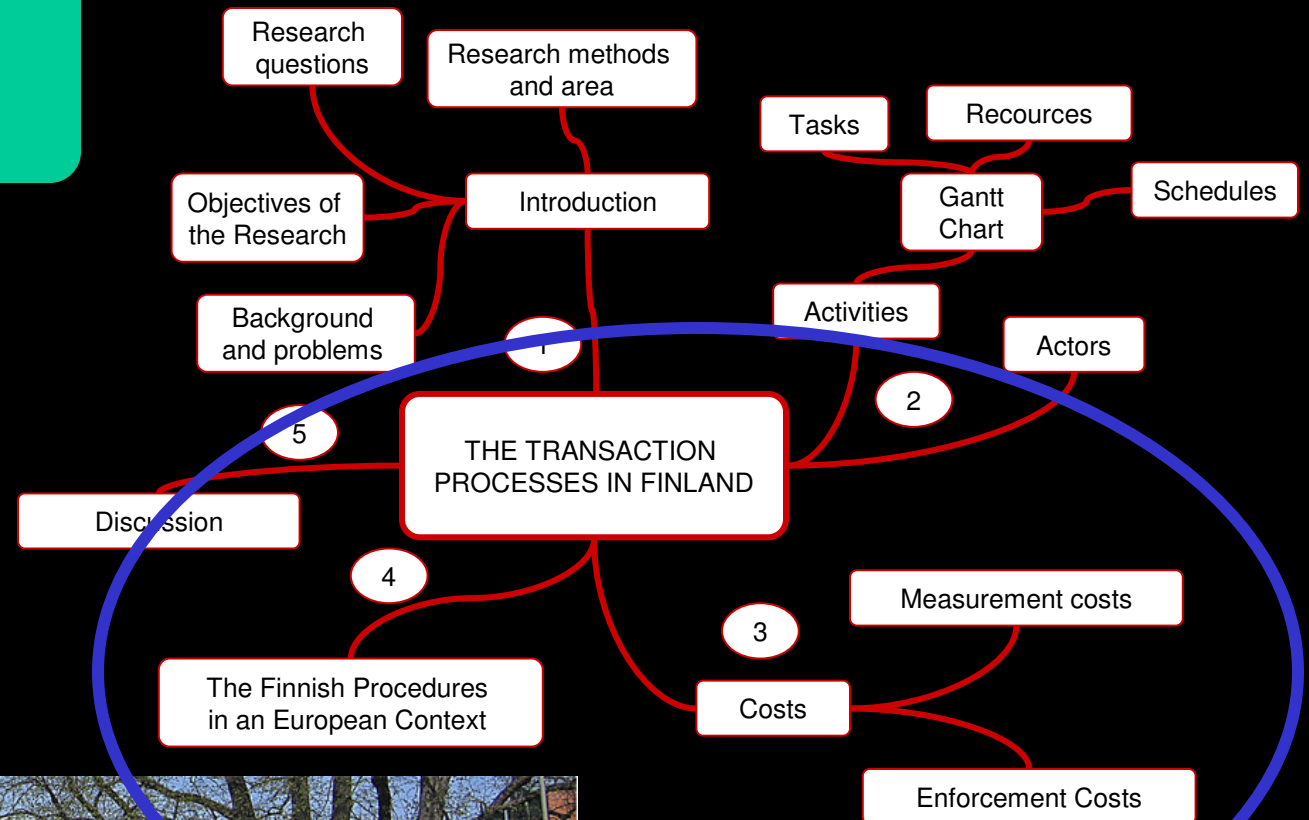


Arvo Vitikainen

# THE REAL PROPERTY TRANSACTION COSTS IN FINLAND

Based on  
Ilkka Mikkonen's  
research

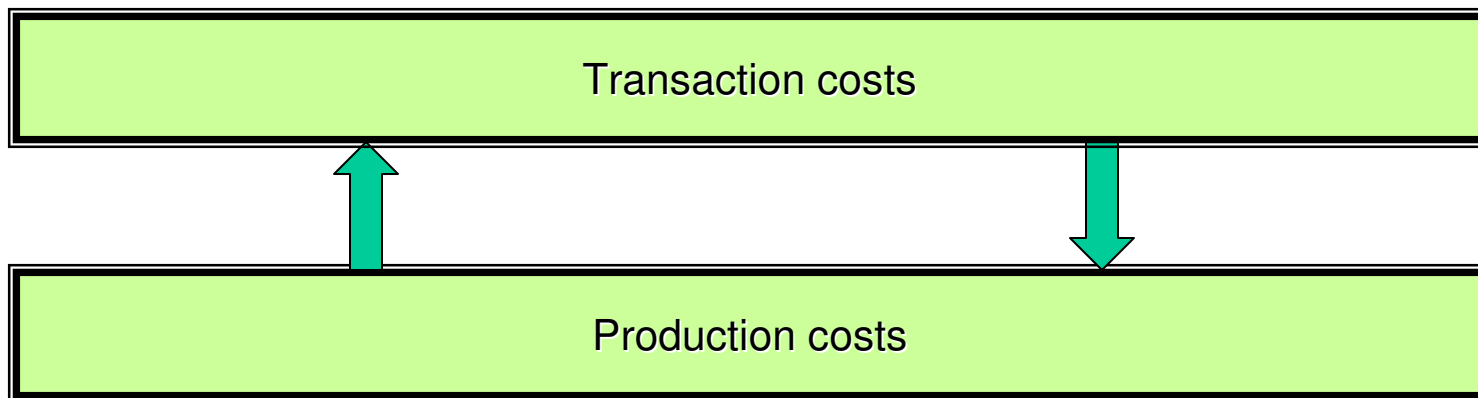


## TRANSACTION COST THEORY BY COASE AND WILLIAMSON

Costs can be classified in two categories: production costs and transaction costs.

**Production costs** are all the costs that are associated directly with productive activities such as manufacturing, logistics, and product development.

**Transaction costs** are the costs of running the economic system (Arrow 1969). Transaction costs are the economic equivalent of friction in physical systems (Williamson 1998). It has been estimated that at least 45% of the gross national product in a developed society is generated by transaction costs (North 1990).



Coase (1937): There are transaction costs that determine what is done in the market, with price as the regulating mechanism, and what is done inside the firm, with bureaucracy as the regulator.

According to Coase (1937) the most important market (external) transaction costs and the most important bureaucratically (internal) are:

## TRANSACTION COSTS

### **EXTERNAL**

#### **Market transaction costs:**

- The cost of determining the price of a product or service
- The cost of negotiating and creating the contract
- The cost of information failure

### **INTERNAL**

#### **Bureaucratic transaction costs:**

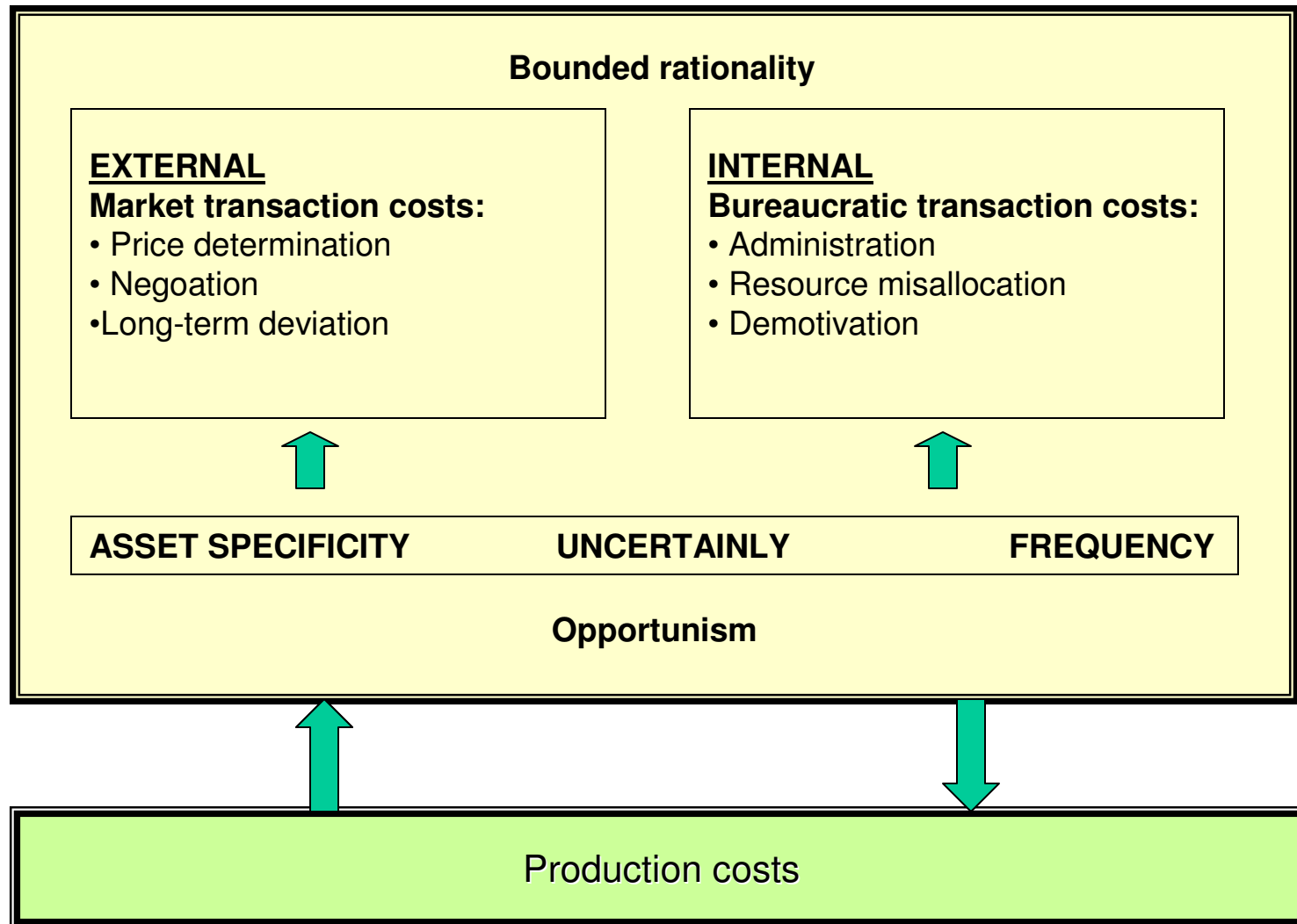
- Administration
- Resource misallocation
- Demotivation

Williamson (1985) extended the argument by noting that two behavioural assumptions are critical:

1. **Individuals in an organisation are boundedly rational** (“human behaviour is intendedly rational, but only limited so”). This limitation makes it impossible to structure perfect contracts, and any contract will be incomplete even if all information is available.
2. **Individuals behave opportunistically**. That means that they will act in self-interest with guile. The implication is that promises of responsible behaviour are only credible when they are supported by enforceable commitment, since individuals otherwise would break an agreement if it is in their self-interest to do so.

Williamson (1985) demonstrated also that three factors play a fundamental role in determining if market or bureaucratic transaction are optimal. The factors are asset specificity, uncertainty, and frequency of transactions.

# TRANSACTION COST FRAMEWORK



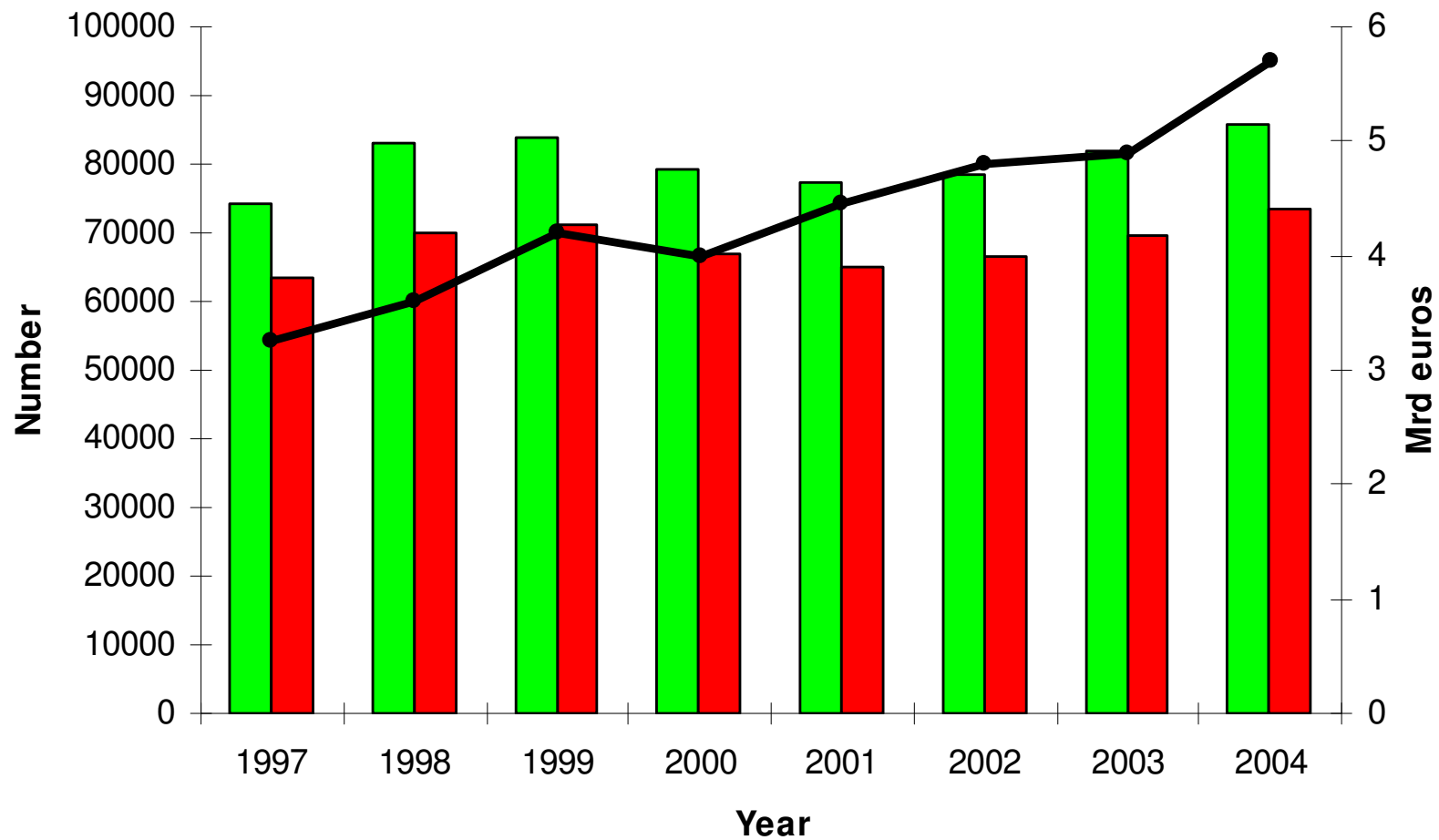
Transaction costs of **ex ante** (Williamson 1985) are the costs of drafting, negotiating, and safeguarding an agreement – Cf. North 1990; Stubkjaer 2004 measurement costs.

Measurement costs are the costs of measuring the valuable attributes of what is being exchanged. A surveyor's measurement of the size of an area might be one example of attributes only, 'measurement' is here taken in its wide sense, and no assumption should be made that the 'measurements' are always quantified. A good or service is characterized by a number of attributes that each contributes to or detracts from the utility of the good for a prospective buyer. The number and value of these attributes tend to vary among potential buyers. Thus, each has to identify and assess (measure) the value of these attributes. Transaction costs are made up of the information costs in ascertaining the level of individual attributes of each unit exchanged (Stubkjaer 2004)

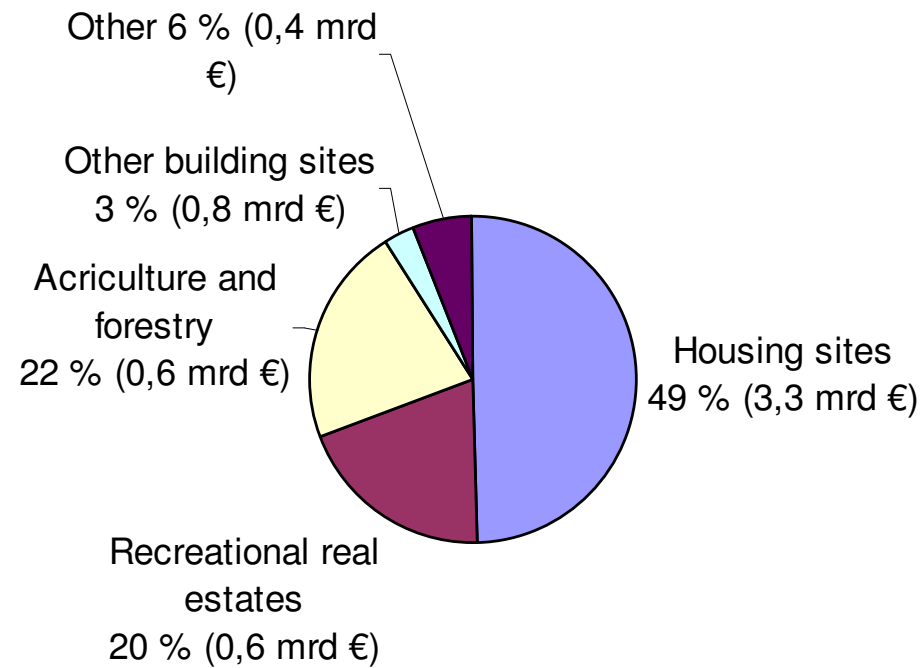
Transaction costs of **ex post** (Williamson 1985) are the enforcement costs.

Enforcement costs are the costs needed to make parties fulfil the obligations they agreed upon. Enforcement can come from internally enforced codes of conduct, from second-party retaliation, or from third-party sanctions, be it social exclusion or state coercive measures. Enforcement measures are cost effective only as far as the costs of policing are less than the benefits of such enforcement. The likelihood of defection by the other party has to be included into the estimate of costs as a risk premium. The amount of the risk premium may be high enough as to prevent more complex exchanges, or the exchange may be restricted to take place within the circle of personally known parties, where the risk can be reasonably taken into account. (Stubkjaer 2004)

## Number of transactions and purchases (sales) and the amount of money in real property transactions in Finland



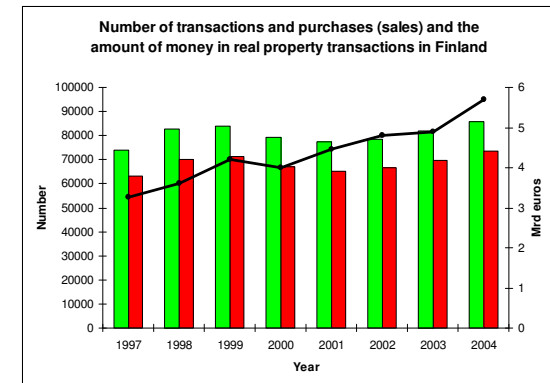
## Number of real property transactions and the amount of money in real property transactions by land use type in 2004





## Case Finland

The number of sales in 2004	73 930
<u>The amount of money in sales</u>	<u>5,685 mrd €</u>
	77 000 €/sale



## THE TRANSACTION COSTS OF REAL ESTATE TRANSACTIONS IN 2004

- Fees of the purchase witness (85.898 x 77 €)	6 600 000 €
- Broker's fees + VAT (4,88 % - 50 % of cases)	280 000 000 €
- Subdivision (27.000 x 850 €)	23 000 000 €
- Fees for title registration (85.898 x 60 €)	5 200 000 €
	<hr/>
	Σ= 315 000 000 €
<u>Transaction tax (4 % of property per capita)</u>	<u>227 000 000 €</u>
<b>Total</b>	<b>542 000 000 €</b>

**This means that transaction costs are about 10 %**

(7 700 €/sale)

cf. Viitanen 2003: In Finland transaction costs for the seller and the buyer are about 10 %

## MAINTENANCE OF THE PUBLIC LAND DATA BANK SYSTEM

**Maintenance of the Cadastre**      **12 400 000 €/year**

(the real Estate Register)

National Land Survey

**Maintenance of the Legal Land**      **18 200 000 €/year**

**Register** (the Register of Property

Ownership and Mortgager)

The Local Court

---

### Cadastre:

- 2 500 000 real estate units      = 5 €/year/real estate unit

### Legal Land Register:

- 110 000 title registrations/year
  - 150 000 mortgages/year
  - 7 600 leasehold registrations/year
- } = 7 €/ year/real estate unit  
(68 €/regisration)

## Transaction costs for seller and buyer in Finland, Slovenia and Sweden in 2004

	Costs ( € )		
	Finland	Slovenia	Sweden
Notar		140	
Purchase witness	77		
Subdivision	850	500	1600
Fee for municipality		40	
Title registration	60	90	88
Summa:	987	770	1688
Tax *)	4 %	2 %	1,50 %
	4000	2000	1500
<b>Total</b>	<b>5.000</b>	<b>2.800</b>	<b>3.200</b>
*) Purchase price 0 100.000 €			

## Number of procedures and time for the title in Finland, Sweden and Slovenia <http://rru.worldbank.org/DoingBusiness/ExploreTopics/RegisteringProperty/>)

	Number of procedures	<b>Time (days)</b>	Cost (fee+ transfer tax)
Finland	3	<b>14</b>	60 € + 4,0 %
Sweden	1	<b>2</b>	90 € + 1,5 % - 3,0 %
Slovenia	6	<b>391</b>	88 € + 2,0 %

