

## Limited Service Brokerage White Paper

### **Introduction**

Six months ago, following the last NAR meeting, OAR developed information and business tools designed to help members deal with limited service and MLS-only listings. At that time, local multiple listing services across the state were grappling with demands from members that the MLS not allow entry of limited service listings. Such demands conflict with NAR's guidance to multiple listing services. That guidance is that MLS participants be allowed to file any exclusive right to sell or exclusive agency listing, as those things are defined under state law, without regard to the services being offered the seller.<sup>1</sup>

The member information and business tools were intended to help agents protect themselves when dealing directly with what is essentially an unrepresented seller. Providing these tools was a critical and necessary first step in dealing with the business problems created by new business models that limit the professional services being provided to sellers by real estate licensees. However, after attending the NAR meeting in Orlando, Florida, it is clear the legal issues raised by limited service listings will continue to challenge members and REALTOR® organizations.

The purpose of this white paper is to examine the business and legal issues raised by limited service listings in a more systematic way. Although the analysis will focus on Oregon real estate license laws, much of the discussion will involve common law concepts of contract and agency applicable in most, if not all, states. Following the legal analysis, recommendations will be made regarding legislative or administrative agency solutions being considered in other states.

### **Limited Service Listings and Antitrust**

The key to understanding the legal issues raised by limited service listings is NAR's admonition to REALTOR® multiple listing services that they allow MLS participants to file any exclusive right to sell or exclusive agency listing without regard to the services being offered the seller. But for this NAR requirement, whether or not to allow such listings in the MLS would be a local political decision. It is, therefore, necessary first to understand why NAR requires REALTOR® multiple listing services to publish limited service listings.

According to NAR:

“NAR's MLS policy requires MLSs to accept listings that under state law are legal exclusive right-to-sell or exclusive agency listings and that offer compensation to cooperating brokers. By the very nature of the MLS and the

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<sup>1</sup> Such listings are identified by code in the MLS data so other participants will know the nature of the listing before attempting to find a buyer or show the property.

MLS rules, submitting a listing for inclusion in the MLS constitutes the listing brokers' offer of compensation/cooperation to other MLS participants. Thus, unless there is some indication that the broker expressly repudiates the making of such an offer of compensation/cooperation to other MLS participants, the MLS may not reject these listings. In particular, MLS policy does not allow a listing to be rejected on the basis that the listing broker provides only a limited degree of service to the seller, or even no service at all other than submission of the listing to the MLS."

NAR's explanation is, of course, completely circular in that it only says NAR's MLS policy requires the result. That begs the question of why NAR MLS policy is what it is.

It should come as no surprise that the basis for NAR's policy, and subsequent recommendation, is federal and state antitrust laws. Multiple listing services are functionally an agreement among competitors. Antitrust laws make any agreement among competitors illegal if the agreement unreasonably restrains trade. It follows that an MLS rule or policy that has the effect of unreasonably restraining trade will create serious legal risk because the policy will, by definition, be the result of an agreement among the competitor members of the MLS.

Access to the MLS is a particularly sensitive antitrust matter because access is often necessary to compete effectively in the local real estate market. If access to the MLS is necessary to compete, denying that access to competitors invites antitrust claims. When access denial places potential competitors at a market disadvantage, the denial can be justified only by showing the market disadvantage suffered by excluded competitors is necessary to gain the pro-competitive advantages of having an MLS in the first place.<sup>2</sup>

Listing property in the MLS is pro-competitive because the property's availability, its attributes and the asking price are made known to brokers who may have clients interested in purchasing the property. The MLS also facilitates market activity by reducing the transaction costs associated with cooperation among competing brokers. A limited service listing has no impact on the first of these two pro-competitive advantages because the property information does not vary with the services being offered the seller by the listing broker.<sup>3</sup> That leaves the broker cooperation advantage to carry the justification necessary to exclude limited service listings from the MLS.

NAR's explanation of its policy addresses the cooperation issue. NAR's policy says: "unless there is some indication that the broker expressly repudiates the making of such an offer of compensation/cooperation to other MLS participants, the MLS may not reject these listings." The focus is on the offer of compensation/cooperation to fellow brokers, not the services being provided the seller by the listing broker.

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<sup>2</sup> The pro-competitive advantages of an MLS flow from the timely exchange of relevant market information and increased cooperation among brokers to the benefit of consumers. MLS rules must support these advantages.

<sup>3</sup> As one buyer broker put it recently at an NAR meeting: "I'd rather the seller list it with a MLS-only broker than go FSBO because at least I know the property is for sale and something about it."

Cooperation for MLS purposes means allowing other MLS members to show the property and get the co-op commission, if any, being offered by the listing broker. As long as the listing broker has an agreement with the seller that precludes other brokers from marketing the property on the seller's behalf during the term of their listing, the listing broker can meet MLS cooperation requirements. All that is necessary is that listing brokers allow other participants to show the property. The amount of compensation being offered, if any, is left to the listing broker.<sup>4</sup> It is for the cooperating broker to decide whether the compensation offered is sufficient to warrant their efforts in finding a buyer.

It would be possible for multiple listing services to change the definition of "cooperation" to increase the duties MLS participants owe each other. Multiple listing services are based on the business relationship between MLS participants, not the relationship between participants and their clients. Demanding that participants provide specific services to clients raises the antitrust issues discussed above. Demanding that participants provide specific services to other participants, without regard to the services participants provide their clients, is another matter.

By focusing on the relationship between participants rather than the relationship between participants and their respective clients, an MLS could require increased cooperation. For instance, an MLS could require as a condition of participation that all contact with other MLS participants regarding listings filed with the MLS be through the listing broker. Rather than demand that participants provide specific services to their clients, the MLS simply redefines "cooperation" to increase the pro-competitive advantages of MLS services.

Redefining cooperation is mostly a matter for NAR. A national approach would be far less risky from an antitrust standpoint. Moreover, NAR provides insurance coverage to member multiple listing services. To get the coverage, the MLS must adopt NAR policies. An MLS with cooperation policies more stringent or inconsistent with NAR's would be taking a substantial risk.<sup>5</sup> NAR will, therefore, have to take the lead on any change in MLS policy to increase participant cooperation requirements.

### **Statutory and Administrative Efforts to Regulate Limited Service Listings**

NAR's MLS policy has driven those who believe limited service listings create unwanted work and legal risk for cooperating brokers to seek other means of solving the problems they see as inherent in limited service listings. Because the limited service "problem" is seen as one of brokers not providing adequate services to their clients, these efforts have focused on trying to control the relationship between the broker and the broker's client. The only way one broker can control the relationship between another broker and that broker's client is through state licensing statutes, administrative rules or both.

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<sup>4</sup> Article 3 of the REALTOR® Code of Ethics covers the "showing" part of cooperation. The compensation part is left exclusively to the multiple listing services. Because of price fixing concerns, the compensation side is really nothing more than a matter of notice to other participants.

<sup>5</sup> Non-REALTOR® multiple listing services and those that provide for their own insurance would not be subject to this limitation.

In Texas, an early participant in the limited service listing battle, industry participants complained to the Texas Real Estate Commission (TREC) that consumers did not understand limited service listings and that, as a result, buyers' agents were being forced to accept more risk and do more work. In response, the TREC adopted an administrative rule defining the minimum level of services a Texas real estate licensee was required to provide in a real estate transaction.

For its trouble, the TREC was sued by discount brokers and accused by consumers of creating a rule that required them to pay for services they did not need or want. Faced with lawsuits and consumer complaints, the TREC repealed its minimum service rule. It is now considering instead a disclosure rule that would require brokers to disclose the services the client is getting for the fee paid and what other services are available for additional fees. Meanwhile some discount brokers in Texas have developed their own "Limited Service Agency Disclosure."

The Texas Real Estate Commission has, to date, issued no new rule to take the place of the one repealed. Instead it has asked the Texas Attorney General whether it has the authority to establish minimum service standards.<sup>6</sup> The Texas Association of REALTORS® filed a brief with the Texas Attorney General arguing in favor of the TREC's authority to demand minimum client services. Pending the outcome of the TREC's request to the Attorney General, the Texas Association of REALTORS® is considering legislation along the lines of that recently enacted into law in Illinois.

In Illinois, the state legislature passed, and the governor signed, legislation establishing minimum client services for "exclusive brokerage agreements."<sup>7</sup> Under the new Illinois law, which went into effect in August of this year, an "exclusive brokerage agreement means a written brokerage agreement that provides that the sponsoring broker has the sole right, through one or more licensees, to act as the exclusive designated agent or representative of the client and that meets the requirements of Section 15-75 of this Act." Section 15-75 of the Act contains the minimum services requirements.

According section 15-75 of the Illinois law, exclusive brokerage agreements must specify that the sponsoring broker will provide, at a minimum, the following services:

- “(1) accept delivery of and present to the client offers and counteroffers to buy, sell, or lease the client's property or the property the client seeks to purchase or lease;
- (2) assist the client in developing, communicating, negotiating, and presenting offers, counteroffers, and notices that relate to the offers and

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<sup>6</sup> The Texas Attorney General has subsequently ruled the Real Estate Commission does have the authority to impose minimum service requirements on Texas licensees. The commission had not, however, enacted such rules as of January 1, 2005, but is in the process of adopting such rules.

<sup>7</sup> The term is taken from the Code of Ethics where it was developed as a way to define exclusive relationships after the advent of buyer agency.

counteroffers until a lease or purchase agreement is signed and all contingencies are satisfied or waived; and

(3) answer the client's questions relating to the offers, counteroffers, notices, and contingencies.”

Failing to provide minimum services is grounds for discipline by the Real Estate Commissioner. A number of other states have expressed interest in the Illinois approach to minimum service requirements.

Other states, rather than enacting new laws, are looking at existing real estate license law to find minimum service requirements. For instance, in Washington, a non-REALTOR® MLS has denied limited service listing brokers access to the MLS based on the belief that such listings are not “legal” under Washington law. The rumor is that the MLS interpretation is being urged on the Washington Real Estate Commission which is presently in the process of making revisions to Washington real estate statutes and rules.<sup>8</sup> It is also rumored that interpretation of existing real estate laws to require minimum service is being pursued in several other states, including California.<sup>9</sup>

In Oregon, the Real Estate Agency has expressed little interest in the issue of limited service listings. This lack of interest stems mostly from a lack of consumer complaints. Interestingly, Oregon license laws are very similar to those in Washington. In particular, Oregon and Washington license laws both impose affirmative agency duties that may not be waived. These “non-wavier” provisions, read in conjunction with plain language statutory agency duties, are being interpreted in other states to require some level of minimum service.

### **Legal Analysis**

Multiple listing services have proved poor vehicles for dealing with limited service listings because of the risk of the MLS being sued for violating antitrust laws. NAR's “recommendations” to the multiple listing services make the antitrust point. If the limited service broker follows existing MLS rules by “listing” the property, there is no procompetitive justification for MLS interference with a participant's relationship with their own client. Accordingly, what it means to “list” property has become an issue.

Some will find it ironic that an industry which worked almost exclusively for sellers for more than a hundred years is still debating what is and isn't a “listing.” In particular, what is or isn't an “exclusive right to sell” listing. The word “listing” means the act of including something on a list. In this case, a list of property that is for sale. Compiling and publishing such a list is the business of the MLS. “Listing” property, at one level, means nothing more than filing it with an MLS. A “listing” in this sense would be no more than an agreement between an owner and a broker to place a property in an MLS.

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<sup>8</sup> The Commission recently released draft rules that do not include minimum services.

<sup>9</sup> If existing laws do in fact require minimum services, that requirement will eventually be brought to light in real license discipline actions and civil lawsuits. To date, no such discipline action or suits have been reported.

“Listing” has also become an industry term of art for a more general marketing agreement between the owner of property and a real estate broker. Real estate brokers, probably because of the sales origin of the business, adopted the sale-of-goods concept of an “exclusive right to sell” to describe a certain type of listings. In the sale-of-goods industry, an “exclusive right to sell” is the name given a contract with the owner of goods that guarantees the salesman an exclusive right to market the goods in a particular territory or to a particular prospect list. In the case of real estate, the exclusivity is territorial according to MLS jurisdiction.

Multiple listing services will not take open listings because without territorial exclusivity there can be no cooperation between brokers. Only when the listing broker has an “exclusive” right to market the property, can they cooperate and, if willing, offer compensation. Limited service listings can, and do, contain exclusive marketing clauses. That is, the seller agrees not to let anyone else market the property during the term of the listing. Compensation, whether between listing broker and seller or listing broker and cooperating brokers, does not change the nature of the listing.

Limited service listings are confusing to an industry that has always functioned by sharing commissions broker to broker at the time of closing because limited service broker takes the listing fee upfront. However, payment for marketing upfront or at closing doesn’t determine whether the marketing agreement is exclusive. As long as the seller agrees not to allow other brokers to market the property during the term of the listing, the listing is an “exclusive right to sell.”

Because exclusive right-to-sell listings typically prevent the seller from entering into a listing with other brokers, they create as a matter of course, exclusive relationships. Most state license laws default to agency relationships upon listing. Thus, listing a property in most states creates an exclusive agency relationship by default. That state laws default to agency relationships does not, however, mean you cannot have a perfectly legal and binding contract that establishes an exclusive right to sell but does not require “representation” for the purpose of negotiating or closing a sale.

If you take another look at the new Illinois statute, you will now see the problem immediately. The Illinois definition of “exclusive brokerage agreement” is written in terms of “representation.” In Illinois you risk your real estate license if you enter into an exclusive brokerage agreement but don’t provide the services mandated by law. Great, but what prevents brokers from NOT entering into exclusive brokerage agreements?

There is nothing in Illinois law that demands exclusive brokerage agreements with clients. Nor is Illinois (or anyone else) likely to adopt such a rule because it would apply equally to buyer representation. Instead, proponents of the new legislation hope multiple listing services will equate “exclusive right to sell listings” with “exclusive brokerage agreements.” Maybe they will, but will it really work when the MLS gets sued in antitrust?<sup>10</sup>

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<sup>10</sup> Even if it does work, is it smart to ask the government to define the services an industry must provide?

Illinois' new law doesn't apply to listings where the "representation" is not exclusive. It is easy to write a contract that allows sellers to have as many "representatives" they might wish, but contains an exclusive right to sell. That is, a contract with a specific term that allows only the listing firm to market the property on the seller's behalf. Such a contract would fall within the MLS definition of an exclusive right to sell but outside the statutory definition of an exclusive brokerage agreement.

What has happened in Illinois, and will likely soon happen in Texas and other states, is that a "listing" for MLS purposes has become confused with "representation." Although compensation and listings are connected, compensation is not connected to representation. Compensation and agency is not the same thing. In fact, most states now have license law provisions like Oregon's ORS 696.840 that specifically divorce agency from compensation.<sup>11</sup>

"Agency" and "representation" are after the fact consequences of a particular kind of business relationship. If the relationship is contractual (it need not be), the scope of the contract controls the scope of the representation, not the other way around. Minimum service laws, like the Illinois law, depend on the mistaken belief that the scope of representation can control the scope of the contract. This is simply not true. It is easy to limit representation and still have the exclusive right to market the property. This simple fact will doom minimum service laws that define service in terms of agency duties.

This same disconnect between agency duty and contractual rights will also doom efforts to interpret existing license law duties to require minimum services. In Washington State, as in Oregon and many other states, real estate license laws contain plain language statements of agency duties. Most of these states, including Washington and Oregon, include among the statutory agency duties one requiring licensees to "present all offers in a timely manner." Most also contain provisions that say the statutory duties of a real estate licensee cannot be "waived."

Duty provisions, like the duty to present offers, are now being coupled with no "waiver" language to imply minimum services. Such interpretations attempt to turn a duty to seller into a duty to the public in general and buyer's agents in particular. Unfortunately, the "rights" that cannot be "waived" under these statutes are the sellers' rights, not the licensees's or those of the public.

The legal duty to present all offers creates a legal right in the seller to have all offers brought to their attention. This right to the seller cannot be waived. That being the case, a licensee who represents a seller must make arrangements to have all offers brought to the attention of the seller. If they fail, they will have breached their duty to the seller. But that does not

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<sup>11</sup> **ORS 696.840 Compensation and agency relationships.** The payment of compensation or the obligation to pay compensation to a real estate licensee by the seller or the buyer is not necessarily determinative of a particular agency relationship between a real estate licensee and the seller or the buyer. After full disclosure of agency relationships, a listing agent, a selling agent, or a real estate licensee or any combination of the three may agree to share any compensation or commission paid, or any right to any compensation or commission for which an obligation arises as a result of a real estate transaction and the terms of the agreement shall not necessarily be determinative of a particular relationship. Nothing in this section shall prevent the parties from selecting a relationship not specifically prohibited by [license law].

mean the seller's agent must personally present all offers. Telling buyer agents to present their offers directly to the seller easily meets the bare legal duty imposed if the broker and seller have agreed to that means of meeting the duty.

Even if making arrangements for a buyer's agent to present the offer didn't meet the statutory duty, breach of a statutory duty does not change the nature of a contract. An exclusive right to sell listing is an exclusive right to sell listing whether conduct under that contract is later judged a breach of statutory agency duties or not. This means that multiple listing services, which must depend upon contractual relationships, will remain on very soft legal ground if they deny access based on agency relationships. That suggests that attempts to change or re-interpret license laws to control MLS access will fail.

## **Recommendations**

OAR has responded to the advent of limited service listings by developing and distributing business information and tools to help buyer agents reduce the risk of working with limited service listings. Based on the analysis above, OAR does not recommend legislative solutions like those enacted in Illinois. OAR also does not recommend administrative rule solutions that involve imposition of minimum services.

At this point, the only further action that seems worthy of consideration is listing service disclosure. There is anecdotal evidence that some sellers do not understand the consequences of limited service listings. In particular, limited service listings impose transaction costs on buyers and their agents by increasing work and risk. Increasing transaction costs tends to lower market price.<sup>12</sup>

In addition to a lack of seller knowledge regarding the potential market impact of limited service listings, there have also been reports of seller confusion about paying the buyer's agent the commission negotiated or stated in the MLS. This suggests sellers may not be getting sufficient information from listing brokers about MLS practices and procedures. The lack of seller understanding can cause significant problems when it comes time to pay the coop commission at closing.

Disclosure is the normal industry solution for problems created by a lack of consumer information. Agency relationships have long been subject to state-mandated disclosures. Such disclosures do two things. First, they help consumers understand the relationship being proposed. Second, they explain the important consequences of the relationship. Such a two step disclosure model could be used to solve seller confusion and misinformation problems associated with limited service listings.

Disclosure does not usually raise the legal or political issues associated with state-imposed minimum services. It is much easier to demand that licensed professionals explain the

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<sup>12</sup> Transaction costs are always paid by the buyer (the only one in the deal with money) and, therefore, taken into account in the price offered. All things being equal, one would expect the additional work and risk associated with limited service listings to result in buyers offering less for the property. To the extent that is not happening, buyer agents are shielding their clients from the market impact of limited service listings.



services they are offering to provide rather than to force them to provide specific services. All that is needed is a rule that requires licensees to provide the potential client with information about the service level being offered and consequences to the client of selecting that service level.

To set up a meaningful listing service disclosure would require defining listing service models. “MLS-only” could be defined in the disclosure statute, so could “limited service” and “full-service.” Parts of these definitions might look something like the minimum service requirements enacted in Illinois. Once service models are defined, a check box listing disclosure (MLS-only, Limited-Service, Full-Service) could easily be incorporated into listing agreements.

The more difficult part of listing service disclosure is the client explanation that needs to accompany the disclosure. In agency disclosure, this is done by giving the potential client a pamphlet that explains the consequences of the various agency relationships available under state law. The same could be done with listing services. Listing agents could be required to give the seller information explaining the listing services being offered.<sup>13</sup>

## **Conclusion**

Limited service brokerage is a fact of modern real estate. Attempts to deny such listings MLS access have raised significant antitrust issues. Antitrust concerns have caused Illinois to enact new license law legislation imposing minimum service requirements upon brokers who enter into “exclusive brokerage agreements.” Other states, including Texas, are following the Illinois lead.

The approach taken by Illinois raises serious legal questions. Ultimately, the Illinois law will probably prove ineffective. It is also of questionable wisdom for an industry to invite government to define industry services. Similar objections can be raised to industry efforts to have existing license law interpreted to require minimum services. OAR legal staff, therefore, does not recommend pursuing minimum service legislation.

Other than continued development of practice tools for members, the only viable approach to dealing with potential problems created by limited service listing appears to be listing service disclosure. This approach is similar, legally and functionally, to existing agency disclosure statutes and rules. If OAR members believe there is the potential for sellers being misled about the nature or market consequences of limited service listings, consideration should be given to developing listing service disclosures.

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<sup>13</sup> This is a very sensitive issue. Brokers are instinctively chary when it comes to providing information about services. This is particularly true of providing such information in a format that allows the potential client to compare services. This problem can be overcome, however, by simply requiring disclosure only of the services offered in the listing. Thus, a full-service listing client would receive information only on full-service listings and so on.