

Transaction Costs of Housing in India : An Analysis

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राष्ट्रीय आवास बैंक



National Housing Bank



National Housing Bank

National Housing Bank (NHB) is the apex financial institution for housing in India, wholly owned by the Reserve Bank of India. It was established in 1988 under an Act of Parliament. NHB has three main functions viz. to regulate the housing finance companies, to promote and develop the housing finance market and to provide financial assistance to housing finance institutions and others. NHB's current focus is on addressing the needs of the unserved and underserved.

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*Prepared by Business Planning & Promotion Group of
National Housing Bank,
Contributed by P K Kaul, General Manager and
Vishal Goyal, Regional Manager*

CONTENTS

Chapter No.	Title	Page No.
	Foreword	5
	Acknowledgements	7
	List of Abbreviations, Tables and Box Items	8-9
	Executive Summary	10-12
I	Introduction	13-14
II	Scope and Methodology	15-18
III	House Acquisition Components and Process	19-24
IV	Acquisition Costs in Housing	25-40
V	Key Findings	41-46
VI	Conclusions and Recommendations	47-50
	<i>Appendix A: Consumer Protection and Education in Housing Finance</i>	53-59
	<i>Appendix B: Transaction Cost in Housing : A Theoretical Framework</i>	60-62
	<i>Key References</i>	63

FOREWORD

Housing is a basic necessity of life, next only to food and clothing in importance. Apart from shelter, home ownership also serves to fulfil many other fundamental objectives, viz. raising the quality of family life in terms of health, education, sanitation, serve as an asset that can be collateralized, generating a sense of physical and emotional satisfaction and achievement. At the macro level, housing generates considerable employment and dispersed economic activity.

There has been a felt need to bring in more transparency and fairness in the process of acquisition of real estate in India, in particular, residential housing. There are a number of expenses associated with buying a house, apart from the capital cost of purchase/construction some upfront costs that are known and expected, and some which are probably not that well known or considered. More often than not, the average house buyer tends to overlook some of these costs while taking the decision to buy.

This publication is an attempt by the National Housing Bank towards providing some insights into the transaction process and the taxonomy of various costs associated with buying a house. To the best of our knowledge, this is the first such study of its kind in the public domain.

This paper is also a part of the Bank's efforts in contributing to greater informed awareness building amongst consumers. It could arguably be the first and most important component of consumer education and protection in housing. It has been commented upon by many eminent persons and more recently by the Governor, Reserve Bank of India that housing finance calls for greater transparency and fairness. As the apex financial institution for housing, NHB has initiated a slew of measures to enhance fairness and transparency in housing finance. Studies such as this are one such measure.

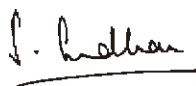
The structure of costs associated with housing transactions requires deep study in view of macro economic and individual consumer level implications. This paper brings out analytically, the known fact that various transaction costs cumulatively constitute a considerable percentage of the cost of acquisition of a house, over and above the capital costs. Some of these costs such as stamp duty, registration charges, etc are State specific. While some States have rationalized these charges in order to expand the housing market and improve affordability, some have not.

A number of recommendations have been submitted. Two merit mention here. One, the paper supports the widely held view that there is need

to put in place quickly a regulator for the real estate industry. Another that pertains to housing finance, is making it mandatory for mortgage lenders to quote an Effective Annual Rate (EAR) which is the annualized rate of interest inclusive of all charges, fees reduced to annualized figure.

We hope that this paper will make a small contribution to public policy formulation. NHB will be happy to consider action consistent with its mandate as well as carry out follow-on studies based on comments and suggestions received.

I seek valuable comments of readers.

A handwritten signature in black ink, appearing to read 'S. Sridhar', written over a horizontal line.

S. Sridhar
Chairman & Managing Director
National Housing Bank

23 May, 2007

ACKNOWLEDGEMENTS

We would like to express our sincere thanks to Ms. Jayashree Kurup, of The Times of India Group, magicbricks.com, who conducted the field study on our behalf. We would like to thank Shri V. Suresh, former CMD, HUDCO for doing a peer review of the paper. Our thanks are also due to our colleagues and others working in various organizations whom we interacted with during the course of preparation of this paper for their valuable inputs.



LIST OF ABBREVIATIONS

RBI	Reserve Bank of India
NHB	National Housing Bank
DDA	Delhi Development Authority
GDA	Ghaziabad Development Authority
HUDA	Haryana Urban Development Authority
HFC	Housing Finance Company
EMI	Equated Monthly Instalment
CML	Council of Mortgage Lenders
CREDAI	Confederation of Real Estate Developers Associations of India
EC	Encumbrance Certificate
VAT	Value Added Tax
NCR	National Capital Region
HDFC	Housing Development Finance Corporation Ltd.
L&DO	Land and Development Office

LIST OF TABLES/CHARTS

Table 1	Design of Sample of Cities
Table 2	Components of Acquisition Costs of a House
Chart 1	Supply Chain in the House Acquisition Process
Chart 2	Flow Chart of House Acquisition Process
Chart 3	Flow Chart of the Booking Process
Chart 4	Parking Charges across cities in India
Table 3	Broker Fee across Cities in India
Table 4	International Commission Rate Comparisons - Brokerage
Table 5	Stamp duty and Registration Charges across States and cities
Table 6	Capital Costs
Table 7	Transaction Costs in Housing
Table 8	Costs in the House Acquisition Process: Capital, Transaction and Financing

LIST OF BOX ITEMS

Box Item 1	Broker Commission International Experience
Box Item 2	Interest Rates on Housing Finance
Box Item 3	Legal Fee
Box Item 4	Stamp duty on mortgages
Box Item 5	Residential Mortgage Backed Securitization
Box Item 6	Introduction of a System of Mortgage Counseling (Appendix A)
Box Item 7	Promoting a Common Forum of banks and HFC's (Appendix B)

EXECUTIVE SUMMARY

Purchase of a house in India involves various costs which in the aggregate may be referred to as acquisition costs, broadly classified under the following sub-divisions:

- **Capital Costs** refer to the cost of the house including land and construction cost, apportioned cost of on-site and off-site infrastructure, parking space costs and basic interiors costs without which the house is not ready for occupation.
- **Transaction costs** which include the charges payable towards stamp duty and registration, document preparation, brokerage charges, transfer and mutation charges etc.
- **Financing charges** in case the property has been financed which would include the pre-EMI interest, loan interest, administrative and processing charges, legal and valuation fee, insurance charges etc.

Only official costs are considered in the paper.

The elements of acquiring a house in India and the transactions in the process have been analysed across 16 cities in the country (6 Tier 1 cities viz Delhi, Mumbai, Chennai, Bangalore, Hyderabad and Kolkata, 6 Tier 2 cities viz. Ahmedabad, Chandigarh, Indore, Ludhiana,

Bhubaneswar and Pune, and 4 Tier 3 cities viz. Lucknow, Kochi, Jaipur and Coimbatore).

The stakeholders through whom this process has been mapped include brokers, developers, public agencies, individual buyers, the housing finance institutions, municipal and State authorities, service providers such as lawyers, chartered accountants, and investment advisors. The data has been gathered across segments and cities through primary data collection methods mainly through personal/telephonic contact. Inherent limitations of data availability, lack of access to government data, reluctance in disclosure, however, are present.

The key findings indicate that the additional charges constitute a substantial percentage of the total acquisition cost of a house depending upon the following three parameters:

- **Source of purchase of the property** - public agency, professional developer or builder or a co-operative society.
- **Type of Purchase** - fresh allotment, re-sale or through a broker;
- **Applicable duties, taxes and charges** payable to the local authorities which can include stamp duty and registration

charges, brokerage, transfer and mutation charges etc.

Each of the above categories has different determinants and variables which are also interlinked.

The transaction costs vary considerably across these 16 cities and range between 8-28% of the capital cost of the house. The lowest transaction cost is in the Union Territory of Chandigarh (Less than 8%) and the highest in the city of Lucknow (around 28%). This is often ignored by both the consumers and the policy makers while computing house acquisition costs.

The brokerage fee which is 2% on an average of the cost of the property is competitive in India and well below global standards which vary between 2-10%.

Stamp duty and registration charges constitute the largest component of transaction cost. The stamp duty rates are extremely high as compared to global standards of 1-2% and impact costs significantly. Some of the States have rationalized the stamp duty and registration charges in respect of residential properties and also in respect of women applicants. The stamp duty still varies between 5-13% and registration fee varies from 1-3%.

The high and varying levels of transaction costs of housing in India impact affordability adversely besides contributing to opacity in the sector. Some of the transaction costs may be considered as inefficient re-

sources. There is a felt need for a joint action on part of all the stakeholders for bringing in rationalization, self regulation and transparency in the sector. Consumer education, awareness and dissemination of the information on various costs involved in buying a house is thus called for. Rationalization of stamp duty and registration charges and making it uniform across the States would be a major step forward. In addition, States may also consider adopting a differential duty structure based on gender i.e. women getting a lower rate, or low income group getting a lower rate may also be considered.

In this context, the need for a real estate regulator to regulate the real estate market and the players viz. developers, contractors, brokers, valuers cannot be overemphasized. Such regulator will seek to impart greater accountability, transparency and efficiency in the real estate market that will benefit the average consumer. Creation of voluntary self regulating bodies of developers and builders as well as accreditation/ licenses of real estate brokers will provide the necessary thrust to the housing and real estate sector. On the part of the Government, bringing and implementing reforms in the land records and other Acts and levies, rationalization of stamp duty and registration charges and statutory provisions with regard to regulation of builders and broker community, will prove to be beneficial to the consumer in the long run.

From the financing angle, mortgage lenders do charge in addition to interest on the loan, service, processing fee, title search charges etc. Upfront charges constitute a percentage of the capital cost or the loan amount approximately 0.06% to 0.10%. However, in the consumer's interest, it should be made mandatory that the Effective Annual Rate (EAR) is quoted by lenders in all loan offers. The EAR is the annualized rate of interest and all other charges, upfront or otherwise. EAR will enable comparison of loan offers from various banks.

Use of technology is an important instrument in reduction of transaction costs. On line property records which enable easy search by poten-

tial customers on payment of suitable fee needs to be an objective in the medium term.

Computerization of land records, creation of a Central Repository of home loan data and linking it with the underlying asset are overdue measures. It may be integrated with the electronic repository of information relating to loans of HFC's launched by NHB. This can then be developed into a national housing information centre, for bringing in authenticity and transparency in the sector.

Dissemination of information and consumer awareness and education also need to go hand in hand with the above initiatives.



Chapter I

INTRODUCTION

1 Overview

In the Mid-Term Review of Annual Policy 2006-07 announced in October, 2006 by the Reserve Bank of India, particular reference was made to the measures that the Reserve Bank of India has been taking on an on-going basis for protection of customers' rights, enhancing the quality of customer services and strengthening grievance redressal mechanisms in the Reserve Bank as well as in banks. In this context, The Governor referred to the introduction of the Fair Practices Code introduced through the Banking Codes and Standards Board of India and the Reserve Bank of India's stipulation regarding reasonableness of bank charges.

In the particular context of housing loans, the importance of fairness and transparency was stressed, for instance in areas relating to the circumstances and factors governing the benchmark in respect of floating rates as well as in regard to reset clauses. The Governor urged review of all practices which are less than fair or transparent and to afford an opportunity to borrowers to obtain fair and transparent terms

consistent with legal requirements and fair practices.

NHB shares the concern in this regard. A house is arguably the most important asset that any individual wants to own in her/his lifetime. Similarly, a housing loan is one of the most important financial decisions taken during the lifetime of a consumer. NHB has launched a number of new initiatives with a view to promote customer protection and education in the housing finance field. A summary of the initiatives is given in **Appendix A**. Following two merit special mention:

- i) Introduction of a system of mortgage counseling, details are given in **Box Item 6 of Appendix A**.
- ii) Setting up of a joint forum of banks and housing finance company to be called Indian Mortgage Lenders which will provide a common platform for all mortgage lenders to address various users including customer service, customer education and protection. Details are given in **Box Item 7 of Appendix A**.

The present study is thus part of NHB's endeavor to promote consumer awareness and education.

2 Study on Transaction Costs of Housing in India

The housing industry in India is characterized by lack of authentic data pertaining to various costs associated in purchasing a house by an individual as well as the various steps involved. Further, the costs in purchasing a house vary on account of various factors such as point of purchase, place of purchase and also type of purchase. Thus, from the common man's (aam admi) point of view, clarity on various aspects are not documented in an authentic manner.

As part of its developmental mandate, NHB seeks to promote transparency and fairness in the housing finance industry and by extension, in the housing industry. A first and important step is to build awareness through analytical information. Accordingly, NHB has conducted a study on costs in acquisition of a house with particular focus on transaction

costs. An external agency viz. Magictricks.com, of the Time of India Group was commissioned to provide a quick field survey of the transaction costs in select cities. Besides endeavoring to provide policy inputs both for the Central and the State Governments, the study seeks to address the entire process of buying a residential house and outlines the various costs involved such as commission, brokerage, stamp duty, registration charges, legal charges etc. in an analytical manner so that it could also prove useful to the average consumer.

The purpose behind the study has been to map the entire process of buying a residential house and the costs involved in the process and arrive at a model representing various scenarios in major States in the country and make necessary recommendations for improving the availability of authentic data and bringing in transparency in the housing sector.



Chapter II

SCOPE AND METHODOLOGY

1 Objectives

The key objectives of the study are:

- i. To map the entire process of buying a residential house and the associated costs involved in the process such as commission, brokerages, stamp duty, registration charges, legal charges, housing finance charges, completion charges etc.
- ii. To arrive at a model representing various scenarios in different States (so as to provide a representative sample on the transaction costs in housing in India) through primary data collection.
- iii. To quantify the impact of these charges on the cost to the consumer.
- iv. To make recommendations to policy makers based on the foregoing analysis.

2 Scope

The study of transaction costs in housing includes:

- Transaction costs pertaining to stamp duty, registration fee, leasehold to freehold conversion charges,

transfer and mutation charges.

- Transaction costs payable to the broker: Broker's Commission
- Transaction costs involving payments to the Developer: Parking space charges, maintenance, water, electricity, society transfer charges (sometimes also included in the cost of the property).
- Financing costs payable to the mortgage lenders viz. banks/housing finance Companies: pre-EMI charges, loan interest rate, processing fee, legal fee, valuation fee, property insurance
- Transaction Costs of expenses incurred on service providers such as lawyers, consultants, Deed writers, Maintenance agencies

3 Methodology

Various tools have been utilized for conducting the study, which include the following:

- Telephonic surveys on pre-determined formats and questionnaire across select States and cities;

- Discussions with end-users, brokers, developers lending institutions and municipal authorities;
- Discussion with select Housing Finance Institutions (HFIs);
- Sample survey of home buyers across cities and categories to assess the awareness of the amount of payouts and hidden costs;
- Analysis of the data to assess the extent of add-on costs and hidden costs, if any, to be borne by home buyers.

The survey has been conducted across six Tier 1 cities, six Tier 2 cities and four Tier 3 cities. The cities surveyed include the following:

Table 1: Design Sample of Cities

Tier 1	Tier 2	Tier 3
Delhi	Ahmedabad	Lucknow
Mumbai	Chandigarh	Kochi
Chennai	Indore	Jaipur
Bangalore	Ludhiana	Coimbatore
Hyderabad	Bhubaneswar	
Kolkata	Pune	

The data has been gathered across segments and cities through primary data collection methods primarily through oral/telephonic sources. Efforts have been made to contact the most authentic sources in the

public and private sectors. A random sample method was used to select brokers and developers.

This data was fed into data sheets and analyzed to draw parallels and differences between cities. All conclusions have been made on the basis of primary data collected as mentioned above.

Market realities as they are present today have been thrown up in vivid detail in the analysis. On the basis of this analysis, conclusions have been drawn and recommendations made.

4 Limitations

- The entire exercise is based on a telephonic and E-mail spot surveys conducted through an intermediary, primarily on account of the absence of authentic primary data and the reluctance of the sources of data to discuss with a Government agency.
- While a credible agency has been used for collection of information and data there are intrinsic limitations on reliability of the data and its completeness.
- The data provided by the officials has been assumed to be updated and correct. However, wherever possible the data has been counter

checked with private market players.

- While collecting the information it was observed that there was no one authentic source of information. There is no commonality of nomenclature of charges across cities. Charges such as stamp duty and registration are often clubbed together as levies. Even at the authority or the broker level a clear distinction between the two was often difficult. Neither the collector nor the payee was aware of the published values. Different cities operate on different norms of property units and in bringing them to a common unit value, there may be slight discrepancies of conversion.

5 Assumptions:

For the purpose of this study following were assumed:

- The median value of houses in Tier 1, 2 and 3 was taken as Rs. 60 lacs, Rs. 40 lacs and Rs. 30 lacs, respectively.
- The size of property was taken as 1800 Sq. Ft or 200 Sq. Yards or 167Sq. Mtrs.
- All calculation of EMI have been done using HDFC EMI calculator, which operates on the monthly rest principle.

- For the purpose of calculation of EMI, the loan component is assumed to be 85% of the total cost, which is generally the maximum Loan to Value Ratio (LTV) that banks offer. An average interest rate of 10.0% for tenure of 15 years has been assumed.
- The processing fee, legal fee, valuation fee and property insurance fee are taken as constant across cities as these are standard charges levied by banks and do not vary from city to city.
- For the calculation of stamp duty, an average value has been taken as in many cities, the stamp duty charges vary on the basis of gender or areas
- For the computation of stamp duty 'value of property' or 'consideration' or 'cost of land' all are considered to be the house value.
- The Delhi region is unique in that the sub cities of Gurgaon, Noida, Greater Noida, Ghaziabad and Faridabad function as one region National Capital Region (NCR). However, Stamp duty, Registration, Leasehold to Freehold conversion charge and Transfer & Mutation charges follow that of the respective states. In the data sheet the aforesaid

charges have been computed on the basis of those applicable in the National Capital Territory of Delhi. However, charges paid to developers reflect those prevailing in the National Capital Region.

- EDC or the External Development Charges are charged by authorities from developers for provision of offsite services and infrastructure. These are recovered by the developers from the end users as EDC charges. This is extremely evolved as a system in Haryana where private consolidation of land by developers has been encouraged. Any developer who develops and markets a township takes the onus of the provision of onsite infrastructure in-house but collects EDC for external development of infrastructure. The quantum of these charges is available for the area in the neighbourhood of Delhi but

in other cities these could not be ascertained from credible sources. It has therefore been included only for Delhi region.

- Due-diligence and document preparation charges have been clubbed together as most brokers offer this service as a composite service. It was found difficult to segregate the cost and arrive at authentic values.
- The transfer and mutation fee have been clubbed together for the purpose of computation.
- Search costs i.e. expenditure incurred by the consumer to identify a house for purchase (money covering the time spent in searching excluding broker fee) is not included.
- The costs do not include unofficial payments to Government authorities, real estate developers, miniscule sundry charges, etc.



Chapter III

HOUSE ACQUISITION – COMPONENTS AND PROCESS

1 Acquisition Costs

Acquisition costs for the purpose of the study has been defined as **capital cost** of the house, **transaction costs** which are charges payable towards taxes, duties, brokerage and documentation and **financ-**

ing cost in respect of the loan if taken for financing the acquisition.

Broadly the costs involved in buying/purchasing a property in India involve the following heads as classified below:

Table 2: Components of Acquisition Cost of a House

Cost	Cost Components	Description
Capital Cost	Land Cost	Cost of the land or apportioned cost of the land for vertical development. Varies significantly from place to place within a city itself.
	Infrastructure Cost	Cost of development of the basic infrastructure within the area/project. Depends upon the extant of work and specifications.
	Construction Cost	Basic Cost of the dwelling Unit. Costs can vary significantly depending upon area, specifications of materials, finishing etc.
	Parking Lot Charges	Usually included in the cost of the house and can vary from Rs. 25,000 to Rs.50,000 in Tier II cities such as Ahmedabad to Rs. 1,50,000 to Rs. 2,50,000 in Tier I cities such as Delhi and Mumbai.
	Maintenance Fee	Typically a monthly fee charged by developers that ranges between Rs.800/- to Rs. 8,000 per month. However, many developers prefer to charge an year's fee in lump sum up-front and maintain it as a corpus payment.
	Water Meter Charges	Usually included in the cost of the property depending upon the charges by the local corporation.

Cost	Cost Components	Description
Transaction Costs	Electricity Charges	Included in the cost of the property. However, some developers charge electrification charges which are approximately Rs.50,000 for providing power back-up also.
	External Development Charges	Usually charged for a new location development, primarily for basic infrastructure amenities such as drainage, roads, sewage, water, electricity etc. These vary significantly, however, broadly range between 5-10% as additional charges.
	Other Capital Costs	Expenditure incurred on interiors and furnishing such as wardrobes, kitchen cabinet, pelmets including fittings and fixtures etc. Can vary between 5-10% of the total cost of the house. The houses cannot be taken for occupation without these investments.
	Stamp Duty Charges	Stamp duty across India varies between 5-13% of the cost of property. In certain States there is a rebate if the property is owned by a woman, etc.
	Registration Charges	Registration fee usually varies from 1 to 3% of the property cost.
	Document Preparation Charges	Drafting charges payable to advocates/lawyers, liaison expenses etc and are collected on a lump sum basis which can vary from Rs. 1,000 to Rs. 15,000 across cities in India. The higher the value of the transaction, the greater is the documentation charges.
	Land Conversion Charges	These are the charges for converting lease hold land to free hold. There are different norms across States in India. In certain States and cities all land is freehold.
	Transfer & Mutation Charges	Transfer charges for transfer of property/ title from one entity/person to another and notifying the same in the concerned municipal authority records known as mutation record/ <i>katha</i> record. The charges vary from city to city.
	Brokerage charges	When the real estate broker closes a deal from an end-user, he charges a commission which varies between 1-5% in medium scale transactions and 0.2-2% in hi-value transactions, varying from city to city.

Cost	Cost Components	Description
Financing	Application Fee	The application fee is a fixed nominal Costs amount. The administrative & processing fee is a percentage of the amount of loan required. Usually varies between 0.5-2%.
	Administrative & Processing Charges	
	Pre EMI	Pending final disbursement, the end user pays the interest on the portion of the loan disbursed.
	Loan Interest Rate	Rate of Interest on the Loan Amount (currently varies between 10-14% p.a.).
	Legal Charges	Ranges between Rs.500-5,000/- depending upon allotment from public agency, developer, re-sale, second or third sale etc.
	Valuation Fee	Normally included in the processing fee. However, at times charged separately for valuation of the property by a valuer.
	Insurance Charges	Insurance coverage of the property financed. It is usually a lump sum payment and can range between Rs. 15,000/- to Rs. 25,000/- depending upon the value of the property.

2 Steps in the Process

Buying or building a house is every one's dream. However, the process of booking a flat through a broker with a private builder or purchasing it from a Government Public Agency such as a Housing Board or Development Authority may require different steps and different charges. Similarly, transfer of a property i.e. resale would also require varied processes and documents.

The steps required in buying/purchasing a property also vary depending upon the type of purchase original booking or resale,

financing of the property and even the place of purchase.

3 Housing Transaction Flow Chart

The entire process of buying a property can be depicted in a flow chart as outlined in **Chart 3**. The chart is indicative of the processes involved in buying/financing of a house.

The first step is a decision taken by an end user for purchasing a house. Once a decision is taken, options of whether to avail the services of a broker, or to book a house directly with a builder or a public agency or even through a co-operative

housing society are available with the end user. One also has to decide whether the services of a lawyer/legal firm are required to ensure that the documents relating to the property are complete and in order. The same may not be required in respect of purchase of a house from development authority/public agencies.

Once the property to be purchased has been identified, the owner has to take a decision whether finance from a housing finance company or a bank is required to purchase the property. In case, finance is required the owner can approach a HFC or a bank for finance. The terms and conditions of availing a housing loan vary between lender to lender based on the profile of the borrower, property financed, and other factors. Sometimes insurance of the property is a part and parcel of the services offered by the HFC/Bank and may not be required separately.

Based on the above, the cost of the property including other

capital charges, necessary taxes, and duties such as stamp duty, registration charges and other land conversion charges are paid to complete the documentation and the process.

4 Supply Chain of House Acquisition Process

Broadly the supply chain of the house acquisition process can be depicted as below. From the same, it can be observed that different players at various stages are involved in the house acquisition process. Further, each of these institutions are either regulated by a different entities or are not regulated in the Indian market.

Banks and HFCs are regulated by the Reserve Bank of India and the National Housing Bank respectively. The Council of Architecture has also put in the necessary guidelines in respect of payments depending upon the nature and extent of work for architects and planners. However, the brokers and valuers community in India is, till date, largely unregulated.

Chart 2: Supply Chain in House Acquisition Process

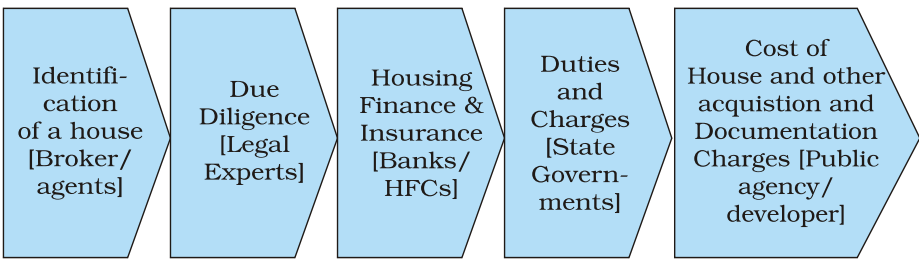
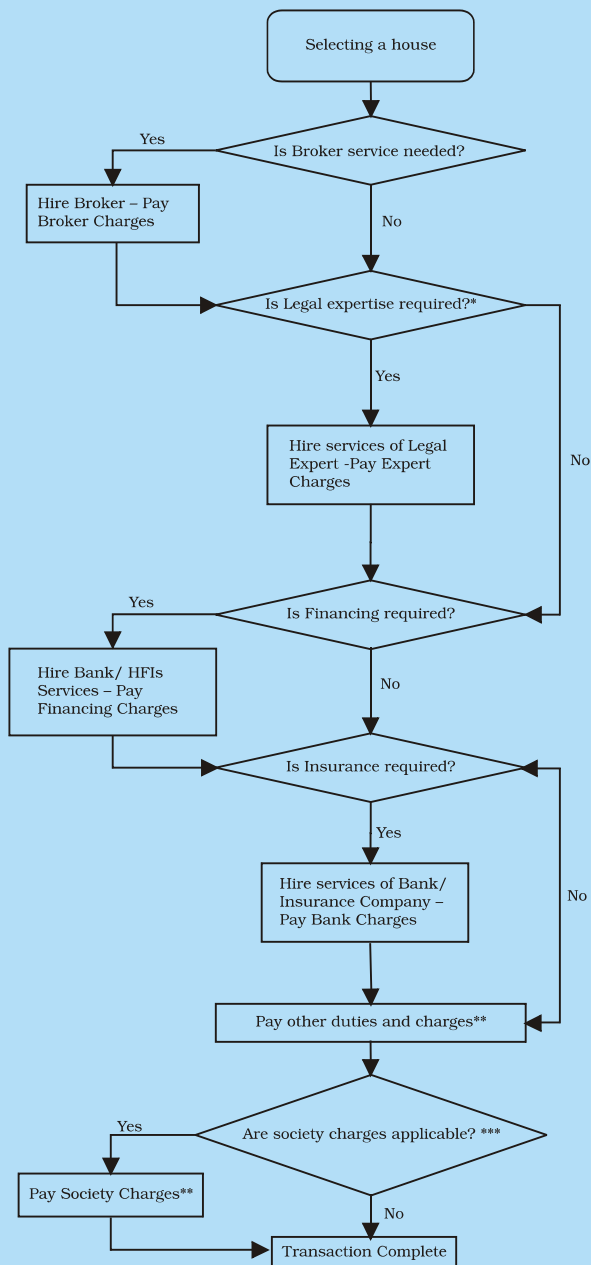


Chart 3: Flow Chart of House Acquisition Process 2



* Legal expertise include: Due-diligence and document preparation charges.

** Other Duties and Charges include – Stamp Duty & Registration Charges, Leasehold to Freehold Charges and Transfer & Mutation Fees

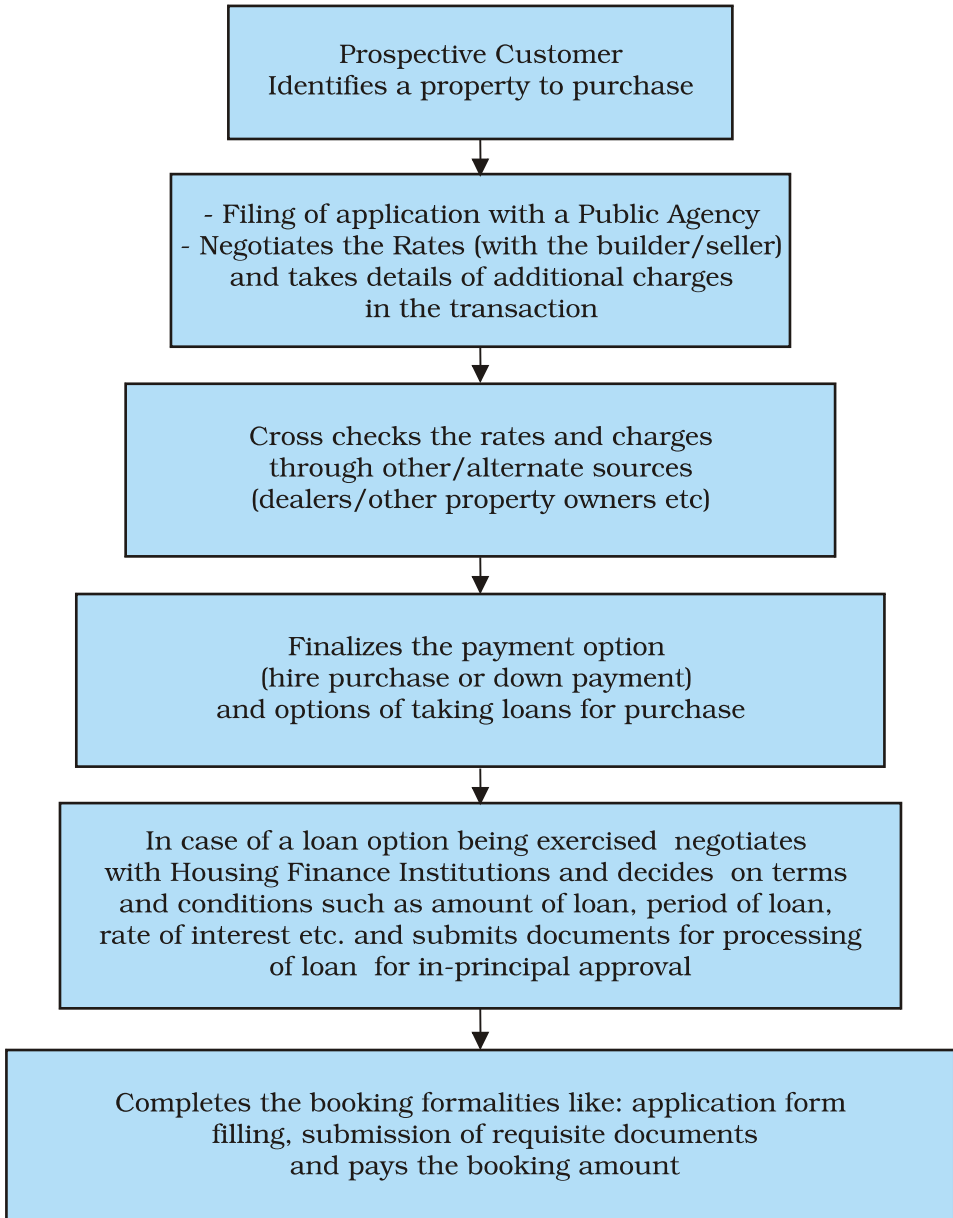
*** Society Charges include – Society Transfer charges, Parking & other services and EDC.

Source: report submitted by magicbricks.com

5 Flowchart of the Booking Process

The flowchart of the booking process can be further broken down in the following steps.

Chart 4: Flow Chart of the Booking Process



Chapter IV

ACQUISITION COSTS IN HOUSING

1 The Buying Process

The purchase of residential property is done in the following ways:

- a. Purchase from the Public Agency- Direct Sale
- b. Purchase from the Developer/Builder- Original Booking
- c. Purchase through a cooperative housing society
- d. Purchase/Resale of property through a broker or directly

The Public Agencies viz. Housing Boards, Development Authorities and Corporations are Government bodies which undertake land acquisition, land assembly, and housing construction. These agencies regularly launch new housing schemes and advertise the same for the general public. At the same time, they also auction certain existing properties.

The builders and developers are playing a significant role in developing housing projects including townships. Usually, they obtain the land for these projects from the public agencies and build housing projects on these lands which are offered

to the public. At times, these builders have a tie up with brokers.

Cooperative housing societies have contributed significantly towards providing housing to large segment of the population. These housing societies are organized groups of usually similar profile in terms of profession, income categories etc.

The resale of existing properties through a broker or directly has also gained ground in India particularly in large cities. These brokers usually charge a fixed percentage fee for the transaction.

Any person who purchases an immovable residential property has to pay certain charges, over and above the cost of the property as has been outlined earlier. In the following chapter, we shall understand the process/transactions undertaken while purchasing the house from the above categories.

2 Public Agency or Developer

As the primary source of development, the public agency or the developer fixes the cost of the property. This would factor in the cost of land, the cost of

input materials in construction, the service charges and taxes paid directly and indirectly by the developer, including value added tax (VAT), sales tax, works contract tax, service tax and cess. This is the agency that determines the primary values and therefore sets price norms in the market.

The developer also charge other charges such as parking charges, maintenance charges, the water meter charges paid at the time of possession, the electricity meter/electrification charges, etc. In case of public agencies, these are included in the cost of the house itself and may not constitute a significant amount in respect of purchase of house from a public agency.

Parking Lot Charges: This is charged by the developer to the owners of the house. These can vary considerably depending upon the city and the area of the city. Further, in case the park-

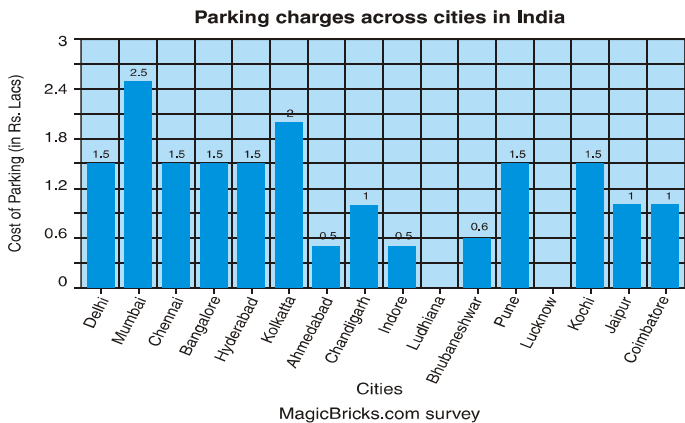
ing is covered, these are additional costs. They vary from Rs. 50,000 to Rs 1.5 lacs in Tier II cities such as Pune to Rs.1.5 lac to Rs.2.5 lac in Tier I cities such as Delhi NCR and Mumbai.

Maintenance Fee: Typically developers charge a monthly maintenance fee that ranges from Rs. 300 to Rs.6,000 per month. Many developers prefer to charge a year's monthly maintenance fee in advance in a lump-sum while a few charge the end-user for creating the maintenance infrastructure.

Water Meter Charges: This charge is included in the cost of the property and most developers do not charge water meter charges in advance but some charge depending upon the charges by the Corporation. It ranges between Rs.700 to Rs.20,000.

Electricity Charges: The charge is included in the cost

Chart 4 : Parking Charges across cities in India



of the property and most developers do not charge electricity meter charges in advance. There is no uniformity of electricity charges across cities. Lump sum payments at the time of purchase may range from as low as Rs.1,000 in Ahmedabad to Rs.90,000 for development and back-up charges in Delhi NCR.

External Development Charges:

External Development Charges (EDC) are usually applicable/collected for a new location development, primarily to provide for basic infrastructure amenities such as drainage, roads, sewage, water, electricity lines etc. These are collected as a lump sum amount or on a per acre or per sqm. basis by the concerned authorities, which in turn is distributed pro-rata amongst the individual occupiers by the developers. In the State of Haryana, private developers consolidate land and provide on-site infrastructure while the state charges External Development Charges for off-site infrastructure.

Society Transfer Charges:

These charges are valid only in the state of Maharashtra. This fee is an amount charged by the society to the person selling his apartment or the person buying an apartment in a society. At the time of transfer, the transferor is requested to give a letter to the society stating that he is giving the donation as a voluntary con-

tribution towards the common amenities fund, maintenance fund or major repairs fund, and that he has instructed his accountant to reflect the same as a voluntary contribution in his books of accounts.

Model Bye-Law No 40(d)(v) of co-operative housing societies as approved by the commissioner for co-operation under the Maharashtra Co-operative Societies Act, 1960 provides for payment of a transfer fee of just Rs 50 by the transferor-member to the society. Also, sub-clause (vii) of the Model Bye-Law No 40(d) provides for a payment of premium at a rate to be fixed by the general body meeting not exceeding 2.5 per cent of the difference between the book value of the flat and the price realized by the transferor on a transfer of flat or Rs 25,000, whichever is less. It also imposes restrictions on accepting an amount exceeding Rs 25,000, whether by way of donation or otherwise, unless it is paid voluntarily by the member.

However, today the transfer fees are not restricted to an amount of Rs 25,000. In fact, there are no guidelines for societies to follow. The amount is fixed by passing a resolution at a special general body meeting of the society. It is paid at a fixed rate per square foot or as a lump-sum. Society Transfer Charges typically range from Rs. 25,000

to Rs. 50,000 lump-sum amount to a maximum of Rs 1 lac for very high-end apartments.

3 Purchase through a Broker

A real estate agent is called by different names in different markets such as broker/ advisor/ consultant/ intermediary etc. A real estate broker is a party who acts as an intermediary between sellers and buyers of real estate and attempts to find sellers who wish to sell and buyers who wish to buy. An agent has many responsibilities which a buyer may not be able to visualize before choosing to buy or sell on his/her own. A competent agent can do much more than find the right space at the right location at the right price. However, the number of services packaged within the brokerage fee varies from city to city and broker to broker.

One concern that drives many people to hire a real estate agent/broker is to have someone familiar with the process to help them and ensure that all activities will happen quickly and make the buying process easier.

Real estate brokers and their agents assist sellers in marketing their property and selling it for the highest possible price under the best terms. When acting as a buyer's agent with a

signed agreement (or, in many cases, verbal agreement), they assist buyers by helping them purchase property for the best possible price under the best terms. They show the buyer various options and if the buyer selects one property it is called 'closing a deal.' Typically agents earn a certain percentage of the selling price or rental value. However, sellers and tenants feel that if they could do it on their own that money could be saved.

If the real estate broker closes a deal for an end-user, this is the first cost that an end-user bears in the life cycle of purchase of a property - this is called the broker's commission/cut/fee. When the real estate broker closes a deal for an end-user, he charges a commission which varies 1% to 2% in medium scale transactions and 0.5 to 1.5% in high-value transactions varying from city to city.

The **Table 3** gives an overview of broker fee in select cities across the country. A medium scale transaction in a metro/ Tier 1 has been assumed to be upto Rs.60 lacs, in Tier 2 city upto Rs.40 lacs and in Tier 3 city upto Rs.30 lacs. A high value transaction in a metro is Rs.1 Crore onwards, in Tier 2 city Rs.75 lacs plus and in Tier 3 city, Rs.60 lacs plus.

Table 3: Broker Fee across Cities in India

	Low to Medium Scale Transactions	Hi-value Transactions
Delhi	2%	0.5- 1%
Mumbai	2%	0.5- 1%
Chennai	2%	1%
Bangalore	2%	1%
Hyderabad	2%	1%
Kolkatta	2%	1%
Ahmedabad	2%	1%
Chandigarh	5%	2%
Indore	3%	2%
Ludhiana	2%	1%
Bhubaneshwar	2%	1.5%
Pune	2%	1%
Lucknow	3%	1%
Kochi	3%	1%
Jaipur	2%	1%
Sonepat	2%	1%
Coimbatore	3%	2%

Source: report submitted by magicbricks.com

This commission is paid to the agent at the time of execution of the Sale/lease/license Agreement or Deed of sale/Lease (when the full purchase prices are being paid) or when the possession of the said property is delivered, whichever is earlier. In case of rent, lease, license the Lessor/Licensors would pay brokerage equivalent to fifteen days rent / license fee.

One can of course save money by acquiring or disposing real

estate assets by oneself, without using an agent. In many cases the hesitation in selecting a broker comes from the fact that there are no yardsticks to determine the efficiency or reliability of the brokers.

Even an agent who represents only the buyer and not the seller has a financial interest in seeing the deal go through as they are paid only when the transaction takes place. Experienced, reputable agents won't let this

interfere with their advice to you. They're more concerned with their professional reputation and long-term ability to attract clients. However, this conflict of interest may cause less scrupulous agents to insist that the client would not get the property unless they bid high, to recommend home inspectors who

make light of potential problems, and to otherwise compromise interests of the clients.

The **Table 4** was compiled by a team of researchers across universities in the United States, shows a wide discrepancy in broker commissions across the world.

Table 4: International Commission Rate Comparisons-Brokerage

Country	Licence	Real Estate Transaction Characteristics
Argentina**	Yes	6%, where 3% paid by the buyer, and 3% paid by the seller; does not require buyer broker.
Australia	Yes	5% on the first \$18,000, 2.5% -thereafter; also properties are sold through auction system; advertising is provided by real estate agent.
Belarus	n/a	6%-15% commission, averaging near 10%. Public information is scarce.
Belgium	Yes	3% commission.
Brazil	Yes	5% commission, less on a higher priced units.
Canada	Yes	3-6% commission rate. An agent handles on average 3 to 5 sales per year.
Caribbean***	Yes	5% - Jamaica, 3-5% - Trinidad & Tobago.
China** & Hong Kong		No set regulations and standards for real estate transactions in China. Commission fees vary from 5% to 10%. Also, there is 15% real estate transfer tax. However, Hong Kong province has significantly lower real estate brokerage fee typically 1% for the seller. Hong Kong does not require dual representation and one agent may deal with both the buyer and seller. However, both parties typically have separate lawyer representation. In Hong Kong, the maximum transfer tax is 3.75%.
Denmark**	Yes	2-4%, buyer pays 25% of sales price transfer tax; advertising is provided by real estate agent.
Finland	n/a	Fees run about 5% of the sale price on condos and 3%-4% on single family homes. Higher priced houses have lower commission fees. The government collects a value added tax (22% of the selling price).
France**	Yes	Only 50% of property sold is listed with a real estate agent; real estate transactions are kept very private; 50% of the real estate is sold by owner.
Germany	n/a	Negotiable commission rate that varies from 3% to 6%.

Country	Licence	Real Estate Transaction Characteristics-Brokerage
Greece	n/a	4% commission rate, where the buyer and seller are responsible for 2% each. Also, there is a 12% value added tax on a real estate transaction.
Indonesia**	No	5% paid by either buyer or seller, but not both; a buyer's broker is required for real estate transactions.
Ireland**	Yes	In cities 1.5-2%, and small towns 2-3%; also properties can be sold through auction system.
Israel	Yes	4% commission rate equally split between buyer and seller agents.
Italy**	Yes	Paid by both buyer and seller: each party pays 2-3%.
Japan**	Yes	3% commission rate.
Malaysia**	Yes	3% on the first \$100,000 and then 2% of the remaining amount of the sale, commission is paid either by buyer or seller, not both.
Mexico**	Varies	5-10% commission rate. Large emphasis on MLS.
Netherlands**	Yes	1.5-2%, broker represents either the buyer or the seller but not both. The seller pays the fees.
Norway**	Yes	2-3%, broker represents both parties in the transaction.
Philippines**	Yes	5%, broker represents either the buyer or the seller but not both.
Russia	Yes	5% to 10% but "net listings" are common; advertising is provided by real estate broker/agent; FSBO very common;
		Buyer broker representation is not required. Some commissions are set in dollar or ruble fee amounts. Reliable market information is difficult to acquire.
Singapore	Yes	1.5-2.0%, FSBOs are very rare; buyer broker representation is not required.
Spain	Yes	Commission rate depends on the property location, averaging 5% of total estate price.
Sweden**	Yes	5%; commission is paid by seller. 10% commission is typically charged for lower priced units.
Thailand	n/a	Commission rates vary from 3% to 5%.
United Kingdom	Yes	1%-2% is typical; in very competitive areas 0.5-0.75%; in low priced areas as high as 3.5%. Advertising is provided by real estate broker/agent; buyer broker representation is not required.
United States	Yes	6%-7%; advertising is provided by real estate broker/agent; in 1999 Some real estate agents charge flat fees that run 2 to 4 percent. Auctions are increasing but usually at the same fees or higher as normally charged by the brokerage firm involved.

Source: International Real Estate Review

* This number is calculated as Total home sales in 1999 (according to NAR Profile) was 6.5 million. According to NARELLO, in 1999, there were 515,225 active real estate brokers and 980,083 active real estate agents.

** Information is obtained from <http://onerealtorplace.com>

*** Jamaica, Trinidad and Tobago. Data was also confirmed through the network of academicians and practitioners attending Real Estate Conferences in 2001.

Source: report submitted by magicbricks.com

Broker Commission International Experience

Based on the table 4 above, it can be observed that there is a wide variation in broker commissions across the world which can vary between 2-10%.

The Indian norm of 0.5-3% in terms of broker's commission is well below global standards. However, unlike the organized real estate markets where the brokers are duly licensed and can operate as real estate advisors only after rigorous training and certification, the Indian market is devoid of any regulation for brokers/agents. In the absence of such regulations, the common man has no means to assess the competence of the broker.

What is required therefore, is simply to list the broker's responsibilities, educate him and the consumer on the same and also to regulate them against malpractices

4 Financing the House through a Bank or Housing Finance Company

The second step in the lifecycle of purchase of residential property is getting the property financed. Apart from an individual's savings and assets, given the property prices today, it becomes necessary for almost everyone to organize additional funds. These funds may come in the form of borrowings from various sources like Housing Finance Institutions, Banks, provident fund, employer, relatives or friends, etc.

In the present scenario, housing finance products are available for almost all the needs of the customer, right from home loans to home improvement loans.

The borrowers usually compare interest rates, terms and conditions of various banks and HFC's and start applying for home loan in the bank/HFCs. Even banks and HFC's have certain guidelines with regard to credit appraisal, property appraisal and verification and loan documentation. These factors are taken into account while arriving at the loan eligibility and repayment capacity of the borrower. Repayment capacity is based on factors such as income, age, qualifications, number of dependants, spouse's income, assets, liabilities, stability and continuity of occupation and savings history apart from the value of the property.

The borrower has to pay the administrative and processing charges at the time of applying

for a housing loan. Once the loan is sanctioned, the banks/HFCs come up with an Equated Monthly Instalments (EMIs) comprising principal and interest, figure to be paid each month by the end-user till the completion of the stipulated tenure of 5/10/15/20 years. Repayment by way of EMI commences from the month following the one in which the end-user takes full disbursement.

The bank or HFC charge to the end-user is Step II in the lifecycle of transaction costs in housing. Typically, the end user is charged the following by a bank/HFC:

a. Processing Fee

To avail of a home loan the end user needs to pay money by way of processing fee, also called Upfront Fees or administrative fees. Although these fees are low as compared to the quantum of loan but at times they appear significant (especially in case of big ticket loans). These expenses go towards the initiation of the loan process. This one-time charge is based as a percentage of the loan amount. The fee could be in the range of 0.5% to 2% of the loan amount depending upon the bank or the housing finance company (HFC). These days the processing fee is 0.5% for most banks. The pre-payment penalty is usually 2% of the outstanding loan amount.

b. Pre EMI Interest

Pending final disbursement, the end-user pays the interest on the portion of the loan disbursed. This interest called pre-EMI interest. Pre-EMI interest is payable every month from the date of each disbursement up to the date of commencement of EMI. There are no tax breaks on the pre-EMI. Therefore it does not contribute to the tax savings of the individual.

c. Loan Interest Rate

This is the interest on the principal amount compounded over the home loan tenure period and payable as part of the EMI every month. The home loan interest is the second and a major expense incurred by the end-user in the purchase of a property. The Interest rate may be a fixed Rate (one which is not impacted by the money market conditions) or floating (which varies with money market conditions). However, with the revision of bank interest rates practically every quarter in the last one year, banks have started offering floating interest rate and they offer fixed rate only if the end-user wishes. The banks' logic is that even the fixed rate of interest is fixed only for a maximum of 3 years. So it is better to offer the floating rate which is usually lower than the fixed rate of interest.

Interest Rates on Housing Finance

The interest rate for loans can vary from Bank to Bank & HFC to HFC. The variation can be upto the extent of 2-4.5% depending upon both internal & external factors. Both floating (an interest rate that changes periodically) and fixed (an interest rate that is fixed over the loan tenure) rates of interest are being offered to the end users.

During the last six months, the rates of interest have been showing an upward trend and currently the floating rate of interest varies in the range of 9.75% to 13.75% while the fixed rate of interest varies from 10% to 14.50%.

d. Legal Fee

Buying a home will probably be the largest and most significant purchase one makes in one's life. It also involves the law of real property, which is unique and raises special issues of practices and problems not present in other transactions. A real estate lawyer is trained to deal with these problems and

has the most experience to deal with them.

Prior to a property purchase, it is advisable to satisfy oneself by having a solicitor inspect the original title documents to that property. If the title were not clear and marketable, most of the major financial institutions would refrain from giving a loan for this property. Hence, as an

Legal Fee

The legal fee varies from institution to institution. At Bank 'A', for direct allotment by public development authorities such as DDA, HUDA, GDA or any authority, there may be no legal fee. However, at Bank 'B', this amount may range from Rs 500-700, depending upon the nature of work e.g. if it's a direct allotment by DDA, the documentation is minimal and the charges are Rs 500 but wherever the cases are complicated the amount goes up to a maximum of Rs 1000. At an HFC 'C' it may range from Rs 700-4000 for resale and it may go up to Rs 4000. In some international banks, the Administrative Fee which is 0.5% of the loan amount includes legal and valuation fee. Again at HFC 'D', the processing fee of 0.5% of the loan amount may include the Advocate's Fee, Valuer's Fee, Inspection charges etc.

additional measure, one could approach a financial institution to check if they would provide a loan for that particular property. They would probably have checked all the documents pertaining to the property. If a loan is being advanced /granted one can probably assume that the title of the property may be clear, as the lending institution would have ensured so, since they would intend to take mortgage of that property, unless of course they are willing to create a charge on the property without the title of the property being clear or may be willing to accept a second/equitable charge on the property. The lawyer/advocate on the panel of the bank who clears the title of the property, charges the end-user a legal fee. The legal fee ranges from Rs 500-5000 depending upon whether it is direct allotment by the development authority, re-sale, second or third sale and other factors such as the standing of the lawyer.

Reputed Solicitors/ Law Firms normally charge by the hour, at rates ranging from Rs. 1000-5000. one may also find Lawyers/ Firms who charge flat fees (upto 1 to 1.5% of the transaction costs) for specific services, such as preparing documents and doing the Title Verifications.

e. Valuation Fee

This is the fee that the borrower pays to the architect/valuer for

valuation of the cost of the property, and ranges typically from Rs. 500- 1,000 and for very high value transactions, it can be upto Rs 2,000. While some banks and HFCs charge this separately, many other banks and HFCs include this in the processing fee of 0.5% of the loan amount.

f. Insurance Charges

Most banks do not provide this facility of insurance coverage of the property financed as also the life of the borrower. However in some cases, property insurance is compulsory and life insurance is optional. In property Insurance, the bank charges Rs 404 per lac to safeguard it against earthquake and natural disasters. This also covers accidental personal coverage. For life insurance, some banks have a tie up with some agencies and the borrower has to pay a lump sum of Rs 20,000 as a one-time premium. However, the product needs to be marketed well as it is not widely used.

5 Transactions Relating to Documentation

After having identified the property & arranged for its financing, certain documents for ownership are to be prepared in respect of the property and the necessary charges associated with it are to be paid.

**Table 5: Stamp Duty and Registration Charges
across various States and Cities**

Sr. No.	State	City	Stamp duty to be calculated on the value of the property in %age	Registration Fee Excl-Vat/cess in %age
1	Delhi	Delhi	8% - Male 6%- Female	Rs. 100/-
2	Maharashtra	Mumbai	< 1 lakh Rs. 100/- Rs.1 to Rs. 2.5 lakhs 0.5% Rs.2.5 to Rs. 5 lakhs 3.5% > Rs. 5 lakhs 8.5%	1% min Rs. 1000/- Max Rs. 30,000/-
3	Tamil Nadu	Chennai	8%	1%
4	Karnataka	Bangalore	8.40%	1%
5	Andhra Pradesh	Hyderabad	9% - sites and houses 7% - flats	0.50%
6	West Bengal	Kolkatta	6%	1%
5	Gujarat	Ahmedabad	4.90%	1.50% Nil- women
8	Haryana	Chandigarh	8% - Male non HUDA 6% - Female non HUDA 7% - Joint Registration 6% - male - HUDA 4% -Female HUDA 5% - Joint Registration	Rs. 5,000/-
9	Madhya Pradesh	Indore	10.3% - male 8.3% - female 9.3% - joint registration	0.8%
10	Punjab	Ludhiana	9% - male 8%- female	1%
11	Orissa	Bhubaneswar	11%	2%
12	Maharashtra	Pune	< 1 lakh Rs. 100/- Rs.1 to Rs. 2.5 lakhs 0.5% Rs.2.5 to Rs. 5 lakhs 3.5% > Rs. 5 lakhs 8.5%	1% min Rs. 1000/- Max Rs. 30,000/-
13	Uttar Pradesh	Lucknow	10% - male 8%- female	Rs.5,000/-
14	Kerala	Kochi	13.5% - corporation area 12% - municipal area 10% - panchayat area	2%
15	Rajasthan	Jaipur	6.50%	1%
16	Tamil Nadu	Coimbatore	8%	1%

Source: CanFin Homes, CREDAI and Magicbricks.com. There are some discrepancies in the information across data sources and as such the figures are indicative only.

Stamp Duty on Mortgages:
Stamp Duty is a tax, similar to sales tax and income tax collected by the government, and must be paid in full and on time. A stamp duty paid instrument/document is considered a proper and legal instrument/document. It gets evidentiary value and stands scrutiny in courts. The stamp duty varies from 4% to 12% across cities.

In certain states, there is a rebate for registering the property in the name of a woman.

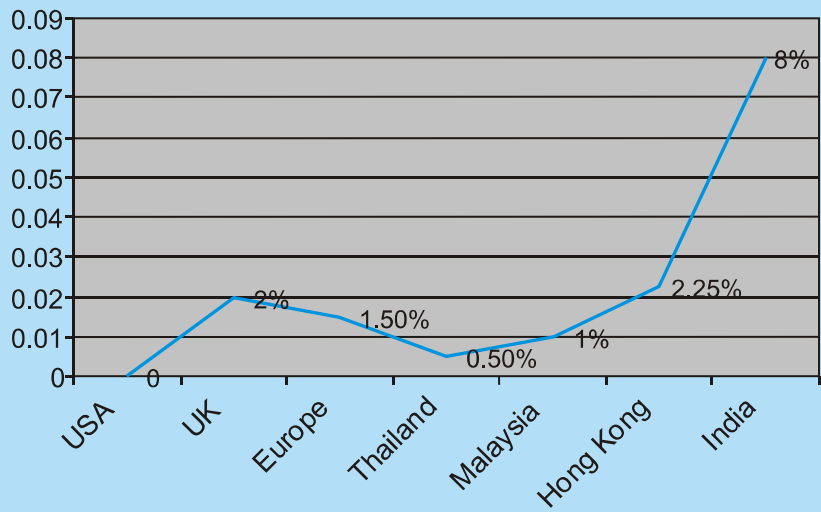
Stamp duty rates are very high and uneven across all States. India has the highest stamp duty rates in the Asia-Pacific region and also as compared to global standards of 1-2% (Please ***(Please see box Item 4)*** and impacts costs significantly.

Box Item 4

Stamp duty on Mortgages

Stamp duty in certain Asian countries, USA, UK are indicated below :

(source: report submitted by magicbricks.com)



Stamp Duty on Securitisation:
The National Housing Bank (NHB) has initiated steps for establishing and promoting the process of securitisation of mortgages in India in terms of the mandate provided under the

National Housing Bank Act, 1987. As a wholly owned subsidiary of the Reserve Bank of India (RBI), NHB's endeavours have been directed towards development of the housing finance system in the country

and facilitating Mortgage Backed Securitisation transactions to enable flow of funds from the capital market into the housing sector, thus enabling greater access and affordability to the borrowers of housing

loans. Presently, the process of securitisation is limited to only a few states on account of prevalence of high stamp duty and registration charges that affect the economics of the process.

Box Item 5

Residential Mortgage Backed Securitisation (RMBS)

The States of Karnataka, Gujarat, Maharashtra, West Bengal, Delhi and Tamil Nadu have issued specific notifications for remission of stamp duties in respect of instruments of securitisation to 0.1% of the size of the pool of securitized housing loans. Further, the stamp duty payable on such instruments has been capped at Rs.1 lakh in most of the above mentioned states. The Registration fees has also been capped to Rs.20,000/- in the state of Gujarat and to Rs.30,000/- in West Bengal. The above has helped NHB in execution and registration of securitization transaction in these States.

Registration Charges: Registration acts as a proof that a transaction has taken place. The registration of a document serves as a notice of the transaction to the persons affected by the transaction. It also serves as an implied notice to any person subsequently acquiring interest in the property, covered by the registered document. When a document, which is to be compulsorily registered, is not registered, it fails to confer any title given by the document. The real purpose of registration is to en-

sure that every person dealing with property, for which compulsory registration is required, can confidently rely on the statement contained in the register as being a full and complete account of all transactions by which the title may be affected.

In certain States in India like Maharashtra, the Agreement for Sale between the builder and purchaser is required by law to be registered. The end-user in his own interest must lodge the Agreement for registration

within four months of the date of the Agreement at the office of the Sub-Registrar appointed by the State Government, under the Indian Registration Act, 1908. The Registration fee varies from 1 to 3%. In certain states, there is a rebate for registering the property in the name of a woman.

Due-Diligence and Document Preparation Charges: Such charges typically involve due-diligence and vetting of property papers by legal experts to check the authenticity of titles. Document preparation charges basically involve document drafting charges payable to the advocates/lawyers, liaisoning expenses incurred with the Govt. authorities. These are usually collected on a lump sum basis. The charges vary from Rs.1,250 to Rs.12,500 across cities in India. The higher the value of transaction, the greater are the charges to be paid.

Leasehold to Freehold Conversion: Leasehold properties (plot/built-up) are those in which leasehold has been granted by the title paramount in favor of the lessee. In such properties in Delhi, the title paramount, i.e. President of India acts through DDA, L&DO, and Leasehold properties are

not freely transferable. Depending upon the covenants of the lease deed, prior permission of the lessor (DDA/ L & DO) is required to transfer the property.

Freehold properties are those where title paramount has conveyed the property in favor of the purchaser by conveyance/sale deed with no restriction on the right of the holder of the property to further transfer the property. Record of ownership of the freehold property can be ascertained from the office of the sub-registrar. It can be transferred by registration of sale deed.

For conversion of leasehold to freehold, there are different norms across states in India. Eg. in Punjab, Haryana, Kerala, Tamil Nadu everything is freehold. Also almost everything is freehold in the cities of Kolkata, Bangalore and Indore. However, there is no freehold in Rajasthan. Annual lease rentals have to be paid to the Authority which is equal to 2.5% of the Reserve price of that area (which is lower than the market value). In Lucknow, the structure has been changed after 1995. The conversion charges are 12% of the sum at which plot is acquired. In Mumbai, there is no conversion,

only renewal of the 99 years lease.

Transfer & Mutation: Once the property is transferred, it is also to be noted in the concerned municipal authority records, which is termed as a Mutation

Record / Khatha record. This means that the property now stands in the name of the new transferee. The charges vary from city to city and there is no fixed formula for this. These charges can go upto 2% of the cost of property.



Chapter V

KEY FINDINGS

1 Key Findings

House Acquisition Cost - Components

The complete process of buying/purchasing a house in India involves various costs which can be broadly classified under the following heads:

- a. **Capital Cost** such as land cost including cost of land conversion, construction cost, on-site and off-site infrastructure costs, parking space cost, works pertaining to basic amenities such as water, power supply as well as basic interiors like cupboards, cabinets, pelmets etc, fitting and fixtures to make the house habitable.
- b. **Transaction Costs** which are charges payable towards stamp duty and registration, document preparation, transfer and mutation, brokerage etc.
- c. **Financing Charges** in case the property is paid for through a loan, include, administrative and processing charges, pre-EMI interest charges, loan interest, legal fees, valuation fees, insurance charges etc.

Transaction Costs Components

- The components of the transaction costs vary, mainly on account of the following three factors:
 - a. **Source of Purchase of the property** which could include purchase from a public agency, a private developer, or a co-operative society.
 - b. **Type of Purchase** which can imply a fresh allotment/original booking, re-sale directly by the owner or through a broker.
 - c. **Applicable duties, taxes, charges** payable to the local Government/authorities.

A Schematic representation is given below.

Chart 5: Structure of Acquisition Costs

Acquistion Costs												
Capital Cost					Transaction Costs				Financing Cost			
Basic of Cost Property	Infrastructure & Development Costs				Stamp duty	Registration Charges	Broker Fee	Transfer & Mutation	Interest & pre-EMI	Processing Fee charges	Legal Fee	Valuation Fee
	Parking	Maintenance	Water Supply & electricity	Others such as society charges								

- Each of the above categories have different determinants and variables which could include charges for conversion of lease hold to free hold, stamp duty and registration charges, brokerage charges, document preparation charges, transfer and mutation charges etc. Certain of these charges are applicable depending upon the source of purchase, type of purchase and place of purchase. Further, these variables are also interlinked.
- For instance while purchasing a property in Delhi from a Development Authority, the end user would pay the capital cost of the house, water and electricity connection charges, registration and stamp duty charges. However, in respect of a purchase of the similar property through a broker, the end user shall also pay brokerage charges, document preparation charges, etc. apart from those paid to a development authority. The cost of a similar house in another city would change since the applicable duties and taxes as applicable in a city would undergo a change. A resale of the same property would also involve transfer and mutation charges besides other charges.
- The cost of property across cities depends upon the demand and supply gaps and the economic drivers of the city. The

location of the land obviously has a considerable impact on the property prices as does the level of infrastructure (both on-site and off-site) and connectivity. The building costs are largely dependent on the quality of specifications, size of the units, costs pertaining to water and electricity connections and in certain Tier I cities, also the parking space cost. The quality of development and the add-ons in terms of lifestyle features such as clubs, recreational and entertainment facilities as well as transport networks and access to business districts also determine the price points for residential real estate.

Findings of the Study

- The acquisition and transaction costs have been analysed in the present study in respect of properties having a value typically up to Rs 60 lacs in Tier 1 city, Rs 40 lacs in Tier 2 cities and Rs 30 lacs in Tier 3 cities. A sample of 16 cities has been chosen 6 metros (Tier I cities viz. Delhi, Mumbai, Chennai, Bangalore, Hyderabad and Kolkatta), 6 Tier II cities (viz. Ahmedabad, Chandigarh, Indore, Ludhiana, Bhubaneswar and Pune) and 4 Tier III cities (viz. Lucknow, Kochi, Jaipur and Coimbatore). These cities cover 15 States viz. Delhi, Maharashtra, Tamil Nadu, Karnataka, Andhra Pradesh, West Bengal, Gujarat, Haryana,

Punjab, Madhya Pradesh, Orissa, Uttar Pradesh, Kerala and Rajasthan.

Capital Costs

- From the analysis of the capital costs, it is observed that approximately 6-10% of the capital costs is towards on-site and off-site infrastructure costs, parking space cost, works pertaining to basic amenities such as water, power supply etc. in cities like Delhi, Mumbai, Bangalore, Kochi, Jaipur and Coimbatore. It is as high as approximately 13% in the city of Pune in Maharashtra mainly on account of high maintenance charges being charged by developers.
- In cities like Chennai, Hyderabad, Kolkata, Ahmedabad, Chandigarh, Bhubaneswar the percentage of costs towards these facilities is approximately in the range of 3-3.50% of the capital of the house.
- The city of Ludhiana, has the lowest costs towards these facilities which works out to approximately 0.55% of the capital cost.

Transaction Costs

- The transaction costs pertaining to services charges (broker and document preparation), stamp duty and registration charges, land conversion charges, transfer and mutation charges and EDC charges can

vary between 8-27% of the house cost.

- Stamp duty and registration charges vary considerably across the country being State specific. Stamp duty is the high in cities like Kochi, Bangalore, Bhubaneswar, Lucknow and Indore. Differential charges based on gender are also prevailing in some States.
- The city with the highest percentage of transaction costs is Lucknow (27.60%). In other cities the transaction costs vary between 10-15% of the capital cost of the house.
- The cities with transaction costs less than 10% of the capital cost of property include Mumbai (8%), Kolkata (8.50%), Chandigarh (around 8%) and Pune (around 8%).
- Tier 3 cities are characterized by high percentage of transaction costs ranging between 10-27%. In fact the transaction costs in Tier 1 cities i.e. all metros are limited upto 12.50% and in Tier 2 cities they range between 8-16%.
- The percentage of the transaction costs may actually fall as the capital cost of the house increases in view of the fact that many of the charges are fixed and in some cases like brokers commission, the percentage is less.
- It can be seen from the above that the transaction costs in various

categories of cities are significantly high and the user actually ends up paying this amount over the cost of the unit as additional charges. This fact often goes unnoticed by the home seeker as well as policy makers.

Financing Costs

- The financing costs depend upon the quantum of loan and interest rate. Other charges such as administrative and processing fee, legal fee, valuation fee, property insurance fee etc. have a minor impact.
- The Effective Annual Rate which includes the rate of interest and processing and administrative charges, legal charges, valuation and insurance charged are not quoted by the lenders and as such comparison of the loan offers cannot be made effectively
- Besides the rate of interest, the component of administrative and processing fee, legal fee, valuation fee, property insurance fee usually works to 1.05-2.0% of the loan component. These are usually one time payments.

The position is summarized in the following Tables.

Table 6: Capital Costs in Housing

[Amount in Rupees]

Sr No.	State	Name of City	Capital Cost of House	Charges towards infrastructure in capital cost (Private developer)				Percentage in capital cost for parking, water, electricity, maint. etc.
				Parking	maintenance	water & electricity	other Charges such as society transfer etc.	
Tier 1								
1	Delhi/NCR	Delhi/NCR	6000000	150000	90000	90000	0	5.50
2	Maharashtra	Mumbai	6000000	250000	80000	25000	20000	6.25
3	Tamil Nadu	Chennai	6000000	150000	0	20000	0	2.83
4	Karnataka	Bangalore	6000000	150000	85000	50000	60000	5.75
5	Andhra Pradesh	Hyderabad	6000000	150000	0	20000	0	2.83
6	West Bengal	Kolkata	6000000	200000	0	10000	0	3.50
Tier 2								
7	Gujarat	Ahmedabad	4000000	50000	0	26000	50000	3.15
8	Chandigarh	Chandigarh	4000000	100000	0	6000	0	2.65
9	Madhya Pradesh	Indore	4000000	50000	135000	45000	25000	6.38
10	Punjab	Ludhiana	4000000	0	0	21500	0	0.54
11	Orissa	Bhubaneswar	4000000	60000	40000	20000	30000	3.75
12	Maharashtra	Pune	4000000	150000	180000	75000	100000	12.63
Tier 3								
13	Uttar Pradesh	Lucknow	3000000	0	25000	3700	25000	1.79
14	Kerala	Kochi	3000000	150000	75000	75000	0	10.00
15	Rajasthan	Jaipur	3000000	100000	30000	38000	100000	8.93
16	Tamil Nadu	Coimbatore	3000000	100000	2500	40000	50000	6.42

source: derived from report submitted by magicbricks.com

Table 7: Transaction Costs in Housing

[Amount in Rupees]

Sr No.	State	Name of City	Capital Cost of House	Transaction Cost (in Rupees)Transaction						Trans- action Charges as a per- centage of Capital Cost
				Broker Fee	Due Dili- gence	Average Stamp Duty & Registra- tion Fee	Lease hold to Freehold	Transfer & Mutation	EDC	
Tier 1										
1	Delhi/NCR	Delhi/NCR	6000000	120000	4500	420000	35370	100	180000	12.7
2	Maharashtra	Mumbai	6000000	120000	0	330000	0	0	25000	8.0
3	Tamil Nadu	Chennai	6000000	120000	7500	540000	0	0	0	11.1
4	Karnataka	Bangalore	6000000	120000	10500	564000	0	10080	0	11.7
5	Andhra Pradesh	Hyderabad	6000000	120000	5000	450000	0	120000	0	11.6
6	West Bengal	Kolkata	6000000	120000	0	390000	0	300	0	8.5
Tier 2										
7	Gujarat	Ahmedabad	4000000	80000	12500	233400	0	0	0	8.1
8	Chandigarh	Chandigarh	4000000	40000	12500	250000	0	500	0	7.6
9	Madhya Pradesh	Indore	4000000	80000	6000	408000	0	300	0	12.4
10	Punjab	Ludhiana	4000000	80000	11000	380000	0	100000	0	14.3
11	Orissa	Bhubaneswar	4000000	80000	0	520000	40000	500	0	16.0
12	Maharashtra	Pune	4000000	80000	2000	240000	0	0	0	8.0
Tier 3										
13	Uttar Pradesh	Lucknow	3000000	60000	15000	333000	360000	30000	30000	27.6
14	Kerala	Kochi	3000000	30000	1250	420000	0	100	0	15.0
15	Rajasthan	Jaipur	3000000	60000	10000	225000	0	2000	8000	10.2
16	Tamil Nadu	Coimbatore	3000000	30000	600	270000	0	500	0	10.0

Source: Derived from report submitted by magicbricks.com

EDC have been included in transaction costs since they are prevailing in only a few cities.

**Table 8: Costs in House Acquisition:
Capital, Transaction and Financing**

[Amount in Rupees]

Sr.	State	Name of City	Capital Cost of House	Transaction Cost as a percentage of Capital Cost	Financing Cost
Tier 1					Applicable rate of interest and upfront charges ranging from 0.5 to 2.0% of the loan amount towards administrative and processing, legal, Insurance, charges, etc.
1.	Delhi/NCR	Delhi/NCR	6000000	12.7	
2	Maharashtra	Mumbai	6000000	8.0	
3	Tamilnadu	Chennai	6000000	11.1	
4	Karnataka	Bangalore	6000000	11.7	
5.	Andhra	Hyderabad	6000000	11.6	
6	West Bengal	Kolkata	6000000	8.5	
Tier 2					
7	Gujarat	Ahmedabad	4000000	8.1	
8	Chandigarh	Chandigarh	4000000	7.6	
9	Madhya Pradesh	Indore	4000000	12.4	
10	Punjab	Ludhiana	4000000	14.3	
11	Orissa	Bhubaneswar	4000000	16.0	
12	Maharashtra	Pune	4000000	8.0	
Tier 3					
13	Uttar Pradesh	Lucknow	3000000	27.6	
14	Kerala	Kochi	3000000	15.0	
15	Rajasthan	Jaipur	3000000	10.2	
16	Tamil Nadu	Coimbatore	3000000	10.0	

source: derived from report submitted by magicbricks.com



Chapter VI

CONCLUSIONS AND RECOMMENDATIONS

1 Conclusions

- The acquisition cost of a house is the aggregate of the base cost of property; infrastructure and development costs; transaction costs comprising of stamp duty and registration charges, land conversion charges, broker fee, transfer and mutation charges etc; and financing costs, should the acquirer seek housing loan.
- The costs towards basic infrastructure (parking, maintenance, water supply, electricity connection etc.) are particularly high in respect of properties developed by builders and developers and can constitute approximately 5-10% of the cost of property.
- The transaction costs on an average can add up to 10-15% of the capital cost of the property. In certain cities the same can account for upto 27% of the capital cost of the property. This implies that the acquisition costs are quite high.
- The Effective Annual Rate is impacted by various charges towards administrative and processing charges, legal and valuation fees and insurance charges constitute around 0.06-0.10% of the loan amount on an annualized basis.
- While the infrastructure and development costs are factored in as the Capital cost of the property at the time of purchase, transaction costs are at times overlooked by the buyers and the policy makers.
- Stamp duty and registration charges account for the dominant share of transaction costs.
- Stamp duty and registration charges vary considerably across the country being State specific.
- Certain States like Delhi, Haryana, Gujarat etc. provide some concessions in stamp duty and registration charges in respect of the property being in the name of a women. Graded structure linked to value of property exists. However, grading of these charges on the basis of income of the buyer may also be an option.
- Other charges such as land conversion, external development charges, transfer and mutation charges, vary significantly from State to State and even city to city. Mutation charges can ac-

count for a significant percentage of costs to the end user in States like Uttar Pradesh, Punjab and Andhra Pradesh.

- On an average, brokerage fee is 2% on an average of the capital cost of the property, however, it can vary upto 5% as in Chandigarh to 3% in cities like Coimbatore, Kochi, Lucknow and Indore. It decreases as the value of the transaction increases and in transactions over one crore, it is upto 1% of the capital cost of the property.
- Going by global standards brokerage fees are quite competitive in India. What needs to be done is to regulate and educate this fraternity so that they adhere to ethical practices and transparency and accountability is brought into the broking process.

2 Recommendations

There is a felt need for coordinated action on part of the policy makers and involvement of the industry which include the Central Government, State Government, Government Institutions, RBI, NHB, Housing Finance Institutions, the developer and builders community and their trade organizations for improving the efficiency of the transaction process of housing in India.

Government of India may set up a high level Inter Ministerial

Committee on transaction costs in housing comprising of representatives of Ministry of Housing and Urban Poverty Alleviation, Urban Development, Finance, State Governments, RBI, and NHB. The Committee will prepare a road map for reduction in transaction costs and oversee its implementation.

The transaction costs in the house buying process are individually and cumulatively quite high and need to be reduced in order to expand the housing market and contribute to making housing affordable for the middle and lower income groups. Transaction process in the housing sector will immensely benefit if various charges in the process are standardized and charged uniformly at similar rates all over the country.

Rationalization of stamp duty and registration charges as well as differential rates based on gender, income, areas etc which some States have already introduced and others are contemplating is a right step towards making housing more affordable. Stamp duty charges in India are amongst the highest in the world way above even the rest of Asia. This needs to be addressed so that the sector will benefit immensely if they can be rationalized across the country according to global norms of 1-2%. In cases where the State

Government may feel that there could be losses in the revenue collection on account of revenue losses, the Government of India may consider creating a Fund that may compensate upto 50% loss of revenue to State Govt. due to lowering of stamp duty. Further, Government may consider reduction of stamp duty and registration charges of residential property as a conditionality of the Jawaharlal Nehru National Urban Renewal Mission.

Disclosure of all charges involved in the house acquisition process to enable the buyer of the house to plan and take into consideration all these costs needs to be introduced and communicated to the buyer at the beginning of the process itself.

The need for bringing in transparency and self discipline amongst the real estate brokers, valuers, as also developers and builders cannot be over emphasized. Valuation of property is central to the purchase transaction particularly, if a loan is being taken. The way that it is used can directly affect the nature, the funding and the prudential norms applicable to the financing. Lenders, consumers and investors need to have full confidence in the qualification of the valuer, broker, the valuation methodology and the results. Regulation of the intermediary community covering

accreditation, standards, activities, reporting, continuous education and oversight is necessary to ensure healthy growth of the real estate sector. In particular the brokers, valuers need to adopt Code of Conduct and ethics as well as a set of professional standards that they need to conform to. These should be given wide publicity and disseminated effectively so that the credibility of these intermediaries is enhanced in the eyes of the general public. Further, simple and transparent mechanisms of complaint and grievance redressal need to be in place.

Setting up of a Real Estate Regulator on the lines similar to those already working in other economic sectors in the country needs to be urgently taken up in order to bring in professional and ethical practices in the interest of the consumer.

A National Council may be set up headed by the Hon'ble Minister of Housing and Urban Poverty Alleviation or by an eminent personality which will be responsible for overall development and growth of the housing sector. Other members could be drawn from State Governments, Ministry of Finance, Reserve Bank of India, National Housing Bank, Planning Commission, Housing and Urban Development Corporation, real

estate developers, Non Governmental Organisations (NGOs), academic institutions, and independent experts.

All mortgage lenders may be required to quote an Effective Annual Rate (EAR). The EAR will represent the effective annual rate on their loan offers i.e. total annualized cost of a loan including the interest rate, service fee, legal charges, processing fee and any other fee/charges reduced to an annual rate. The EAR will facilitate comparison across the lenders and enable borrowers to make informed choices.

Use of technology has reduced transaction costs particularly in the banking industry, as demonstrated in reduction of transaction cost per distribution channel. The transition from the teller system to telephone then to mail, to Automated Teller Machines to PC Banking and presently through the internet/mobile phones has proved the benefits both for the banks and the customers. Similarly in the housing delivery process, computerization of land records and creation of a central data base would be effective in reducing transaction costs as well as bringing in greater authenticity in the real estate market. Link-

ing of home loan data disbursement through the use of information technology to National Housing Bank by HFCs/Banks can create a central repository of home loans. This data repository can be linked to the underlying asset. This will ensure authenticity in transactions and prevent possible frauds. Thus a national immovable property registry can be set up. Initially, pilots may be taken up in some of the States which have computerized their land records. As National Housing Bank has already developed an electronic repository of information relating to loans of HFCs, and is launching shortly a Housing Price Index, the same infrastructure can be used for developing it into a national housing information centre. For the purpose of dissemination of information on housing, for the average consumer, National Housing Bank may set up a housing information portal for capturing all relevant information.

A public awareness campaign maybe undertaken to sensitize users that purchasing a house is much more than bare or even the capital cost of the house. The acquisition costs are high and need to be factored in when purchasing the house.



Appendices

Appendix A

1 **Consumer Protection in Housing Finance: Cross Country Experience**

In most countries like the UK, USA, Australia etc, safeguarding the consumers interest is a matter of serious concern. Public education is sought to be achieved, inter alia, through information on the websites of the individual lenders as also of lenders associations, regulators and consumer groups. Such awareness initiatives cover a vast range of aspects of interest to consumers, such as information on consumer protection laws, rights and responsibilities of customers as well as lenders, grievance redressal mechanism etc.

The Financial Services Authority in UK, the independent regulator set up by Government to look after the financial services industry and protect consumers, provides detailed information on aspects such as Guidance and tips for prospective home buyers, Procedure and precautions for obtaining loans, Financial planning, FAQs, etc.

Under the Truth in Lending Act, in USA, full disclosure of all

costs in lending is made mandatory. There are several other Federal and State Laws compelling disclosure of lending practices to customers and the general public.

The Council of Mortgage Lenders (CML), UK whose members include banks, building societies and other mortgage lenders provides a range of general consumer information including downloadable guides on home buying and selling, loan products and mortgage payment protection insurance, besides a list of frequently asked questions about mortgages and the mortgage market.

A statement summarizing consumer protection measures in three major mortgage markets in the world, viz. USA, UK and Australia is placed at Annexure.

2 **Initiatives of the National Housing Bank in Consumer Protection and Education**

With the growth of the housing finance sector, NHB has felt an urgent need for consumer education in India in order to facilitate the following:

- Consumers being able to access information which is simple, clear and understandable and not ambiguous or misleading;
- Borrowers being treated fairly post disbursement of the loan as well and in particular being informed of relevant changes to their loan terms and conditions, where applicable;
- Consumers being capable and confident of understanding the terms and conditions of housing loans, including all costs involved;
- Consumers being explained by the lenders, the various requirements for taking loans and their interpretations;
- Lenders (HFCs) being adequately capitalised, managed and regulated;
- Consumers, being able to take decisions on their own and the responsibility connected with their decisions.

In keeping with best practices in this regard, the National Housing Bank has framed guidelines on a **Fair Practices Code for Housing Finance Companies (HFCs)**, based on which each HFC is to adopt a code for itself. The Code seeks

to promote good and fair practices by setting minimum standards in dealing with customers, increase transparency so that the customer can have a better understanding of what he / she can reasonably expect of the services, encourage market forces, through competition to achieve higher operating standards, promote fair and cordial relationship between customer and HFC and foster confidence in the housing finance system.

The main objectives of the Fair Practices Code for HFCs are :

- a. promote good and fair practices** by setting minimum standards in dealing with customers;
- b. increase transparency** so that the customer can have a better understanding of what he/she can reasonably expect of the services;
- c. encourage market forces**, through competition, to achieve higher operating standards;
- d. promote a fair and cordial relationship** between customer and HFC; and
- e. foster confidence** in the housing finance system.

Introduction of a System of Mortgage Counselling

At present, prospective house/flat buyers, take the services of some brokers, agents and/or consultants. Direct Sales Agents of banks/ HFCs or other tied agents provide advice which is often biased. There is no standard or uniformity in their advice, fees and/or charges, quality of advice, responsibility or accountability. This leads to complaints later. Professional advice also required by those who want to buy new dwelling units without availing loans. To meet this gap, it is proposed to introduce a system of mortgage counseling to be done by independent Mortgage Counsellors. They would not only enhance fairness and transparency in housing loans but would also provide a good service to the borrowers and mortgage originators as well.

Promoting a Joint Forum of banks and HFCs

NHB proposes to promote a Joint Forum of banks and HFCs. The forum will be modeled broadly on the Foreign Exchange Dealers' Association of India (FEDAI) and Fixed Income and Money Market Dealers Association of India (FIMMDA).

The objectives of the Forum would be to:

- Define and maintain high professional and ethical standards in all areas of operation of the housing finance industry,
- Promote and exchange opinions on best business practices and code of conduct,
- Project image of the housing finance lenders as responsive, caring to customer requirements and demands,
- Embrace best practices in customer services,
- Act as a clearing house for professional information exchange and development of suitable data base.
- Standardization of documentation of underwriting, new products etc.
- Interact with regulators and government on common issues of housing finance,
- Facilitate the functioning and growth of housing finance market in a healthy and holistic manner,
- Assist NHB in its efforts for consumer protection, financial education, fairness and transparency in lending.

In other countries, such industry bodies have emerged as significant voices in the financial sector such as the Council of Mortgage Lenders, UK, Mortgage Lenders' Association, USA, European Mortgage Federation etc.

I. Consumer Protection	USA	UK	Australia
i) Legislation	Truth in Lending Act The Truth in Lending Act requires disclosure of the "finance charge" and the "annual percentage rate"--and certain other costs and terms of credit--so that a consumer can compare the prices of credit from different sources. It also limits liability on lost or stolen credit cards. Home Equity Loan Consumer Protection Act The Home Equity Loan Consumer Protection Act requires lenders to disclose terms, rates and conditions (APRs, miscellaneous charges, payment terms, and information about variable rate features) for home equity lines of credit with the applications and before the first transaction under the home equity plan. Home Mortgage Disclosure Act (HMDA) The Home Mortgage Disclosure Act (HMDA) requires certain lending institutions to report annually on their originations and purchases	Financial Services and Marketing Act, 2000 The Financial Services Authority (FSA) was set up in 1997 as a one stop regulatory shop for all financial services regulations in the UK. With effect from October 31, 2004 FSA's regulatory role was extended to cover mortgages. FSA is required to regulate lending, advice administration and arranging of mortgages given by lenders, brokers and intermediaries and to make lenders and intermediaries comply with new disclosure requirements. FSA's consumer agenda rests on the following four pillars: - Capable and confident consumers - Simple and understandable information for the use of consumers - Well managed and adequately capitalized firms treating consumers fairly and - Risk based and proportionate regulation	Australian Property Legislation varies between each jurisdiction in every State of Australia there is a different scheme of regulating property rights that combines legislation. Despite differing statutes, the substantive effect in each jurisdiction is quite similar. Property Legislation in all states is grounded upon the Torrens principle of registration of title. This posits that each state have a central register of all land in the state and that the register also show the 'owner' of the land. Another major principle of this system is 'indefeasibility' of title - where a right has been entered on the register, it cannot be defeated by later rights except in certain circumstances.

	USA	UK	Australia
	of home purchase and home improvement loans as well as applications for such loans. Real Estate Settlement Procedures Act The Real Estate Settlement Procedures Act requires that a consumer be given advance information about the services and costs involved in the closing of a residential mortgage. It also limits the amount that can be collected for mortgage escrow. Fair Debt Collection Practices Act The Fair Debt Collection Practices Act is designed to eliminate abusive, deceptive and unfair debt collection practices. Predatory Lending Bill Although not yet precisely defined, "Predatory Lending" is understood to encompass a series of unfair credit practices. Such practices can typically be in relation to mortgages. Practices such as making unaffordable loan to consumers based on their assets rather than their ability to pay, loan	Mortgage Rights (Scotland) Act 2001 Deals with: Sec 1. Application to suspend enforcement of standard security Sec 2. Disposal of application Sec 3. Registration of order under section 2 Sec 4. Notices to debtors, proprietors and occupiers Sec 5. Crown application Sec 6. Interpretation Family Act 1996 The Consumer Credit Act, 1974 Association of Home Information Pack Providers (AHIPP) code of practice All Home Information Pack (HIP) providers subscribing to the code will be subject to stringent standards to ensure consumers purchasing a	

	USA	UK	Australia
	flipping, credit insurance packing, deceptive lending, i.e. concealing the specifics of a loan obligation from a borrower, excessive fee charging, charging illegal or excessive fees or point, falsifying documentation, including appraisals and credit information.	pack through an approved provider can place total confidence in the finished product.	
ii) Regulatory/ Self Regulatory Organisation/ bodies	i) Independent Mortgage Brokers Association Of Ontario ii) Federal National Mortgage Association (Fannie Mae) iii) Federal Home Loan Mortgage Corp. iv) Federal Trade Commission	(i) The Financial Services Authority in its role as the Regulator (ii) The Office of Fair Trading enforcing rules of the Consumer Credit Act	(i) The Mortgage Industry Association of Australia (ii) Australian Securities and Investments Commission (ASIC)- ASIC is the consumer protection regulator for financial services.
iii) Consumer Organisation	i) AARP Consumer Protection, Washington DC ii) American Council on Consumer Interests iii) Consumer Action, California iv) Consumer Alert, Washington v) Consumer Federation of America, Washington DC vi) National Coalition for Consumer Education, Washington DC	National Consumer Council	National Community Housing Forum Australia - It is an information forum for stakeholders involved in community housing in Australia.

	USA	UK	Australia
	vii) National Consumer Law Centre, Boston viii) National Fraud Information Centre, Washington DC ix) US Public Interest Research Group, Washington DC		
II. Consumer Awareness			
i) Mortgage Counselors	Housing Counseling Agencies approved by Department of Housing and Urban Development	Association of Independent Financial Advisors	MIAA Mortgage Consultants
ii) Lenders Association	(i) Mortgage Lenders Network	(i) The Building Societies Association (ii) Association of Mortgage Intermediaries	(i) The Mortgage Industry Association of Australia (MIAA) is a provider of service and representation to mortgage brokers, mortgage managers, mortgage lenders (bank and non-bank), and originators to assist them develop, foster, and promote the mortgage industry. It advocates ethical business practices, works closely with national and state Governments, offers industry specific education, provides compliance and legal information, runs a consumer information programme and industry networking events.

Appendix B

Transaction Cost in Housing: A Theoretical Framework

The real estate market is not single neoclassical exchange market, but is rather a set of overlapping submarkets differentiated by tenure, location, size and quality (MacLennan, 1982, *Housing Economics*, London and New York: Long man, pp 59-75).

There could various sources of transaction cost in housing which act as impediment and inhibit the adjustment of the market to a neoclassical equilibrium.

A. Search cost:

The unique features attached to the housing market viz. heterogeneity and locational considerations makes it costly venture to identify the house of choice. Identifying and evaluating the various attributes typically involves the physical inspection of dwellings at different locations. Home purchasers and renters can avail the services of brokers and middlemen by paying commission.

B. Legal and Administrative Costs

The amounts of legal and administrative costs are different for consumers who choose to be renters and homeowners. Rental contracts may specify the payment of security deposits amounting to couple of months rent and other costs. For

home purchasers, the legal and administrative fees due at the time the contract is executed may be far larger.

C. Adjustment Costs

The adjustment costs of moving include both out-of-pocket and psychic costs. Out-of-pocket costs include the costs of transporting the movables and the value of furnishings rendered unusable after the move. It is difficult to ascertain the amount of psychic costs of moving to a different residence. The psychic and transactions costs could be revealed by the maximum amount that a household is willing to pay to continue residence in its current dwelling.

D. Expectations and Uncertainties

The transactions cost of moving to a house of choice is also affected by household uncertainty and expectations about the future. Studies reveal that expectations of interest rates, price trend and tax change affects tenure choice, time of decision and mobility likelihood.

E. Financing Costs

In addition to legal and administrative cost there may be purely financial costs associated with housing market transactions. Home mortgage interest rate could be varying

or fixed. Empirical studies reveal that incidences of home moves decline when interest rates rise (Quigley, 2002). Declines in house prices increase the costs of mobility which would force households to realize capital losses on their homes (Chan, 2001; Stein 1993). Transactions in a declining market are less numerous due to loss aversion by sellers (Genesove and Mayer, 2001).

Model of Transaction Cost in Housing Market

John H. Quigley in his working paper on Transaction Costs and Housing Market has developed a simple model to ascertain the transaction cost that prevents a homeowner from moving to a house that would maximize his utility given the income level.

The model assumes a Cobb-Douglas utility function in housing (H) and other goods (X). Unit price of housing is P_H .

$$U = H^\alpha X^{1-\alpha} = H^\alpha (Y - P_H H)^{1-\alpha} \quad (1)$$

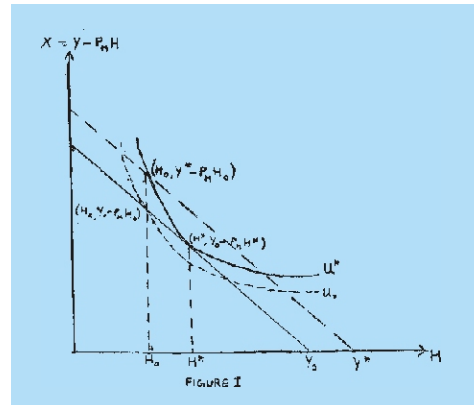
Where Y is the household income and α is the parameter of consumption preference. From (1), we can derive a demand function for housing as

$$P_H H = R = \alpha Y \quad (2)$$

Equation (2) implies that in equilibrium, the household spends a fixed fraction of its income on rent (R).

Let Y_0 and H_0 be the observed level bundle of income and housing consumption. Let H^* be the optimal level

of housing consumption at the given level of income Y_0 . Thus moving from H_0 to the optimal level H^* will make the household better off. This is shown below in the figure I:



U^* is the optimal level of utility that the consumer can achieve by consuming $(H^*, Y_0 - P_H H^*)$ at the given level of income Y_0 . However, the observed level is $(H_0^*, Y_0 - P_H H_0)$ which gives him utility U_0 which is lower than U^* .

An alternative option to make this household as well as moving to H^* is to let his income increases to Y^* , such that he consumes the bundle $(H_0, Y^* - P_H H_0)$. Then the following equation holds:

$$H_0^\alpha (Y^* - P_H H_0)^{1-\alpha} = H^{\alpha} (Y_0 - P_H H^*)^{1-\alpha} \quad (3)$$

The household's utility is equivalent in bundle $(H^*, Y_0 - P_H H^*)$ and $(H_0, Y^* - P_H H_0)$. Thus, the income equivalent of the utility gain of moving from $(H_0, Y_0 - P_H H_0)$ to $(H^*, Y_0 - P_H H^*)$ is $Y^* - Y_0$. If the household does not move to H^* and stay at H_0 , it must be because that the transaction costs associated with moving outweigh the utility gain from moving or its income equivalent.

Using equation (2) and (3) we can express Y^* in terms of Rent R as,

$$Y^* = \left(\frac{R^*}{R_o}\right)^{\alpha/(1-\alpha)} [Y_o - R^*] + R_o \quad (4)$$

Then the income equivalent of utility gain from moving is expressed as

$$Y = Y^* - Y_o = \left(\frac{\alpha Y_o}{R_o}\right)^{\alpha/(1-\alpha)} (1 - \alpha) Y_o + R_o - Y_o \quad (5)$$

Equation (5) says that, if a household is consuming its desired equilibrium level of housing services (i.e., if $H_o = H^*$), the right hand side of (5) is zero. If the household is not consuming its desired level of housing, this is because the transactions costs of moving for this household are larger than the income equivalent of the utility gain from moving. Equation (5) provides a lower bound

estimate of the transaction costs incurred in the housing market.

Similarly, the lower bound estimate of transaction cost can also be estimated in case the demand function for housing services is known.

Thus it can be seen that transaction costs acts as an impediment in optimal allocation of resources. Government can assist in improving the allocation of resources by facilitating flows of information and by providing online property records. Technology can reduce some of these costs for homeowners by making available the information on web-sites where home purchasers can search for dwelling with various features matching their requirement.



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राष्ट्रीय आवास बैंक

(भारतीय रिज़र्व बैंक के संपूर्ण स्वामित्व में)



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Head Office :

India Habitat Centre, Core 5A,
3rd Floor, Lodhi Road, New Delhi-110003
Tel.: 011-2464 9031-35 • Website: www.nhb.org.in

Regional Office :

Bombay Life Building, 3rd Floor,
45, Veer Nariman Road, Mumbai - 400 023, INDIA
Ph.: 2285 1560-64 Fax: 2285 1555

Representative Office :

Reserve Bank of India Building,
1st Floor, 6-1-56, Secretariat Road,
Saifabad, Hydrerabad - 500 004, INDIA
Ph.: 23230984 Fax: 23230983