr. TAYLOR. Senator, antitying can actually be waived. You can get exemptions from the Federal Reserve. And indeed, that is just what Citibank did last year. It received a favorable exemption from antitying prohibitions to offer incentives to their credit card, mortgage, or loan customers who maintained a combined balance in a package of products and services that included annuities, a homeowners life and long-term care insurance for insurance affiliates of Citibank.

So the regulators currently have the ability and I could foresee them having the ability to create other exemptions, which would include real estate brokerage.

Mr. HANNA. This all, I believe, comes under RESPA which prohibits real estate firms or mortgage lenders, from requiring the use of an affiliated product.

Senator ALLARD. Thank you for your responses.

Thank you, Mr. Chairman.

Senator JOHNSON. Thank you. My Democratic colleagues unfortunately had to leave for a ceremony event. They have left questions to be submitted to the panel. And we will respectfully be extending those questions on to the panel members to respond to those at the appropriate time.

Senator Bennett.

Senator BENNETT. Thank you, Mr. Chairman.

We have heard a lot of dire predictions and we have heard a lot of rosy scenarios. I would like to stay away from conjecture for just a moment and go to experience.

Mr. Smith, you say that your bank has the right to do this at the present time.

Mr. SMITH. That is correct.

Senator BENNETT. All right. Have you done it?

Mr. SMITH. No, I have not.

Senator BENNETT. Why not?

Mr. SMITH. Only in the last 2 or 3 years has it become a need in order to compete with the real estate agent, the Re/Max agency. Only has it become apparent in the last 2 or 3 years that there is need for me to get into this line of work in order to offer the products and the services.

Senator BENNETT. So you are telling me that the reason you are now contemplating it is because Re/Max is cutting into some of your mortgage business, not because you see this as a great opportunity to do any of the predatory things that concern Mr. Taylor.

Is that a fair assertion?

Mr. SMITH. I think that certainly is fair. Also, and we have a test case here with the insurance agencies, it is very difficult to start something *de novo.* And it is very critical to the success of an operation to be able to partner with someone that has the expertise and the experience in doing this business.

So in order to take my bank into this market, I am going to want to partner with a real estate agency in order to have the experience and the expertise to offer these products.

Senator BENNETT. Okay. Mr. Hanna, you have real estate agents that you do partner with, and you say they are pretty independent people.

Mr. HANNA. Our agents, our sales associates, are independent contractors.

Senator BENNETT. Independent contractors.

Mr. HANNA. Independent contractors.

Senator BENNETT. Can they take a loan some place else if they do not like what you are giving them?

Mr. HANNA. They not only can, but they do 70 percent of the time. Our capture ratio is about 30 percent. Our mortgage company, our financial service company, captures about 30 to 32 percent of our total sales.

Senator BENNETT. So you would insist that the experience would not produce the result that Mr. Murphy is talking about of driving agents out of business.

Mr. HANNA. We have been in the mortgage business since 1982, and as I mentioned, in the real estate business since 1957. So we have a very long track record. We would like to convert more of our buyers' sales to our mortgage company, but we are happy with 30 percent because we are providing great service and great pricing to our real estate associates to provide to their customers.

Senator BENNETT. You are suggesting, then, that the relationship that these agents have with you does not produce a circumstance where they can use their leverage with the homebuyer to get a higher price for you.

Mr. HANNA. Our sales associates are very independent and they are looking for long-term relationships with their client. So they want to make sure that they get the best terms and conditions in that mortgage and closing process for their homebuyer so they can get future referrals from that homebuyer.

Their primary responsibility is to create a comfortable and happy sale for that homebuyer. And they are out looking for the best possible mortgage product for them.

Hopefully, it is with Howard Hanna Financial. But we don't require that they use our mortgage company, and RESPA would prohibit us from doing so.

Senator BENNETT. So you would insist that the experience indicates that the consumer is better served?

Mr. HANNA. No question in my mind that the consumer is better serviced.

Senator BENNETT. And so, you—well, obviously, your testimony here—now, Mr. Murphy, I have some experience.

Unfortunately, I have not only bought a lot of homes. I have six children who have come to me for help in buying homes.

Mr. MURPHY. I have two teenagers, so, I understand the feeling.

Senator BENNETT. Yes. My wife and I, plus our six children, all of whom are married, of that group of seven, six are moving this year.

Mr. MURPHY. Good. I would have liked their referrals, Senator.

Senator BENNETT. No, the reason that I bring that up, when we made our first move to Salt Lake City, we came across an agency whom we really liked. I thought her service was outstanding. She shopped for the very best mortgage rate for us.

Quite frankly, Mr. Smith, the experience we had with the bank was less than satisfactory. I remember being enormously frustrated with the difficulties we had with the bank.

This was the bank that she took us to, pointed us to as having the lowest rate. But they were not user-friendly in the way that we finally got our loan.

Mr. Murphy, my point is that this particular woman has changed agencies several times. She's a hot property. Maybe I shouldn't put it in those terms.

[Laughter.]

Lest this be misunderstood.

[Laughter.]

She is a very competent professional who is in high demand for what she does in the area.

[Laughter.]

And consequently, independent real estate agencies keep trying to steal her from each other. I have gone back, and my family has gone back to her for her services repeatedly. She has not only handled all of our homes, she has handled a number of our children's homes. I have a little trouble assuming that she would be driven out of business if a bank were to come in and be able to offer other services.

Can you help with that one?

Mr. MURPHY. I think in any community, Senator, there is going to be a number of REALTORS® who have established themselves over the years, 10 years, myself 15, my partner, who the Chairman knows, over 25 years.

Most of our business is repeat business. The problem that we have is we need new people in our business regularly. Even in a State like South Dakota, which is small, with only 1,400 REALTORS®, we need, on the average, of 150 to 200 new agents getting into our business.

If you have to go to work for a bank because of the options of being new, the banks do not need you. Smaller offices cannot afford to have you around. They have a desk cost, just like anyone else. It doesn't matter that you are an independent contractor. We are all independent contractors.

But I can tell you, I have seen a poor REALTOR®. I have never seen a poor banker when it comes to what they can live on. And the new people in our business just do not generate the income that it takes to sustain themselves to get themselves established.

Senator BENNETT. Well, I am very much aware of the fact that many real estate agents do not earn a full-time living at this. It becomes almost a part-time job or an adjunct to what else they do.

I have some cousins that are in that circumstance. And frankly, I have not used their services.

[Laughter.]

Mr. MURPHY. You should have sent them a referral, though.

[Laughter.]

Senator BENNETT. Yes. I am trying to see if we can get any evidence or experience, rather than prospective assumptions, that the pool of agents will shrink if the banks go into this business.

Now, Mr. Smith, I was hoping could help us. But he is not in the business, so his vision of this is prospective as well.

The best place I think I can look is in the examples that Mr. Hanna has given us, and Mr. Taylor, I would like you to comment on this, too.

As these large, presumably reputable, firms have come into the real estate business, have they either dried up the number of available agents or have they engaged in the kind of predatory practices that you so rightly deplore?

Or has there been a reverse? That is, the more prestigious and national the firm, the less likely that firm is to engage in that kind of practice and the more likely they are to look for agents who would welcome the opportunity of an affiliate.

I do not know. You have had some experience. We have heard from Mr. Hanna. Now let us hear from those of you who have had experience. With these large firms coming into the business, what has happened in the area of consumer protection and agent employment?

Mr. TAYLOR. First of all, let me say I think that is an excellent question. If you do not mind, I would like to go back and actually do some research and see what the kind of performance was versus what the numbers are relative to how the industry is either growing or shrinking and what the performance of the large firms are versus the smaller firms.

But I cannot say, I was listening to Mr. Smith. And you cannot help but sympathize with the fact that he's sitting here saying, look, my business as a small bank, I have to find other ways to survive. And I appreciate that.

But I think his problem has more to do with the consolidation of the banking industry and then the evolution of the banking industry. There is still *de novo* bank applications coming in. So, obviously, people are getting into the banking industry, starting small, specialized banks.

But I would say his problem is more with that and perhaps some of the many decisions that this Congress has made relative to allowing for mergers and the superconglomerates.

Now, having said that, it is interesting to look at some of the large institutions and the way they have gone. The old Bank of America was one of the best community banks when it came to small business lending. They got acquired by NationsBank and NationsBank eliminated all of that very good small business lending opportunities.

And so, you had one very large bank being acquired by another large bank, and there was a difference at the end of the day as to their performance was.

You can look at the home mortgage disclosure data of some of these large institutions and you will see some doing a pretty decent job and others who you wonder whether they have just decided,

and indeed, many of them have, decided to get out of the business of mortgage lending. So, I do not think that there is this one blanket statement that you can make relative to a large institution versus a small institution.

Indeed, some of the minority-owned institutions might be doing a very excellent job, or are doing a very excellent job in some cities serving underserved populations. And yet, they are small institutions. Some of the community banks.

I am a big believer in banks. And the reason I believe in banks is because there are laws, fair lending laws like CRA and the Fair Housing Act and others, which they are obligated to do.

I think, left to their own demise, and this is just the way that you have to tweak the capitalist system so it works for everybody. But left to their own demise, they might only want to lend to the well-healed. And for others, we would be really struggling with much higher costs and much more difficult access to credit and capital. But we have laws against that, thank God.

Well, that is not true for a lot of the other industries. So, again, if this were to occur, I would really hope that those same kinds of obligations that allow all Americans to build wealth, all Americans to have the opportunity.

What I hear from your experience is, you know what, we have a heck of a brokerage industry and you have had a good experience working with an independent broker, not owned by a bank. And if it is not broken, why are we going to fix it, would be one of my conclusions.

And the other would be, if we must go in that route to make sure that, in the same way that the banks are obligated to make sure that people are treated fairly and equitably and get access to credit and capital, their brokers do that same thing.

They do not just open offices in the suburbs, but they have offices in rural America and inner-city America, so that people have access to the services.

Mr. SMITH. Senator, if I may respond?

Senator BENNETT. Let me hear from Mr. Murphy on the issue. You have raised a whole series of issues that we could have a whole series of hearings on.

Mr. SMITH. Right.

Mr. MURPHY. I liked his answer, first of all.

Senator BENNETT. Yes.

Mr. MURPHY. A large real estate firm in South Dakota, the largest one that I can think of, has 42 people in it. That is the largest. And everyone that I know of, anyway, in our industry in South Dakota is an independent contractor.

We do not see problems with what we have right now. My arrangements with my loan officers, half the people that come to our noon monthly luncheons are the affiliates. We like the arrangement that we have right now. None of them wants to get into this business. Or at least, would come right out and say it, to be honest with you. They feel the same way. It is not broken.

They believe that they need separation of commerce and finance. There is no doubt in any of their minds. They are not convinced that there would be separation, I think. But they are not going to come right out and say that, I guess.

Senator BENNETT. Mr. Smith, you were going to comment.

I apologize for going on. But I apparently touched a nerve here.

Mr. SMITH. Very quickly, I would like to say something about the consolidation.

My community is 8,500 people. We have five banks. Three of them are community banks. I would tell you that our office, as well as two of the other offices of the banks, are downtown.

I would like to point out that we have a highway bypass, of course, around our community like a lot of small communities. The real estate agencies have moved out on the bypass.

But our office is downtown. We worked very hard to maintain a very viable downtown where we have a town square. And in fact, something that you will not see very often, our bank offers interest-free loans to the business owners if they will repair and remodel their storefronts so that we can keep a very attractive downtown area to pull people into our community, to spend their money and provide jobs, et cetera.

Senator BENNETT. Thank you. Sorry to open up the floodgates about bank consolidation.

Senator JOHNSON. Thank you, Senator Bennett. Let me just ask a couple real quick questions here of the panel.

Let me branch out here. Brokerage and property management are two distinct activities, but they are lumped together in the proposed regulation as if they are linked in some manner.

There hasn't been a lot of discussion in the testimony from this panel relative to property management. Would any of you choose to elaborate on whether these should be viewed as separate and distinct activities as we consider this issue?

Any of you.

[No response.]

It may be that there are no strong opinions one way or another.

Mr. MURPHY. In South Dakota, they are all lumped under the same licensing program.

Mr. HANNA. That is the way they are in most States, I believe. It is under real estate licensing. It is hard, I think in most States, to distinguish the difference. It is part of the real estate brokerage activity.

Mr. TAYLOR. I would like the opportunity to submit a comment in the future on that, if I could.

Senator JOHNSON. So the licensure process in most States, you are suggesting, would lump them together, even though, conceptually, it would seem that there would be a difference between property management and actual brokerage activities.

Mr. HANNA. In most areas, the residential real estate brokerage firm is not involved in property management as we know it. This might not be true in some of the smaller markets, but typically, of commercial real estate brokerage companies, who are all under the same licensing law, that would be most responsible and part of their business model.

Senator JOHNSON. Well, a follow up question probably has the same response, then, but let me ask.

The focus we have had here today has been primarily in residential real estate and the importance of local REALTORS® in providing communities with that personalized service that they need.

Do you see any difference between bank getting involved in commercial real estate transactions versus residential? Are there different issues that we should consider in terms of determining the potential impact on consumers?

Mr. TAYLOR. I would hate to be the business owner who's trying to rent commercial property in a downtown building that is not managed by the major lender or lenders in that area, and then be going to those lenders trying to access credit and capital when they are obligated and have a financial interest in seeing to it that the other properties are leased out. I can see a conflict there that makes me somewhat uncomfortable.

Senator JOHNSON. Anyone else care to comment on the difference between residential and commercial?

Mr. HANNA. Well, certainly, commercial brokerage lending, in particular, does not come under RESPA laws. So, I think you probably have to look at that as an issue.

Senator JOHNSON. Anyone else?

[No response.]

Mr. Smith, one area of concern is a potential for conflicts of interest, or the appearance of conflict of interest, if banks were to get into the real estate business.

I know that there are strong antitying and privacy laws that provide protection against doing things, such as recommending inappropriate title insurance or property insurance products.

But it would seem that there could be a temptation that could exist to steer customers to related areas of the banking organization, notwithstanding these restrictions.

Could you very briefly elaborate a bit on what safeguards exist inside banks to ensure that this would not happen? And what would be the enforcement mechanism to ensure that any firewalls are maintained?

Mr. SMITH. Well, under the RESPA, we have to identify all those things that we have in the bank. And again, the customer has to acknowledge the fact that we have those products and services and has to sign off on that.

And the regulatory bodies review those documents whenever they come into the bank. They look at the mortgage documents to make sure that we have complied with all the various provisions that we have to comply with.

I sincerely apologize to Senator Bennett for having an unfortunate experience with a bank. Sometimes we bankers get very frustrated with the regulatory process that we have to comply with. But, again, that is ensuring that we provide to the customer the proper safeguards that we have to comply with.

So that is part of the process in making sure that the consumer fully understands what they are signing and what the transaction involves.

Senator JOHNSON. Mr. Taylor, are you satisfied with those constraints?

Mr. TAYLOR. Well, actually, I wanted to raise a related point that I think your question raises because what is interesting is, if you watched over the last several years as, indeed, mortgages have become more affordable and interest rates have gone down, is you

have seen the banks continuously lower fees and do the kinds of things that competition drives them to do.

But you mentioned some of the other products that are also offered and that are necessary as part of the deal. Title insurance, for example.

That hasn't gone down. Lawyers' fees haven't gone down. You look at some of those costs associated with that and I am wondering if—I do not know if you have picked it up in American Banker, but what we are looking at is, we would like to see more competition in those arenas because, indeed, those closing costs mean a lot, particularly for the populations we care about.

Title insurance, you refinance or you get a home equity loan or anything like that, you get title insurance again. Well, you may not know this, sir, but the title insurance you originally had already covers you as the borrower, and it stays with you until you have sold off or until you drop dead.

And yet, the bank hands you an additional title insurance policy for another $800–$900 dollars, on average, and if you are not savvy enough in some States to know that you are asking for a reissue policy, because if you ask for that, you actually get a discount. But, still, it is this incredibly inflated cost that has nothing to do with anything, except covering that new lender for that period of time that there are no liens on the property since the original title.

I did not mean to get off on this, but the point of this is that, I think, in the same way with brokers, I am hoping that by keeping the industry separate, by keeping the competition at the level it is at, we have seen the broker fees go down.

In some of these other industries where we have seemingly no influence, in spite of the market, in spite of the competition, I think there are all of five major title insurance companies, they have a nice little game going in which the consumer gets gouged.

I like the idea of separate, competing industries that have to compete for the consumer dollar, rather than being just lumped together. That doesn't answer your question and I apologize for that, but it gives me the opportunity to talk about title insurance.

[Laughter.]

Senator JOHNSON. Mr. Murphy, last week, we were chatting a little bit, and I thought you raised an interesting point that goes to one of the more fundamental issues that this whole hearing is about, and the difference between transactions that are fundamentally financial in nature versus those that are commercial in nature.

You shared with me an observation appropriate to our home State about selling cattle. You asked how real estate as an asset is different from selling head of cattle.

In both cases, one has documented rights of ownership. Both types of transactions generally involve financing through a bank or other financial intermediary, and in both cases, the purchaser has the expectation that the asset will increase in value over time.

Yet, buying and selling cattle is universally viewed as a commercial enterprise. Whereas, we have heard today the argument that buying and selling a home or investing in real estate is financial in nature.

I think this is an interesting observation you have raised, and I wonder if you would comment a bit about, as you see it, the differences between transactions that are fundamentally financial versus those that are commercial.

Mr. MURPHY. Thank you, Senator. Well, obviously, in the Midwest, we look at things pretty straightforward. We raise 1.8 million head of cattle in South Dakota, which is twice as many cattle or livestock as we have people in our State.

We also had 400 million bushels of corn in our State. And farmers and ranchers, it wouldn't matter which operation you look at, they all feel the same way, everything that you can touch is real. That is the way they look at this issue.

They look at real estate the same way. You could never convince, at least anyone that I know of in South Dakota, that real estate is financial in nature. It just doesn't go that way.

And if you were going to go on that route, then we would only need four or five banks, but they'd have to be extremely large because on one side of the bank, you are going to have to have a livestock holding company and a grain elevator, and on the other side, you are going to have to hold farm machinery, boats, campers, and every car that is sold in the State of South Dakota, too. But maybe I could get involved in that land sale.

We like separation. We like the separation in government. We like the idea that we have 535 people out here that can make a decision on whether something should be done that is in the best interest of the people.

Senator JOHNSON. My time is expired, but Mr. Smith, just a brief observation on your part about financial versus commercial transactions.

Mr. SMITH. Well, I personally have a farm and I personally own cattle. But I own it. That is a product. And so, I personally buy and sell the cattle myself.

So that is a product, much like hardware items, shoes, or clothes. That is a completely different situation than the real estate agents acting as a third party in the transaction of buying and selling a home.

Mr. HANNA. And I will say that for 96 percent of the American public, the largest single asset they buy or sell is their own home.

I think, as a statistic, 93 or 94 percent of the American families finance that purchase. So, I am not sure it is the same example as the cattle, but it is an example.

Senator JOHNSON. My time has expired. Senator Bennett, any questions?

Senator BENNETT. Yes, I would like to make just a few observations here.

My number-one concern here, I think of all the Members of the Subcommittee, is for the consumer. It is the buyer of the home.

We want to structure a circumstance where the buyer of the home gets the best deal, gets the best service, and is protected, Mr. Taylor, from the predatory activity that you have described. And we have had hearings on that activity here in the Banking Committee.

I am sympathetic to the idea of real estate agents liking the way things are. But if things can get better for the consumer by having

a change, the way our dynamic capitalist economy works is that people who do not keep up with that have got to find something else to do, or start keeping up with that.

As I say, the agent that I have described, I think she will thrive no matter what kind of a structure we have put here because she has the skills for which people will pay.

But if there are marginal agents that the present circumstance is keeping in place who will get hurt, Champater called it, the creative destruction of capitalism? And we all have to go through it.

I have certainly lost plenty of jobs in my life. I may lose this one for the comments I am making. I do not know.

[Laughter.]

But the bottom line should be, what is the best deal for the consumer?

Mr. Smith, tell us why the consumer would be better off as the proposal that we have from the Fed and the Treasury goes into place.

And Mr. Murphy, you tell us why the consumer would be damaged if this goes.

Now I will warn you in advance, I do not think the predatory example you gave us is a legitimate example of what might happen because my experience is, if you have, just to pick some names, Welles Fargo or Bank of America, you will have a higher level of ethical procedure than you would have in the independent mortgage lender whom you talked about who doesn't want anybody looking at him.

Whereas, the CEO of a very large national company will say, our reputation is our corporate crown jewels and we will not jeopardize our reputation for this kind of market.

Now, obviously, I was wrong in that assumption as far as Arthur Anderson is concerned, but, generally that is the case.

Mr. TAYLOR. Or J.P. Morgan or Merrill Lynch.

Senator BENNETT. Well, J.P. Morgan has an interesting history.

But, generally, you do get a higher level of ethical behavior when you are dealing with a company that has a higher reputation than if you have a company that is kind of a fly-by-night outfit put together in the local community.

Mr. TAYLOR. So are you going to limit this to those high-end, big companies? Is that what you are talking about?

Senator BENNETT. It is going to be limited to Federally chartered banks.

Okay, Mr. Smith, and then Mr. Taylor.

Mr. SMITH. Senator Bennett, I alluded to the fact that in my community we have a Re/Max agency, and there are other real estate agents in town. And I think if you eliminate banks from having the opportunity to partner with those other real estate agents, maybe the mom-and-pop real estate agent, you will be eliminating choices for that consumer.

If that small real estate agency, the mom-and-pop agency, doesn't have the capital or the technology to compete with the Re/Maxes of the world, they may look to a bank to partner in order to have the capital, in order to have the technology to stay in business.

And I think keeping those people in business will obviously provide more choices for people wanting to purchase houses. And I

think the banking industry can bring the capital and the technology resources to the table and partner with those real estate agencies in order to continue to provide the products and services to the community, which would mean many more options for the consumer.

Mr. TAYLOR. Senator Bennett, I agree. I think, for the most part, large financial institutions really do care about their reputation.

In fact, in some ways, that probably influences them as much as some of the fair-lending laws that reputation risks.

So, I do not believe that there isn't some truth to that. Of course, this law wouldn't limit it to those institutions. In fact, some of the institutions that are subprime lenders and, indeed, do predatory lending, would also have access to being able to offer these brokered services.

But one thing we should look at is, as these institutions have become bigger and bigger, what is interesting for the consumer is that the fees have gone up—ATM fees, check-cashing fees, basic banking fees.

The Federal Reserve just did a study on this, looking at some of the largest institutions and what has happened to the consumer as they have gotten bigger and bigger and their reputations have grown and so on, is that the consumer is paying more and more for basic financial services.

I know that my colleague, Mr. Hanna, talks about how RESPA would limit any steering toward a particular financing institution by a broker. But the truth is, if you are directly affiliated with a financial institution in such a way that that financial institution is steering mortgages or prospective borrowers to you because of the nature of their business and their customers say, "you know, I think it is time to refinance or to buy a house or whatever—well, here, call your friend." What did you call the professional? A hot prospect.

Senator BENNETT. Never mind.

[Laughter.]

Mr. TAYLOR. But, in other words, that person, if I were she, if that bank was feeding me a line of business regularly, I would go out of my way to make sure that whatever opportunity I had to make sure that the people who were coming to me looking for houses, that I exposed them to that financial institution in a very positive way.

I think that that will limit consumer choice. And again, I think the bottom line is, is the consumer being ill-served by the brokerage industry?

I do not think so. I, like you, this year I have refinanced and paid that second title insurance fee. By the way, we will talk about that at another hearing.

Senator BENNETT. I agree with you about title insurance. Let's make the record very clear on that one.

Mr. TAYLOR. But I was happy to deal with an independent broker who was able to bring me to a lot of different institutions and a lot of different products and gave me the best deal, and it really worked well.

So that would be my comment, sir.

Senator BENNETT. Thank you.

Anyone else? Any comment on what is best for the consumer?

Mr. HANNA. Somehow, this conversation has gone that we will not have independent brokers any more. If you look at the example of GMAC, they have all independent brokers and they have been in the business for a number of years. GMAC is, I consider it a financial institution that owns real estate companies.

And clearly, they are an example of someone in the business, a conglomerate financial group that has independent REALTORS® and they have a mortgage company also, and if they had their figures here, they have those same great independent REALTORS® who are making recommendations to the best mortgage products and the best other closing products possible in the marketplace.

The financial conglomerates and State-chartered banks that have entered the real estate business over the years have not converted the sales force of independent contractors into salaried employees.

I haven't seen this trend that Mr. Taylor alluded to, or Mr. Murphy. If banks come into the business and hire salaried people right off the get-go and change the industry model, they will not be in the business very long.

Mr. MURPHY. The problem with that is that GMAC, they are not banks. There is the difference.

Mr. HANNA. Metropolitan Financial Corporation, which owned Edina Real Estate in the Minneapolis-St. Paul area for years before it merged into First Bank System, was a Federally insured savings and loan. It kept Edina's sales force of independent contractors intact.

Senator BENNETT. Mr. Chairman, my time is up and we will leave the hearing and allow these four to continue their debate.

[Laughter.]

Mr. MURPHY. Which we will continue.

Senator JOHNSON. Thank you, Senator Bennett.

I want to thank the members of the panel. I think this has been a very constructive, very positive contribution to the issues that we are wrestling with here in the Banking Committee, and I thank you for your contribution.

With that, the hearing is adjourned.

Mr. HANNA. Thank you, Mr. Chairman.

Mr. MURPHY. Thank you.

Mr. TAYLOR. Thank you.

Mr. SMITH. Thank you, Mr. Chairman.

[Whereupon, at 11:50 a.m., the hearing was adjourned.]

[Prepared statements, response to written questions, and additional material supplied for the record follow:]

PREPARED STATEMENT SENATOR JACK REED

Thank you Mr. Chairman, and I appreciate the timeliness of the hearing, coming so closely after the National Association of REALTORS® engaged in some Capitol Hill visits last week.

This is certainly an issue eliciting a lot of comment and excitement, and I am glad we have the opportunity this morning to delve further into the details of what this regulation would mean for the banking and real estate industries, and most importantly, for the consumer.

Both sides in this issue continue to make compelling arguments,and I look forward to a further enlightening discussion this morning. Certainly the National Association of REALTORS® should be commended for their efforts in this debate, and I want to congratulate them for garnering so many cosponsors for their legislation in the House. Now I understand that their focus has shifted to the Senate.

As a Member of the Conference Subcommittee on the Gramm-Leach-Bliley Act a few years ago, I recall the many discussions we had in the context of banking and commerce. Obviously there are many varied views on the subject, and I made my position clear with regard to the unitary thrift "loophole," for which I believed there were enough safeguards in place to allow for limited mixing of banking and commercial activities.

The situation before us at this hearing presents a much more nuanced part of that argument, and I am certainly mindful of the effect it could have on my constituents that are part of the real estate industry, as well as consumers in general.

Mr. Chairman, thank you again for the opportunity to have this open and frank discussion on such a relevant and important issue.

PREPARED STATEMENT OF TOM MURPHY

PRESIDENT, ASSOCIATION OF REALTORS®, SIOUX FALLS, SOUTH DAKOTA
REALTOR®, CHELL REALTORS®
REPRESENTING THE NATIONAL ASSOCIATION OF REALTORS®

MAY 23, 2002

Chairman Johnson, Senator Bennett, and Members of the Subcommittee, my name is Tom Murphy. I am a REALTOR® with Chell REALTORS®—a small residential real estate firm in Sioux Falls, South Dakota. I am also President of the South Dakota Association of REALTORS®. Our State association membership of over 1,400 REALTORS® are engaged in helping people buy, sell, and manage real estate every day.

I am here on behalf of the National Association of REALTORS®, which represents more than 800,000 members engaged in all aspects of commercial and residential real estate. I want to thank you for the opportunity to testify today on this critical issue.

It is important for all of us to take a good look at how the economy and consumers would fare if banks are allowed into the real estate business. That is one reason why I am glad we have the views of consumer groups represented on this panel.

Mr. Chairman, you and your Subcommittee Members are to be commended for examining all perspectives on this proposed regulation—those of the little guy, as well as those of the big guy.

As I mentioned, my business is a small, one-office real estate firm, just like nearly 80 percent of REALTOR® firms. My colleague from Pennsylvania here represents a large regional, multioffice firm. Obviously, we come here today to present different perspectives of this Nation's dynamic and diverse real estate market.

The fact that some of our members can differ on an issue, while respecting and supporting each other on most, is a great example of the vitality of the National Association of REALTORS®. It is a sign of the hearty competition of the real estate business today.

My comments today represent the overwhelming majority of NAR's members. Ninety-six percent of our members support the position of the National Association of REALTORS® to oppose this rule. Eighty-two percent of large broker/owners support this position, while 81 percent of our members believe we should be doing even more to stop the banks from unfairly entering our business.

We firmly believe that redefining real estate brokerage, leasing, and property management as financial in nature is totally unacceptable because it mixes banking and commerce. If the Nation's most aggressive megabanks are allowed to add real

estate to their long list of approved activities, you can be sure that consumer choices in real estate services will shrink.

The Nation's bankers, who petitioned the Federal Reserve and Treasury for this proposed rule, should not gain by regulation what they failed to gain by legislation. In 1999, Congress clearly went on record supporting the separation of banking and commerce.

Oddly enough, the American Bankers Association strongly supported an amendment you offered, Mr. Chairman, during the Gramm-Leach-Bliley debate to bar unitary thrift holding companies from engaging in commercial activities like real estate brokerage. It now appears that members of the ABA would like to corner the market on commercial businesses like real estate brokerage, leasing, and management.

Currently, we have a balanced marketplace for commerce, banking and financial services. Let me direct your attention to the two charts I have enclosed.

The first chart shows how the commercial and banking industries compete in the "financial services" arena. REALTORS® do not engage in banking. They do not take deposits or run ATM's.

Again, REALTORS® are not engaged in banking. Banks do not sell real estate. Banking and commerce are separate. It is that simple. Otherwise, why shouldn't banks sell cars or appliances?

The second chart shows that in the arena where banks and REALTORS® *do* compete on mortgage originations, banks are already the winners. REALTOR®-affiliated mortgage lending companies only originate about 5 percent of mortgages, while the large banks handle 44 percent.

Today's competition occurs in the financial services arena where it belongs. Consumers benefit from this arrangement because the direct competition for financial services between commercial companies and banks results in greater consumer choice and customer service. When banks say they want "one-stop shopping" what they are really saying is they want "one-bank shopping."

The reality is that the entry of Federally chartered banks into the real estate brokerage business would tilt this balanced marketplace toward the Nation's megabanks. It would pit Government subsidized banking companies against privately funded real estate enterprises. It would put taxpayer money at risk.

Mr. Chairman, the National Association of REALTORS® believes this issue is just too big to be decided by the regulators. The decision belongs with the Nation's lawmakers. That is why we have called on Congress to enact The Community Choice in Real Estate Act, S. 1839, and H.R. 3424, a companion bill in the House, to clarify Congressional intent.

REALTORS® from all over the country have sent more than 100,000 letters to their Congressional representatives urging support for this bill. We have sent more than 40,000 letters to the Federal Reserve and the Treasury expressing our opposition to the proposed regulation. And we have sent more than 50,000 letters to President Bush urging his support.

So far, H.R. 3424 has generated tremendous support in the House, with more than 230 cosponsors. So far, a dozen Senators have cosponsored S. 1839. Last month, Treasury Secretary O'Neill announced that he plans to postpone making a decision on this issue until next year. The ball is back in your court. It is time for Congress to resolve this issue.

Mr. Chairman, REALTORS® are not alone on this issue. A diverse group of trade associations and consumer groups stand with us on this one.

Passage of The Community Choice in Real Estate Act will set the record straight. At the same time, it will ensure more balanced competition and more consumer choice.

This legislation will help to keep local entrepreneurs and businesses operating in our communities. It will help to keep some of our best community leaders and volunteers in place.

REALTORS® are more than business people. We are community leaders. Look in countless cities and townships across America and you will find it is a REALTOR® serving as a den mother; a REALTOR® who is leading the city-wide clean up; a REALTOR® who is hosting the candidate meet-and-greet; and a REALTOR® who is coaching Little League. REALTORS® are linked to their communities in more ways than simply through their businesses. REALTORS® have a stake in the same neighborhoods where their clients live or want to live.

Finally, this proposal just does not make sense. Banks have it backwards. Real estate brokerage is not incidental to a financial activity. It is the mortgage that is, in fact, incidental to buying a home. Twenty percent of all the homes sold in America involve no lender financing at all.

America's system of homeownership is the envy of the world. Homeownership is at an all time high. Five out of six homebuyers and home sellers are satisfied with

their real estate agent and they would use him or her again. Let us not destabilize this pillar of our economy and relationship that works in communities throughout America.

Well over a year ago, the Federal Reserve and the Treasury Department issued a proposed rule that would allow financial holding companies (FHC's) and financial subsidiaries of national banks to engage in real estate brokerage, leasing, and property management activities. The National Association of REALTORS® (NAR) strongly opposed this regulation on the grounds that real estate brokerage and property management are neither financial activities, nor are they incidental to finance, and approval of the proposed rule would thus effect a mixing of banking and commerce. This regulation would not only result in negative market and consumer consequences. An affirmative decision by the Federal Reserve and Treasury on this proposal would also violate Congressional intent, evident in several key banking laws which make it very clear that Congress specifically intended to maintain the separation of banking and commerce.

Congress adopted the Gramm-Leach-Bliley Act in 1999, which established a legal and regulatory framework for financial subsidiaries of banks and financial holding companies to engage in designated financial activities under the new law. The Act created a new entity, the financial holding company that would compete in the financial services area offering services that were prohibited to bank holding companies. By distinguishing the permissible activities of bank holding companies from financial holding companies, the Act also reaffirmed the longstanding national policy that separated banking from commerce because of the unique powers and advantages granted to banking institutions by their Federal charters.

NAR-supported legislation was introduced in both the U.S. House of Representatives and the U.S. Senate (H.R. 3424 and S. 1839) that will clarify Congressional intent that real estate brokerage and management are not incidental or complimentary to a financial activity. The proposed legislation, The Community Choice in Real Estate Act, will maintain the status quo regarding FHC's ability to expand into real estate brokerage and property management activities through regulation. The Community Choice in Real Estate Act returns the issue back to its proper forum—the U.S. Congress.

The National Association of REALTORS®-supported legislation and its position on this issue is based primarily on two strong beliefs:

- The Congress, *not* the Board of Governors of the Federal Reserve or the Secretary of the Treasury, is the proper judge of what is commerce and what is banking or financial services. The 535 elected Congressional representatives, not the seven Federal Reserve Board Governors or the Secretary of the Treasury, should be responsible for any changes in current law that would result in a dramatic restructuring of the real estate industry. Real estate brokerage and property management are clearly *commercial activities*. This view was central throughout the 25-year debate on the Glass-Steagall Act and the passage of the Gramm-Leach-Bliley Act of 1999, and clearly is reflected in historical and present Congressional intent.
- Permitting financial holding companies and national bank subsidiaries to enter the real estate brokerage and management industry would have wide-ranging, adverse market effects. Industry concentration would increase, competition would decline, and consumer choice would be limited with no real benefits from economies of scale or scope. The unprecedented expansion of banking powers into the real estate brokerage/management industry would clearly expose the financial holding companies' and their banking subsidiaries' inherent conflicts of interest in selling financial services (banking products) rather than serving customers in the brokering of real estate property.

NAR's position was eloquently stated by Congressman Jim Leach of Iowa, the sponsor of the Gramm-Leach-Bliley Act:

> *The movement to go beyond the integration of financial services and eliminate the traditional legal barriers between commerce and banking is simply a bridge we should not cross. It is a course fraught with risk and devoid of benefit and one for which there is no justification.*
>
> *Such a step would open the door to a vast restructuring of the American economy and an abandonment of the traditional role of banks as impartial providers of credit, while exposing the taxpayer to liabilities on a scale far exceeding the savings and loan bailout. At issue with financial services modernization is increased competition. At issue with mixing commerce and banking is economic conglomeration, the concentration of ownership of corporate America.*

Financial holding companies, their representative associations and other groups, including some large real estate brokerage companies, argue against the National

Association of REALTORS® position. They claim that the Association is being "protectionist," and that the entry of banks into real estate would encourage more open competition in the real estate marketplace. On the contrary, the National Association of REALTORS® position promotes open and fair competition. Indeed, its members would welcome FHC's as competitors if FHC's truly competed in a free market without the advantages of their bank subsidiaries' Federal charters and without creating the risks outlined by Chairman Leach.

Currently we have a balanced marketplace for commerce, banking, and financial services. Real estate brokerage firms do not engage in banking. Financial holding companies do not engage in commercial activities, such as real estate brokerage and property management. Banking and commerce are separate. The arena of financial services allows competition from both financial holding companies *and* commercial firms. Both real estate brokerages and financial holding companies (banks) have diversified their business lines into financial services that have served as a buffer between commerce and banking activities. This was the intent of Congress throughout its deliberations on financial modernization.

The reality is that the entry of Federally chartered banks or financial holding companies into the real estate brokerage business would tilt this balanced marketplace toward the FHC's. It would pit Government-subsidized banking companies (putting taxpayer money at risk) against privately funded real estate enterprises. Furthermore, if FHC's are permitted to enter the real estate business, REALTORS® and builders would be placed in the awkward position of having to go to banks which are subsidiaries of FHC's—their direct competitors—for loans and financial services.

Why REALTORS® Support The Community Choice in Real Estate Act

The Community Choice in Real Estate Act of 2001 was introduced by Congressmen Ken Calvert of California and Paul Kanjorski of Pennsylvania. The Act, H.R. 3424 was introduced with more than 30 original cosponsors and today has more than 225 cosponsors. The legislation, along with its companion bill in the Senate, S. 1839, is designed to address concerns expressed by both real estate professionals and consumers if financial holding companies and subsidiaries of national banks (FHC's) are permitted to engage in real estate brokerage and property management activities.

In brief, The Community Choice in Real Estate Act stipulates that Federal regulators prohibit these financial institutions from engaging in real estate brokerage and management activities. More specifically, H.R. 3424 and S. 1839 specify that the Federal Reserve Board and the Secretary of the Treasury may not determine that real estate brokerage or real estate management activities are financial in nature, incidental to any financial activity, or complementary to a financial activity.

The Community Choice in Real Estate Act Returns the Issue to the Proper Forum—the U.S. Congress

The National Association of REALTORS® position on banks entering the real estate business aligns with both historical and current Congressional intent. The legislative history of banking laws demonstrates that real estate brokerage has been consistently interpreted as a commercial, not a financial activity. Although the Gramm-Leach-
Bliley Act of 1999 (GLB) made specific reforms in the Nation's banking and financial services laws, the separation of banking from commerce remains a tenet of national policy. While the Federal Reserve and the Treasury Secretary are authorized by Gramm-Leach-Bliley to expand the list of financial activities, Congress has clearly indicated its intent to maintain the separation of banking and commerce.

Financial modernization—the term that advocates used to characterize the legal changes that allowed banks, securities firms, and insurance companies to enter each other's businesses—has been interpreted by some as removing all barriers to banks entering nonbanking businesses. But in its deliberations on the Gramm-Leach-Bliley Act, Congress stopped short of mixing banking and commerce. The GLB Act was quite specific from the outset in describing what a financial activity may be. The current activities of banks and financial holding companies principally relate to financial instruments: loans, checking accounts, mortgages, etc. While these represent value between two parties (usually a bank and a depositor or borrower), they are not tangible goods and rarely take any physical form.

Commercial activities, such as real estate brokerage and property management, offer to consumers something that is tangible—a house, an appliance, a car, for example. Although banks argue that real estate has financial attributes, even the Federal Reserve Board and the Secretary of the Treasury in the proposed real estate regulation observed that bank-ascribed financial attributes might not be enough to

treat real estate as a financial asset.[1] And while purchasing tangible assets, such as a car, computer, or a home, may entail the use of financial instruments—usually cash or loans—this does not mean that commerce is "financial in nature" or "incidental to a financial activity." Rather, it can be argued that financial activity *is incidental to the real estate transaction.*

In the GLB Act, Congress enumerated those activities that it deemed to be financial in nature, but *specifically omitted real estate brokerage and management.* (For specifics, see *12 U.S.C. 1843 (k)(4)).*[2] Congress did make provisions to expand the list of financial activities. It devised specific criteria that such activities must meet, based on new technological developments to deliver financial products to consumers and how the marketplace itself evolved. Congress also authorized the Federal Reserve Board and the Treasury Department to agree on such new financial activities.

However, Congress did not anticipate nor intend for that list of financial activities to include commercial ones. There has been no significant change in the relevant technology, or in the business of real estate brokerage or management, since enactment of the GLB Act in late 1999. The businesses of real estate brokerage and management remain, for all practical intents and purposes, the same today as they were on the date of enactment: the transfer of real property and such commercial activities related to such transactions. The very purpose of the regulation proposed by the Federal Reserve and the Treasury Department is to overturn the long-held understanding that real estate is commerce by redesignating it as a financial activity for purposes of the Gramm-Leach-Bliley Act. The proposal from the Federal Reserve and the Secretary of the Treasury runs counter to Congressional intent.

The proposal to redefine real estate brokerage as a financial activity has met opposition from a full spectrum of consumer and industry groups. In support of that opposition, Congress is reasserting its authority in the arena by introducing The Community Choice in Real Estate Act. This bill amends the Bank Holding Company Act to preclude any such action by the Federal Reserve or Treasury, and clarifies Congressional intent by prohibiting banks and financial holding companies from entering real estate brokerage or property management. The bill's intent is to maintain the status quo; it does not seek to preclude any current activities that banks and their affiliated businesses are authorized to do. It reasserts Congressional intent in maintaining the separation of banking and commerce.

Members of Congress overwhelmingly are signaling their support for retaining the commercial distinction of real estate activities and their intention to maintain the separation of banking and commerce. In fewer than five months after The Community Choice in Real Estate Act was introduced in Congress, more than 225 Members of the House of Representatives and at least 10 Members of the Senate signed on as cosponsors of the bills.

The Act Supports A Diversified Real Estate Services Marketplace

During the past two decades, the financial services marketplace has grown substantially due, in part, to the entry of both commercial firms and banking companies. Commercial firms that are involved in the selling and/or brokering of durable goods (such as refrigerators, automobiles, and homes) have naturally expanded into financial services to facilitate the transaction by offering consumer financing that is complementary to their primary service—the brokering/selling of a tangible product. Similarly, banking companies that are involved in the selling of banking services (such as consumer loans and commercial and industrial loans) have also expanded into financial services so that they can capture a greater market share by offering their customers financial services that complement their primary service—banking.

However, unlike a commercial firm, which risks its own capital funds, a bank's ability to expand its powers and diversify into financial activities has historically been constrained by Congressional oversight. Because of the "special nature" of banks and the many Federal subsidies that flow through a bank (that is, deposit insurance, privileged access to credit), Congress has continually repeated its intent to separate banking activities from commerce activities in an effort to avoid conflicts of interest, adverse market outcomes, and fairness issues that can be caused by a bank's special privileges.

The Gramm-Leach-Bliley Act provided an opportunity for financial holding companies to expand their product/service lines into financial activities and activities that

[1] See *Federal Register,* Vol. 66, No. 2, Wednesday, January 3, 2001, p. 310.

[2] Further evidence of Congressional intent regarding holding company expansion into non-financial areas can be discerned by the vote in the House of Representives in 1998 in which an effort to permit banks to engage in commerce—up to 5 percent of their annual net revenue and five percent of their total assets—was defeated by a vote of 229 to 193.

are incidental to finance. It is very clear that the GLB Act set the foundation for a shared competitive playing field for both commercial firms and banks—the financial services marketplace. Commercial firms that have subsidiaries involved in financial activities compete head on with bank-owned financial subsidiaries. This competition was not "created" by the GLB Act; it already existed because bank-affiliated mortgage lenders already existed and, in fact, dominated—and still dominate—mortgage originations. (In 1999, commercial banks and subsidiaries of commercial banks accounted for the largest market share—44 percent—of mortgage originations, according to the Home Mortgage Disclosure Act. The top 25 diversified real estate brokerage firms accounted for only 0.8 percent of mortgage originations.) For example, the General Motors Acceptance Corporation (GMAC)—a financial services subsidiary of General Motors competes against Wells Fargo and other banks to sell financing services to customers purchasing a General Motors automobile. Similarly, Circuit City competes directly with Bank of America to sell financing services to customers purchasing Circuit City-electronic products.

In the real estate marketplace, companies like John Doe, REALTOR®, compete directly with banks, like Bank of America, in the financial services marketplace by providing real estate—related financial services—principally mortgage brokering services and title insurance—to customers purchasing a home that was brokered/sold by John Doe, REALTOR®. Both the real estate brokerage company and the bank offer a number of real estate related financial services to homebuyers and sellers.

In the post-GLB Act marketplace, the real estate brokerage company does not offer banking services and banks do not offer commercial services—real estate brokerage and management. The separation of banking and commercial activities is intact. *The competition is in the financial services arena where it belongs.* Consumers benefit from this arrangement because the direct competition for financial services between commercial companies and banks results in greater consumer choice and customer service. Prohibitions against the encroachment of Federally subsidized banks into the world of commerce limit conflicts of interest or unfair competition.

The ability of real estate brokerage companies to diversify their business lines into the financial services marketplace has produced a number of diversified real estate services companies to better serve consumers. Even the smaller and less diversified real estate brokerage companies now look to offer ancillary services to their homebuying and selling clients. Moreover, there are examples where banks and real estate brokerage companies have joint ventured in the financial services marketplace. A prominent example is Prosperity Mortgage, which couples Wells Fargo Bank and Long & Foster, REALTORS®.

Diversified real estate brokerage companies compete directly against the large financial holding companies (banks) in the financial services marketplace each and every day. The competitive dynamics in this marketplace are no different from the competitive nature of the automobile and electronics marketplaces. The beneficiaries in all of these markets are consumers.

The Community Choice in Real Estate Act Will Benefit Consumers and the Real Estate Industry

The Community Choice in Real Estate Act will help to maintain a competitive, efficient, and balanced real estate marketplace, providing the consumer with choice at low cost and with no risk to the U.S. taxpayers. The entry of Federally insured depository lending institutions into the real estate brokerage business would tilt the competitive playing field by pitting Government subsidized financial holding companies and national bank subsidiaries against privately funded real estate enterprises. Passage of the Act will help preserve a fiercely competitive real estate brokerage marketplace.

The real estate brokerage industry as it exists today has large numbers of independent real estate professionals and brokerages actively competing for prospective buyers and sellers. Competition is fierce, efficiencies are high, and there are relatively few barriers to entry. These characteristics make it highly unlikely that the proposed regulation would benefit either business or consumer interests.

The residential real estate brokerage industry is a competitive marketplace, where more than three quarters of a million REALTORS®[3] and tens of thousands of real estate brokerages compete for customers' business each day. The underlying

[3] There are approxiamtely two million people who hold real estate licenses. However, not all of those are active practitioners. It should be noted that Realtor®, REALTORS®, and Realtor-Associate® are registered collective membership marks that identify, and may be used only by, real estate professionals who are members of the National Association of REALTORS® and subscribe to is strict Code of Ethics.

cost structure of the industry and the relative ease of entry into the market serve as checks to the concentration of market power. The large number of industry players ensures homebuyers and sellers access to service providers who best meet consumers' needs at the lowest price possible.

Real estate firms tend to compete actively for business in three different arenas. First, firms compete for the best real estate agents. Second, firms compete for sellers' listings and homebuyers against other real estate firms in their market area. Finally, real estate firms and agents compete against the other homebuying and selling options, including For Sale by Owner (FSBO's). The result of this three-pronged competition revenue and cost pressures that limit profitability for most real estate brokerages. But this competition also results in excellent service provided efficiently by real estate firms and agents for both buyers and sellers. The Community Choice in Real Estate Act would preserve this system.

Mixing Banking and Commerce Will Stifle Competition in the Real Estate Industry

Today any commercial firm can enter real estate brokerage, but FHC's have Government-imposed barriers to entry. National banks and financial holding companies have long been able to own mortgage companies and engage in joint ventures with real estate firms. They now claim that real estate brokerage and management are financial activities, without acknowledging their current competition in this area through their existing mortgage lending affiliates. Financial holding companies now want to directly own commercial firms in the form of real estate firms and compete with other commercial firms using the Federal subsidies available to their banking subsidiaries. This is not the competition that Gramm-Leach-Bliley envisioned.

The expansion of banking powers that would permit FHC's to engage in real estate brokerage activities will have a detrimental effect on the real estate brokerage industry. The Federal banking charter provides Federal deposit insurance and privileged access to credit—advantages not offered to real estate brokerage firms. Most of the advantages of the bank charter directly add to bank profitability that would flow up to the financial holding company, thus offering FHC's and their real estate brokerage subsidiaries a competitive advantage over commercial firms in the real estate industry.

Allowing FHC's to provide brokerage, funding, and investment services for real estate would increase the power of these integrated firms. This power could be used to limit the entry of new real estate firms and thus limit the competition characterizing the market today in two distinct ways.

First, FHC's would have the ability to fund new real estate brokerages with revenues from the banking side of the business, thus tilting the playing field toward FHC's. Financial holding companies would be able to use banking fees or even profits from their mortgage operations both to increase profitability and to subsidize their entry into insurance and other financial services. Few traditional real estate brokerages have access to outside income streams to subsidize the real estate brokerage business. The result could be an increase in industry concentration as real estate brokerages exit the industry unable to respond to their well-financed new competitors. The same dynamic would limit entry of new real estate firms.

Second, FHC's could leverage their privileged access to capital, access to numerous subsidiaries, and outside income streams to engage in a sustained period of below-cost pricing designed to eliminate other firms providing the same service. This could damage any real estate brokerage firms that do not have the resources to defend themselves against a well-financed and subsidized FHC. Again, formerly viable real estate brokerages could be forced to dissolve—not because of an inability to provide efficient and quality service to consumers, but because below-cost pricing can unfairly eliminate the competition. The result could be a smaller number of firms that are less likely to provide the benefits that competition brings to today's real estate brokerage market.

Mixing Banking and Commerce Hurts Consumers

The National Association of REALTORS® agrees with the message sent by the U.S. Congress: mixing commerce and banking will adversely affect the real estate industry. If big banks are allowed into the real estate business, the market could soon be dominated by a smattering of large banking conglomerates whose primary goal is to cross-sell various financial products, not to put people in homes and commercial properties. The end result could be fewer choices for consumers, higher fees and less competition.

In the banking industry a few dominant firms control a significant share of the total market. FHC's' entry into the real estate brokerage market would likely increase concentration and introduce unfair competition because of their Federal sub-

sidies. There is likely to be a significant decline in the number of firms and the number of small firms that represent a key segment of the industry. The real estate brokerage business could change from a localized, highly competitive industry to one that is dominated by nationwide Federally chartered firms.

It is unclear what FHC's could bring to the market that would increase competition. Any additional entry will not necessarily lower costs. FHC's claim that consumer costs will go down, but those lower costs can only be realized by introducing economies of scale or scope, cross-subsidization, or predatory pricing. The latter two reasons are not permanent benefits for consumers. Only the first—economies of scale—enhances consumer welfare. Without an increase in efficiency, there would be no cost savings to pass along to consumers. But there are limited economies of scale in the real estate brokerage industry.

Even if FHC's were able to reduce real estate brokerage fees temporarily, any savings to homebuyers would be offset by higher costs for bank customers. Absent economies of scale, lower real estate brokerage fees can only come via cross-subsidization from other business arenas. The higher banking fees are likely to become permanent features of the banking system, given barriers to entry and concentration of market power, while reductions in real estate brokerage fees could be temporary as firms exit the industry.

The expansion of banking powers that would permit financial holding companies into the real estate brokerage business could also limit consumer choice in the selection of a real estate professional and other real estate-related service providers. FHC's have an inherent conflict of interest in selling financial services (banking products) rather than serving customers in the brokering of real property. The parental relationship between FHC's and their subsidiary real estate brokerage business would likely steer consumers to the FHC's' subsidiaries. Agents working for an FHC-owned real estate brokerage firm would have less incentive to find an outside loan provider or other real estate settlement service vendor that best fits their customers' needs.

There is also the likelihood that FHC's entering the real estate brokerage industry would retain their real estate agents as salary-based employees, rather than as commission-based independent contractors. As FHC employees, these real estate agents would focus on the FHC's profits, cross-selling the holding company's other services. This is contrary to the current real estate market where there is fierce competition among a large number of firms ensuring that consumers receive valuable, *impartial* advice when they most need it.

The Act Benefits Consumers and the Real Estate Industry

In summary, passage of The Community Choice in Real Estate Act will ensure more competition, and thus more consumer choice. More competition will maintain the lowest cost real estate brokerage services as well as lower banking fees. Taxpayers will be protected from risks associated with commercial endeavors underwritten by Federally insured depository lending institutions. Consumers will continue to be served by real estate professionals whose interests are aligned with theirs.

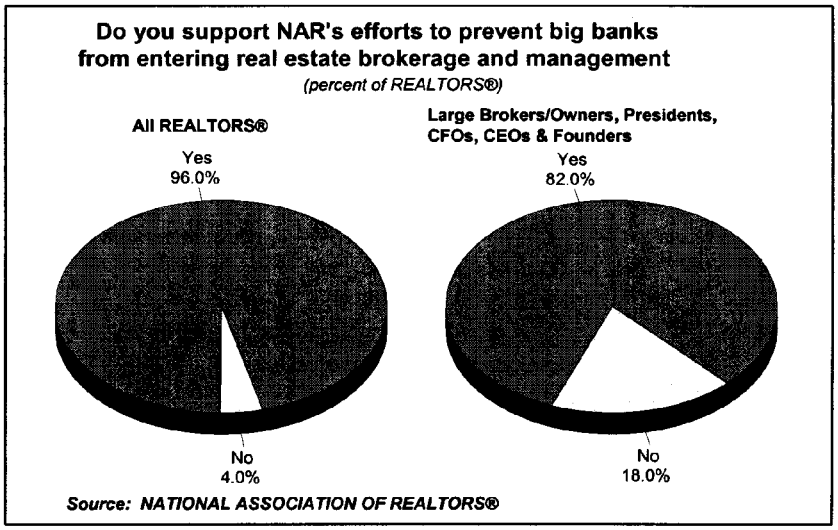
The Community Choice in Real Estate Act defines real estate brokerage and management as commercial activities, outside the scope of a Federal bank charter. The Community Choice in Real Estate Act will limit banking institutions to activities permitted under their current charters, and maintain the current environment that provides for an efficient and competitive real estate brokerage market that benefits both the real estate industry and America's consumers.

Overwhelming Industry Support for the National Association of REALTORS® Position

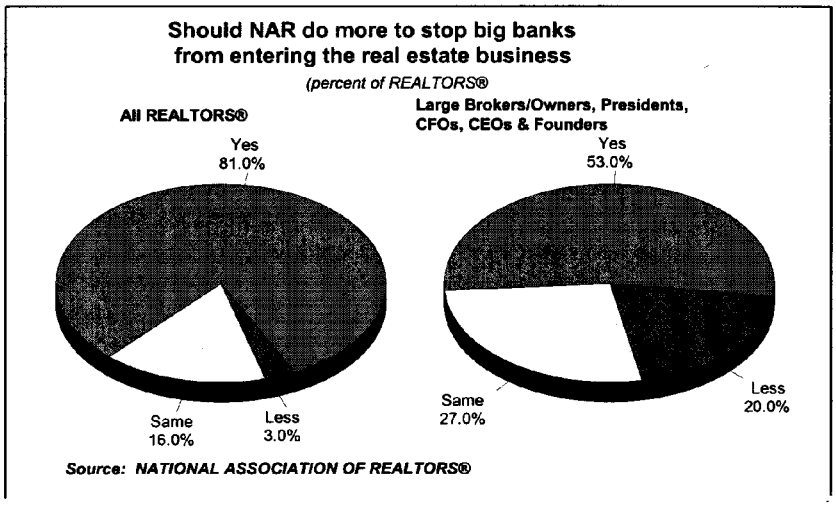
The National Association of REALTORS® represents all of its members and the real estate industry as a whole. In the last 14 months, the association has spoken for its 800,000 members with one voice, as *The Voice for Real Estate.* A unified voice is crucial in maintaining a competitive and highly efficient real estate industry that serves America's property owners. It is even more vital on the issue of allowing financial holding companies and national bank subsidiaries (FHC's) to engage in real estate brokerage and property management activities.

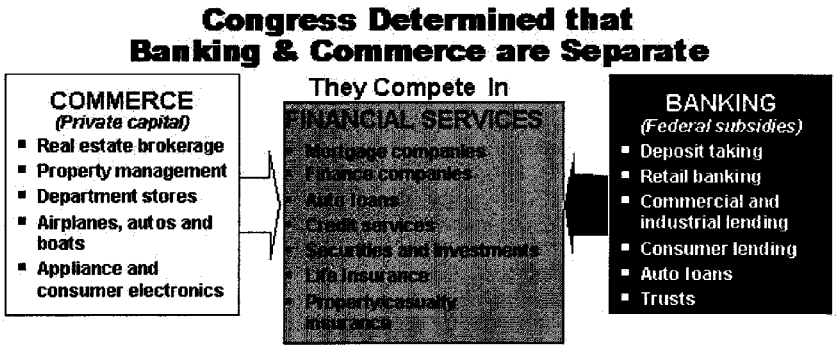
Recent research indicates that the National Association of REALTORS® does speak for an overwhelming majority of its members who oppose FHC's' entry into the real estate brokerage and management business. In a recent survey (February 2002), more than 9 out of 10 REALTORS® oppose the pending Federal Reserve and Treasury Department rule that would allow big banking conglomerates to enter real estate brokerage and management. Perhaps more importantly, 96 percent support

efforts by the National Association of REALTORS® to prevent FHC's from entering real estate brokerage management.

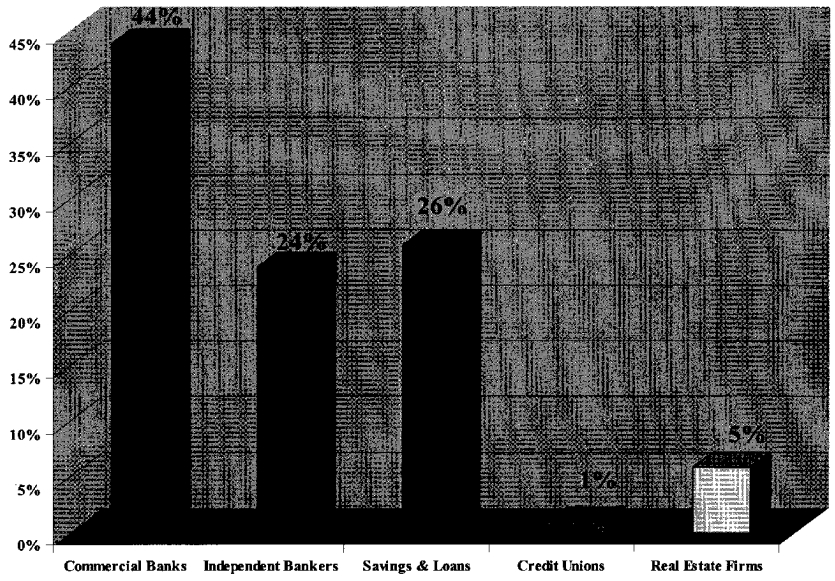


The survey found widespread support among broker-owners as well as sales agents. Some 82 percent of large brokers support NAR's position, according to the survey. The survey also found that 81 percent of REALTORS® want NAR to be even more aggressive in its efforts, and majority of large brokers also want NAR to do more to stop FHC's from entering the real estate business.




Congress Determined that
Banking & Commerce are Separate
COMMERCE
(Private capital)
Real estate brokerage
Property management
Department stores
Airplanes, autos and boats
Appliance and consumer electronics
They Compete In
FINANCIAL SERVICES
Mortgage companies
Finance companies
Auto loans
Credit services
Securities and investments
Life insurance
Property/casualty insurance
BANKING
(Federal subsidies)
Deposit taking
Retail banking
Commercial and industrial lending
Consumer lending
Auto loans
Trusts

Mortgage Loan Originations



* Data according to 1999 Home Mortgage Disclosure

State Banking and Real Estate Activity

Few state-chartered banks engage in real estate brokerage

- Only 6 states have banks with residential real estate brokerage operations
- Only 18 banks in these states have residential real estate brokerage operation
- These banks represent 0.2 percent of all banks and serve areas with 0.57 percent of U.S. population.

	State	Bank Name	City	County	County Pop
1	Iowa	Tama State Bank	Marshalltown	Marshall	39,311
2		Northwest Federal Savings Bank	Storm Lake	Buena Vista	20,411
3		Sac City State Bank Real Estate	Sac City	Sac	11,529
4		Mercantile Bank-Rock Rapids	Rock Rapids	Lyon	11,763
5		United Bank of Iowa	Odebolt	Sac	11,529
6		First Central Bank	Dewitt	Clinton	50,149
7		Maquoketa State Bank	Maquoketa	Jackson	20,296
8		Hardin County Savings Bank	Eldora	Hardin	18,812
9		St. Angar State Bank	St. Angar	Mitchell	10,874
10		First Federal Bank	Sioux City	Woodbury	103,877
11		Tranor State Bank	Tranor	Pottawattami	87,704
12	Georgia	Community Bank	Cornelia	Habersham	35,902
				Jackson	41,589
				Stephens	25,435
13	Wisconsin	Bank of Alma	Alma	Buffalo	13,804
14		Anchor Bank	Madison	Dane	426,526
15		Union State Bank	Kewaunee	Kewaunee	20,187
				Brown	226,778
16	Michigan	First Bank	Escanaba	Delta	38,520
17	North Carolina	People's Bank	Newton	Catawba	141,685
18	Nebraska	Security First	Lincoln	Lancaster	250,291
				TOTAL POP	1,808,972

Source: Research conducted by the NATIONAL ASSOCIATION OF REALTORS® July 2001. Information collected through telephone calls with state banking and real estate regulators and state REALTOR associations.

PREPARED STATEMENT OF JAMES E. SMITH

PRESIDENT, AMERICAN BANKERS ASSOCIATION
CHAIRMAN AND CHIEF EXECUTIVE OFFICER
CITIZENS UNION STATE BANK AND TRUST COMPANY, CLINTON, MISSOURI

MAY 23, 2002

Mr. Chairman, I am James E. Smith, Chairman and CEO of Citizens Union State Bank and Trust, Clinton, Missouri and the President of the American Bankers Association. I am pleased to be here today on behalf of the American Bankers Association (ABA). ABA brings together all elements of the banking community to best represent the interests of this rapidly changing industry. Its membership—which includes community, regional, and money center banks and holding companies, as well as savings institutions, trust companies, and savings banks—makes ABA the largest banking trade association in the country.

I want to thank you, Mr. Chairman, for holding this hearing. It allows all parties to get beyond the heated rhetoric and focus on the issues. In the debate over allowing banks to engage in real estate brokerage, we bankers have sometimes been portrayed as somehow working against real estate agents. We disagree with this characterization. The reality is that many agents and bankers already work closely with one another. In fact, I believe that bankers and many in the real estate industry are much closer aligned on the issue of real estate brokerage than the rhetoric suggests. We all believe that customers deserve to have the best possible service, regardless of what company provides it. We all want customers to have many choices of whom to deal with so they can seek out that agent or company that they trust. And we all believe that the provision of any financial service should be done in a safe and sound manner—including adhering to all licensing, qualification, sales practices, and continuing education requirements.

If banking institutions offer real estate brokerage and management services there would be more choices available for everyone. Consumers would have more choices of real estate firms when buying or selling a home. Real estate brokers would have more choices of potential employers. And real estate companies would have more choices of companies to partner with that could provide new sources of capital and technology. By prohibiting bank involvement, S. 1839 would do just the opposite—consumers, real estate agents, and real estate companies would have fewer choices. We believe a competitive market is the best way to provide quality real estate brokerage and management services.

As we begin our discussion, it is important to note that combining real estate brokerage and banking services is not a new or unusual activity. Real estate firms do it. Insurance companies do it. Securities firms do it. And well over half the Federally insured depository institutions in this country, including many of the largest banks and savings institutions, have authority to do it. In fact, my community bank in Missouri has the authority to do it. The ABA believes that all banking institutions should have the same opportunity to provide services that meet the needs of our customers.

This issue of open and fair competition is not new—in fact, it has been debated in this legislative body for many years. However, the statutory context within which today's discussion will take place is quite different. In 1999, Congress took an historic step to modernize the regulation of the financial services sector by passing the Gramm-Leach-Bliley Act (GLB Act). In the more than 15 years of debate on the Act, Congress often found itself in the middle of arguments between financial services industries about who should do what. The result was gridlock and an out-of-date financial system that did not reflect changes in consumer needs or in the use of technology.

To be sure that the procompetitive goals of the GLB Act continued to be met in a dynamic marketplace, Congress established a flexible, yet conservative regulatory process that would permit the financial industry to offer new services without the need for further legislation. This regulatory system gives the Federal Reserve and Treasury the flexibility and responsibility to determine what activities should be approved, including considering what is necessary to permit financial holding companies and national bank subsidiaries to "compete effectively with any company seeking to provide financial services in the United States." This authority is consistent with the Federal Reserve's and Treasury's role to ensure efficient, safe, and competitive financial markets.

The GLB Act promotes competition, safety and soundness, and enables Congress to avoid becoming embroiled in every competitive issue. S. 1839 would take out the flexibility built into this new system, and put Congress back in as referee for future competitive disputes. Simply put, the bill would reverse the most important long-

term provision in the GLB Act over the very first proposal put forth under it. Having worked so hard to develop a mechanism to keep our financial system up-to-date on an ongoing basis, Congress should not reverse itself less than 3 years later because some group wishes to protect itself from competition. The system established in the GLB Act should be allowed to work and S. 1839 should not be enacted.

Banking institutions should be allowed to offer real estate services for three key reasons:

- It's good for consumers—It means more choices, better service, competitive prices, and greater convenience.
- It's only fair—Since real estate firms offer banking and insurance services, it's only fair that banking institutions be allowed to provide real estate services. This is what the Gramm-Leach-Bliley Act is all about—promoting free and fair competition by leveling the playing field.
- It's safe—All consumer protections, including all State licensing, qualification, sales practices, and continuing education requirements, plus strict privacy laws and antitying rules, would apply to bank-affiliated real estate agents. And because brokerage and management are agency activities, they pose no risk to the bank.

I will discuss these points in detail in the remainder of my statement. Before I do, let me assure you that the competitive issues we are talking about here this morning are important to banks of all sizes. In fact, the ability to offer real estate brokerage may be more important for smaller institutions. Rural communities may lack real estate agents or are served only by branches of brokers in other towns because there is insufficient business to warrant a local brokerage office. In such small communities, the bank is perceived as the place that will have the greatest amount of information on what properties are for sale, including farmland acreage in agricultural communities. I believe, as do my fellow colleagues who run small community financial institutions, that these services would significantly benefit our customers and our communities.

Competition is Good for Consumers

The benefits of competition are well known. In a free market, businesses choose to offer new products if they believe they can provide better services at competitive prices. Obviously, not all banking organizations will choose to offer real estate services, but those that do will enter the market because they believe they can meet or beat the competition. Increasing the number of providers raises the bar for all the participants, forcing improvements in efficiency, pricing, and service levels—all to the benefit of homebuyers and sellers.

Allowing all banking institutions to provide real estate services expands the choices for everyone: consumers, real estate agents, and real estate companies. This is not only the opinion of bankers, but increasingly, it is a view shared by real estate agents and particularly real estate companies.

More Choices for Consumers, Real Estate Agents, and Realty Companies

If banking institutions were allowed to offer real estate brokerage and management services there would be more choices for everyone.

- More Choices for Consumers—More players in the real estate business mean more and better products for consumers. In any competitive market, new participants bring new, creative ideas to the market—all designed to provide better service and greater convenience, at reasonable prices. In fact, businesses can only be successful in new markets by providing services that meet the needs of customers. Free competition among a wide variety of providers is the cornerstone of our economic system.
- More Choices for Real Estate Agents—Real estate agents pride themselves on being independent contractors, choosing the best companies to work for. If there are more companies to choose from, agents' employment opportunities will be much broader. Banks will only be able to attract good agents by offering competitive commissions and other incentive-based compensation packages. And because the real estate business requires expertise, licensing, and other requirements, banks would seek out experienced real estate agents. Banks know that converting tellers to real estate agents would be a poor business strategy.
- More Choices for Real Estate Companies—Forward-looking businesses are always looking for opportunities to improve their franchise value—strengthening, expanding, merging, or even selling their business. Allowing banking institutions to engage in real estate brokerage and management services gives real estate companies more options for bringing additional capital and technology to the table, through joint ventures, for example. Banking institutions also represent potential buyers if agencies choose to sell their businesses. Indeed, in some communities,

partnering with the local bank may be the only way for the local real estate broker to compete with the growing national chains. This is why many real estate firms also oppose S. 1839. It is interesting to note that many insurance agencies thought that bank involvement was going to hurt their business—until they realized that it provided many more options than they had before. To that end, the Financial Service Coordinating Council, consisting of the ABA, the American Council of Life Insurers, the American Insurance Association, and the Securities Industry Association, supports open competition and is on record opposing S. 1839.[1]

S. 1839 reduces choices: consumers would have fewer choices of whom to do business with, agents would have fewer choices of whom to work for, and businesses would have fewer choices for joint marketing, fewer potential merger partners, and fewer potential buyers. ABA believes a competitive market is the best way to provide quality real estate brokerage and management services—simply put, more competition means more choices.

Many Real Estate Agents Support Open Competition

Many agents and real estate companies are not concerned by the prospect of banking organizations offering real estate services. Many look forward to the opportunity to partner with a local bank. Independent agents who provide good service today know that they will be competitive with anyone, whether the competitor is another independent agent or one affiliated with a bank. The views of these real estate agents are often lost in the emotional rhetoric of their trade association. Here are a few examples of comments filed by real estate agents with the regulators on this proposal:

- A broker from California writes: "Additional competition will be healthy for the industry. Banks and other financial institutions have learned how to meet the needs of consumers and to handle their financial matters. One's home is the biggest financial asset most consumers will ever deal with. If agents are so special for consumers, then they have nothing to fear. Maybe we could see commissions come down!"
- A real estate broker in North Carolina writes: "I am a 38-year veteran of the real estate industry and do not agree with our National Association of [REALTORS®] . . . There are several reasons I feel this way, primarily because our small family-owned business has always faced stiff competition from large real estate firms, yet we have been able to earn a good, honest living. I believe that competition is the American way and if you're good at what you do, you can survive whether large or small."
- Another real estate agent notes: "I would welcome the hopefully more professional business management that banks would likely bring to this business. With most real estate being part-time people with limited training, the real estate business is full of misinformation, poor service, etc., a situation that could be improved with bank involvement. Furthermore, the American consumer deserves more true competition in this business. Bank-owned real estate agencies may be able to lower transactions costs to consumers through aggregation of services benefiting the public as a whole."
- A real estate broker in Wisconsin writes: "I don't recall the NAR [National Association of REALTORS®] concerning themselves with real estate brokers having access to online companies therefore cutting the independent mortgage banker and local lender out of the transaction."
- Another real estate agent writes: "NAR predicted the doom and gloom many, many years ago when franchise brokerage was in its formative stages. ERA, Re/Max, Coldwell Banker et al., were all predicted to end 'mom and pop' real estate firms. These franchises have come; many have gone or merged with others. And yet still, 'mom and pop' brokerage firms continue to survive because of the personal attention. I welcome the competition, and I will continue to survive."

Many Real Estate Companies Also Support Open Competition and Oppose S. 1839

The real estate industry, like banking and most other industries, is constantly changing. Larger real estate brokerage firms are increasing their market share every time you turn around. In 1990 there were 150,000 residential real estate firms. Today there are about half that many. The large chains are buying up more and more local firms. Today Cendant—which owns Century 21, Coldwell Banker, and ERA—has 23 percent of the existing home sales market and has been aggressive in acquiring real estate companies. In some communities a partnership with the local bank may be the only way to compete with the national chains and maintain

[1] The letter, dated January 16, 2002, is attached to this testimony.

a local presence. The Internet is playing a bigger and bigger role with customers, allowing them to surf for the perfect home, at the perfect price, financed with the perfect mortgage loan, and covered under the perfect insurance policy—24 hours a day, 365 days a year. More and more real estate services are being combined, including brokerage, insurance, and mortgage services that are offered as "one-stop shopping" packages, a subject I will speak to at length below.

In this new, competitive environment, bankers and real estate professionals have much to offer to each other—and to consumers. Banks like mine could provide needed capital, crossmarketing opportunities, and technology to support the growth of local real estate firms. Real estate professionals could provide the personalized services and experience that is their strength. Many real estate companies realize the strengths that both industries bring to the table. They also realize the severe limitations S. 1839 would impose on their ability to joint market, merge, be acquired, or even to buy a bank.

In February of this year, The Realty Alliance—comprised of many of the Nation's largest and most successful independent real estate companies with a total of 62,000 agents—went on record in opposition to NAR's position. In its letter to NAR, The Realty Alliance stated, "Our members favor and support a fair, free-market environment unbound by legislative restrictions. We find it hypocritical and fundamentally wrong to ask that national bank subsidiaries be barred from real estate brokerage activity, while real estate brokerages operate mortgage banking, insurance and title insurance businesses. . . . We believe, in fact, that consumers would benefit from the influx of capital that may result from nationally chartered banks entering this arena. We also believe that increased competition from companies of size would benefit consumers by making all of us sharpen our skills and improve the services we provide. In our view, the role of Government is not to limit competition, as your legislation would do, but rather to foster a business environment in which consumers benefit from competition. The members of The Realty Alliance look forward to working, and prospering, in such an environment."

Paul Harrington, President of DeWolfe New England, which is one of the largest real estate firms in the Northeast, summed it up when he said, "We believe that banks should be able to compete with us as long as there are safeguards to ensure that deposits are not being improperly invested. It would be hypocritical for us to say otherwise because we promote the fact that we offer customers convenience through one-stop shopping."[2]

Promoting Free and Fair Competition—The Fundamental Tenet of the Gramm-Leach-Bliley Act

The Gramm-Leach-Bliley Act established a framework for modernizing our financial system. After working on this for the last 20 years, Congress recognized the need for flexibility in the face of a rapidly evolving financial landscape. As Senator Phil Gramm said at the signing ceremony for this Act, "The world changes, and Congress and the laws have to change with it. We have learned that we promote economic growth and we promote stability by having competition and freedom."

Providing the same opportunities under the same rules and regulations is a key to promoting free and fair competition. In today's real estate market, it is commonplace for real estate companies, securities firms, and insurance companies to provide end-to-end services, including brokerage, mortgages, and insurance. Yet not all financial service players have equal ability to offer these same services. The Gramm-Leach-Bliley Act was designed to address these inequalities. To examine this in detail, this section looks at three key issues: (1) the market reality that real estate firms are already providing banking and other financial services and that the real estate industry is more concentrated than the banking industry; (2) the system established in the Gramm-Leach-Bliley Act to correct disparity in the provision of financial services among providers and thereby promote free and fair competition; and (3) the changing real estate and financial marketplace that demands a flexible regulatory approach to address the inequities that exist today and may exist in the future.

Combining Real Estate Brokerage and Banking Services is Not a New or Unusual Activity

As I previously noted at the outset, real estate companies, securities firms, insurance companies, credit unions, savings associations and, in half the States, State-

[2] *The Boston Globe,* February 25, 2001.

chartered banks can offer real estate services.[3] Ironically, the National Association of REALTORS® is now objecting to the very combinations that their members have undertaken—offering brokerage, mortgage banking, and, often, insurance under one roof.

Take, for example, two of the biggest real estate companies in the Washington DC area—Weichert and Long & Foster. Both offer the full range of financial services. Weichert calls it "One Stop Gold" and Long & Foster calls it "Real-Edge Services." These packages provide valuable cost, convenience, and service options for customers. These examples show the importance companies—and their customers—place on having the option to combine real estate brokerage, mortgage and insurance services. On the following two pages, I have included several examples of how real estate companies that offer both banking and brokerage services characterize—in their words—their services.

All banks should have the same options. In fact, according to NAR's own survey in 1999 and a recent 2002 survey by Murray Consulting, not only is one-stop shopping viewed extremely positive by homebuyers, but banks, mortgage companies, and real estate companies are all viewed equally as appropriate providers of these services.

Simply put, if real estate services and other financial products are already combined by many real estate and other financial firms, there is no reason why all banking organizations should not be accorded the same opportunities to provide these products to their customers.

In my opening remarks I made the point that this is an issue for banks of all sizes, not just large banks, as NAR has suggested. More than 40 percent of all banks—over 4,000 institutions—have fewer than 25 employees. These are truly small businesses that would like the opportunity to broaden the financial products they can offer their customers and to compete with real estate firms offering loans and homeowners insurance. For the typical community bank, the intent is not to turn real estate brokerage into a major income-producing center, but rather to provide high-quality, high-personal-touch services for customers whose needs the bankers intimately understand and whom they already serve in other capacities. Generally, this is likely to take place by a combination with a local real estate firm—often one that needs the joint effort to complete with the national chains.

[3] See attachment developed by the Conference of State Bank Supervisors (CSBS) for a listing of the authorities for each State. Regarding credit unions, recently several in Wisconsin jointly purchased a majority interest in one of the State's larger real estate brokerage firms.

Long & Foster—More Than A Great Real Estate Company.

We're Also A Great Mortgage, Title, And Insurance Company, Too!

Since 1968, the LONG & FOSTER COMPANIES have grown to become the largest and most respected real estate company throughout our five-state Mid-Atlantic region, with annual sales of $13.3 billion.

We've also become quite a powerhouse in mortgages, title, and insurance, too.

Imagine the convenience of buying a home, securing the mortgage, arranging the title work, and getting homeowners' insurance—all in one place!

That's precisely what the LONG & FOSTER COMPANIES do for their clients and customers: deliver top-quality real estate and related financial services—all in one place—from a name synonymous with customer satisfaction and trust.

Convenience costs no more with the LONG & FOSTER COMPANIES. In fact, it could cost you much less. Stay on your professional Long & Foster Sales Associate to discover how the other members of the LONG & FOSTER COMPANIES family, whose expertise in mortgages, title, and insurance fully complements that of our Sales ASSOCIATES.

LONG & FOSTER REALTORS

PROSPERITY MORTGAGE COMPANY

MID-STATES TITLE INSURANCE AGENCY, INC.

LONG & FOSTER INSURANCE AGENCY, INC.

Real-Edge Services, All in One Place.

The largest independent real estate broker in Illinois, with more than $4 billion in annual sales.

The nation's oldest real estate company actually started in the financial arena nearly 150 years ago, when Baird & Warner began making loans on downtown Chicago properties. We continue to play a dominant role today, with Key Mortgage Services and its subsidiary, North Shore Mortgage, closing more than $500 million per year in residential mortgage loans — ranking among the top five mortgage companies in Illinois. Baird & Warner is once again leading the field, offering the convenience of "one-stop shopping" for a wide variety of real estate-related services.

Emphasis added
Source: http://www.bairdwarner.com/about/default.asp

The nation's largest individually owned real estate company, with over 370 loan products to choose from, including Conventional, FHA, and VA loans.

Weichert Financial Services' Weichert Gold Services Program is raising the performance guarantee from $250 to $1,000 for all new Gold Services applications. If Weichert Gold Services fails to meet its performance guarantees, the homebuyer will receive a $1,000 credit towards their mortgage related costs at the time of settlement.*

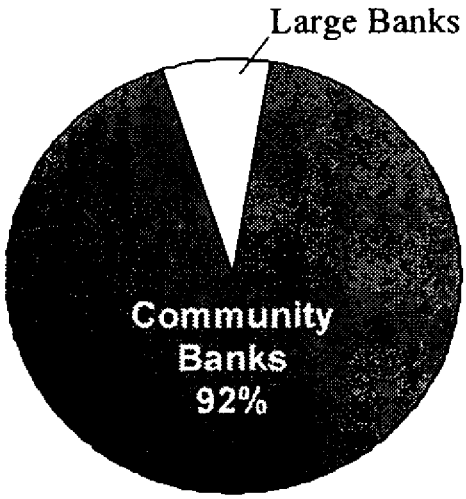
*To participate, the buyer must elect to use Weichert Financial Services to obtain a mortgage, Weichert Insurance Agency to obtain homeowners insurance and Weichert Title Agency or Weichert Closing Services to obtain title insurance.

Emphasis added
Source: http://www.weichert.com/

It is also a misconception that all national banks are large (see Chart 1). In fact, over 90 percent of national banks are community banks. Moreover, of the 10 largest banking firms, four appear to already have the legal authority to engage in real estate activities. There certainly has been no market disruption from the fact that well over half of the insured depository institutions in this country have the ability to offer real estate brokerage and management services today.

Chart 1

Over Ninety Percent of National Banks are Community Banks*

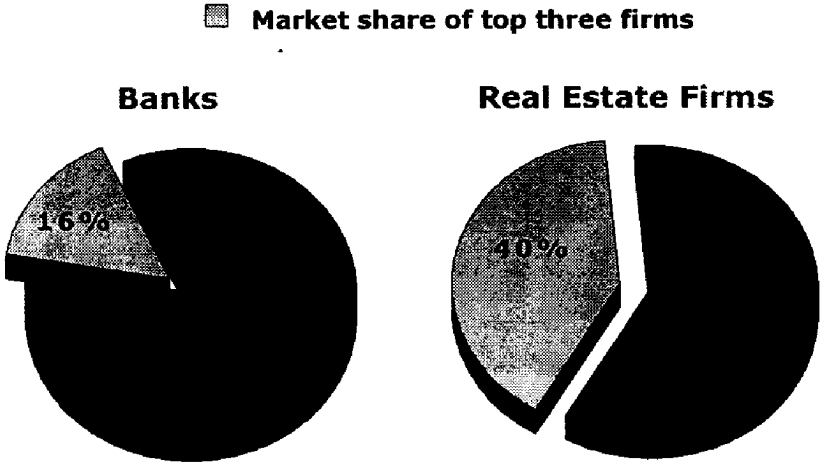


*** Defined as banks with less than $1 billion in assets**

Banks that already offer real estate services through the trust department frequently find themselves having to explain to customers that the bank cannot help them with these services outside the trust relationship. These customers do not understand why the bank is unable to do so. Authority to offer real estate services by the banking organization would bridge this unnecessary gap.

What is ironic about NAR's false assertion about large banks wanting to dominate the real estate market, is the fact is that the real estate industry is significantly more concentrated than the banking industry. Today, a few firms dominate the real estate brokerage industry (see Chart 2). In fact, the top two firms in the brokerage business (Cendant and Re/Max) have 33 percent of the market. By comparison, the top 10 banks have the same 33 percent of the banking market. Cendant Corporation accounts for one out of every four real estate agents and alone has a 23 percent market share of existing home sales.

Chart 2
The Real Estate Industry is Much More Concentrated than the Banking Industry



And because consolidation within the real estate industry is occurring at breakneck speeds, small realty companies are far more likely to be bought up by one of the major real estate firms than by a bank. Many real estate brokers have told the ABA that they would welcome approval of the proposal because it would provide a potential local partner to help them compete with the large national chains. In fact, the local bank can help the small firm, through joint ventures and capital, to compete with the large national real estate firms.

Thus, the marketplace reality is that real estate firms already provide end-to-end services and the largest real estate companies have been increasing their domination over the market.

The GLB Act Was Designed to Allow Flexibility to Adjust to the Marketplace

In the years immediately preceding passage of the GLB Act, Congress recognized that the statutory standard for regulatory approval of new activities for bank holding companies—the "closely related to banking" standard—was woefully inadequate in an economy transformed by technological progress. Thus, Congress agreed to a new, considerably broader, standard to enable banks and bank holding companies to remain competitive no matter in what direction financial services evolved. That new standard—activities that are financial in nature or incidental to a financial activity—was intended to provide the flexibility Congress knew would be necessary. Those activities may be conducted only in financial holding companies ("FHC") or financial subsidiaries meeting certain safety and soundness and community needs standards enumerated in the statute.

Congress did not give the FRB and the Treasury unfettered discretion to make the determination that an activity is appropriate for approval. GLB Act specifically sets forth certain traditional banking activities that Congress knew were clearly financial in nature.

In addition to these currently recognized activities, the Act authorizes activities that the FRB and Treasury determine, by regulation or order, to be "financial in nature or incidental to such financial activity." This authority to permit new financial activities is considerably broader than the FRB's comparable authority before the GLB Act was enacted, which had only extended to a new activity that was "so closely related to banking as to be a proper incident thereto."

One specific aspect of this new authority is that the FRB is directed to define the extent to which three types of activities are "financial in nature": (1) lending, exchanging, and engaging in certain other transactions with financial assets other than money or securities; (2) providing any device or instrumentality for transferring money or other financial assets; or (3) arranging, effecting, or facilitating finan-

cial transactions for the account of third parties. ABA believes the proposed real estate activities qualify under the first and third statutory categories. For example, real estate brokerage is generally the business of negotiating a contract for the purchase, sale, exchange, lease, or rental of real estate—which we believe is a financial asset—for others.

The Fed and Treasury, in their request for public comment, note that many of the essential aspects of real estate brokerage are already permissible under national bank "finder" authority. The regulators already authorize financial holding companies, as well as national banks and their subsidiaries, to act as finders in bringing together buyers and sellers for financial or nonfinancial transactions. Permissible finder activities include "identifying potential parties, making inquiries as to interest, introducing or arranging meetings of interested parties, and otherwise bringing parties together for a transaction . . ."[4] This description of finders authority is the essence of every real estate transaction.

Apart from their authority with respect to these three specified activities, the Fed and Treasury have broad discretion to determine that other types of activities are "financial in nature or incidental to such activity." In making such a determination, the regulators are directed to consider a number of factors. Among the specific factors to be considered are:

- Changes or reasonably expected changes in the marketplace in which financial holding companies compete or the technology for delivering financial services; and
- Whether the proposed activity is necessary or appropriate to allow a financial holding company to—
  - Compete effectively with any company seeking to provide financial services;
  - Efficiently deliver information and services that are financial in nature through the use of technology, including applications involving systems for data transmission or financial transactions; and
  - Offer customers any available or emerging technological means for using financial services or for the document imaging of data.

The GLB Act standard is a significant expansion of the Fed and Treasury's capacity to consider the competitive realities of our Nation's financial marketplace when determining permissible activities for financial holding companies and financial subsidiaries. It is our contention that the marketplace, and the technology associated with it, in the case of real estate brokerage and property management, have already changed and will continue to change dramatically in ways that significantly impact the ability of banks to effectively compete with other companies that provide financial services.

Finally, in addition to the newly authorized financial activities described above, the Act authorizes financial holding companies to engage in certain nonfinancial activities. Specifically, a financial holding company may engage in a nonfinancial activity, or acquire a company engaged in a nonfinancial activity, if the Fed and Treasury determine by regulation or order that the activity: (1) is complementary to a financial activity; and (2) does not pose a substantial risk to the safety or soundness of depository institutions or the financial system generally.

The NAR would have this Subcommittee believe that Congress meant to preclude real estate activities in the GLB Act and that the legislation accomplished that goal. This is simply untrue, and we have seen no specific evidence to back up this unfounded charge. There is absolutely nothing in the legislative history to support this allegation. To the contrary, the plain language of the statute and the legislative history show the Treasury and Federal Reserve are following exactly the process and using the factors Congress intended.

The GLB Act itself demonstrates Congress's knowledge of this issue in its determination that financial subsidiaries of national banks should be prohibited only from engaging in real estate development activities—the riskier aspect of the business in which the banking organization takes an ownership position. Had Congress intended to prevent banking organizations from engaging in the agency activities of real estate brokerage and real estate management, it clearly knew how to do so. The fact that Congress chose only to prohibit real estate development leads to the conclusion that Congress did not intend to restrict agency activities.

Despite comments to the contrary, anyone who paid attention to the debate over the many years that led up to GLB Act would not have been surprised to see the current proposal. The ABA negotiated with NAR over 10 years ago the rules under which banks would enter the real estate brokerage business. This negotiation took place with respect to criteria in a previous version of the GLB Act which was, in fact, much more restrictive than the criteria enacted in 1999. Thus, over 10 years

[4] 12 CFR 7.1002.

ago, the NAR recognized that even a more restrictive version of financial modernization could be interpreted as permitting banking companies to offer real estate brokerage. Furthermore, in 1995, NAR testified on another forerunner of the GLB Act before the House Banking Committee. In that testimony, NAR stated unequivocally that the language must be clarified to exclude brokerage and management. It was neither clarified then, nor was it in the GLB Act. That 1995 bill, the Financial Services Competitiveness Act of 1995, contained similar, but less broad, language to that ultimately enacted in the GLB Act.

Certainly the NAR had every opportunity to raise the issue with Congress in 1999 and either chose not to or did so without success. Rather, NAR's simplistic argument is that the proposal involves "commerce" and is, therefore, beyond the scope of the GLB Act. However, the issue is not at all that simple. The language of the relevant provisions of the GLB Act does not prohibit commercial activities; rather they set out specific criteria to determine permissible activities. The authors clearly recognized that there was no exact or permanent line to define services that should be permissible. That is why they left the determination of whether or not a given activity is "financial in nature" or "incidental to a financial activity" to the Fed and the Treasury, and why they developed the specific criteria that are in the statute. To reiterate, if the Congress had wanted to make such a determination to exclude the proposed activities, it would have explicitly done so—as it did with real estate development.

It is worth noting, since NAR has raised the specter of banking and commerce, that the Fed has, for many years, been the primary opponent of breaching the wall between banking and commerce. Based on this record, one would certainly expect the Fed to look very closely at any question relating to commercial activities.

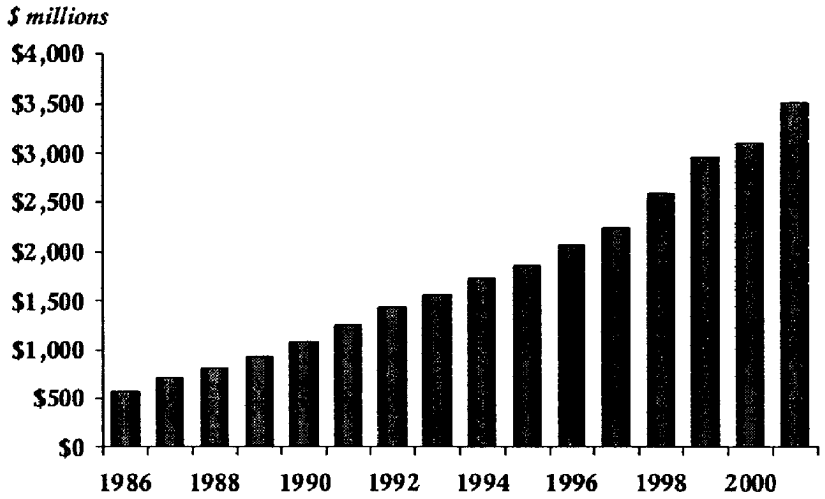
The Changing Real Estate and Financial Marketplaces Require a Flexible Regulatory Approach

As noted above, the GLB Act requires that the regulators consider competitive factors and technological innovations when determining whether activities are financial in nature. A particularly applicable statutory phrase to focus on in this context is whether the activity is "appropriate" to allow institutions to "compete effectively with any company seeking to provide financial services in the United States." Other types of insured depository institutions have the authority to provide—and are providing—real estate brokerage and management services. We have already demonstrated that real estate brokerage firms are providing financial services throughout the United States. Clearly, the fact that real estate brokerage firms are offering mortgages and other financial services must be part of the regulatory consideration. Competitive imbalances like this are the very thing that Congress sought to correct when it enacted the GLB Act, and we believe that the use of the flexibility granted to the regulators under Section 103(a) is clearly justified in the case of real estate brokerage and management authority for banking organizations.

Technological innovations have also had a dramatic impact on real estate markets. One major change is the development of the secondary market for mortgage loans and the efficient process that bundles individual home loans into highly liquid, globally traded securities (see Chart 3).

Chart 3

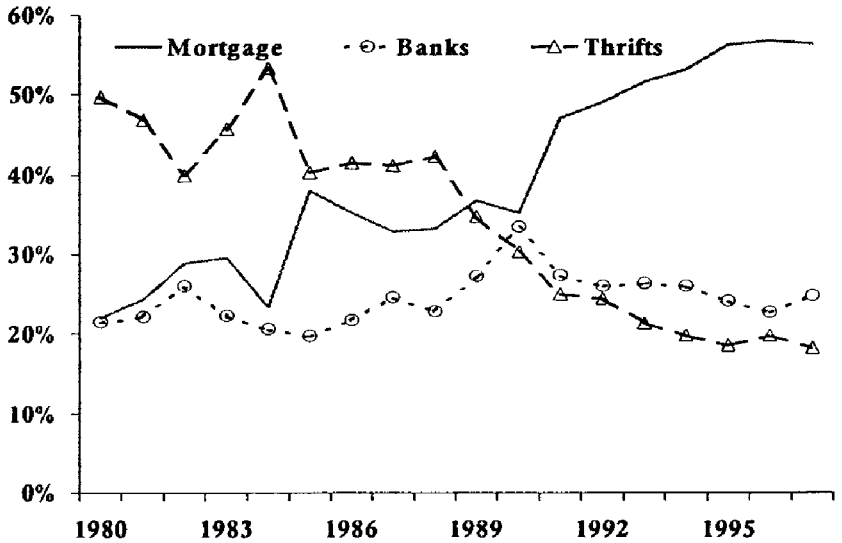
Mortgage Backed Securities Outstanding



Source: Federal Reserve

The increasing importance of the secondary market has facilitated the rapid growth of 50 percent mortgage lending outside traditional banking and savings institutions (see Chart 4).

Chart 4
Mortgage Originations



Source: MBA

In fact, securitization has significantly changed the very nature of mortgage funding, enabling real estate firms to establish their own mortgage companies and to offer end-to-end real estate transactions—helping a buyer find a home, finance it, and insure it. The result is that traditional deposit-based lenders—banks and thrifts—are often bypassed completely. These are exactly the kinds of technological changes the GLB Act authorized the Treasury and the Fed to address.

The dominance of the secondary market is clear evidence that this form of funding for plain vanilla mortgage loans is generally superior in terms of costs to funding with bank deposits. If banks somehow enjoyed some special benefit from deposits, or deposit insurance (which banks pay for through premiums and extensive regulatory costs), banks would not be selling into the secondary market, and the secondary market would not control an ever-increasing share of the marketplace. No amount of deposit insurance can counteract this fundamental principle of efficient markets. More importantly, access to this secondary market source of funding is available equally to mortgage and banking organizations, and is clearly why real estate companies increasingly are affiliating with mortgage banking companies.

To summarize this section, the GLB Act recognized that achieving the goal of promoting competition necessarily required regulatory flexibility. Section 103(a) provides that flexibility by authorizing the Fed and the Treasury, subject to certain statutory guidelines, to approve additional activities for banking organizations. The ABA believes strongly that real estate brokerage and management meet the criteria. Of course, the Fed and Treasury have not made any determination on this proposal. Regardless of their ultimate decision, the Fed and Treasury should be allowed to follow the process Congress created only two and a half years ago.

All Consumer Protections Are Maintained and Bank Safety and Soundness Is Protected

If banking organizations offer real estate services, consumers would actually have more protections under the law than they do today. All rules applicable to real estate brokers, including all State licensing, qualification, and sales practices will apply equally to bank-affiliated real estate agents. NAR has raised the specter of customers being taken advantage of as a result of conflicts of interest that may potentially arise when a real estate broker is affiliated with a lender. The simple fact is that the exact same potential for such abuse occurs, for example, each time an

agent from Century 21, Coldwell Banker, ERA (all of whom are affiliated with Cendant) GMAC, Long & Foster, or USAA helps a customer buy or sell a house. And yet, although these integrated real estate organizations, as well as State banks in many States, savings institutions, and credit unions, have been selling real estate and funding mortgages for years, there has been no outcry about these conflicts of interest. Why?—Because the Real Estate Settlement Procedures Act (RESPA)[5] requires REALTORS® affiliated with lenders to disclose that fact to customers before the purchase occurs.

The RESPA disclosure,[6] which must be on a separate piece of paper, must state the relationship between the real estate agent and the lender and provide the estimated charges or range of charges of the lender. It must also notify the customer that he or she is not required to use the lender and is free to shop around for a better deal. If the real estate agent requires the use of its affiliated lender, that agent violates the kickback and unearned fee provisions of Section 8 of RESPA. The customer is expected to sign an acknowledgement of the disclosure.

In addition, consumers have even more protections when their real estate agent is affiliated with a banking organization. This is because banks and bank holding companies and their subsidiaries and affiliates are subject to the antitying provisions of the Bank Holding Company Act.[7] These restrictions prohibit banks and their affiliates from conditioning the provision of credit on the purchase of another product or service.

Another false impression put forward by NAR is that somehow bank involvement is contrary to the spirit of the Community Reinvestment Act. Nothing could be further from the truth. Approval of the proposal would help low income and minority communities. Because banks are subject to CRA, they have every incentive to use the real estate authorities to enhance their outreach to communities. The bank would bring real estate services to areas now shortchanged and could use the combination of real estate and financial services to better serve their low-income and minority communities. Moreover, if the real estate unit were a subsidiary of a national bank, that subsidiary would be covered by CRA.

Bank involvement in real estate brokerage and management services is also consistent with safe and sound banking. First, providing these services will help to diversify the income stream of these institutions and help to improve their financial base. Real estate brokerage and management services are activities where a bank acts only as an agent for a third party, but does not take an ownership position in the property. By their very nature, agency activities pose very little risk to the safety and soundness of depository institutions.

Second, under the GLB Act, the bank regulators must deem a bank to be well-capitalized and well-managed before a banking organization can participate in any of the expanded financial activities permitted under the GLB Act, including real estate brokerage and property management. Thus, only financially strong institutions would be authorized to engage in these activities.

Third, banking organizations are also subject to Sections 23A and 23B of the Federal Reserve Act, which limit the amount of credit and other forms of support that a bank could provide to a real estate brokerage affiliate or subsidiary. Such limits ensure that the safety and soundness of the bank will not be negatively impacted by its subsidiaries or affiliates.

Fourth, many banking organizations already have years of experience in providing real estate activities. In fact, the purchase, sale and management of real estate are frequently significant aspects of fiduciary asset management in many bank trust departments. Because banks currently have trust personnel who provide real estate brokerage and management services on a daily basis to trust customers, providing the service outside of the trust department would not be a new activity in which banking organizations lack expertise. Thus, no new safety and soundness issues would be raised.

Finally, it is important to note that a precedent already exists for bank involvement in real estate activities. In over half of the States, State banking regulators have the authority (either explicitly, through regulatory interpretations, and through wildcard and parity statutes) to allow State-chartered banking organizations to engage in real estate activities (see the attached State-by-State listing developed by the Conference of State Bank Supervisors). Moreover, savings institutions and credit unions already have brokerage authority. Allowing banks the same rights and privileges should enhance the competition for real estate services.

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[5] 12 U.S.C. § 2601 et seq.

[6] The requirement for affiliated business disclosures is part of the regulations of the Department of Housing and Urban Development that implement RESPA. 24 CFR § 3500.15.

[7] Section 106(b) of the Bank Holding Company Act Amendments of 1970.

Conclusion

In July, it will be 2 years since the filing of the original petition requesting a determination that real estate brokerage and management be deemed financial in nature. It is now certain that this determination will not be made until 2003, as was indicated in an April 22, 2002 letter from Treasury Secretary Paul H. O'Neill to Congressman Michael G. Oxley, indicating that, in consultation with the Fed, the Treasury will not make a final decision on this proposed rule until next year.

A fundamental purpose of GLB Act was to enable banking institutions to compete with other financial services providers, and there is ample evidence demonstrating that the real estate competition is touting the advantages of one-stop homebuying services. While we as an industry have always looked at real estate brokerage and management as providing us with more options to compete in the long term, with each passing day, real estate firms become more deeply involved in financial services such as mortgage and insurance, and banks like mine cannot effectively compete for this business. With each passing day, the case for allowing banks to offer real estate services only gets stronger.

As an industry we have grave concerns about the broader effects of this controversy and whether it sets a precedent that could hinder future approvals of new powers under GLB. The Act was designed to keep our financial system up-to-date by delegating those decisions to the Fed and Treasury. This goal is being frustrated by efforts to take the case for determining what is appropriate back to Congress, placing Congress in the very role that it delegated to the agencies with the greatest level of expertise to make these decisions based on specific statutory criteria.

S. 1839 not only frustrates the GLB Act process, it reduces consumer choice. Consumers would have fewer choices of whom to do business with; agents would have fewer choices of whom to work for; and businesses would have fewer choices for joint marketing, fewer potential merger partners, and fewer potential buyers. We believe a competitive market is the best way to provide quality real estate brokerage and management services. Increased competition clearly benefits consumers and the economy. It is a catalyst for innovation, more customer choice, better service, and competitive prices. I have no doubt that my customers and my community would benefit if my small bank could offer these services.

Not only would consumers benefit from bank involvement in real estate services, but also bank involvement is consistent with safe and sound banking. All consumer protections that apply to independent REALTORS® would apply to bank-affiliated real estate agents—plus bank-affiliated agents would be subject to additional antitying regulations. And because brokerage and management are agency activities, they pose no financial risk to the safety and soundness of the banking organization.

Just 2½ years ago Congress made the decision to leave this type of determination to the regulators—so that they could keep the financial structure up-to-date and keep Congress out of the middle of competitive disputes. NAR now wants to put Congress back in the uncomfortable position of referee. Congress explicitly gave the Fed and Treasury the flexibility and authority to make these determinations based on their expert knowledge of the changes in the financial services marketplace. Those agencies should be allowed to carry out the authority that Congress wisely provided to them.

I thank you, Mr. Chairman, for this opportunity to present the views of the American Bankers Association.

Real Estate Brokerage

State	Available	Subsidiary Required	Authorization	Citation
Alabama	Yes	No	Statute	5-5A-18
Alaska	No	No	Statute	AS 06.05.272(d)
Arizona	Yes	Yes	Statute	ARS 6-184(A)(7)
Arkansas	No	No	Not Authorized	NA
California	Yes	No	Statute	Cal. Corps. C. Sec. 206 and Cal. Fin. C. Sec. 751.3
Colorado	No	No	Not Authorized	N/A
Connecticut	Yes[1]	Yes[1]	See Footnote[1]	See Footnote[1]
Delaware	Yes	Yes	Statute	Title Five, Delaware Code § 761(a)(3)
DC	Yes[2]	NR	NR	NR
Florida	Yes	Yes	Statute	658.67(6), F.S.
Georgia	Yes	No	Statute & Regulation	7-1-261, operational powers of banks; Regulation 80-5-5
Guam				
Hawaii	No[3]	No	Wildcard	NR
Idaho	Yes	No	Wildcard	NR
Illinois	No	No	Not Authorized	N/A – Express prohibition exists within IL wildcard statute that grants parity with federal thrifts, among other entities
Indiana	Yes	No	Statute	I.C. 28-1-3.1
Iowa	Yes	No	Statute	Section 524.802
Kansas	No	No	Not Authorized	N/A
Kentucky	No	No	Not Authorized	N/A
Louisiana	No	No	Not Authorized	N/A
Maine	Yes[4]	No	Regulation	Maine 9B Section 131(6-A); 9B Section 446-A; Regulation #7
Maryland	No	No	Not Authorized	N/A
Massachusetts	Yes	Yes	Statute	G.L.c.167F §2 p. 25
Michigan	Yes	No	Statute	MCL 487.14104(1)
Minnesota	No	No	Statute Is Silent	N/A
Mississippi	No	No	Not Authorized	N/A
Missouri	No[5]	No	Not Authorized	N/A
Montana	No	No	Not Authorized	N/A
Nebraska	Yes	No	Incidental Powers Regulation	Department Statement of Policy #9
Nevada	No	No	Not Authorized	N/A
New Hampshire	Yes[6]	No	Regulation & Wildcard	Ban 525, Federal Savings Associations Powers
New Jersey	Yes	No	Regulation	NJAC 3:11-11.5(a)(4)

Real Estate Brokerage

State	Available	Subsidiary Required	Authorization	Citation
New Mexico	Yes	No	Wildcard	58-1-54
New York	No	No	Not Authorized	N/A
North Carolina	Yes	Yes	Statute	NCGS 53-47c(3)
North Dakota	No	No	Not Authorized	N/A
Ohio	No	No	Not Authorized	N/A
Oklahoma	No	No	Not Authorized	N/A
Oregon	No	No	Not Authorized	N/A
Pennsylvania	Yes	No	Parity Statute	7P.S. §201
Puerto Rico	No	No	Not Authorized	N/A
Rhode Island	No	No	Not Authorized	N/A
South Dakota	Yes	No	Interpretation	51-A-2-14(3)
Tennessee	Yes	No	Statute, Regulation & Wildcard	T.C.A. § 45-2-607(d); Regulation Chpt. 0180-19; 45-14-105
Texas	Yes	No- Preferred	Statute	Texas Real Estate License Act
Utah	No	No	Not Authorized	N/A
Vermont	No	No	Not Authorized	N/A
Virginia	No	No	Not Authorized	N/A
Washington	Yes[7]	No	Wildcard Authority	RCW 30.04.127
West Virginia	No	No	Not Authorized	N/A
Wisconsin	Yes	No	Statute & Regulation	221.0322 & DFI -Bkg#16
Wyoming	Yes	No	Statute	W.S.13-2-101(a)(xiii) & W.S.13-2-101(a)(xii)
SUMMARY	Yes 26 / No 25	Yes 6 / No 45		

NR: Not Reported.
N/A: Not Applicable.

[1] The activity is permissible through a subsidiary. It may also be conducted directly under the authority provided by the "closely related activities" statute [Sect 36a-250(a)(40) of CT General Statutes] or "wild card" statute [Sect. 36a-250(a)(41) of the CT General Statutes]. To date, The Department has not formally acted on any request to conduct the activity.

[2] The DC Office of Banking & Financial Institutions is presently modernizing its bank, mortgage banking, trusts, savings and loan, and credit union statutes, regulations and chartering requirements.

[3] Real estate brokerage is expressly prohibited by state law, unless otherwise allowed through wildcard authority because the activity is permissible for national banks.

[4] The Department would review on a case-by-case basis and refer to Sections 416 and 419-A of the Maine Banking Statute, together with Regulation 7.

[5] Depository Trust Companies have real estate brokerage powers under 362.105

[6] Effective March 16, 2001, Ban 525 allows commercial banks, trust institutions and savings banks to engage in activities and make any investment in the same manner and to the same extent that the activity is permissible for federal savings associations.

[7] See also the followings Pursuant to RCW 30.04.215(3), 32.08.140(16) and 32.08.146, banks can perform the same activities federal banks can, provided that the activities are approved by the Director of the Department of Financial Institutions.

January 16, 2002

To the Members of the United States House of Representatives:

The Financial Services Coordinating Council (FSCC) is an alliance of the principal trade organizations in each of the financial service sectors formed to address issues that cut across financial industry lines. Its members, the American Bankers Association, the American Council of Life Insurers, the American Insurance Association, and the Securities Industry Association, wish to express their opposition to H.R. 3424.

The fundamental purpose of the Gramm-Leach-Bliley Act (GLBA) was to develop a flexible structure for our financial system that could adjust to changes in technology and other aspects of the marketplace. Congress believed, and we agree, that such a flexible structure would increase the soundness of our financial system, promote economic growth, decrease costs, and provide consumers and businesses with more choices. Congress recognized that the legislative process is too slow to keep pace with changes in technology and the global marketplace, as demonstrated by the long history of Congressional gridlock prior to GLBA.

Congress expressly gave the Federal Reserve Board and Treasury the authority to authorize financial holding companies to engage in new activities in addition to the products and services enumerated in the statute. In delegating this authority, Congress sought to empower experienced and independent financial regulators to make such determinations, based upon elaborate statutory criteria, that match marketplace realities. This is what financial modernization legislation is about: the ability to evolve. H.R. 3424 seeks to return to the pre-GLBA environment where industry competitors ask Congress to choose winners and losers.

The financial services industry, the regulatory agencies, and Treasury are in the very beginnings of interpreting GLBA. Reopening one of its most central provisions would raise a great deal of uncertainty within the industry. We therefore strongly oppose H.R. 3424.

Sincerely,

American Bankers Association
American Council of Life Insurers
American Insurance Association
Securities Industry Association

PREPARED STATEMENT OF JOHN TAYLOR

PRESIDENT AND CHIEF EXECUTIVE OFFICER
NATIONAL COMMUNITY REINVESTMENT COALITION, WASHINGTON, DC

MAY 23, 2002

Good morning Chairman Johnson, Senator Bennett, and distinguished Members of the Subcommittee on Financial Institutions. My name is John Taylor, and I am President and CEO of the National Community Reinvestment Coalition (NCRC). NCRC is a national trade association representing more than 700 community-based organizations and local public agencies who work daily to promote economic justice in America and to increase fair and equal access to credit, capital, and banking services to traditionally underserved populations in both urban and rural areas. NCRC has represented our Nation's communities on the Federal Reserve Board's Consumer Advisory Council (CAC), Community Development Financial Institutions (CDFI) Advisory Board, Freddie Mac's Housing Advisory Council, Fannie Mae's Housing Impact Council and before the United States Congress.

On behalf NCRC, I thank you for the opportunity to testify before you here today on an important issue that will impact our Nation's progress in extending the American Dream of homeownership to minority and low- and moderate-income families: banks becoming real estate brokers. NCRC's community organizations are at the helm driving the reinvestment movement. Today, as a result of fair lending laws like the Community Reinvestment Act (CRA), which turns 25 this year, poor neighborhoods have been empowered by bank partnerships with community organizations to address credit needs and missed market opportunities. As a result, the number of loans to minority and working class borrowers over the last decade has increased faster than the number of loans to more affluent borrowers.[1] Bank CRA commitments have grown from a few million dollars a year to over $50 billion annually.[2] Without these loans and commitments, the economic flow of private credit and capital into our communities would be extinct and hence, certain death for disinvested neighborhoods.

NCRC is very concerned about the ramifications of financial holding companies and national banks entering the real estate brokerage business. As you can imagine from the industries represented here today, you will hear varying perspectives on banks and real estate for consideration. I would like to emphasize that my testimony today will focus on three areas that will be affected if the banking and real estate industry are allowed to merge: competition, consumer protections, and serving our communities.

Competition

NCRC has always maintained the position that competition is beneficial for the revitalization of communities. Healthy competition provides low-income and working families with more housing and lending options, and offers them alternatives to high-cost and abusive loans. However, in our rapidly shifting financial marketplace in which our largest banks now own subprime lenders and insurance agencies, we wonder whether product choice is increasing for our communities or whether financial conglomerates are steering consumers into costly and unnecessary products, often layering one product on top of another to maximize their profits.

Over a decade ago, banks had a corner on the mortgage lending business with an overwhelming 80 percent market share.[3] Today, however, is a different story. In 2001, the mortgage broker industry estimated that their market share has dramatically grown to 65 percent of all residential mortgage originations.[4] Does this mean that banks are hurting for mortgage business? Absolutely not. Instead of relying on loan officers, banks now depend upon mortgage brokers to make loans in minority and low- and moderate-income communities. And too often, banks do not engage in sufficient due diligence or do not require brokers to follow fair lending safeguards.

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[1] The Joint Center for Housing Studies, Harvard Univeristy, *The 25th Anniversary of the Community Reinvestment Act: Access to Capital in an Evolving Financial Services System,* (March 2002).

[2] National Community Reinvestment Coalition, *CRA Commitments* (2002). Note: The Joint Center for Housing Studies, Harvard Univeristy used NCRC's database to find that low- and moderate-income communities received a higher portion of loans in geographical area in which lenders and community groups negotiated CRA agreements than in areas in which they did not.

[3] David Olson, Testimony before the Senate Committee on Banking, Housing, and Urban Affairs' Hearing, *Predatory Mortgage Lending Practices: Abusive Uses of Yield Spread Premiums* (January 8, 2002).

[4] Ibid.

The situation would deteriorate if banks now owned a fleet of brokerage companies that combined lending and real estate services.

The arena of competition has dramatically shifted in the wake of Gramm-Leach-Bliley (GLB), which blurred the distinction among financial industries. In March 2000, the Federal Reserve Board issued a list of the first 117 bank holding companies that elected to become financial holding companies to take advantage of the opportunities of entering into the insurance and securities markets. As of April 2002, over 600 bank holding companies have elected to become financial holding companies in order to diversify their businesses.[5] Conversely, less than a dozen nonbank firms have converted to financial holding companies for the purpose of seeking a banking charter.[6] Banks are also taking advantage of an ownership stake (less than a controlling interest) in a financial subsidiary, meaning they form partnerships with firms offering a plethora of financial services including: investment planning, estate planning, asset protection, retirement planning, income tax planning and preparation, and education planning.

To reiterate, NCRC supports competition in its truest sense—when parties act independently and offer the most favorable terms to secure business. But one must wonder if today's financial market upholds the true meaning of competition when it seems like GLB has allowed all roads to lead back to the bank. While nonbank lenders own real estate companies, they have not utilized GLB to amass the market power that banks now enjoy after their mad rush to become financial holding companies. Would adding real estate to the menu of businesses that banks can own level the playing field between banks and nonbanks or only serve to make banks more powerful to the detriment of real competition in the financial industry?

NCRC maintains that the addition of real estate to the already dizzying array of products now offered by "financial supermarkets" will lead to even greater consolidation of bank market power and result in fewer choices for consumers. Our worst nightmare in a consolidated financial market that includes real estate brokerage is:

- A bank offers favorable loan terms to its real estate affiliate, giving it significant advantage over a competing real estate business that does not have an affiliate.
- The bank with the real estate affiliate stops offering loans to customers of nonaffiliated real estate competitors.
- The number of product choices offered to customers of nonaffiliated real estate businesses decreases, resulting in higher cost loans.

During consideration of GLB, NCRC and other observers worried that the consolidation afforded under GLB would lead to only higher prices. That is why GLB commissioned the Department of Treasury to study the effects of mergers among banks, insurance companies, and securities firms on access to loan and bank products for low- and moderate-income communities. Treasury's study in January 2001 concluded that it was too early to assess the impact on cross-industry mergers.[7] NCRC urges Congress and the Federal financial supervisory agencies to delay allowing banks to enter yet another industry, specifically the real estate industry, until the Treasury rigorously measures the impacts of GLB on affordability and accessibility of financial services.

When considering banks in real estate, policymakers have not adequately addressed the negative impacts on small real estate businesses of further industry consolidation. Women- and minority-owned small businesses have played a significant role in community revitalization. Many of these real estate entrepreneurs have established themselves in working class communities and dedicated their business to helping rebuild formerly redlined neighborhoods through partnerships with affordable homeownership programs.

According to the most recent Economic Census, over 375,000 small women- and minority-owned real estate businesses operate in this country, generating over $41 million in sales annually. The wealth generated by these new-markets businesses plays a vital role in building a solid foundation from which veritable community reinvestment will flourish. Local real estate brokers are more likely than financial conglomerates to bring wealth back into their community and enter into business relationships with other neighborhood enterprises. The financial independence of small businesses in local communities increases an individual's stake in the economic empowerment of a community and improves the collective well being of our society.

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[5] Financial Markets Center, *Firms Electing to Become Financial Holding Companies Under the Gramm-Leach-Bliley Act* (April 26, 2002).

[6] Rick Lazio, President and CEO of Financial Services Forum, Remarks at American Enterprise Institues's Roundtable on the Gramm-Leach-Bliley Act (November 13, 2001).

[7] Robert E. Litan, Nicholas P. Retsinas, *et al.* for the Department of the Treasury, *The Community Reinvestment Act After Financial Modernization: A Final Report* (January 2001).

NCRC strongly takes that position that by allowing banks into the real estate business, small real estate businesses will be forced out of the marketplace by the monopolized "financial supermarkets." Gone will be the days in which an entrepreneur dreams of opening a specialized financial business to serve his or her neighborhood customers. Instead, small real estate businesses, insurance businesses, and small investment companies will be forced to make a decision: forfeit their ownership and affiliate with a bank or face going under when a larger "financial supermarket" opens next door. Not only will our Nation's communities hurt, our entire economy will suffer.

Consumer Protection

Existing Problems in the Lending, Insurance, and Real Estate Markets

The next area I would like to address in regards to today's subject matter is consumer protection. Repeatedly, I have been told by industry representatives advocating for banks in real estate that cross-ownership within these markets will benefit the consumer by offering greater choice, greater convenience, and lower costs. NCRC, as a leader in fighting predatory lending, takes the issue of "benefiting the consumer" very seriously. Last summer, NCRC testified before the Full Committee during the 2-day hearings on predatory mortgage lending practices about the plague of abusive lending and equity stripping from communities of color. Lenders are not alone at the receiving end of NCRC criticism. Our membership organizations who are entrenched in the frontlines of protecting homeowners, also battle insurance redlining and unscrupulous real estate "property flippers." In testifying before you today, I must be honest to NCRC's mission of economic justice and state emphatically that injustice exists in the banking, insurance, and real estate industries. Until the problems are solved to protect borrowers and consumers, these markets should not be commingled.

According to the Department of Housing and Urban Development's (HUD) just released report *Black and White Disparities in Subprime Mortgage Refinance Lending,* subprime refinance mortgages accounted for 36.3 percent of total refinance mortgages in low-income neighborhoods compared to 23.8 of total refinance lending nationwide in 2000.[8] Borrowers in prominently African-American low-income neighborhoods were 1.5 times more likely in 2000 to refinance with a subprime lender than borrowers in all low-income neighborhoods. Borrowers in upper-income African-American neighborhoods were 2.9 times more likely to refinance with a subprime lender than borrowers in upper income neighborhoods overall.

NCRC research has found similar disparities. For example, major subprime and manufactured home lenders made 47 percent of the refinance loans in predominantly African-American and Hispanic neighborhoods in the District of Columbia in 2000, a significant increase from 39 percent of the loans in 1999 and 25 percent of the loans in 1994. In contrast, subprime and manufactured home lenders made less than 4 percent of the loans in predominantly white neighborhoods in the 3 years of the study.

Substantial evidence suggests that subprime borrowers in minority communities experience price discrimination. Over the last several years, Home Mortgage Disclosure Act (HMDA) data has indicated that African-American applicants are denied twice as often as whites. NCRC believes that it does not necessarily follow that African-American are twice as likely to have bad credit. And given that African-Americans are denied twice as often for conventional loans as whites, it does not follow that minority communities should be five times as likely to receive subprime loans as documented in an earlier HUD study.[9] In some geographical areas, the disparity is much greater than five to one.

The major secondary market institutions have found pricing inefficiencies in subprime loans. Freddie Mac states that up to 30 percent of subprime borrowers were creditworthy for prime loans. Fannie Mae's CEO, Franklin Raines, is quoted as saying that half of all subprime borrowers could have received prime loans.[10]

A study by the Research Institute for Housing America (RIHA) concludes that minority borrowers are more likely to receive subprime loans after controlling for

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[8] Randall M. Scheessel for the Department of Housing and Urban Development, *Black and White Disparities in Subprime Mortgage Refinance Lending* (April 2002).

[9] Ibid. *See also National Anti-Predatory Lending Policy is Good for America,* NCRC Anti-Predatory Lending Toolkit (March 2002).

[10] Kathleen Day, "Fannie Mae Vows More Minority Lending." *Washington Post,* March 16, 2000, E1. Freddie Mac, *Automated Underwriting: Making Mortgage Lending Simpler for America's Families,* Chapter 5 (Spetmeber 1996).

credit risk factors.[11] RIHA cautions against a conclusion that price discrimination alone explains this since minority borrowers may have different techniques of searching for lenders. However, considering the totality of the research by NCRC, HUD, Fannie Mae, Freddie Mac, RIHA, and others, it seems fair to say that the burden of proof lies with those who assert that discrimination does not occur in the subprime market.

The issue of insurance redlining is also a problem, but unlike home mortgage lending, insurance data is limited to only a handful of States. Since 1995, California has required insurance companies to file data indicating the race and gender of policyholders, the number of policies sold and cancelled, and location of offices and agents, all sorted by ZIP code. Working with the California Department of Insurance, consumer advocate Birny Birnbaum of the Center for Economic Justice (CEJ) obtained data that show disparities between the rate at which insurance companies write policies in low-income communities and the rate at which policies are written in middle- to upper-income communities. For example, in 1995, CEJ reported that approximately 16 percent of California's population lived in underserved communities; however, the data reported by State Farm revealed the company had only 2.59 percent of its agents in those communities.[12] CEJ further concluded that the average insurer wrote only 5.57 percent of its private passenger automobile liability policies and only 6.62 percent of its homeowners policies in low-income, minority ZIP codes.

State Farm, one of the Nation's largest insurance companies, is also a Federally chartered thrift. As such, it offers a full range of banking services, including taking deposits and making various types of home mortgage, auto and home equity loans, in addition to full range investment products. Interestingly enough, 1 month ago, State Farm, California's largest insurer of homes, indicated it has stopped writing new homeowner policies in the State due to a surge in the amount of claims over the last two years.[13] If lawmakers add real estate services to the roster of State Farm products, would this only increase the clout of State Farm and other giants? Would conglomerates turn product flow "on" or "off" in order to obtain concessions from regulatory agencies in States dependent upon their services?

As I mentioned, the real estate market is not without its unscrupulous actors either. Property flipping involves buying a home at a low price and then reselling it at fraudulently inflated price within a short time frame, often after making only cosmetic improvements to the property. NCRC has seen the following practices employed in property flipping schemes:

- Real estate investors continually buying neglected properties at sheriff sales and reselling homes at escalated prices to unsophisticated first-time homebuyers;
- Using real estate agents, licensed and nonlicensed individuals, as a front;
- Targeting immigrant communities, particularly nonEnglish speaking individuals;
- Colluding with property appraisers to inflate property value;
- Colluding with home inspectors to secure clean reports; and
- Tricking homeowners into thinking they are dealing with legitimate real estate companies.

In 2000, the Department of Housing and Urban Development Inspector General (IG) testified about the rampant flipping rings the Agency was combating.[14] One investigation alone uncovered over 1,200 flipped loans totaling approximately $160 million. Twenty-five percent of the loans were in default. The IG indicated that approximately 100 representatives of lending and real estate industries colluded on this scheme. Another IG flipping investigation involved a HUD employee who conspired with a real estate agent to carry out a systematic scheme of selling HUD-owned properties at prices far below HUD's listed price. The FHA Insurance Fund lost several million dollars as a result of this scam. If Congress allows banks and real estate firms to combine without strengthening the consumer protection laws,

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[11] Anthony Pennington-Cross, Anthony Yezer, and Joseph Nichols for the Research Institue for Housing America, *Credit Risk and Mortgage Lending: Who Uses Subprime and Why?* (October 2000).

[12] Consumer Union Press Release, *State Farm Loses on Attempt to Block Disclosure of Insurance Redlining Data* (March 8, 2000).

[13] E. Scott Reckard, "State Farm Won't Write New Homeowners Policies." *LA Times,* April 23, 2002.

[14] Susan Gaffney, Inspector General, Department of Housing and Urban Development, Testimony before the Senate Permanent Subcommittee on Investigations, Committee on Governmental Affairs' Hearing, *HUD's Government Insured Mortgages: The Problem of Proerty "Flipping"* (June 30, 2000).

our communities are more likely to be victims of scams than beneficiaries of greater product choice and lower prices.

Consumer Choice

As I previously mentioned NCRC was vocal during the consideration of Gramm-Leach-Bliley about the potential of banks product packing without regard of true customer needs.[15] Banks are not shy about advertising their cross-marketing strategy: targeting an existing customer is easier and more profitable than acquiring a new one.

The Bank Holding Company Act, as amended, prohibits a bank from extending or varying the consideration for credit on the condition that the customer obtain any other nonbanking product from the bank holding company or any other subsidiary of the bank holding company. This prevents a bank from offering a reduced interest rate on a loan that may be used only to purchase products made or sold by an affiliate of the bank. However, the statute provides exceptions and exemptions that "financial supermarkets" can take advantage of when cross-selling their products.

Another problem for unsophisticated banking consumers is the perception that approval of their loan is contingent on their purchasing insurance or other products from bank affiliates. NCRC believes that banks should not force consumers to buy unwanted or unnecessary products, nor should they offer incentives to induce borrowers to purchase more products than they can afford.

Last year Citibank sought and received a favorable exemption from antitying prohibitions to offer incentives to their credit card, mortgage, or loan customers who maintain a combined minimum balance in a package of products and services that include annuities, auto, homeowners, life, and/or long-term care insurance from insurance affiliates of Citibank.[16] The incentives would include lower interest rates and/or other items, such as airline frequent flyer miles or contributions to accounts maintained by a customer with other Citibank affiliates.

Is it really in the best interest of the consumer to be bombarded with credit card applications, insurance product brochures, investment fund prospectuses, and now perhaps real estate marketing materials when they go to a bank simply to open a checking account? Allowing banks into yet another industry would only compound the abuses associated with incentives and inducements to purchasing an array of products.

Where are banks' priorities when there are over 10 million Americans who do not have checking accounts?[17] Today, NCRC issues a challenge to the lenders to open your doors to the unbanked; for every product package you market to existing customer, dedicate the same energy to marketing Individual Development Accounts and lifeline and low-cost accounts to underserved communities.

Finally, on the issue of choice, NCRC is very concerned that if banks are allowed in the real estate business, consumers using a bank affiliated real estate agent will be at a disadvantage when attempting to shop for the best priced loan product, particularly if a bank employs exclusivity with its affiliate.

Serving Our Communities

The final point that I would like to address is the stake our Nation's communities have in the decision to expand banking business lines even further to include real estate. At the start of my testimony, I mentioned the great success story of how CRA has lead to the introduction of bank partnerships and commitments in formerly divested communities. I would briefly like to elaborate how CRA must be updated to cover all of the activities that financial institutions are now permitted to undertake.

As you know, CRA only applies to the depository subsidiaries of financial holding companies. Other parts of the holding companies have no obligation to serve the entire community in which they do business, including low- and moderate-income communities. As CRA increasingly applies to a smaller portion of burgeoning holding companies, the risk that low- and moderate-income communities will once again become neglected—after years of steady progress in expanding homeownership opportunities down the income ladder—increases. Despite the Federal Reserve Board's findings in its study mandated by GLB that CRA-related loans are profitable, financial holding companies will become tempted to overlook low- and moderate-income markets as they enter new lines of business.

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[15] John Taylor, Testimony before the Senate Committee on Banking, Housing, and Urban Affairs' Hearing, *Financial Services Legislation* (February 25, 1999).

[16] Opinion Letter of J. Virgil Mattingly, General Counsel, Federal Reserve (May 16, 2001).

[17] The Federal Reserve Board, *Survey of Consumer Finances* (1998).

It is a travesty to each and every underserved rural community and inner city neighborhood in our country that CRA basically ends with checking products and lending activities. When the Unites States Congress passed GBL, it missed a tremendous opportunity to extend community reinvestment requirements to all bank affiliates, insurance companies and securities firms. Thirty-six Members of the House of Representatives support our position and have cosponsored the Community Reinvestment Modernization Act (H.R. 865). As an addendum to my testimony, I have attached the first few pages of this bill detailing purposes, findings, and sections covered, and ask for your consideration of this important measure.

If the banks are allowed into the real estate market NCRC strongly advocates for CRA coverage to be extended to the real estate affiliates to ensure these companies have agents in low- and moderate-income communities to serve minority and working class families. NCRC also strongly encourages Congress to enact a strong antipredatory law to prohibit abusive lending and property flipping.

In closing, I leave you with a true story of how a REALTOR® helped identify a discriminatory, predatory lending practice and subsequently brought it to the attention of NCRC's Civil Rights Department for Assistance.

The victims were an elderly minority couple who owned their home in the Mount Pleasant neighborhood, here in the District of Columbia, for over 43 years. In order to pay medical expenses, an independent mortgage company convinced the couple to take out an adjustable rate mortgage with a prepayment penalty and a loan payment that exceeded the couple's monthly income. Faced with imminent foreclosure, the couple was forced to consider a "short sale" of their home. The victims retained a REALTOR® to facilitate the sale of the home, who quickly identified that the appraisal conducted by the mortgage company was substantially inflated. Ultimately, a buyer was identified and a purchase contract placed. Unbeknown to all the parties involved the victims had prepayment penalty of $13,791.06 included in the note that stalled the real estate transaction. It was only after victims' REALTOR® requested NCRC to intervene that the sale took place.

If the real estate agent had been affiliated with a predatory lender or any lender for that matter, it is doubtful that the agent would have acted as an independent watchdog. When we allow additional industry consolidation without providing stronger community protection laws, we remove the checks and balances that guard against abuses in power. Fewer independent businesses with stakes in their communities exist to protect against the exploitation and plunder of greedy conglomerates.

I thank you, Mr. Chairman, for this opportunity to testify and present the views of the National Community Reinvestment Coalition. I will be happy to answer any questions you may have.

I

107TH CONGRESS
1ST SESSION

H. R. 865

To enhance the availability of capital and credit for all citizens and communities, to ensure that community reinvestment keeps pace as banks, securities firms, and other financial service providers become affiliates as a result of the enactment of the Gramm-Leach-Bliley Act, and for other purposes.

IN THE HOUSE OF REPRESENTATIVES

MARCH 6, 2001

Mr. BARRETT (for himself, Mr. GUTIERREZ, Mr. FRANK, Mrs. JONES of Ohio, Ms. BALDWIN, Ms. MCKINNEY, Mr. MCGOVERN, Ms. HOOLEY of Oregon, Mr. CAPUANO, Mr. BONIOR, Mr. BLAGOJEVICH, Mr. ACEVEDO-VILÁ, Mr. FILNER, Mr. HINCHEY, Ms. ROYBAL-ALLARD, Mrs. MEEK of Florida, Mr. ENGEL, Mr. MCDERMOTT, Mr. TOWNS, Mr. RUSH, and Ms. NORTON) introduced the following bill; which was referred to the Committee on Financial Services

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A BILL

To enhance the availability of capital and credit for all citizens and communities, to ensure that community reinvestment keeps pace as banks, securities firms, and other financial service providers become affiliates as a result of the enactment of the Gramm-Leach-Bliley Act, and for other purposes.

1 *Be it enacted by the Senate and House of Representa-*
2 *tives of the United States of America in Congress assembled,*

1 **SECTION 1. SHORT TITLE; TABLE OF CONTENTS.**

2 (a) SHORT TITLE.—This Act may be cited as the
3 "Community Reinvestment Modernization Act of 2001".
4 (b) TABLE OF CONTENTS.—The table of contents for
5 this Act is as follows:

Sec. 1. Short title; table of contents.
Sec. 2. Findings.
Sec. 3. Purposes.

TITLE I—MODERNIZATION OF COMMUNITY REINVESTMENT ACT OF 1977 AND COMMUNITY SERVICE OBLIGATIONS

Sec. 101. Extension of community reinvestment obligations within a financial holding company.
Sec. 102. Provisions relating to improved responsiveness of insured depository institutions to Community Reinvestment Act of 1977.
Sec. 103. Reduction of CRA rating due to predatory lending and other negative credit practices.
Sec. 104. Responsiveness to community needs for securities and investment services.
Sec. 105. Responsiveness to community needs for mortgages and mortgage related services by mortgage banks.
Sec. 106. Responsiveness to community needs for insurance services.
Sec. 107. Satisfactory ratings required by securities company, mortgage bank, and insurance company affiliates of financial holding companies.

TITLE II—DATA DISCLOSURE REQUIREMENTS

Subtitle A—Disclosure of Insurance Availability and Insurer Investment Information

Sec. 201. Short title.
Sec. 202. Establishment of general requirements to submit information.
Sec. 203. Reporting of noncommercial insurance information.
Sec. 204. Reporting of rural insurance information.
Sec. 205. Waiver of reporting requirements.
Sec. 206. Reporting by private mortgage insurers.
Sec. 207. Reporting of information regarding investments by insurers.
Sec. 208. Submission of information to Secretary and maintenance of information.
Sec. 209. Availability and access system.
Sec. 210. Designations.
Sec. 211. Enforcement.
Sec. 212. Exemption and relation to State laws.
Sec. 213. Regulations.
Sec. 214. Definitions.
Sec. 215. Effective date.

Subtitle B—Improvements in Other Data Disclosure Requirements

Sec. 221. Improve small business and agriculture lending data disclosure.
Sec. 222. Maintenance and disclosure of information by the Financial Institutions Examination Counsel.

TITLE III—REGULATORY AND STRUCTURAL REFORMS

Sec. 301. Antiredlining requirement for financial holding companies.
Sec. 302. Notice and public comment required before establishing a financial holding company.
Sec. 303. Public meetings for bank acquisitions and mergers.
Sec. 304. CRA examination schedule for small banks.
Sec. 305. CRA sunshine requirements.
Sec. 306. Continuing community reinvestment requirement for financial holding companies.
Sec. 307. Changes in reporting requirements under the Home Mortgage Disclosure Act of 1975.

SEC. 2. FINDINGS.

The Congress hereby finds as follows:

(1) It is necessary to increase homeownership and small business ownership for low- and moderate-income borrowers and persons of color.

(2) The United States has an overall homeownership rate of 66.7 percent, while Hispanic and African-American homeownership rates are 46.2 percent and 46.9 percent respectively.

(3) The homeownership rate in central cities is 50.3 percent, compared to 73.5 percent for the suburbs.

(4) It is necessary to close the wealth gap in the United States and to increase access to insurance products.

(5) In 1998, the median net worth for Hispanic, African-American, Asian, and other minority families was $16,400, which was 17.3 percent of the

1 median net worth of $94,900 for nonhispanic white
2 families.
3 (6) Families earning $10,000 to $25,000 had a
4 median net worth of $24,800 in 1998 but $31,000
5 in 1995.
6 (7) Research conducted by the chief economist
7 of the National Association of Insurance Commis-
8 sioners found that after controlling for risk of loss,
9 a 10 percentage point increase in the number of mi-
10 norities in a zip code is associated with a 2 percent-
11 age point increase in the number of "FAIR plans",
12 which are government-sponsored insurance plans of
13 last resort for those who cannot obtain insurance in
14 the private market.
15 (8) In order to increase access to credit, wealth
16 and insurance, it is necessary to modernize the Com-
17 munity Reinvestment Act of 1977 to reflect shifting
18 trends in the financial services industry.
19 (9) Currently, about 40 percent of the assets in
20 the financial industry reside in bank and thrifts and
21 are covered by the Community Reinvestment Act of
22 1977, down from about 60 percent in the early
23 1980s.
24 **SEC. 3. PURPOSES.**
25 The purposes of this Act are as follows:

(1) To enhance the availability of financial services to citizens of all economic circumstances and in all geographic areas.

(2) To enhance the ability of financial institutions to meet the capital and credit needs of all citizens and communities, including underserved communities and populations.

(3) To ensure that community reinvestment keeps pace with the affiliation of banks, securities firms, and other financial service providers, as provided by the Gramm-Leach-Bliley Act.

TITLE I—MODERNIZATION OF COMMUNITY REINVESTMENT ACT OF 1977 AND COMMUNITY SERVICE OBLIGATIONS.

SEC. 101. EXTENSION OF COMMUNITY REINVESTMENT OBLIGATIONS WITHIN A FINANCIAL HOLDING COMPANY.

Section 4(l) of the Bank Holding Company Act of 1956 (12 U.S.C. 1843(l)) is amended by adding at the end the following new paragraph:

"(4) COMMUNITY NEEDS.—

"(A) IN GENERAL.—All nonbank affiliates of bank holding companies that engage in lending or offer banking products or services shall

PREPARED STATEMENT OF HOWARD W. HANNA, III

VICE CHAIRMAN, THE REAL ESTATE SERVICES PROVIDERS COUNCIL, INC. (RESPRO®)
PRINCIPAL AND FORMER CHAIRMAN, THE REALTY ALLIANCE
PRESIDENT AND CHIEF EXECUTIVE OFFICER, HOWARD HANNA REAL ESTATE SERVICES
PITTSBURGH, PENNSYLVANIA

MAY 23, 2002

Good morning, Mr. Chairman and Members of the Subcommittee. My name is Howard W. Hanna, III and I am President and CEO of Howard Hanna Real Estate Services, a family owned and operated full service real estate brokerage company headquartered in Pittsburgh, Pennsylvania.

Howard Hanna Real Estate Services has 65 residential and commercial real estate brokerage offices doing real estate sales and leasing in Pennsylvania, Ohio, West Virginia, and New York State, and a mortgage banking company. Hanna Financial Services, which is licensed in those four States and also Illinois, Maryland, Colorado, Wisconsin, and North Carolina.

Our firm has 1,500 associates and employees, of which 1,128 are members of the National Association of REALTORS®, and I am proud to be a 32-year member of the REALTORS® Association of Metropolitan Pittsburgh, the Pennsylvania Association of REALTORS®, and the National Association of REALTORS®.

I currently serve as Vice Chairman of The Real Estate Services Providers Council, Inc. (RESPRO®) and I am a Member of The Realty Alliance. I represent both organizations today.

RESPRO® is a national nonprofit trade association of approximately 200 residential real estate brokerage, mortgage, home building, title, and other settlement service companies who united in 1992 to promote an environment that enables providers to offer diversified services for homebuyers and owners (one-stop shopping) through strategic alliances across industry lines.

Approximately 55 percent of RESPRO®'s members engage in residential real estate brokerage, either directly or as a franchisor. Most of our real estate broker members are what I will refer to as "integrated" real estate brokerage firms, which means that we also offer mortgage, title, and/or other settlement services to our customers.

The Realty Alliance is a national organization of 45 regional, residential real estate brokerage firms that provides its members with idea sharing venues, industry forecasts and analysis, financial benchmarking, and technology information.

Together, RESPRO® and The Realty Alliance members who are in the real estate brokerage business have closed over one million residential real estate transactions for a sales volume of over $1.8 trillion, utilizing over 300,000 sales associates and over 78,000 employees in over 50,000 offices nationwide.

Position of RESPRO® and The Realty Alliance Position on Bank-Real Estate Affiliations

Both RESPRO® and The Realty Alliance have formally decided, on a vote of their respective Boards of Directors, to support the 2001 proposal by the Federal Reserve Board (Fed) and Treasury Department to allow financial holding companies and national bank subsidiaries into the real estate brokerage and related businesses by declaring these activities to be "financial in nature", and to oppose legislation (S. 1839, H.R. 3424) to block this proposal.

All available evidence shows that homebuyers like one-stop shopping, and that realty-based one-stop shopping offers potential consumer benefits such as convenience and lower costs. RESPRO® and The Realty Alliance believe in free enterprise and a competitive marketplace that would allow *any* company to offer consumers these benefits, regardless of its industry or affiliation.

Today's Realty-Based One-Stop Shopping Programs

According to a 1999 study conducted by the independent consulting firm of Weston Edwards & Associates, the top 350 real estate brokerage firms closed $22 billion in mortgage loans in 1998, and realty-based and builder-based lending accounted for about 10 percent of all purchase money mortgages that same year.[1] Edwards estimated that this amount would double to 20 percent within 3 years.[2]

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[1] "Changes in the Way Homes Are and Will Be Bought and Sold", By Weston Edwards & Associates, 1999.

[2] Weston Edwards & Associates is expected to publish 2002 statistics in the area sometime in 2003.

Edwards also found that 66 to 69 percent of the 250 largest residential real estate brokerage firms in the country offer mortgages, 31 percent offer title, closing, escrow or personal insurance in 1996.[3]

The Potential Consumer Benefits of Realty-Based One-Stop Shopping

Since real estate brokerage firms have entered mortgage and other financial services businesses, there have been several consumer surveys and economic studies to assess their impact. All have conclusively shown that realty-based one-stop shopping programs in today's marketplace offer many potential benefits to the homebuyer.

The most recent survey of consumer attitudes toward realty-based one-stop shopping, which is attached to this testimony, was performed in March of this year. Harris Interactive, the parent of Harris Poll, surveyed 2,052 recent and future homebuyers and found:

- That 82 percent of homebuyers would "strongly" or "somewhat" strongly consider using a one-stop shopping service for their home purchase.
- That when a homebuyer is aware that a real estate brokerage firm offers a full range of services, it positively affects their selection of a real estate agent 44 percent of the time.
- That the three preferred sources of one-stop shopping programs are mortgage companies, banks and credit unions, and real estate brokerage firms.
- That 64 percent of homebuyers who recently used one-stop shopping programs had a much better overall experience with their home purchase transaction.
- That over 90 percent of homebuyers who did not use one-stop shopping programs believed that if they had used one, they would have had a better overall home purchase experience because:
  - They would have had just one person to contact,
  - They would have saved money if the company offered discounted prices,
  - It would have sped up the homebuying process,
  - It would have prevented things from falling through the cracks; and
  - It would have assured one standard level of brand-named service from all providers of the home purchase services.[4]

The Edwards study I mentioned earlier found that mortgages offered by realty-based one-stop shopping programs are competitive in both price and service. It concluded that real estate agents prefer using outside lenders unless the in-house mortgage service is exceptional, and that they only recommend the in-house product to the homebuyer when the loan product is within 1/8th of a percent of the best rate and when he or she believes the service is superior to outside mortgage products. The Edwards study also found that 96 percent of realty-owned mortgage brokerage operations use multilender systems, in order to give their real estate sales force and their customers a choice of mortgage lenders.

A 1994 economic study commissioned by RESPRO® and conducted by Lexecon, Inc., a national economic consulting firm, also found that realty-based one-stop shopping programs potentially offer lower costs.[5] The study compared title and closing costs between realty-owned title companies and independent title companies in over 1,000 home purchase transactions throughout seven States—Florida, Minnesota, Tennessee, Wisconsin, Mississippi, Pennsylvania, and California—and concluded that title and closing costs for realty-owned title companies were not only competitive with those of independent title companies, but actually resulted in a 2 percent cost savings.[6]

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[3] "One-Stop-Shopping For The Homebuyer: A Rapidly Expanding Channel of Distribution", by Weston Edwards & Associates, 1997. The business structures of these realty-owned one-stop shopping programs vary. Many of the largest firms have created wholly-owned mortgage lending or brokerage, title, and/or insurance subsidiaries. Smaller firms have created joint ventures with local or national mortgage lenders, financial institutions, or mortgage subsidiaries of financial holding companies, title underwriters, or title agencies that are jointly owned (e.g. 50 percent–50 percent) by the partners.

[4] The survey also asked homebuyers how they felt about financial institutions entering the real estate brokerage business. Sixty-nine percent believed it would positively affect the range of services available through one company, 47 percent believed it would positively impact the number of choices of companies to conduct their home purchase transaction, and 46 percent believed it would positively affect the price they paid for the services needed to conduct the home purchase transaction.

[5] "Economic Analysis of Restrictions on Diversified Real Estate Services Providers", by Lexecon, Inc., January 3, 1995.

[6] In a 1996 Economic Analysis accompanying a final RESPA regulation, the Department of Housing and Urban Development (HUD) offered its independent analysis of both the Lexecon, Inc. study and the Edwards study. It concluded that ". . . referral activity among affiliates

Continued

The bottom line is that every consumer survey and empirical study to date has shown that homebuyers prefer and potentially benefit from realty-based one-stop shopping programs.

Integrated Real Estate Brokerage Companies Favor Open Competition

As you know, the banking industry has argued that financial holding companies and national bank subsidiaries should be able to compete with integrated real estate firms such as Howard Hanna Real Estate Services, Long & Foster Real Estate, and other RESPRO® and Realty Alliance members. In addition, some participants in this debate have accused the real estate brokerage industry as being "hypocritical" by wanting to be in the financial services business without letting financial institutions compete with us in the real estate brokerage business.

I can assure you that the vast majority of RESPRO® and Realty Alliance members favor open competition and believe that banks should be able to compete with us in our primary business in the same way we compete with them in the mortgage and other settlement service businesses.

Over the last 20 years, a number of financial conglomerates have entered the real estate brokerage business, with varying degrees of success: in the 1980's and early 1990's, Sears Roebuck owned Coldwell Banker, Metropolitan Life owned Century 21, and Merrill Lynch owned Merrill Lynch Realty. Today, General Motors Acceptance Corporation (GMAC) owns GMAC Real Estate, Prudential Insurance Company owns Prudential Realty, Cendant Corporation operates the Century 21, ERA, and Coldwell Banker franchises, and Warren Buffet's Berkshire Hathaway owns Home Services of America, Inc.

Initially, these companies appeared to have significant competitive advantages over traditional real estate brokerage companies, such as national distribution outlets, consumer marketing lists that made it easy to reach everyone, valuable data about buying habits, and tremendous name recognition. Sears even had access to Federally insured deposits through its affiliate Sears Savings Bank.

Their entry into the business real estate brokerage business concerned many independent real estate brokerage firms at the time. In fact, in 1981, the long range planning committee of a national network of large regional independent brokerage firms issued a report to its members that stated that Merrill Lynch and Sears were the two greatest threats to the solvency of real estate brokerage firms ever faced by the industry.

But this prediction was unfounded. Sears, Merrill Lynch, and Metropolitan Life have since left the real estate brokerage business. While Prudential, GMAC, Cendant, and Berkshire Hathaway remain competitors, their presence in the real estate marketplace has not changed the basic character of the real estate brokerage business. In fact, we believe that their entry contributed to the development of a wider range of services and caused traditional real estate brokerage firms to become more efficient and more consumer-focused than they were before.

Federally insured financial institutions also have entered residential real estate markets over the years. This is not surprising, since over 50 percent of financial institutions (State-chartered banks in 26 States, Federal savings associations, and credit unions) can currently engage in real estate brokerage.

Metropolitan Financial Corporation owned Minneapolis-based Edina Realty from 1988 to 1995, Sears Savings Bank was affiliated with Coldwell Banker, and Twin Cities Federal (TCF) and Great Western at one time owned real estate brokerage firms. Savings institutions or State-chartered banks have also acquired real estate brokerage firms in Connecticut, Pennsylvania, Delaware, Texas, New York, and Florida. But over time, most of these financial institutions sold their real estate brokerage businesses and retreated from the marketplace.

Finally, it's important to remember that real estate brokerage firms would have the ability to acquire Federally chartered financial institutions if the Fed-Treasury rule is finalized. Earlier this month, a bank in Pittsburgh with 25 offices and assets of $800 million that Howard Hanna Real Estate Services had a close working relationship with was sold to another bank. This was a bank that our real estate company would have been interested in purchasing if we were allowed to do so under Federal law.

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might still benefit consumers because of the possibility of immediate savings in shopping time and hassle and future reductions in prices due to lower marketing and other costs. Taking these benefits into account, referrals among affiliated firms are probably neutral and possibly beneficial to consumers."

There Should Be A Level Playing Field Between Bank-Owned and Non-Bank Real Estate Brokerage Firms Under RESPA and State Laws

While RESPRO® and The Realty Alliance support the ability of financial holding companies and national bank subsidiaries to enter the real estate brokerage business, we also believe that bank-owned and nonbank real estate brokerage firms should compete under a similar Federal and State regulatory environment.

The Real Estate Settlement Procedures Act (RESPA)

At the Federal level, all settlement service providers, including integrated real estate brokerage firms and our real estate agents, must comply with the Real Estate Settlement Procedures Act (RESPA), which requires that a lender give a Good Faith Estimate (GFE) of the closing costs 3 days after the application and a HUD–1 Settlement Statement at closing. Section 8 of RESPA also prohibits settlement service providers from giving or receiving referral fees, or "kickbacks".

Integrated real estate brokerage firms also are subject to RESPA's "affiliated business" restrictions, which requires us, before we refer business to our mortgage, title or other settlement service affiliates, to (1) disclose the nature of the financial relationship; (2) not require the use of the affiliated settlement service; and (3) not give or receive any payments (referral fees) that are otherwise prohibited under RESPA. Under the last requirement, neither the real estate brokerage firm nor its real estate sales associates can accept any "thing of value" from an affiliated mortgage or other settlement service provider for referrals of business.[7]

Financial holding companies and national bank subsidiaries that enter the real estate brokerage business would be subject to these RESPA guidelines, which we believe is appropriate.

But in the near future, HUD is expected to issue a proposed RESPA rule that would exempt providers from Section 8 of RESPA if they guarantee the lump-sum cost of a settlement service "package".

For there to continue to be a level playing field between bank-owned and nonbank real estate brokerage firms, it is essential that HUD allow nonmortgage lenders such as real estate brokerage firms to offer a guaranteed "package" to our customers in the same manner as mortgage lenders. We urge Congress to closely monitor the progress of this HUD rulemaking proceeding to assure that all providers have the ability to compete under any new regulatory environment under RESPA, regardless of their industry or affiliation.

State Laws Affecting Integrated Real Estate Brokerage Firms

Integrated residential real estate brokerage firms also are subject to a myriad of State laws and regulations that prohibit or restrict their operations.

In 2001, 37 States had statutes, regulations, or policies that place percentage limitations on the amount of business a title insurer or agent can receive from an affiliate, including an affiliated real estate broker, real estate agent, home builder, mortgage lender, or financial institution.[8] Other States have enacted laws that prohibit a person from receiving a fee as real estate broker or salesperson and mortgage broker in the same transaction.

As you know, the Gramm-Leach-Bliley Act (GLBA) prohibited States from (1) preventing a depository institution or affiliate from being affiliated with any entity authorized by the Act; (2) preventing or significantly interfering with the ability of a depository institution or affiliate to engage in insurance sales, solicitation or cross-marketing; or (3) preventing or significantly interfering with the ability of an insurer or affiliate to become a financial holding company or to acquire control of a depository institution.

Since GLBA passed Congress, some financial institutions have successfully exempted themselves from these State restrictions under GLBA's State preemption provisions. For example, the Kansas Insurance Department ruled in 2001 that GLBA preempted Kansas financial institutions *only* from a Kansas State law that

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[7] In addition, any mortgage, title, or other settlement service joint venture created by a real estate brokerage firm must comply with guidelines issued in a 1996 Department of Housing and Urban Development (HUD) Policy Statement that intended to prevent "sham" joint ventures created primarily as a conduit for violating Section 8 of RESPA. Under these joint venture guidelines, HUD announced that it will look at a variety of factors to determine whether a joint venture is a "sham" or a legitimate joint venture, including whether both partners invest capital in the entity, whether the entity performs "core" settlement services, whether the entity has separate management and employees, and whether the partners' return on their ownership interest is proportional to the capital they invested in the joint venture entity.

[8] "State Survey of Affiliated Business Laws", by the Real Estate Services Providers Council, Inc. (RESPRO®), 2001.

prohibited a title agency from receiving in excess of 20 percent of its operating revenue from an affiliate.

As a result, Kansas financial institutions may own a title company but nonfinancial institutions, including real estate brokerage firms, may not. If financial holding companies and national bank subsidiaries are allowed to own real estate brokerage firms, then bank-owned real estate brokerage firms could own title agencies but nonbank real estate brokerage firms could not.

RESPRO® and The Realty Alliance members have consistently opposed these state antiaffiliation laws over the years, and we support their preemption or repeal for both financial institutions and nonfinancial institutions. If the Fed and the Treasury approve a final rule, we urge Congress to assure that State laws apply equally to all real estate brokerage firms, regardless of their affiliation. This would better enable all real estate brokerage firms to offer homebuyers the benefits of one-stop shopping programs, regardless of whether they are affiliated with a financial institution.

Mr. Chairman, I again thank you for the opportunity to testify, and I would be glad to answer any questions.

1090 VERMONT AVENUE NW, SUITE 800 • WASHINGTON, DC 20005
TEL (202) 408-7038 FAX (202) 408-0848
E-MAIL INFO@RESPRO.ORG WEB WWW.RESPRO.ORG

Effective May 22, 2002

MEMBERSHIP

Board Members

Arvida Mortgage Services
Clearwater, Florida
Baird & Warner, Inc
Chicago, Illinois
Cendant Corporation
Parsippany, New Jersey
Chase Manhattan Mortgage Corp.
Edison, New Jersey
Countrywide Home Loans
Calabasas, California
Detrick Companies
Tulsa, Oklahoma
DeWolfe New England
Lexington, Massachusetts
F.C. Tucker Company, Inc.
Indianapolis, Indiana
Fidelity National Financial, Inc.
Santa Barbara, California
First American Financial Corporation
Santa Ana, California
First Nationwide Mortgage Corporation
Frederick, Maryland
First Ohio Mortgage Corporation
Cleveland, Ohio
GE Capital Mortgage Corporation
Raleigh, North Carolina
General American Corporation
Medina, Ohio
GMAC Home Services
Des Moines, Iowa
HomeServices, Inc.
Edina, Minnesota
HomeFocus Services, LLC
St. Louis, Missouri
Howard Hanna Financial Services
Pittsburgh, Pennsylvania
Investors Title Insurance Company
Chapel Hill, North Carolina
John L. Scott Real Estate
Bellevue, Washington
LandSafe Appraisal Services
Plano, Texas
Lawyers Title Insurance Corporation
Richmond, Virginia
Long & Foster Real Estate, Inc.
Fairfax, Virginia
Metropolitan Title Company
Howell, Michigan
North American Title
Houston, Texas
Old Republic National Title Insurance
Minneapolis, Minnesota
Prudential California Realty
Walnut Creek, California
Prudential Resource Management
Valhalla, New York
Pulte Corporation
Bloomfield, Michigan
RE/MAX of California & Hawaii, Inc.
Palos Verdes Estates, Ca
Shelter Mortgage Corporation
Brown Deer, Wisconsin
Sibcy-Cline Realtors
Cincinnati, Ohio
Smythe, Cramer Co.
Seven Hills, Ohio
Stewart Title Guaranty Company
Houston, Texas
Title Alliance, Ltd.
Media, Pennsylvania
Transnation Title Insurance Company
Richmond, Virginia
The Trident Group
Devon, Pennsylvania
Title Insurance Company of America
Austin, Texas
Weichert Realtors
Morris Plains, New Jersey
Wells Fargo Mortgage
Des Moines, Iowa
Woods Bros. Realty, Inc.
Lincoln, Nebrask

General Members

Abrams, Garfinkel & Rosen
New York, New York
Affiliated Title Management
Baltimore, Maryland
The Agent Owned Realty Company
Mt. Pleasant, South Carolina
Allen Tate Mortgage Services
Charlotte, North Carolina
Alliance Title of America, Inc.
Tampa, Florida
Allied Mortgage Capital Corp
South Toms River, NJ
American Residential Mortgage Corp.
Maplewood, Minnesota
Atlantic Assurance Group
Charlotte, North Carolina
ATM Corporation of America
Coraopolis, Pennsylvania
Beltway/Network Settlement
Crofton, Maryland
BNY Mortgage Company
Tarrytown, New York
Cablish, Gentile & Gay CPAS
Bradenton, Florida
CNA Home Warranty
Madison, Wisconsin
Coastal Title Agency, Inc.
Freehold, New Jersey
Coldwell Banker Homesale Services
Lancaster, Pennsylvania
Coldwell Banker Howard Perry and Walston
Raleigh, North Carolina
Coldwell Banker Sammis
Huntington, New York
Coldwell Banker Success Realty
Scottsdale, Arizona
Colonial Valley Abstract Company
York, Pennsylvania
Consumer Title Company
Fayetteville, NC
Coquicom, L.L.C.
Cleveland, Ohio
Cressy & Everett/Better Homes & Gardens
South Bend, Indiana
Cumberland Title Company
Nashville, Tennessee
Detroit Title and Insurance Agency, Inc.
Southfield, Michigan
Deutch & Greenberg
Milwaukee, Wisconsin
Devon Title Company
Bloomfield Hills, Michigan
DRH Financial Services
Austin, Texas
Edward Surovell Realtors
Ann Arbor, Michigan
Enterprise Abstract Services, Inc.
Melville, New York
Equity Title & Closing Services, Inc.
East Providence, Rhode Island
Family Lending Services, Inc.
Newport Beach, California
Financial 2000, Inc.
Redlands, California
First Southwestern/First Financial Title Group
Pasadena, CA
Fonville Morrisey Realtors
Raleigh, North Carolina
The Fountainhead Title Group Corporation
Columbia, MD
Frank Howard Allen Realtors
Novato, California
Gambino Realtors/GMAC
Rockford, IL
Georgia Mortgage Services, Inc.
Fayetteville, Georgia
Gilpin Mortgage Company
Wilmington, Delaware
GreenLink, LLC.
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Home Buyers Resale Warranty Corporation
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Home Closer, LLC
New York, NY
Homegain.com
Emeryville, California
Home-Link Services, Inc.
Shelton, Connecticut
Home Network Online
Novi, Wisconsin
Homeowners Club of America
Chicago, Illinois
Houlihan/Lawence, Inc.
Bronxville, New York
HouseMaster
Bound Brook, New Jersey
Hubbard and Quinn, P.A.
Amherst, New Hampshire
Hunt Real Estate Corporation
Williamsville, New York
Insignia Title Agency
Seven Hills, Ohio

Integrated Loan Services
Rocky Hill, Connecticut
Irwin Home Equity Corporation
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Miami, Florida
King Thompson Realtors
Dublin, Ohio
K. Hovnanian Title Division
Eatontown, New Jersey
L & G Mortgage Banc
Scottsdale, Arizona
Land Title Insurance Corporation
Denver, Colorado
Latter & Blum\CJ Brown
New Orleans, Louisiana
The Laughlin Companies
McLean, Virginia
Lyon Associates
Sacramento, California
McColly GMAC Real Estate
Crown Point, Indiana
McMillin Realty
San Diego, California
Metrociti Mortgage, LLC
Encino, California
Michael J. Aheron
Roanoke, Virginia
Midwest Title
Topeka, Kansas
Morris & Schneider, P.C.
Atlanta, Georgia
MRIS
Rockville, MD
National City Insurance Agency of PA, Inc.
Aspinwall, Pennsylvania
National Real Estate Information Svcs.
Pittsburgh, PA
The New York Mortgage Company, LLC
New York, NY
North Coast Mortgage Company
Larkspur, CA
Northwood Realty/Better Homes & Gardens
Allison Park, Pennsylvania
Old Republic Home Protection Co., Inc
San Ramon, California
Orange Coast Title Company
Santa Ana, California
Pacific Alaska Mortgage
Anchorage, AK
PCFS Mortgage Resources, LLC
Atlanta, GA
Personal Lines Insurance Brokerage, Inc.
Warren, New Jersey
Preferred Empire Mortgage Company
Melville, New York
Preferred Title
Madison, Wisconsin
Premier Title Company, LLC
Palm Beach, Florida
Professional Home Mortgage Lenders
Winston-Salem, North Carolina
Prudential Gardner, Inc.
Metairie, Louisiana
The Prudential Preferred Realty
Pittsburgh, Pennsylvania
Realty Executives of Tucson
Tucson, Arizona
Realty South
Birmingham, Alabama
RELO
Chicago, IL
ReMax Integrity
Eugene, Oregon
RE/MAX Central Realty
Virginia Beach, Virginia
ReMax International Relocation Services, Inc.
Englewood, Colorado
Realink.com
Tempe, Arizona
Realty Title Agency, Inc.
White Plains, New York
Relocation Resources International, Inc.
Norwell, Massachusetts
Rose & Womble Realty Company
Virginia Beach, VA
Rudy Title & Escrow
Nashville, FL
Safeco Land Title of Dallas
Dallas, TX
Service Link
Aliquippa, PA
Security First Title Affiliates, Inc.
Largo, FL
Security Title Services, Inc.
Indianapolis, Indiana
SHEA Mortgage, Inc
San Diego, CA
Shorewest Realtors
Brookfield, Wisconsin
Surety Title Corporation
Marlton, New Jersey
Southern Title Insurance Corp.
Richmond, Virginia
Starck & Co., Realtors
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Title Clearance Services, Inc.
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Irwin Home Equity Corporation
San Ramon, California
Kansas Association of Realtors
Topeka, Kansas
Leonard, Street & Deinard
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Morreale Real Estate Services
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Equity Title Agency, LLC
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Frontier Title, LLC
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Mortgage Quote Service, Inc.
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Latter & Blum, Companies	New Orleans, LA
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Lyon & Associates, Realtors	Sacramento, CA
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Windermere Real Estate Co.	Seattle, WA

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MURRAY CONSULTING, INC.

STEPHEN H. MURRAY
PRESIDENT

STATEMENT

OF

STEPHEN H. MURRAY
PRESIDENT
MURRAY CONSULTING, INC.

AND

ANNE RANDOLPH
PARTNER
MURRAY CONSULTING, INC.

SUBMITTED TO THE

SENATE SUBCOMMITTEE ON FINANCIAL INSTITUTIONS

OF THE

SENATE COMMITTEE ON BANKING, HOUSING AND URBAN AFFAIRS

ON BANK-REAL ESTATE AFFILIATIONS

6898 SOUTH UNIVERSITY BLVD., SUITE 200 • LITTLETON, CO 80122
PHONE: (303) 741-1000 FAX: (303) 741-1070 E-MAIL: realtrends@aol.com
WEB: REALTRENDS.COM

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Consumers are turning to real estate brokerages that offer "one-stop" shopping with increasing frequency. In 1999, consumers acquired 109,918 mortgages and 70,477 title insurance policies from the nation's 75 largest real estate brokerage firms. In 2001, consumers acquired 200,389 mortgages and 277,651 title insurances policies from among the largest 125 firms. All of this data was derived from the REAL Trends 500 Report, a compilation of verified data from the country's leading residential real estate brokerage firms. The desire of consumers to utilize a variety of providers is increasing quickly.

American housing consumers felt strongly that real estate brokerage firms, mortgage lenders and banks were roughly equally capable of providing "one-stop" shopping; in fact, consumers slightly favored mortgage lenders (76%) and banks (74%) over real estate brokerage firms (72%) in providing "one-stop" shopping service packages;

Among all participants in the study, consumers said that they felt the entry of banks into the real estate services business would be a positive trend. The reasons for consumers positive view of banks entering the real estate services business were 1) increasing the range of services from one supplier (68%), the opportunity have better prices (48%) and improving the choices among providers (47%);

Among American consumers who identified themselves as being in favor of "one-stop" shopping in real estate services were even more favorable towards allowing banks to offer a full range of real estate services. Almost 80% of all consumers favored the entry of banks into real estate services because it will improve the range of services available; nearly 56% because it would lower prices for these packaged services and 58% because the choices available to consumers would improve.

Stephen H. Murray
President
Murray Consulting Inc

Anne Randolph
Partner
Murray Consulting, Inc

May 20, 2002

In June of 2001, Murray Consulting, a prominent residential brokerage industry consulting and research firm, and Harris Interactive, among the world's most respected research firms, conducted a survey to determine the habits, practices and perceptions of American home buyers and home sellers. The report, entitled "Room for Improvement: Perspectives of Consumers and the Professionals Who Serve Them" was completed in January 2002. In total, over 3,500 recent and future buyers and sellers were asked questions about their experiences and/or plans with respect to the use of real estate associates and brokerage firms. An additional 2,000 consumers were polled via telephone survey as well.

In March of 2002, Murray/Harris returned to the study group with additional questions concerning "one-stop" shopping in the purchase and sale of housing and the prospect of banks and financial institutions entering the real estate services/brokerage business. This second study resulted in the receipt of 2,052 responses from consumers who had recently purchased a home or were planning to do so in the next twelve months.

The survey had a confidence level of 95 percent plus or minus 2 points. All questions were reviewed by Harris Interactive to insure that they were not leading or biased for or against the proposition as far as "one-stop" shopping and financial institutions were concerned.

The key findings were as follows:

American housing consumers were strongly inclined to believe that "one-stop" shopping, being able to find and purchase a home, and procure all necessary financing, insurance, inspections, etc. was in their best interest. Further over 82 % indicated they would strongly consider or somewhat consider using a single supplier of such services;

These results were up substantially from a similar study done in 1999 by the National Association of Realtors (NAR). In fact, the questions used were identical to those used in the previous NAR study.

The satisfaction rate with the services that purchasers utilized during the process of buying a home were progressively higher as they used more services from a single supplier. For example, of all buyers the satisfaction rate was 62%; for those using a real estate agent the satisfaction rate was 66%; and for those who utilized financing or other services the satisfaction rate was 78%;

CONSUMER PERSPECTIVES ON REALTY-BASED ONE-STOP SHOPPING

April 2002

PURPOSE OF THE STUDY

The purpose of the study was to extend the learning gained in the study on consumer and agent perspectives in residential real estate entitled *"Room For Improvement: Perspective of Real Estate Consumers and the Professionals Who Serve Them"*, released in February of this year to understand more specifically the home buying consumers response to one stop shopping. This study was to address:

- Overall concept response
- Appropriate sources for one stop shopping
- Impacts on consumer behavior and a satisfaction in the purchasing process

As a secondary purpose, the study was intended to identify any change in perceptions by home buying consumers that might have occurred since the National Association of Realtors study of 1999, which addressed many of the same issues. To aid in comparability, exact wording of several questions from that study were used, as were the rating scales. That survey was conducted from July 25 to 30, 1999 by Hart-Riehle-Hartwig Research and was based on 801 homebuyers nationwide who purchased their homes within the past two years.

RESPONDENT PROFILES

This survey was conducted from March 18th to 25th, 2002 by Harris Interactive, the parent company of the Harris Poll. A total of 2052 recent and future homebuyers were interviewed, including 687 Recent Buyers and 1365 Future Buyers. To be qualified, the buyers had to have purchased their home within the past 12 months, or to be planning on purchasing a home in the next 12 months. 76% of the recent buyer groups used a real estate agent, and 23 % did not use an agent.

FINDINGS FROM THE SURVEY – SUMMARY

I. SERVICES TO THE TRANSACTION: USE AND PROVIDERS

Most of the buyers used or planned to use many of the services traditionally seen as important to the real estate transaction.

Which of the following did you use the last time you purchased a home. (Or which do you plan to use when you purchase your home) Please check all that apply.

Service	Total Buyers	Recent Buyers	Future Buyers
Real Estate Agents	**76%**	**71%**	**79%**
Mortgage Lending	**80**	**83**	**79**
Title Insurance	**56**	**58**	**56**
Homeowners Insurance	**86**	**78**	**90**
Home Inspection	**70**	**58**	**76**
Home Warranty	**41**	**32**	**45**

Most buyers continue to obtain the required services for the transaction from multiple sources versus a single source. Future Buyers expect that they will do the same.

Did you get the services that you required (e.g. real estate agent, mortgage lending, title insurance, homeowners insurance, home inspection, home warranty, etc) from one source or multiple sources? In the case of Future Buyers, worded as do you think you will get the services you will require…?

	Total Buyers	Recent Buyers	Future Buyers
One Source	21%	20%	22%
Multiple Sources	79	80	78

Real estate agents have a significant impact on the service providers used by their home-buying clients. Real estate agents frequently provide recommendations to buyers on where to obtain many of the services needed during the transaction, and when offered a recommendation, most buyers follow the recommendation.

Please indicate whether the real estate agent who handled your recent home purchase offered a recommendation on where you could obtain the following services. (Base: Respondents who used a real estate agent and were recent buyers only – 471 respondents)

	Agent provided recommendation	Agent didn't provide recommendation	Not Sure
Home Inspector	72%	21%	7%
Title Insurance	60	29	11
Home Warranty	47	35	18
Mortgage Lender	66	29	5
Homeowners Insurance	32	64	4

Did you use the service (s) recommended by your agent? (Base: Respondents whose agents offered the services listed)

	Used Recommended Service Provider	Used Service Not Recommended by Agent	Did Not Use
Home Inspector	83	6	12
Title Insurance	82	8	10
Home Warranty	72	2	26
Mortgage Lender	77	17	6
Homeowners Insurance	68	24	7

It appears however that either few real estate brokerage companies offer the services, or that real estate agents are not recommending the services of their real estate brokerage company (if offered), because few of the services offered by the real estate agents were from the agent's brokerage company. This is supported by the high percent of buyers who were unsure of whether the agent's brokerage company offered a full range of services or not. Where the buyer was aware, they were almost equally likely to learn about it before contacting an agent as to learn after contacting the agent.

Which of the services that were offered to you by your real estate agent were from the real estate brokerage company for whom the agent worked?

	% from real estate brokerage company
Home Inspector	8%
Title Insurance	11
Home Warranty	9
Mortgage Lender	13
Homeowners Insurance	6
None of these	57
Not Sure	15

Did your real estate agent's brokerage firm offer a full range of home buying services (for example: home inspection, title insurance, home warranty, mortgage lending, etc.)? Base: respondents that used real estate agent and was recent buyer –471 respondents)

Yes	30%
No	42
Not Sure	28

Were you aware that your real estate agent was affiliated with a real estate brokerage that offered a full range of home buying services prior to engaging your real estate agent, or were you made aware after selecting an agent? (Base: respondents whose real estate brokerage firm offered a full range of services – 141 respondents)

Was aware prior to engaging an agent	44%
Was made aware after selecting an agent	38
Not Sure	12

It is interesting to note that when a buyer was aware that the real estate brokerage offered this full range of services, in 44% of the cases, it had a positive impact on the selection of a real estate agent.

Did the fact that the real estate brokerage offered this full range of services have no impact, a positive impact or a negative impact on your selection of a real estate agent?

(Base: respondents who were aware prior to contacting a real estate agent – 62 respondents)[1]

No Impact	56%
Positive Impact	44%
Negative Impact	0

[1] Please note that when sample sizes get small, care should be taken in assuming predictability of the results.

II. ONE STOP SHOPPING CONCEPT RESPONSE

When offered the option of a simplified one stop shopping process where all services required for the transaction were provided through one source, consumers clearly indicated a strong preference for this option. 82% of all buyers would strongly or somewhat consider using this type of one stop shopping service, with almost 50% (47%) indicating a high degree (strongly consider) of willingness to consider this process.

If a company offered to set up a simplified, one-stop shopping process for you, in which they provided all required services, how strongly would you consider this process? (Base: All Respondents)

	Total Buyer	Recent Buyer	Future Buyer
Top 2 Box – Total[2]	82%	77%	85%
Consider Strongly	47	41	49
Consider Somewhat	36	36	36
Bottom 2 Box – Total	16	21	13
Consider a Little	12	14	11
Would Not Consider	3	6	2
Not Sure	2	2	2

This is a significant increase from the total levels of acceptance found in the NAR Survey of 1999, when 58% of buyers were interested in one stop shopping. Not only has total interest increased, but the strength of the buyer's interest as indicated by "consider strongly" has risen by 29 points, and the buyers not willing to consider one stop shopping at all has dropped 18 points to a minimal 3%.

	NAR Survey 1999	Murray Survey 2002
Top 2 Box	58	82
Consider Strongly	18	47
Consider Somewhat	40	36
Bottom 2 Box	39	16
Consider a Little	17	12
Would Not Consider	22	3
Not Sure	3	2

[2] The Top 2 Box notation represents a combination of the responses for Consider Strongly and Consider Somewhat – the top 2 responses. Bottom 2 Box represents the total of the lower two responses – Consider A Little and Would Not Consider

Among the types of companies that the buyer would consider using for this one stop shopping process, mortgage companies, banks/credit unions and real estate companies were all regarded very favorably, without a huge preference for one type company over the other, although a directional preference appeared to exist for a mortgage company. Insurance companies, tax preparation companies and credit card companies had much lower acceptance from buyers as a source of one stop shopping service.

*How strongly would you consider using this kind of company for one stop shopping for purchasing a home – **A Mortgage Lender or Mortgage Provider**? (Base: all respondents)*

	Total Buyer	Recent Buyer	Future Buyer
Top 2 Box – Total	76%	72%	78%
Consider Strongly	35	37	35
Consider Somewhat	40	35	43
Bottom 2 Box – Total	23	26	21
Consider a Little	17	19	16
Would Not Consider	6	7	5
Not Sure	2	3	1

A Bank or Credit Union?

	Total Buyer	Recent Buyer	Future Buyer
Top 2 Box – Total	74%	68%	77%
Consider Strongly	34	31	35
Consider Somewhat	40	37	42
Bottom 2 Box – Total	25	29	22
Consider a Little	17	20	16
Would Not Consider	7	10	6
Not Sure	2	3	1

A Real Estate Brokerage Company?

	Total Buyer	Recent Buyer	Future Buyer
Top 2 Box – Total	71%	66%	73%
Consider Strongly	32	30	34
Consider Somewhat	38	36	40
Bottom 2 Box – Total	27	32	24
Consider a Little	20	21	19
Would Not Consider	7	11	5
Not Sure	2	2	2

An Insurance Company?

	Total Buyer	Recent Buyer	Future Buyer
Top 2 Box – Total	44%	36%	48%
Consider Strongly	13	12	13
Consider Somewhat	31	24	35
Bottom 2 Box – Total	51	59	46
Consider a Little	30	34	28
Would Not Consider	21	25	18
Not Sure	5	4	6

A Tax Preparation Company like H&R Block?

	Total Buyer	Recent Buyer	Future Buyer
Top 2 Box – Total	16%	14%	16%
Consider Strongly	4	4	3
Consider Somewhat	12	10	13
Bottom 2 Box – Total	78	81	76
Consider a Little	25	24	26
Would Not Consider	52	57	50
Not Sure	7	5	8

A Credit Card Company?

	Total Buyer	Recent Buyer	Future Buyer
Top 2 Box – Total	10%	11%	10%
Consider Strongly	3	3	3
Consider Somewhat	7	8	7
Bottom 2 Box – Total	82	84	82
Consider a Little	22	21	22
Would Not Consider	60	62	59
Not Sure	7	6	8

Similar to the finding of increased interest in the concept of one stop shopping since the NAR study done in 1999, the *acceptance of all three major sources has also increased.* Mortgage Companies, and Banks gained almost 10 points of acceptance each, while Real Estate Brokerage Companies gained 8 points.

	Top 2 Box		Bottom 2 Box	
	1999	**2002**	**1999**	**2002**
Mortgage Company	66%	76%	33%	23%
Banks or Credit Unions	64	74	35	25
Real Estate Companies	63	71	36	27
Insurance Company	39	44	60	51
Tax Preparation Company	24	16	75	78
A Credit Card Company	10	10	89	82

III. IMPACT OF ONE STOP SHOPPING ON BUYER BEHAVIOR AND SATISFACTION

The survey attempted to look at existing and potential behavior impacts from one stop shopping, using a mortgage company as an example. When buyers applied for a mortgage prior to contacting an agent, they were only infrequently offered a variety of other services (with the exception of closing service like title insurance).

Did you apply for a mortgage prior to contacting a real estate agent? (Base: Respondents that used a real estate agent and is a recent buyer – 471 respondents)

Yes	34%
No	66%

Which, if any, of the following services did your mortgage company offer you? (Base: respondents who were recent buyers who applied for a mortgage prior to contacting an agent – 159 respondents).

Selection of real estate agent	23%
Homeowners insurance	33
Closing services (i.e. Title Insurance, etc.)	70
Home Warranty	19
Home Inspectors	23
None of These	21

This seems unfortunate, because for at least 47% of buyers, if mortgage companies, banks or other lenders have services such as real estate agents, insurance, and closing services, the buyers would prefer to work with that company. For those that said it would have no impact, it would not be to avoid the company, but rather to choose which services to use. In only 10% of the cases would there be a negative impact on the buyer's perception of the company.

If a mortgage company (or bank, other lender, etc.) had services such as real estate agent selection, homeowner's insurance, and closing services like title insurance available, would it affect your choice of which mortgage company to use? (Base: all respondents)

	Total Buyers	**Recent Buyers**	**Future Buyers**
Yes, if the mortgage company offered all of these services, I would prefer that company	47%	40%	51%
Yes, if the mortgage company offered all of these services, I would stay away from that company because I only want to use a mortgage company for a mortgage.	5	3	6
No, even if the mortgage company offered all of these services, I would just use those services I want to use	43	49	40
No, if the mortgage company offered all of these service, I would think that they are trying to do too much and I would avoid that company	5	8	4

Recent buyers were relatively satisfied with the overall experience of buying their last home, with few being completely unsatisfied. At 64% top 3 box (high levels of satisfaction) however, there is clearly room for improvement. This is especially true in mortgage lending and title insurance as well as homeowners insurance services.

Overall, how would you rate your satisfaction with the overall experience of buying your last home? (Base: recent buyers – 667 respondents). Scale of 0-10 where 10 is completely satisfied and 0 is not at all satisfied.

Top 3 Box[3] (8, 9, 10)	**64%**
Completely Satisfied – 10	21
9	14
8	29
Bottom 3 Box (0,1,2)	**4%**

How would you rate your experience with the service you received in each of the following areas? (Base: Recent Buyers – who used each service).
Scale of 0-10 where 10 is completely satisfied and 0 is not at all satisfied.

	Real Estate Agent	**Mortgage Lending**	**Title Insurance**	**Home Insurance**	**Home Inspection**	**Home Warranty**
Top 3 Box	72%	63%	64%	72%	63%	67%
10	39	24	25	34	27	28
9	15	18	13	18	16	15
8	19	21	26	20	20	23
Bottom 3 Box	4	8	4	4	5	4

[3] Top 3 Box here is a combination of the responses for levels 8, 9 and 10 on a scale from 0 to 10 where 0 is Not At All Satisfied, and 10 is Completely Satisfied. Bottom Three Box represents the combination of 0, 1 and 2 on that same scale.

Interestingly, recent buyers who used one source for all the services required for the transaction had a much better overall experience, as well as more satisfactory experiences in virtually all the individual service areas.

Top 3 Box Scores for each service – All Recent Buyers vs. Recent Buyers Who Used One Source instead of Multiple Sources for required services:

	Recent Buyers	**Recent Buyers Who Used One Source**
Overall Experience	64%	71%
Real Estate Agent	72	72
Title Insurance	64	71
Mortgage Lending	63	67
Homeowners Insurance	72	78
Home Inspection	63	79

Among buyers who used multiple sources, one third thought they could have had a better experience if they had purchased all services through one source. Combined with the 20% of recent buyers who used a single source and indicated higher levels of satisfaction, more than 50% of recent buyers either believe they can or have received a better experience through one stop shopping.

Do you think that your real estate experience would have been more satisfactory experience is you could have purchased all the necessary services/products from one source? (Base: respondents using multiple sources).

Yes	34%
No	66%

Among buyers who used multiple sources but believed they would have had a more satisfactory experience, virtually all of the benefits outlined had merit as reasons to believe they would have had a better overall home buying experience, including ease of the transaction, potential cost savings, speed, safety (prevent things from falling through the cracks), and the assurance of a standard level of service.

How much merit do the following reasons have for why you think you would have been more satisfied if all the needed services were available from one source. (Base; respondents who thought the experience would have been more satisfactory – 181 respondents)

	Easier process with just one person to contact	**Save money if companies offered discount prices**	**Speed up the home buying process**	**Prevent things from falling through cracks**	**Assures one standard level of brand-named service from all service suppliers**
Top 2 Box Total	99%	97%	99%	93%	91%
1-A great deal of merit	87	74	73	72	56
2- Some merit	11	22	26	21	34
Bottom 2 Box Total	1	3	1	7	8
3- Only a little merit	1	3	1	7	8
4- No merit at all	1	0	0	0	0
Not Sure	0	0	0	1	1

IV. INFLUENCES IN CHOOSING REAL ESTATE FIRMS AND MORTGAGE COMPANIES

Among all respondents, there is general agreement about what is important in helping them make a selection of real estate firm or mortgage company. Referrals and existing relationships continue to dominate over brand or size and reputation of the company.

Overall, how important is each of the following in helping you make a selection of a real estate agent /brokerage firm? Scale of 0-10, where 0 is not at all important and "10"is extremely important. (Base: all respondents)

Total Buyers	Well known brand in my local area	Size and reputation of the company	Referral from a friend, assoc, or colleague	Existing relationship with broker/loan officer or salesperson
Top 3 Box (8,9,10)	35%	42%	55%	55%
Bottom 3 Box (0,1,2)	14	13	8	12

Overall, how important is each of the following in helping you make a selection of a mortgage company? Scale of 0-10, where 0 is not at all important and "10"is extremely important. (Base: all respondents)

Total Buyers	Well known brand in my local area	Size and Reputation of the company	Referral from a friend, assoc, or colleague	Existing relationship with agent
Top 3 Box (8,9,10)	35%	45%	52%	50%
Bottom 3 Box (0,1,2)	14	10	9	13

V. IMPACT OF FINANCIAL INSTITUTIONS IN REAL ESTATE BROKERAGE

When asked about the potential impact on buyers of having financial institutions enter the real estate brokerage business, overall the response was positive, with 69% of buyers thinking that it would have a positive impact on the range of services available through one company, and 47% believing that it would have a positive impact on the number of choices to meet their needs.

If financial institutions, such as banks, were allowed to own real estate brokerage companies and offer real estate services, what is the impact you believe it would have on you, the customer, in your real estate transaction? (Base: all respondents).

1. **Range of services that are available to you through the company**

	All Buyers	Recent Buyers	Future Buyers
Positive Impact	69	65	71
Negative Impact	12	14	11
No Impact	19	21	18

2. **Price you pay for services required to conduct a real estate transaction**

	All Buyers	Recent Buyers	Future Buyers
Positive Impact	46	46	46
Negative Impact	39	36	40
No Impact	15	18	14

3. **The number of choices you have in companies to serve your real estate needs.**

	All Buyers	Recent Buyers	Future Buyers
Positive Impact	47	39	51
Negative Impact	31	33	30
No Impact	22	27	19

When looking at people who would strongly consider one stop shopping (those that would consider it strongly = 47% of all buyers), the perceived positive impact increased significantly.

Measure of positive impact of financial institutions entering real estate brokerage:

	All Buyers	Buyers Who Strongly Consider One Stop Shopping
Range of services from one company	69	79
Price you pay	46	55
Number of choices of companies	47	58

VI. CONCLUSIONS

- Home buyers, both recent and future, have a very positive view toward one stop shopping and the benefits that can derive from being able to acquire all necessary services from one source. The benefits address the issues of simplicity and convenience: it's an easier process that can be conducted faster, with less room for error and with assurance that each service will be conduced with equal quality. The jury may be out somewhat on the issue of whether there might be an economic impact in terms of lowering overall cost, however, even in this case, most buyers think that there is a possibility of reduced costs from one stop shopping.

- Real estate agents continue to have an enormous impact on the mortgage and settlement service providers that the buyers use, and may not be communicating with their clients that services other than buying or selling are available through the agent's brokerage company. From previous work by Murray Consulting, this appears to come from a desire by the agent to use his or her own personal trusted resources and to protect the agent/buyer relationship from encroachment by his or her real estate brokerage firm.

- While still early in development, it appears that a real estate brokerage firm that has a full range of services may have a positive impact on a buyer's selection of agents.

- Mortgage companies, banks/credit unions and real estate companies are all seen as appropriate sources for one stop shopping in a residential real estate transaction. This comfort with a range of company types has increased significantly from when a previous study that was conducted by the National Association of Realtors in 1999, with mortgage companies building the strongest approval both overall, and in the "strongly consider" category. Buyers clearly have a comfort and trust level in certain types of institutions, and may be trading off what they perceive as the "expertise of the real estate industry" for existing relationships with their banking or other financial institutions.

- Having a one stop shopping process has positive impacts on the selection of company (mortgage company and agent), as well as positive impacts on the satisfaction of buyers in the overall process as well as the individual services. Buyers who have already experienced one stop shopping report much higher levels of satisfaction than those who have not. This would suggest that companies in these three industries who assemble, market and deliver one stop shopping can have a measurable advantage in serving the buying customer over those who don't.

- There is certainly nothing is this data that would suggest consumers believe they would be disadvantaged were financial institutions such as banks/credit unions or mortgage lenders to enter into residential real estate brokerage. On the contrary, they perceive that they can obtain benefits in one stop shopping and in the number of choices that they have in serving their needs. Additionally, they perceive there could be an opportunity for a positive impact on the total cost of the services required in the buying transaction.

RESPONSE TO WRITTEN QUESTIONS OF SENATOR REED FROM TOM MURPHY

Q.1. During the few years before the enactment of Gramm-Leach-Bliley in 1999, a huge disagreement existed between insurance agents and brokers, and commercial banks, about whether banks should be allowed to engage in insurance activities. A compromise was finally reached which allowed Gramm-Leach-Bliley to proceed, and opened a new chapter in which banks were able to affiliate with insurance companies, and to sell insurance. However, certain State consumer protection laws affecting those sales were able to stand, or be enacted, if they did not "significantly interfere" with a bank's sales of insurance.

A.1. An important point to make is that Congress wrote that new insurance powers chapter, not the regulators. Even after that carefully crafted compromise was enacted, there are still regulatory problems arising from it. As late as April 2002, the Comptroller of the Currency encouraged preemption of the Massachusetts Consumer Protection Act. The Comptroller avoided the "significantly interfere" language of the GLBA and instead utilized a much lower standard that the Consumer Protection Act "stands as an obstacle." (See attached letter from Chairman Mike Oxley to Secretary Paul O'Neill) Several other examples exist of national banks and financial holding companies seeking preemption of State and local statutes and regulations due to their national charter. It is very simple for the regulators to now claim that all existing regulations will be followed. But these examples prove their actual conduct is far different.

Q.2. How is this situation different from the one we are currently facing between banks and real estate agents and brokers? I understand that the concern among agents is that they might "disappear" once banks get into their business, and that people in the community will no longer turn to them for their services. However, anecdotal evidence in the case of the insurance agents would suggest differently, showing essentially that there is still a viable market for the agents and that people in the community do still turn to them because they trust them and like using them. Won't that situation hold out in the case of real estate agents as well?

A.2. Banks maintain that insurance companies and agents are actually benefiting from banks exercising insurance powers. There is no doubt that big banks will attempt to capture larger and larger market share. But what do the statistics say? What do consumers say? And what do the independent insurance agents say? In South Dakota, banks entering the real estate business will reduce the number of independent real estate brokerage companies and agents.

This situation is quite different from that facing the real estate industry. The types of problems described above arising from "functional regulation" of insurance products offered by banks provide further evidence that the time is not ripe to grant additional powers to banks. Real estate regulation is far more localized than the insurance industry. Not only are there Federal and State rules and regulations, but also every local county, town, and village has individual requirements for the property located within their jurisdic-

tions. There is no evidence that the regulators considered this when proposing their rule. There can be no comparison of real estate and financial products such as securities and insurance. Those products are fungible assets that have a value wherever they may be. A life insurance policy can "follow" its insured to any State or country. A piece of real estate can never move from where it is first located. It is earth itself. It is the most locally regulated industry there is, by necessity. The problem with allowing the huge banking conglomerates into the real estate industry is that they can dominate a market due to their size and Federally granted advantages. If we assume they would seek to build a national brand and marketing plan, we must also assume they would seek preemption of local and State regulations that would burden that national approach. Past experience shows this is the path they would take, along with their regulators. The result would be weaker consumer protections, less competition, and a less efficient real estate marketplace.

Q.3. Opponents of the REALTOR® argument have accused the REALTORS® of acting uncompetitively in this situation. In fact, allowing the entrance of banks into the real estate brokerage and management market will ensure a healthy and competitive environment for all.

What is your response to those comments? Do you not believe the assertion that many small and community banks are looking to these possible activities as a way to remain competitive with credit unions, as well as REALTORS®?

A.3. We do not believe the assertion that many small and community banks are looking to these possible activities as a way to remain competitive. The fact is the petitions to the Federal Reserve Board and the Treasury Department that lead to the proposed real estate regulation were at the behest of the largest diversified financial holding companies and bank holding companies. The Financial Services Roundtable and the New York Clearing House represent these huge financial conglomerates and money center banks, not small community banks. The American Bankers Association also petitioned the Agencies for the real estate regulation. But they identified only one bank—Fremont National Bank and Trust (Fremont, Nebraska)—that should engage in real estate. Significantly, the Independent Community Bankers Association was not a petitioner to the Agencies.

During hearing testimony Mr. Smith stated that he has had real estate powers since 1984. Although he argued that it is only in the last 2 to 3 years that he thought he might need to utilize that authority to compete, he still has not done so. He has the power to do so and has not. We believe this would hold true across the country for small community banks. The ABA has tried to sell this proposal as an aid to small institutions, but it is the top 5 to 10 largest banking conglomerates that really want this authority. If it is true that 26 States allow their State-chartered banks to operate real estate businesses, why aren't more of them doing it? Only 18 banks in six States are involved in residential real estate according to our research (see written testimony). It has been a precept of the dual banking system since its inception that each charter offers dif-

ferent advantages and disadvantages. There is no reason that any bank today could not apply for a State charter in any of these States and accomplish their goals, other than that they want to seek preemption of State and local rules because of their national charter. If small banks want to offer these services, they can become State chartered, or as explained below, partner with a real estate broker under existing rules.

Credit unions account for less than 1 percent of mortgage originations in this country, and so the competitive argument is a red herring. Not long before the Gramm-Leach-Bliley Act was finally adopted by Congress, the banking industry failed to prevent credit unions' growth through a court challenge. That effort was overwhelmingly defeated by legislation passed by Congress. The competition among financial institutions is a legacy of the Nation's dual banking system and other financial policy decisions. Congress created these institutions, not the regulators.

More specifically, how is it that banks entering brokering, leasing, and managing real estate will make banks more competitive with credit unions? Credit unions, by Federal law, can engage in real estate brokerage only through service organizations and those activities cannot exceed 1 percent of the contributed assets of the credit unions. Moreover, there are not more than half a dozen credit union service organizations operating residential real estate brokerages.

Q.4. As part of the ongoing discussion of this issue, some people have cited the fact that there are numerous real estate companies and brokerages that conduct services that are currently defined as traditional banking activities, such as mortgage lending and title insurance.

Why do you feel this situation is different than one allowing banks to get into some traditional realty activities, such as brokerage and management?

In fact, don't some State banks, thrifts, and credit unions already engage in real estate brokerage activities? How is this case different than national banks entering into this arena?

A.4. First, real estate companies are not offering traditional banking products. Mortgage lending and title insurance are financial products that both traditional banks and commercial firms such as real estate brokers offer (see chart in testimony). This "gray" area is where many commercial and banking industries compete. It is where automobile companies and banks compete for auto financing. It is where retailers and banks compete on personal loan financing. Real estate firms do not take deposits and cash checks. Those are traditional banking activities.

Today, many of the financial services activities performed by real estate brokers are done in partnership with banking subsidiaries. Under the affiliated business arrangement rules of RESPA, a bank owned mortgage company can partner with a real estate broker to offer mortgage loans. They share in the profits resulting from that partnership, and operate under strict consumer protections such as disclosures and prohibitions against kickbacks. Mr. Smith's bank not only could offer real estate brokerage directly today as a Missouri trust company, but he could also partner with an existing

real estate broker to offer mortgage and insurance services through an affiliated business arrangement. This is exactly what Mr. Smith claims banks are seeking through this proposed rule. But if they can do this today, what could be the true reason for seeking this rule? Could it be to avoid the tough RESPA-affiliated business arrangement rules by directly operating the real estate brokerage, or could it be to seek preemption of State and local regulations as discussed in question one above?

Banks make much of the real estate company affiliation with mortgage companies and other real estate service providers giving the impression that "capture rates" of clients' business is automatic and complete, much like what occurs when a bank customer enters a banking institution. The simple fact is that real estate clients using real estate company-affiliated businesses rarely exceed 30 percent annually. Commercial bank mortgage originations still dwarf all other competitors.

The difference in allowing huge national banks (that are the true proponents of this rule) in real estate and those already in the business is the size of these institutions. The top two or three national banks and holding companies have more assets than all of the existing real estate companies combined. This huge market power, along with Federal advantages, would allow these megabanks to dominate any market. As you know, once the market has been won, competitive forces will disappear and consumers will suffer.

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Chief Counsel and Staff Director

U.S. House of Representatives
Committee on Financial Services
2129 Rayburn House Office Building
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April 22, 2002

The Honorable Paul H. O'Neill
Secretary
U.S. Department of the Treasury
1500 Pennsylvania Avenue, NW
Washington, D.C. 20220

Dear Secretary O'Neill:

I am concerned about the recent opinion by the Office of the Comptroller of the Currency (OCC) trying to encourage preemption of the Massachusetts Consumer Protection Act. I am sending this letter in response to clarify our Congressional intent in enacting the Gramm-Leach-Bliley Act (GLBA) and to seek your assistance in addressing this issue with the Comptroller in the future.

First, I am disappointed that the OCC is mischaracterizing its authority to make determinations regarding the insurance provisions of GLBA. When we were drafting GLBA, Congress specifically chose not to make section 104 or Title III part of the National Bank Act or the Bank Holding Company Act. This was to avoid giving the OCC or the Federal Reserve Board any special authority to interpret these provisions. Unlike the National Bank Act, Congress did not include any provisions governing the preemption of state laws by the OCC in the GLBA because the drafters were attempting to end the practice of policy changes and state law preemption through agency litigation. In fact, in contrast to the OCC's assertion that it is "uniquely positioned to evaluate... the Massachusetts Law" and that "Congress clearly envisioned that the federal banking agencies would be making determinations as to whether state laws regarding insurance sales and solicitations were preempted", the conference report explicitly states that it was "recognizing the primacy and legal authority of the States to regulate insurance activities of all persons."

When negotiating the provisions of GLBA governing insurance activities, Congress specifically added the parenthetical "(including a national bank exercising its power to act as agent under the eleventh undesignated paragraph of section 13 of the Federal Reserve Act)" to section 301 stating that "The insurance activities of any person... shall be functionally regulated by the States, subject to section 104". Congress was concerned that the OCC would try to somehow use the National Bank Act provisions to circumvent the clearly expressed requirement that the States be the functional regulators of bank insurance activities, and thus added the specific reference to trump the National Bank Act. Now the OCC is trying to undo this provision. Congress further enacted section 304 of the GLBA precisely in order to prevent overreaching and aggressive misinterpretations of insurance law by Federal regulators. The conference report to the GLBA clearly sates that

"States are the regulators for the insurance activities for all persons, including acting as the functional regulator for the insurance activities of federally chartered banks."

I am equally troubled by the OCC's misinterpretation of the standard for measuring discrimination in State insurance laws under section 104 of the GLBA. Section 104(d)(2)(A) states that in accordance with the legal standards for preemption set forth in *Barnett Bank*, no State may prevent or significantly interfere with a depository institutions insurance sales activities. Few sections and words were fought over as long and hard as this provision, with Congress explicitly codifying the standard to measure preemption of state law -- "prevent or significantly interfere". I was chagrined to read the OCC's avoidance of this standard, attempting to replace it with a standard of "stands as an obstacle to the accomplishment and execution of the full purposes and objectives of Congress."

The full purpose and objective of Congress (not to mention the explicit statutory language) was to use "prevent or significantly interfere" as our standard for potential preemption, not "stands as an obstacle". It is difficult to contemplate how Congress could make clearer its understanding of *Barnett Bank* and the preemption standard to be used. If the Congress had merely intended the courts to continue using the case law of *Barnett Bank* without defining the specific standard to be used, there would have been no point in singling out such language.

I would also note that the OCC apparently is not reading the language of the GLBA, since the OCC incorrectly cites 104(d)(1) as setting forth the *Barnett Bank* standard instead of the appropriate paragraph 104(d)(2), and misstates and misconstrues 104(d)(2)(C) as a "CONSTRUCTION" subparagraph, when the provision is actually a clause (iii) that's a part of the subparagraphs (C)'s "LIMITATIONS". The OCC also rewords clause (iii), rewriting that the paragraph does not limit the "applicability of *Barnett*", when the clause actually states that the paragraph should not be construed to limit the applicability <u>of the decision</u> of the Supreme Court in *Barnett Bank*. Congress in GLBA was attempting to avoid overturning the Supreme Court decision. But Congress also clearly gave voice to the standard of the court that it wanted used for future analysis. The drafters had read *Barnett* numerous times, and specifically chose the standard to be used – "prevent or significantly interfere".

It is interesting that the OCC chose in its opinion letter to rely on the Senate report language to interpret section 104, when the provision was originally drafted in the House, and the conference report clearly specifies that under the conference substitute, "the House discrimination standard was adopted with modifications". The House report states that:

> *Subsection 104(b)(1) clarifies the general rule that States may not prevent or significantly interfere with the activities of an insured depository institution or wholesale financial institution (or their affiliates) that are authorized or permitted under this Act--activities that are financial in nature, such as set forth in section 103. The 'prevent or significantly interfere' standard maintains the test established in the decision of the <u>United States Supreme Court in Barnett Bank of Marion County N.A. v. Nelson</u>, 15 U.S. 25 (1996).*

> *Subsection 104(b)(2), in conjunction with Title III, establishes a comprehensive structure for determining the appropriate applicability or preemption of State law regulating the insurance sales or solicitation or cross-marketing activities of an insured depository institution or wholesale financial institution or their affiliates. Section 104(b)(2)(A) affirms the 'prevent or significantly interfere' standard set forth in Barnett, which shall continue to be used for all Federal preemption determinations of State statutes, regulations, orders, interpretations, or other actions governing insurance sales, solicitation, or cross-marketing activities.*

Here, the House clearly denotes that the "prevent or significantly interfere" standard is the critical standard to be used for litigating potential preemption of State law.

The OCC's approach in trying to overturn the Massachusetts consumer protections are particularly troublesome because Congress in the GLBA clearly stated its desire for the financial regulators to work out disagreements instead of resorting to continual litigation. For example, the conference report states that "the Federal banking agencies and the State insurance regulators are directed to coordinate efforts to supervise companies that control both depository institutions and persons engaged in the business of insurance." The OCC's unilateral action to encourage preemption of Massachusetts consumer protections do not reflect an effort to coordinate bank insurance supervision, and clearly contravene the desire by Congress for the agencies to work out problems with each other, not through the courts.

Congress did recognize that while discouraged, some disagreements between the Federal banking and State insurance regulators were inevitable, given their widely differing missions. That is why Congress enacted section 304 of the GLBA, "to guide the courts in deciding conflicts between Federal and State regulators regarding insurance issues" (conference report p.167). Section 304(a) of GLBA governs any "regulatory conflict between a State insurance regulator and a Federal regulator regarding insurance issues, including whether a State law, rule, regulation, order, or interpretation regarding any insurance sales or solicitation activity is properly treated as preempted under Federal law". After attempting to resolve the disagreement with the Massachusetts insurance regulator if the OCC continued to believe that the Massachusetts consumer protection laws should be preempted, Congress explicitly provided the remedy – an expedited and equalized dispute resolution with neither side given unequal deference. Accordingly, to the extent the OCC has any legal authority to argue against a State law or regulation, it should seek to overturn the offensive State provision in court, not to urge noncompliance by banks through unilateral opinion letters.

It is neither my intent nor my desire to comment on the appropriateness of the Massachusetts consumer protection laws, nor to consider whether they are similar to the safe harbor protections of GLBA or would alternatively prevent or significantly interfere with a national bank's insurance activities. These are questions to be worked out together by the appropriate regulators in the proper forums. Rather, I am trying to unequivocally express my discontent with the Comptroller's misinterpretation and misapplication of the GLBA standards and our Congressional intent.

Please contact me directly to inform me of the Department's efforts to ensure that the Comptroller coordinates with the Massachusetts insurance regulators to resolve this issue, and what further actions the Comptroller plans to undertake on this issue consistent with the requirements and clear intention of the GLBA. In addition, please ensure that the Comptroller informs this Committee before issuing any further opinion letters preempting State insurance laws, including a description of his efforts to resolve the issue directly with the appropriate insurance regulators.

Yours truly,

Michael G. Oxley
Chairman
Committee on Financial Services

MGO/rg

RESPONSE TO WRITTEN QUESTIONS OF SENATOR MILLER FROM TOM MURPHY

Q.1 As you know Georgia has allowed one State-chartered bank to offer real estate brokerage and management services. We have heard anecdotally that the local REALTORS® have found it useful because the bank has placed its properties on the multilist and the REALTORS® have more properties to sell. Don't you think this is a good thing?

A.1 Although we have no research to indicate the Georgia experience, it is true that the Georgia REALTORS® and bankers agreed to withhold any further State bank applications to perform real estate brokerage until it is decided on the Federal level. This is another reason why Congress should act on S. 1839, the Community Choice in Real Estate Act. It can be argued that Georgia State-chartered banks would be better served if huge national megabanks were not granted real estate powers. These State-chartered banks have very good business relationships with local real estate offices, and would be able to continue that practice under existing law. Entrance of the banking conglomerates would also unfairly squeeze the State bank markets.

Q.2. What aspects of the activities that your opponents are claiming to be "financial" or "incidental to a financial activity" do you specifically disagree with?

A.2. Banks claim that real estate brokerage, leasing, and management are financial activities or are incidental to a financial activity. The business of brokering, leasing, or managing real estate does not involve lending. It is financing the mortgage that facilitates the transfer of real property that involves lending. More than 20 percent of residential home purchases involve no lender financing whatsoever. If anything, the mortgage is incidental to the real estate sale, not the other way around. Real estate is better compared to a retail department store that provides consumer products to its customers. If the department store has a credit card, does that make the department store a bank because the credit card involves financing?

Q.3. What is your response to the position that The Realty Alliance, representing 45 member firms, has taken against your efforts? [The NAR is roughly 12 times the size of The Realty Alliance. However the NAR only represents about 40 percent of all those with a real estate licenses—though not all of the two million license holders are practicing.]

A.3. The Realty Alliance and the National Association of REALTORS® are two different associations. The Realty Alliance is an organization of 45 independent real estate broker-owners. The Realty Alliance itself has members who do not share that organization's position. (see attached Op-ed from Lennox Scott, member of Realty Alliance)

The National Association of REALTORS® is an organization of 810,000 members that includes real estate broker-owners, brokers, and agents. The National Association also has affiliates that have their own membership that practice real estate specialties, all of

which require a real estate license. (see written testimony chart on support for NAR position)

Q.4. How can banks restrict themselves from "product packing," their clients believing that they must use a bank for all available services to receive easier credit approval or lower financing rates? What is to stop FHC salary-based real estate representatives from tying in other bank products? [Real estate firms have RESPA requirements which force them to have clients sign disclosure statements that ensure understanding that real estate lending partners do not *have* to be used, and that the customer is free to shop around for a better deal.]

A.4. It seems inconceivable that banks would restrict themselves from product packing, despite the existence of antitying provisions. Even Fed Chairman Alan Greenspan made a critical point during hearings on Gramm-Leach-Bliley: Firewalls leak and in today's closely integrated financial institutions they leak quickly. Chairman Greenspan had the "Asian contagion" fear in mind when making these comments. Given the failure of the Japanese universal banking system these comments were well founded. The whole point in banks getting these additional authorities is to cross sell their proprietary products. Banks call this "one-stop" shopping. We call it "one-bank" shopping. Banks do not have an agency relationship with their customers. Banks necessarily will promote their bank and financial products to the exclusion of any competitive products. That is the nature of banking. The business of banking requires capturing customers for proprietary product and service sales. Real estate brokers and agents have a completely different relationship with their clients based on an agency relationship and the unique nature of selling and marketing real estate. Their only goal is to assist in the marketing or purchase of their client's real estate. Although they may recommend ancillary services, their only compensation comes from the completion of that transaction. Thus their motivations are completely different from a banker's. A real estate agent's sole obligation is to their client.

To:
Joann Byrd
Seattle Post-Intelligencer
Editorial Page Editor

From:
J. Lennox Scott
Chairman & CEO
John L. Scott Real Estate

April 30, 2002

Since January of 2001, the Federal Reserve Board and Treasury Department have been working to enact a regulation that would allow big banking conglomerates to enter the real estate business, thus enabling them to provide real estate services. To those in the real estate industry this has become known as 'The Big Grab'.

As an independent business owner and real estate professional, I adamantly oppose this proposed regulation. It has far-reaching ramifications for independent business owners in all industries across the nation. I will explain.

The argument between the banks and the real estate industry lies within the question of whether or not real estate services are considered financial in nature, therefore making them "incidental" as a financial activity. This statement is open to broad interpretation, which is what allowed banking interests to put the proposal on the Federal Reserve Board's agenda. According to current legislation, the only way that banks can enter into real estate is if the Federal Reserve Board and Treasury Department define real estate services as "financial services" rather than "commercial services."

I strongly argue that real estate is strictly a commercial business transaction, which focuses on customer—not financial—service. The real estate profession is built upon trust, honesty and integrity. Customers look to us to be their advocate and they entrust us with their most expensive asset—their home. Our very success relies upon providing our clients with valuable services, none of which are directly financial in nature. The overall real estate transaction is very extensive and the financial aspect is only a component of the entire transaction—it does not define it.

Banking interests have already proposed this action to Congress, who has stated three times in the past three years that banks should not be in the real estate business. Now they are trying to circumvent the clear intent of Congress by approaching the Federal Reserve Board and Treasury Department.

The issue at hand has nothing to do with competition, but rather it's about the fact that banks should not be allowed to operate in any commercial transaction-type industries, such as real estate, when they benefit from taxpayer-insured operations. It is equal to having a federally chartered monopoly because they gain huge financial advantages through federal banking. Not only do they receive federal deposit insurance, they also have favorable tax treatment and privileged access to credit. Additionally, banks have ready access to information pertaining to the credit history of nearly every American. If bankers were allowed to operate real estate services, there would be a clear conflict of interest, of which we would all feel the effects—not just REALTORS®.

This past week the REALTORS won an important victory in our campaign to keep the nation's banks from entering our industry thanks to the determination and conviction of hundreds of thousands of REALTORS and consumers. We have delivered such a powerful and compelling message to Washington

that Treasury Secretary Paul O'Neill announced that he would delay a decision on the regulation until next year because of the tremendous public controversy it has generated.

Last week, the REALTORS were also able to get more than half the members of the House of Representatives to co-sponsor H.R. 3424, the Community Choice in Real Estate Act, to prevent this power grab. In light of the overwhelming public congressional opposition, National Association of REALTORS president Martin Edwards, Jr. has asked the banking lobby to back down and give up on their power grab.

Ultimately, the deciding factor comes down to this: real estate brokerage is not a financial service. We are professionals who provide the home buying community with valuable customer support and service. If the Federal Reserve Board and Treasury Department validate banking interests in 2003, the way will be cleared for future expansion into anything banks finance, threatening independent businesses of every sector all across the United States.

About J. Lennox Scott

J. Lennox Scott is Chairman and CEO of John L. Scott Real Estate. John L. Scott has 112 offices with over 2,800 sales associates in the states of Washington, Oregon and Idaho. Last year John L. Scott closed over 42,000 transactions for more than 8.2 billion dollars in volume and is ranked as the 4th largest regional real estate company in the United States.

Lennox is the third generation to run the family business, which was founded in 1931 by his grandfather. He began in the real estate industry in 1976, taking over as president of the company in 1980. Lennox has been recognized by *REALTOR® Magazine* as one of the nation's Top 25 Most Influential People in Real Estate. He has also been honored as one of the Top 5 Most Admired Individuals in Real Estate in the nation, by *REAL Trends*. Most recently, Lennox was appointed to the Executive Committee for the National Association of REALTORS®.

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For More Information Contact:
Shelley Rossi
Director of Public Relations
John L. Scott Real Estate
206-230-7627 (phone)
206-230-7601 (fax)
shelleyro@johnlscott.com

RESPONSE TO WRITTEN QUESTIONS OF SENATOR REED FROM JAMES E. SMITH

Q.1. During consideration of the Gramm-Leach-Bliley Act in 1999, was the banking industry pushing to have real estate brokerage and management services considered as financial activities? Although real estate sales and development were explicitly prohibited by the Act, why do you believe that the Fed and the Treasury were correct in promulgating rules that would make brokerage and management activities "financial in nature," or "incidental to financial services?"

A.1. There was no attempt to incorporate specific "financial in nature" activities in the statute other than the securities and insurance activities that are included. Congress recognized the dynamic nature of the financial services industry and designed a statute that could evolve with the industry. Accordingly, the Gramm-Leach-Bliley Act (GLBA) provides a flexible regulatory framework to make certain that the new statute would resist obsolescence and adapt to innovations in the marketplace. That framework grants the Federal Reserve and Treasury Department the authority to determine whether future activities are financial in nature. Furthermore, GLBA provides that financial subsidiaries of national banks should be prohibited only from engaging in real estate *development* activities—the riskier aspect of the business in which the banking organization takes an ownership position. Had Congress intended to prevent banking organizations from engaging in the agency activities of real estate brokerage and real estate management, it clearly knew how to do so. The fact that Congress chose only to prohibit real estate development leads to the conclusion that Congress did not intend to restrict real estate agency activities.

Q.2. Do you believe, should banks be allowed to enter into these new activities, that they should be held to a higher standard? In other words, that the Community Reinvestment Act should apply to other affiliates of the bank, such as real estate brokerage and management parts, in addition to the deposit-taking part of the bank?

A.2. Approval of the proposed rule would actually enhance a bank's ability to assist low-income and minority communities. Since banks are subject to the Community Reinvestment Act (CRA), they have every incentive to use the real estate authorities to further their outreach to communities. The banks would provide real estate services to areas that are currently underserved in this respect and could use the combination of real estate and bank services to better serve their low-income and minority communities. Moreover, if the real estate agency were a subsidiary of a national bank, that subsidiary would be covered by CRA. On the other hand, nonbank-affiliated mortgage companies, such as those affiliated with real estate companies, have no CRA or other obligation to low-income communities. Moveover, an institution's record of compliance with CRA already is a consideration pursuant to GLBA. That is, all insured depository institutions of a holding company must have a "satisfactory" or better CRA rating in order to engage in new financial activities. With respect to requiring affiliates of the bank to comply with CRA, we believe that directly subjecting a real estate

affiliate of a bank to CRA would place them at a competitive disadvantage to nonaffiliated real estate agencies that are not subject to CRA requirements.

Q.3. Do you believe that as part of the regulation being considered by the Fed and the Treasury, there should be a strict firewall between the deposit-taking part of the bank and the real estate brokerage part, similar to those State laws enacted in the context of insurance sales by a bank?

A.3. The proposed rule provides that real estate brokerage activities must be conducted through a subsidiary or affiliate and not the bank itself. Furthermore, all State licensing, qualification, sales practices, and continuing education requirements would apply to bank-affiliated real estate agents. Thus, similar to the situation with insurance agency activities, bank-affiliated agents would be subject to the same sales practice requirements as those agents not affiliated with banks. In addition, banks are subject to Sections 23A and 23B of the Federal Reserve Act, which limit the amount of credit and other forms of support that a bank could provide to a real estate brokerage affiliate or subsidiary. Consumers have even more protections when their real estate agent is affiliated with a banking organization because banks and bank holding compamies are subject to the antitying provisions of the Bank Holding Company Act. These restrictions prohibit banks and their affiliates from conditioning the provision of credit on the purchase of another product or service.

Q.4. As part of the ongoing discussion of this issue, some people have cited the fact that there are numerous real estate companies and brokerages that conduct services that are currently defined as traditional banking activities, such as mortgage lending and title insurance. Why do you feel this situation is different than one allowing banks to get into some traditional banking activities, such as brokerage and management? In fact, don't some State banks, thrifts, and credit unions already engage in real estate brokerage activities? How is this case different than national banks entering into this arena?

A.4. This question recognizes an important point in this debate: real estate companies, such as Long & Foster, Century 21, and Prudential, provide end-to-end services for the home purchasing process, including real estate brokerage, mortgage, and insurance services. It is ironic that the National Association of REALTORS® is now objecting to the very combinations that their members have undertaken—offering brokerage, mortgage banking, and, often, insurance under one roof. Furthermore, in 26 States, State banking regulators have the authority to allow State-chartered banking organizations to engage in real estate brokerage activities. In addition, savings institutions and credit unions already have brokerage authority. Restricting national bank subsidiaries and financial holding companies from offering the same end-to-end combination of real estate services and mortgage lending places them at a tremendous competitive disadvantage. We lose not just an opportunity in the brokerage field, but also the opportunity to interact with the customer in the first place and to offer one of the most traditional of banking products—the mortgage loan.

RESPONSE TO WRITTEN QUESTIONS OF SENATOR MILLER FROM JAMES E. SMITH

Q.1. Aren't there already in place antitying provisions that would prohibit a bank from offering favorable loan terms to its real estate affiliate?

A.1. Yes. Sections 23A and 23B of the Federal Reserve Act would limit the amount of credit and other forms of support that a bank could provide to a real estate brokerage affiliate or subsidiary. Consumers have even more protections when their real estate agent is affiliated with a banking organization because banks and bank holding companies are subject to the antitying provisions of the Bank Holding Company Act. These restrictions prohibit banks and their affiliates from conditioning the provision of credit on the purchase of another product or service.

Q.2. Why do you not think banks will have an unfair advantage after new proposed regulations are enacted? Others claim that Government subsidies (for example deposit insurance) as well the "deep pockets" of your institutions will allow for an unfair advantage that would create an opportunity for FHC's to exploit the market—perhaps going as far as using your subsidies to provide below-market prices?

A.2. The subject of whether deposit insurance and the Federal Reserve's discount window provide a competitive advantage to banks was fully debated during discussions that ultimately led to the Gramm-Leach-Bliley Act of 1999. Testimony and statements at that time from Federal banking regulators (Office of the Comptroller of the Currency (OCC)[1] and Federal Deposit Insurance Corporation (FDIC))[2] and other experts[3] support the conclusion that no subsidy exists in the Government's provision of services to banks. If a subsidy existed, banks would be expected to dominate in businesses where they compete directly with nonbanks. In fact, banks have been losing market share in terms of both assets and household savings since the 1970's. The mortgage markets provide the most striking example of how the market has shifted away from depository institutions. The reason for this shift is the secondary market—not insured deposits—has become the most cost-efficient way to fund most mortgages. Investor demand is so great for mortgage-backed securities that mortgage banks have access to the lowest-cost funds available in the world. Traditional deposit-based lenders—who pay for deposit insurance and face a host of regulatory expenses like higher capital requirements, exam costs, and CRA—are often bypassed completely. If banks enjoyed a subsidy, nondepository institutions would not control an ever-increasing market share.

Q.3. Why do you not think banks will have a conflict-of-interest situation, with either lending favorable loans to their affiliates, or

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[1] "The Competitive Implications of Safety Net-Related Subsidies," Gary Whalen, Economics Working Paper 97–9, OCC, May 1997.

[2] Testimony by Ricki Helfer, Chairman, FDIC, before the House Committee on Banking and Financial Services, March 5, 1997.

[3] "Federal Subsidies in Banking: The Link to Financial Modernization," Frederick Furlong, *Federal Reserve Bank of San Francisco Economic Letter,* number 97–31, October 24, 1997.

"The Battle for Bank Regulatory Supremacy," Carter Golembe, *The Golembe Reports,* volume 1997–2 (March 1997).

even going as far as not lending to nonaffiliated firms—essentially to your competitors?

A.3. Banking organizations are subject to Sections 23A and 23B of the Federal Reserve Act, which limit the amount of credit and other forms of support that a bank could provide to a real estate brokerage affiliate or subsidiary. Such limits ensure that the safety and soundness of the bank will not be negatively impacted by its subsidiaries or affiliates. Moreover, the exact same potential for such conflicts exists today given that a number of real estate firms such as Century 21, Coldwell Banker, ERA, and Long & Foster all offer mortgages to homebuyers. Although these integrated real estate organizations, as well as State banks in many States, savings institutions, and credit unions, have been selling real estate and funding mortgages for years, conflicts of interest has not been a problem. The Real Estate Settlement Procedures Act (RESPA) addresses such conflicts (explained in further detail below).

Q.4. What aspects of "banking" that real estate agencies currently have access do you think give them an unfair advantage?

A.4. Real estate companies, such as Long & Foster, Century 21, and Prudential, provide end-to-end services for the home purchasing process, including real estate brokerage, mortgage, and insurance services. It is ironic that the National Association of REALTORS® is now objecting to the very combinations that their members have undertaken—offering brokerage, mortgage banking, and, often, insurance under one roof. Such combination of services provides valuable cost, convenience, and service options for customers. All banks should have the opportunity to compete in the same manner as the real estate companies.

Q.5. How can banks restrict themselves from "product packing," their clients believing that they must use a bank for all available services to receive easier credit approval or lower financing rates? What is to stop FHC salary-based real estate representatives from tying in other bank products?

A.5. First, as explained in the first question, banks and bank-holding companies are subject to the antitying provisions of the Bank Holding Company Act. Second, RESPA applies to banks in the same manner as it applies to real estate firms. Specifically, RESPA requires REALTORS® affiliated with lenders to disclose that fact to customers before the purchase occurs. The RESPA disclosure, which must be on a separate piece of paper, must state the relationship between the real estate agent and the lender and provide the estimated charges or range of charges of the lender. It must also notify the customer that he or she is not required to use the lender and is free to shop around for a better deal.

STATEMENT OF THE AMERICAN HOMEOWNERS GRASSROOTS ALLIANCE

The American Homeowners Grassroots Alliance (AHGA) is a national bipartisan advocacy organization representing the Nation's 70 million homeowners. AHGA believes that preserving and enhancing homeownership should be a national policy priority. AHGA believes that homeowners and homeownership are generally benefited by domestic and international free market policies.

AHGA has carefully reviewed policy documents and testimony from the real estate, lending sectors, and other sources on the issue of allowing banking organizations to be involved in real estate brokerage. From the consumer perspective there are significant potential benefits of such a policy. Those benefits clearly outweigh the limited potential risks. Also, a substantial majority of consumers would like the option of "one-stop" shopping for real estate services. For these reasons AHGA believes that consumers will benefit if banking organizations are involved in real estate brokerage and urges Congress to support the entry of banks into this market.

Opponents argue that because banks lack the invaluable experience in local real estate markets and the in-depth knowledge of real estate law, consumers will suffer. While it is true that most banks currently do not have core real estate brokerage competencies, both experience and common sense suggest it is unlikely that consumers will suffer. Companies in the banking and real estate sector have successfully entered each other's markets without serious problems. Federal savings institutions, credit unions nationwide, and commercial banks in about half of the States have had the ability to engage in real estate brokerage for a number of years. Many real estate companies, including Long & Foster, Century 21, and Coldwell Banker and many others currently provide brokerage, mortgage lending, title insurance, and property insurance. Consumers have substantial protection in the fact that real estate practice is heavily regulated, and State licensing requirements establish minimum competencies that all participants must demonstrate. Rather than build those competencies from scratch, it is likely that many banks will enter the real estate brokerage market through partnerships with or the acquisition of small local real estate agencies that have substantial experience in their real estate markets and in-depth knowledge of real estate law. Another argument against permitting banks to enter real estate brokerage is that it will accelerate the consolidation process currently underway in both the real estate and lending sectors. This would reduce competition and increase costs to consumers. This is not a strong argument either. Other larger economic factors are driving the consolidation that will almost certainly continue in banking and real estate (and many other sectors as well), whether or not banks are allowed to enter real estate brokerage. AHGA believes that any contribution of this new policy to the consolidation process will be small. If banks are permitted to enter real estate brokerage the most visible difference will likely be that banks instead will purchase some of the small real estate brokerages that would otherwise be purchased by large real estate brokers. Because there will be more bidders the small independent brokers will benefit from higher selling prices when they sell their businesses. Fortunately there are a very large number of existing competitors in both sectors, so it would take many years before consolidation reduces the number of competitors in either sector to the point that any company or small group of companies could override market forces in determining prices of banking and real estate services. If and when we ever reach the point that market forces do not prevail in setting real estate service prices and lending prices and rates, U.S. antitrust laws are available to stop anticompetitive behavior.

Last, opponents argue that permitting banks to enter real estate brokerage creates a conflict of interest in that a lender owning a real estate brokerage will try to sell follow-on products or services to its clients its other services, and in many cases those products or services will not represent the best value for the consumer. Most consumers recognize that the products or services of only a few companies in a given industry can represent the very best value for a particular consumer. They also recognize that the consumer is in the best position to determine his or her needs and priorities and it is the consumer's responsibility to sort out which products or services represent the best value. Cross-selling of follow-on products is a very common practice in many sectors, and the products and services a company seeks to cross-sell are no different with respect to their potential fit to a consumer's needs that the product or service that attracted the consumer in the first place. AHGA believes that most consumers are sophisticated enough to recognize that any company's follow-on products or services also may or may not be the best value for the consumer and act accordingly. There is therefore no greater conflict of interest between a consumer and business regarding a follow-on product or services or the product or service that attracted the customer in the first place. Most consumers

do a lot of research regarding competing real estate and mortgage lending services before buying, selling, or financing a home. There is a wealth of free, inexpensive information that is available to consumers on those subjects from a wide range of sources, including AHGA's sister education and research organization, the American Homeowners Foundation (*AmericanHomeowners.org*). Almost every source strongly urges consumers to comparison-shop every major component of real estate services.

There are several arguments in favor of permitting banks to enter real estate brokerage. Businesses cross-sell because it is more efficient way to market, for example the costs are lower. In a competitive marketplace a share of marketing cost savings will inevitably be passed on to consumers in the form of lower fees and/or rates. In addition to potentially saving homeowners money, the closer coordination of home brokerage and lending services under one roof also potentially reduces the time between purchase and settlement, which can often be very important to consumers as well. These likely cost and time savings are a substantial potential consumer benefit. They would indirectly benefit individual real estate agents, because they will get their commissions sooner and the reduced costs and time savings will likely mean more homebuyers and sellers. Consumers are very concerned about the protection of their financial and other personal data. Currently RESPA requires that all real estate companies and banks provide disclosure notice to the customer of multiple services offered by affiliated firms. In addition banks are currently subject to greater privacy regulation than real estate companies. The current regulatory proposal to allow banks to enter the real estate brokerage requires real estate brokers to provide greater protection to the privacy of consumer data. Consumers support this requirement and will benefit from greater protection. One-stop shopping is by itself a substantial benefit to many time-starved consumers. Many homebuyers are couples with two demanding jobs and often more demanding children. We believe many of those homebuyers consciously and intentionally trade convenience for economy in many decisions. They make that choice with full awareness that they will likely be forgoing a better offer if they took the time to shop around.

From a policy standpoint the question is whether Federal legislators should deny consumers this freedom of choice, and if so, what is the appropriate alternative. While AHGA strongly encourages consumers to take the time to shop competitively for all real estate and financing services, AHGA also believes consumers have the right to make their own choice. In addition, recent home sellers favor allowing banks to offer real estate brokerage by a 2 to 1 margin according to a 2001 survey.

For this reason AHGA urges Members of Congress to oppose S. 1839 and H.R. 3424. If Congress concludes that the risks of permitting banking organizations to be involved in real estate brokerage outweighed the benefits, then consistency would require that Federal savings institutions, credit unions nationwide, and commercial banks in several States that engage in real estate brokerage to divest themselves of their real estate businesses. Since the primary arguments against the bank's market expansion go to core competencies and potential conflicts of interest, then conversely the many real estate companies that currently provide mortgage lending should also be required to divest themselves of their real estate lending businesses. While these steps would apply the principles contained in S. 1839 and H.R. 3424 on a consistent basis, it would deny many consumers what they want—one-stop shopping. If Congress truly believes action is necessary to protect consumers it would be more effective to require consumers to meet some minimum level of due diligence before entering a real estate or lending transaction (for example demonstrating that they have interviewed three real estate agents before listing a home, looked at three houses before making an offer to buy a house, or considered three lenders before applying for a loan). However as previously stated AHGA believes this would be too much of a restriction of personal choice. In deciding whether to support real estate companies or bankers on this contentious issue, AHGA recommends that Congress choose the side consumers. Congress can best serve consumers by supporting the implementation of regulations to permit banking organizations to be involved in real estate brokerage.

The American Homeowners Grassroots Alliance (AHGA) is a national bipartisan advocacy organization representing the Nation's 70 million homeowners. AHGA believes that policies that encourage and protect homeownership are in our national best interest. Those policies encourage and sustain the maintenance of a strong and broad middle class, build a sense of community and responsibility, and facilitate investment in homes, which are the largest, most universal savings/equity-building vehicle for most Americans. AHGA's positions and more information about the organization are available at *www.AmericanHomeowners.org*. The American Homeowners Foundation's section of the website also contains free educational materials to help homeowners and future homeowners buy, sell, remodel, and finance their homes.

STATEMENT* OF THE FINANCIAL SERVICES ROUNDTABLE

MAY 23, 2002

The Financial Services Roundtable ("Roundtable") appreciates the opportunity to submit testimony on the proposal by the Federal Reserve Board ("Board") and Treasury to allow greater competition in the real estate brokerage industry by permitting financial holding companies and national bank subsidiaries to enter the business. The Roundtable represents 100 of the largest integrated financial services companies providing banking, insurance, and investment products and services to the American consumer. Member companies participate through the chief executive officer and other senior executives nominated by the CEO.

Roundtable member companies provide fuel for America's economic engine, accounting directly for $12.4 trillion in managed assets, $561 billion in revenue, and 1.8 million jobs.

The Roundtable strongly opposes the Community Choice in Real Estate Act (S. 1839 and H.R. 3424). Despite its name, the Act would limit the ability of consumers to choose the real estate agent or broker of their choice, and would artificially restrain competition in the brokerage industry. As a result, the Act would harm both consumers and the financial services industry.

S. 1839 would prohibit the Board and the Treasury from completing the administrative rulemaking process required by the Gramm-Leach-Bliley Act. (the GLB Act) and from ruling—if the statutory factors are met—that real estate brokerage and real estate management are "financial in nature" and therefore permissible for financial holding companies and national bank subsidiaries.

The Roundtable believes that the Board and the Treasury should be allowed to complete the rulemaking process. In addition, the Roundtable believes that the Board and Treasury should ultimately rule that real estate brokerage is a permissible activity, for several reasons. First, permitting financial holding companies to enter the real estate brokerage business is good for consumers. Second, it is good for the financial services industry. Third, real estate brokerage is a financial activity consistent with the Gramm-Leach-Bliley Act.

Consumers Will Benefit From the Proposed Rule

The Roundtable strongly believes that consumers will be the real winners if the proposed regulation is adopted. Adoption of the rule will increase competition in the brokerage industry. More competition means more consumer choice, lower prices, and better customer service.

Adoption of the regulation is necessary to meet the demands of consumers for one-stop shopping for all their homebuying needs. In 1999, a study of recent homebuyers was conducted on behalf of the National Association of REALTORS® (NAR). (See Attachment A). According to this NAR study, 76 percent of homebuyers said that getting all or some of their homebuying services handled through one company was appealing. Eighty-one percent supported the idea of one-stop shopping for all of their homebuying services and were evenly split on whether the best provider of such services would be a bank, a REALTOR®, or a mortgage company, although a slight majority stated they would prefer a bank as the one-stop shopping provider. The NAR study concluded that 77 percent would consider using a bank for those one-stop shopping services in future transactions.

If the proposed regulation is adopted, consumers will be able to receive in one location all the services necessary to buy a home: preapproval for a mortgage loan; assistance in finding a home; a mortgage loan after a contract to purchase a home has been signed; and insurance for the property (including title insurance, property insurance, and private mortgage insurance) prior to closing. The consumer's life will be simplified and services will be expedited. Many traditional real estate brokers already have responded to consumer demand for one-stop shopping and are offering mortgage and, insurance services in addition to real estate brokerage services.

Proponents of the Community Choice in Real Estate Act oppose letting financial holding companies compete in the real estate brokerage business. They argue that consumers are worried about their privacy when purchasing a home, and that letting financial holding companies compete would hurt consumer privacy. Concluding that brokerage is a financial activity in fact greatly enhances consumer privacy. While customers of financial holding companies and national banks are entitled to the GLB Act's far-reaching privacy protections, customers of real estate brokers currently have no Federal privacy protections.

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*Due to size and quality of attachments, they will be held in Senate Banking Committee files.

If adopted, the Board/Treasury regulation will afford brokerage customers the same Federal privacy protections now afforded to bank customers: real estate brokers will have to disclose their privacy policies to homebuyers and will be prohibited from sharing certain nonpublic information about the homebuyer with any nonaffiliated third parties unless the homebuyer has been given notice and the opportunity to opt-out of such information sharing. Ironically, enactment of S. 1839 would in effect harm consumers by depriving them of the Federal privacy protections currently afforded the consumers in other sensitive financial transactions.

Proponents of S. 1839 also argue that allowing financial holding companies to offer real estate brokerage services could result in harmful tying and other coercive practices. This argument is easily refuted by the fact that many brokerages are already affiliated with mortgage lenders, insurers, thrifts, credit unions, and State banks, and there is no evidence of these harmful practices occurring. Moreover, existing banking laws are more than adequate to preclude these types of practices within a financial holding company. Sections 23A and 23B of the Federal Reserve Act prohibit a bank from making below-market loans to any affiliates or subsidiaries, including those that would be engaged in real estate brokerage, and severely restrict a bank's ability to provide equity contributions and other support to the real estate brokerage affiliate.[1] Furthermore, Section 8 of the Real Estate Settlement Procedures Act[2] and the antitying provisions of Section 106 of the Bank Holding Company Act Amendments of 1970[3] preclude any coercive practices against the bank's (or brokerage's) customers. In fact, a customer dealing with a brokerage affiliated with a bank will enjoy far greater consumer protection than if he or she were dealing with a real estate brokerage firm not affiliated with a bank.

The Financial Services Industry Will Benefit From the Proposed Rule

Adoption of the regulation is prudent for the financial services industry. Traditional real estate brokers are now actively competing with banks and financial holding companies by offering financial services—in particular, loans and insurance. Of the 10 leading real estate brokers cited by *REALTOR*® magazine, nine provide financial services and compete with financial holding companies by offering loans or insurance. According to the "1999 National Association of REALTORS® Profile of Real Estate Firms," 56 percent of its residential real estate brokerage firms with more than 50 agents are involved in mortgage lending. (See Attachment B).

Additionally, Federal thrifts[4] and credit unions,[5] as well as State-chartered banks in 26 States, are permitted to act as real estate brokers. (See Attachment C for data on the States). In fact, the only financial institutions that uniformly cannot engage in real estate brokerage are financial holding companies and national banks. The Roundtable asks only that more competition be allowed by permitting financial holding companies and national bank subsidiaries to offer these services as well.

NAR argues that permitting financial holding companies to engage in real estate brokerage would create an unlevel playing field due to alleged "Federally chartered advantages." NAR contends, without support, that Federal deposit insurance and access to the Federal Reserve system, for example, creates "Federal subsidies" enjoyed by depository institutions which give banks an unfair advantage. NAR further alleges that the proposed regulation would result in an unsafe and unsound banking system.

Brokerage poses very little risk to the banking system. A real estate brokerage company does not act "as principal," but rather acts in an "agency" capacity by being an intermediary in a transaction between a buyer and a seller. Banks have historically been permitted to conduct "agency" activities either directly or through affiliates. Financial holding companies are currently permitted to provide their customers with a wide array of agency services, including travel, securities, commodities, and insurance brokerage.

Any Federal subsidy is far outweighed by the heightened regulatory burden and cost of supervision borne by depository institutions. The proposed regulation would permit real estate brokerage only in nonbank affiliates and financial subsidiaries—entities which, by law, are firewalled away from their affiliated depository institutions and therefore cannot enjoy any such alleged "Federal subsidy." In any event, NAR's contention that the proposal would result in an unsafe and unsound banking system has not been evidenced in the 26 States that currently permit real estate brokerage by banks, or by the thrift, or credit union industries.

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[1] *See* 12 U.S.C. §§371c, 371c–1 and 1828(j).
[2] 12 U.S.C. §2607.
[3] 12 U.S.C. §1971, *et seq.*
[4] *See* 12 CFR §§559.4(e)(3) (thrift service corporations), 584.2–1(b)(8) (thrift affiliates).
[5] *See* 12 CFR §712.5(g) and (p).

There is no evidence that consumers have been hurt in any way by the current involvement of these depository institutions in the real estate brokerage industry, and there is no evidence that depository institutions in these markets dominate the brokerage industry or enjoy significant market power. Prohibiting real estate brokers from affiliating with financial holding companies seems to be out of step with the current marketplace. The most vocal proponent of the Act—NAR—does not speak for the entire real estate industry. The Realty Alliance, a real estate brokerage trade organization with over 62,000 members (most of whom are also members of NAR), publicly opposes NAR's efforts. (See Attachment D for a copy of a White Paper delivered by The Realty Alliance to the NAR). The Realty Alliance, like the financial services industry, welcomes increased competition and recognizes the potential benefits to consumers that the regulation could bring.

Real Estate Brokerage is a Financial Transaction Consistent with the Gramm-Leach-Bliley Act

Finally, the Roundtable believes that the proposed regulation is entirely consistent with the GLB Act which was designed to modernize and expand the financial services marketplace. The specific purpose of financial modernization, as stated in the preamble to the GLB Act, was to "*enhance competition in the financial services industry* by providing a prudent framework for the affiliation of banks, securities firms, insurance companies, and *other financial service providers,* and for other purposes." [emphasis added].

Title I of the GLB Act created the "financial holding company" structure and permitted financial holding companies to conduct a much broader range of financial activities than was historically permissible for bank holding companies. The GLB Act permits financial holding companies to engage in all activities that have been determined by the Federal Reserve Board to be "financial in nature," or incidental or complementary to a financial activity.[6] Given the historical experience of the Glass-Steagall Act and the practical limitations of creating a rigid regulatory structure, the GLB Act established a flexible framework that allows regulators to respond to changes in technology, the marketplace, and consumer demand. The GLB Act provides the Board, in consultation with Treasury, the authority to expand the statutory list of financial activities.[7]

Consistent with Congress' directive and following the request of the American Bankers Association, the Roundtable, and others, the Board and Treasury issued a joint notice of proposed rulemaking in December 2000 to determine that real estate brokerage and real estate management activities are "financial in nature" or "incidental to a financial activity" and, consequently, permissible for financial holding companies and national bank subsidiaries. By issuing this proposal, the agencies were simply fulfilling their obligation under the GLB Act to ensure that financial holding companies and national banks have the ability to compete with other financial service providers. In doing so, the Board and Treasury have followed the objective rulemaking process contemplated by the GLB Act and have sought public comments on the rule. We ask that the Board and Treasury be allowed to continue their deliberative process.

The broader scope of the "financial in nature" standard for nonbank activities of financial holding companies is reflected in both the legislative history of the GLB Act and the diverse range of activities that financial holding companies are currently permitted to conduct. First, the Conference Report to the GLB Act states that "[p]ermitting banks to affiliate with firms engaged in financial activities represents a significant expansion from the current requirement that bank affiliates may engage only in activities that are closely related to banking."[8] Second, financial holding companies are currently permitted to conduct a broad range of activities that bank holding companies are prohibited from conducting, such as unrestricted securities underwriting, merchant banking, unrestricted insurance underwriting, unrestricted insurance agency, travel agency, and acting as finder.[9] The financial services marketplace has changed dramatically in the past 30 years, and what may have been inappropriate for bank holding companies in the early 1970's may be entirely appropriate for the diversified financial holding companies of the early 21st century.

With respect to the permissibility of real estate brokerage under the GLB Act, the GLB Act permits the Board to define certain activities as "financial in nature," including "transferring . . . for others financial assets other than money or securities." The Roundtable believes that real estate brokerage is exactly that type of ac-

[6] *See* Bank Holding Company Act § 4(k)(1)(A), (B) (12 U.S.C. § 1843(k)(1)(A), (B)).
[7] *See* Bank Holding Company Act § 4(k) (12 U.S.C. § 1843(k)).
[8] H.R. Conference Report No. 106–434, at 153 (November 2, 1999).
[9] *See* BHCA § 4(k)(4) (12 U.S.C. § 1843(k)(4)); 12 CFR § 225.86(d)(1) (finder activities).

tivity. Real estate is the largest financial asset owned by most consumers and is the most widely used source of collateral for consumers seeking credit. The purchase of real estate is the largest financial transaction for most consumers. For many, real estate is the largest source of individual wealth; the decision to purchase, sell, and finance real estate plays a significant part in retirement planning. Real estate is conferred special status under Federal and State tax laws, distinguishing real estate from other large-ticket items. For these reasons, we believe that real estate is a "financial asset" and that brokerage is "financial in nature."

In addition, the GLB Act defines as "financial in nature" all activities that involve "arranging, effecting, or facilitating financial transactions" for others.[10] Real estate brokerage is part of the overall financial activity of helping a consumer receive preapproval for a mortgage loan, find a home, appraise the property, receive final approval for the mortgage loan, close the transaction, and insure the home with property insurance, title insurance, and, in certain cases, private mortgage insurance. Each of the services and products offered as part of the overall financial transaction are integrated with one another. Such integration is reflected in several ways. First, consumers frequently enlist the services of a real estate broker at the same time that they seek the products of a mortgage lender and an insurance agency. Second, consumers generally pay the loan fees, the REALTOR®'s commission, and the initial insurance premiums together at the closing. Third, the documents that consumers sign with respect to the mortgage loan, real estate brokerage, and the insurance generally cross-reference and are conditioned upon each other.

In determining whether an activity is "financial in nature," the GLB Act also requires the Fed to consider "changes in the marketplace in which financial holding companies compete" and whether such activity is "necessary or appropriate" to allow a financial holding company or its affiliates to "compete effectively with any company seeking to provide financial services in the United States."[11] As highlighted earlier, approval of the regulation is both necessary and appropriate to allow financial holding companies to compete effectively with real estate brokerage companies, as well as with Federal thrifts, credit unions, and State banks in 26 States.

As a result, the Roundtable firmly believes that real estate brokerage is "financial in nature," consistent with the GLB Act. At the very least, the Board and Treasury should find that it is "incidental to a financial activity." Banks and financial holding companies are involved in virtually every other aspect of residential and commercial real estate transactions, ranging from rendering advice; acting as a finder; appraising the property; issuing abstracts of title and performing title searches; selling and underwriting hazard, title, and mortgage guaranty insurance; arranging or providing financing; providing loan closing, settlement, and escrow services; and securitizing mortgage loans or underwriting and selling mortgage backed securities. Clearly, acting as a real estate broker is incidental to the performance of these other real estate related services that are already considered to be "closely related to banking" or "financial in nature."

In sum, assertions that the Board and Treasury may not rule on real estate brokerage are without basis under the GLB Act. Such an interpretation of the GLB Act would chill future proposals for activities to be considered "financial in nature" and would effectively turn the clock back on financial modernization.

Conclusion

In conclusion, the Roundtable strongly supports the proposed regulation and believes that its adoption would be a win-win proposition for consumers and the financial services industry. The regulation would allow financial services companies to build alliances with real estate brokerages, creating tremendous benefits for consumers, including one-stop shopping, lower prices, more choice, and increased competition. The Community Choice in Real Estate Act is nothing but an attempt to derail the deliberative rulemaking process—thereby preserving artificial barriers to entry in the brokerage market for the purpose of preserving market share and reducing threatened competition. While NAR wants to compete in the financial services markets by making loans and selling insurance, NAR wants Congress to protect them from competition in their own backyard. For the foregoing reasons, the Roundtable opposes S. 1839 and supports the rulemaking process commenced by the Board and the Treasury in December 2000. This rulemaking process is an appropriate delegation of authority to the regulators, who have expertise and experience in this area and are fully equipped to consider all the substantive issues and make an objective ruling in the best interests of both the consumers and the industry.

Thank you for the opportunity to submit our views.

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[10] *See* Bank Holding Company Act § 4(k)(5)(B)(iii) (12 U.S.C. § 1843(k)(5)(B)(iii)).

[11] Section 103(a), new Bank Holding Company Act (BHCA) section 4(k)(3)(A)&(D)(i).

May 20, 2002

Honorable Tim Johnson
Chair, Senate Banking Subcommittee on Financial Institutions
U.S. Senate
Washington, DC 20510

Dear Chairman Johnson:

We are writing to express our support for the Judiciary Subcommittee on Commercial and Administrative Law hearing on the proposed regulation to authorize real estate brokerage, leasing and property management powers for financial holding companies and national bank subsidiaries.

As you know, we have opposed this regulation as an improper use of regulatory authority that exceeds congressional intent. The Community Choice in Real Estate Act (H.R. 3424/S.1839) was introduced on December 6, 2001 in the House and already has over 225 cosponsors. This legislation would clarify congressional intent that real estate brokerage, leasing and property management are not financial in nature or incidental to finance, and therefore the regulators do not have the authority to grant these powers to banks.

We look forward to hearing the testimony and hope this is an additional step toward enactment of the Community Choice in Real Estate Act. Thank you for your efforts to ensure that the regulatory process has been followed on this matter.

Sincerely,

CCIM Institute
Consumers Union
Institute of Real Estate Management
International Council of Shopping Centers
National Association of Auctioneers
National Association of Home Builders
National Community Reinvestment Coalition
National Fair Housing Alliance
National Association of Industrial and Office Properties

Dear Financial Institutions Subcommittee Member:

On behalf of our 800,000 members involved in all aspects of the real estate industry, I wanted to remind you of the hearing on Thursday, May 23rd, at 10 A.M. in the Financial Institutions Subcommittee, and to provide you with a few facts that may be helpful to you in advance.

As you know, NAR is supporting S. 1839, The Community Choice in Real Estate Act. This bill would clarify congressional intent that real estate brokerage, leasing and property management are commercial activities off limits to financial holding companies and national bank subsidiaries. The entry of large mega banks into real estate would cause harmful market concentration and force many of our members out of business. Once the country loses many of its independent REALTORS® there will be less choice for consumers.

Bankers argue that they will lower costs to home buyers and sellers. What they don't tell you is that by cross-subsidizing the real estate activities, they will need to make up those costs somewhere. Will that mean an increase in ATM fees, or credit card fees? Will all banking consumers end up paying higher banking fees to underwrite the real estate operations of the bank?

Did you know that:

77% of all residential real estate firms consist of a single office?
84% of all residential real estate firms are independent, not affiliated with a franchise?
92% of all REALTORS® are independent contractors?
Typical sales agents earn a gross personal income of $34,100?
97% of all sales agents work on commission?
The median age of sales agents is 50 years?
18% of residential real estate firms engage in mortgage lending, and originate less than 2% of mortgages?

We are hopeful that Thursday's hearing is another step toward enactment of the Community Choice in Real Estate Act, and that you will be able to participate. We look forward to working with you as this session of Congress continues.

Sincerely,

Martin Edwards, JR., CCIM