F. BROKER/CONSUMER RELATIONSHIPS

1. Overview

a. Significance of the Relationships

The residential real estate transaction is usually the largest financial transaction in a consumer's life. It is a transaction in which both primary parties are consumers. The broker's role is strictly one of assisting the consumers in accomplishing the transaction. Brokers' functions, as we have emphasized before in this Report, can be categorized generally as market making and advising these consumers.

Consumers not only rely upon brokers, they depend on them. Consumers so infrequently undertake this complex transaction that their level of knowledge and understanding about the possibilities, costs, risks, and advantages of particular transactions is generally much lower than that of the brokers -- and the monetary size of the transaction makes the potential for monetary loss very high. Reliance upon brokers for critical advice in this transaction is reinforced -- perhaps necessitated -- by the brokers' control of the MLS in those markets where a MLS exists. The MLS is both the principal marketing mechanism for residential real estate and the major source of a great deal of critical information, such as the prices being asked for comparable properties. Consumer access to the MLS and the important information it contains, in every market, is through the individual real estate broker.

In light of the high labor intensity of this industry and the important strategic position of the individual brokers (including salespersons), it is not surprising that industry experts generally consider the behavior of the brokers to be the key to understanding the industry.[499/]

b. Legal and Ethical Duties

The duties of real estate brokers to buyers and sellers are governed by state law. The basic framework for the brokers' duties is set by the real estate licensing law, sometimes supplemented by regulations issued by a state regulatory body. Detail is then supplied by cases interpreting both that law and general state agency law.[500/] Real estate agents are also subject to general statutes

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499/ See F. Case, Residential Brokerage: History, Characteristics, Problems (1979) (hereinafter cited as "Case Report"), Part 5, at 1, 6; see also L. Shuster, J. Vigen, "A Study of the Professional Performance and Development of Realtors in California," California Real Estate (June 1973), at 26.

500/ B. Brown and E. Green, The Role of the Broker in Residential Real Estate Transactions (1979) (hereinafter cited as "Brown and Green"), at 8. Law professors Barry Brown and Eric D. Green, as consultants of Commission staff, with the assistance of students at Boston University Law School, compiled

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and the common law concerning fraud, misrepresentation, and unfair or deceptive business practices.

(1) Agency Law

Because the broker is treated in every state as an agent, a general understanding of agency law is required to understand real estate law.[501] The existence of an agency is a question of fact. An agency relationship is created by one person (the principal) manifesting to others a wish that another person (the agent) act on his or her behalf and subject to his or her control, and by the agent giving some indication that he or she will so act. Agency relationships usually are created by an explicit contract, either written or verbal, but may also be implied from the words and conduct of the parties under the circumstances of a particular case. The presence of compensation does not determine whether an agency relationship exists, but the absence of it may be used as evidence supporting the non-existence of an agency relationship.

As a fiduciary, an agent has a duty to act in the best interests of the principal. In particular, a broker has a duty to disclose to his or her principal all material facts within the scope of the agency, except for those facts which the agent is under a countervailing legal duty not to disclose.[502]

An agent may appoint others to aid him or herself on behalf of the principal. These others are often referred to as "subagents," and their appointment, like the appointment of an agent, may either be pursuant to an explicit agreement or may be implied from the words and conduct of the parties. To the extent that a principal, directly or by implication, authorizes the appointment of subagents, both the principal and the appointing agent may be responsible for the actions or representations made by subagents on the principal's behalf within the scope of the agency, depending on state law. The subagents may correspondingly be legally responsible to both their principal and to the agent who appointed them.[503] Where the appointment of subagents by an agent has not been authorized or implicitly ratified by the principal, it is the agent alone who is legally liable for any misrepresentations or unlawful or tortious acts by the subagents, and their duties in that case run to the party who has appointed them. The agent in that situation is, of course, liable directly to the principal for any injury which he or she allows his or her subagents to do to the principal or the principal's interests.

A broker may act legally as the agent of both parties to a transaction, as long as both are aware of the dual agency and give their consent. However,

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an extensive survey and report on state agency law as it affects the role of residential real estate brokers. This report is available to the public.

501/ This section draws heavily from Brown and Green, supra, note 500, at 8-17.

502/ Such as, for example, information previously disclosed to a lawyer in confidence by a former client whose interests are presently adverse to those of the lawyer's principal. See Restatement of Agency, § 381 (1933).

503/ For the general rule, see Restatement of Agency, §§ 361, 362 (1933).

generlly speaking, a dual agent may not act when one principal has interests adverse to the other, without making full disclosure of such and obtaining both principals' consents. Even where brokers disclose and obtain consent for their dual agency, some attorneys believe that the inherent conflicts of interest will lead to unavoidable breaches of their fiduciary obligations to the principals. While escrow agents are dual agents, it is unusual for a broker to intentionally or explicitly agree to act as a dual agent for both buyer and seller when functioning as a broker, giving advice to the consumers and aiding them in negotiations. The courts in some states, however, have shown a tendency to find in particular circumstances that brokers have, through their acts and words, assumed a legal status equivalent to that of dual agents.

(2) Real Estate Licensing Law

Every state licenses real estate brokers and salespersons and establishes, to some extent, the duties that brokers owe to the parties in the transaction. State licensing laws, in general, also reiterate certain of the duties owed to a principal under the state's common law of agency, including the duty not to act for more than one party without the knowledge and consent of all parties, and establish general prohibitions against deceptive and dishonest practices.[504/] Real estate licensing laws generally do not specify under what particular conditions the broker is the agent of the seller, the buyer, or both parties.[505/] These issues are resolved in somewhat different ways under each state's common law.

(3) Realtor Code of Ethics

In addition to the state licensing law standards, many brokers, being also Realtors, have agreed to abide by the Realtors' Code of Ethics. The code generally establishes standards of conduct which are aimed at facilitating cooperation among brokers, outlining basic agency duties to the client (principal), and calling for fair and honest conduct toward the customer (the other party). The code does not specify who the client is or who the customer is. That is, the Code of Ethics, as it relates to broker/consumer relations, is to a large degree a restatement of agency principles. The code does not, however, determine what creates the agency, when agency attaches, or to whom the agency relationship runs.

In summary, the basic duties of a broker to his or her principal in the real estate transaction are agency duties established by state law. The state licensing laws and the Realtor Code of Ethics, to the extent that they merely restate agency duties, are, in this respect, alternative methods of enforcing these duties. There are many cases interpreting the brokers' duties to the parties. These will be discussed below as they relate to specific issues.

c. Financial Incentives

While the state agency laws establish the primary duties of the parties, the

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504/ See Ch. IV, Part B and Appendix B of this report; and Brown and Green, supra, note 500, at 8-11.

505/ Brown and Green, supra, note 500, at 11.

listing contracts and the specified form of payment are the instruments that establish the primary financial incentives of the broker. Brokers generally are compensated on a contingency basis. The amount collected by the listing broker, which may be split among the broker who produced the listing, the broker who procured the buyer, and the firms involved, is usually payable only when a ready, willing, and able buyer has been found. Brokers, thus, are highly motivated to find such buyers and to close the deal.

While the contingent nature of their compensation strongly motivates brokers to achieve a sale, brokers also have a long term financial incentive to keep both buyers and sellers satisfied. Repeat and referral business is a primary source of both listings and future buyers for brokers. Thus, a broker has a financial interest in establishing and maintaining a good reputation with those with whom he or she deals.

d. Conflicts in the Broker's Role

Articulating realistic and appropriate roles and duties for brokers relating to consumers has long been a problem for the industry.[506/] There are two areas in which conflicts between brokers' incentives and consumers' expectations frequently arise.

First, there is an inherent tension between a broker's brokerage function and his or her representation function. The broker is paid to make a deal, but is relied upon to advise and represent the parties. Brokerage often involves minimizing differences to consummate a deal. Advice and representation often involve emphasizing potential differences which may interfere with quick consummation of a deal.

Second, the broker performing the representation function also faces the problem of whether he or she is serving the seller's or the buyer's interests. This problem is most acute for brokers when they are dealing directly with buyers. The Realtors' position is that brokers dealing with buyers are legally subagents of the seller. However, brokers who spend a large amount of time working with a buyer sometimes may develop both a personal and a business interest in working on the buyer's behalf. And, as we have repeatedly indicated, the buyer in such a situation may come to believe that the broker is working in his or her behalf.

William D. North, General Counsel of the National Association of Realtors, in an article entitled "Identity Crisis — Realtors Style," came to the following conclusion regarding these problems:

> Conclusion: In searching the cases for the identity of the real estate broker, it becomes evident that the classic legal labels — fiduciary, agent, middleman — do not fit the realities of the real estate business. It is apparent that the courts are no longer willing to permit the traditional principle of caveat emptor to define the obligations of the real estate broker. At the same time, the courts have yet to clearly identify the alternative principle or principles which will

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506/ See, e.g., California Real Estate (January 1914), at 74; California Real Estate (June 1957), at 12.

govern.[507]

2. Broker/Seller

a. Formal Relationship

Listing brokers and their salespersons normally are considered under state law to be agents of the seller, the principal. As agents, they have fiduciary duties to the seller. These duties include acting in the best interests of the seller, selling the house for the highest price possible, and disclosing all material facts to the seller.[508]

The listing agreement that the seller signs with the listing broker is the primary document establishing the relationship between the seller and broker. It not only specifies the terms of payment for the broker, but also generally is found to be the source of the agency relationship.

The vast majority of listing agreements are of the "exclusive right-to-sell" type. These agreements specify that the listing broker will collect his or her commission regardless of who sells the property. Exclusive right-to-sell contracts (as well as the less common exclusive agency contracts) are also usually read to authorize the listing broker to cooperate with subagents — to cooperate with other brokers in the sale of the property -- and this often is interpreted by brokers as an authorization to use the MLS.

Most listing agreements do not specify precise services to be performed by the broker. However, they generally specify that the broker will use his or her "best efforts" or "diligence" in selling the property.[509]

b. Problem Areas

(1) In General

As discussed at length in Chapter III, Part B.3. of this report, three problem areas relating to the relationships between the seller and the listing broker have been regularly highlighted by industry commentators. These problem areas involve the practices of self-dealing, vest-pocket listings, and double dealing (violations of fiduciary duties in negotiations).

All of the above problems relate to the seller's not receiving objective and unbiased information, especially concerning the probable selling price of his or

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507/ Real Estate Today (November/December 1973), at 55. Mr. North in this article also expresses his opinion that the Realtors' Code of Ethics protects all parties. Mr. North is Senior Vice President as well as General Counsel of the NAR.

508/ Brown and Green, supra, note 500, at 14, 17.

509/ Brokers often use forms supplied by their associations or by private concerns. For a typical example, see California Association of Realtors, Realtors, Real Estate Standard Forms (1979), at 21.

her home, and to the broker's dual role as advisor and broker. In each case the injury that might occur consists of the seller receiving less for his or her home than might otherwise be obtainable.

Most sellers rely heavily on the advice of their brokers[510] and believe that their brokers "represent" them.[511] Specifically, consumers rely on brokers in determining the appropriate price at which to list and sell the home and in negotiating with the buyer. Most industry experts agree that the advice and counsel of the broker is probably the most important influence in establishing the initial listing price.[512]

Our survey of sellers indicated that they placed considerable reliance on brokers in determining asking prices. Sixty-nine percent of sellers agreed that an important characteristic of a broker was the "agent's ability to recommend a listing price."[513] Eighty-six percent of sellers agreed that the "agent's willingness to provide information about sales price of similar homes" was important to them.[514] Further, 31 percent of sellers indicated that the "advice of agents" was the most important factor in their determining the price at which to list their property.[515]

Due to the contingency form of payment, brokers have a bias toward quick sales.[516] Brokers make more money on an hourly basis if the property sells quickly, even if at a slightly lower price. A relatively low price is an easy way to make a quick sale.[517] But the broker, as agent and ficuciary, has a duty to act in the best interests of the seller. Brokers, therefore, often find themselves facing a conflict between their duties to the sellers as confidential advisors and their financial self-interest as brokers paid on a contingency.

The two services — advice and brokerage — could be separated. Sellers are free, for example, to obtain independent appraisals for their properties. As discussed above, however, sellers most often rely on their brokers for

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510/ Seventy-five percent of sellers agreed that they relied on their agents' advice a great deal. FTC Consumer Survey, Seller Question 60. The sellers' general reliance upon the brokers is also indicated by the characteristic which they think is most important in a broker. By far the most important characteristic which sellers are looking for in selecting a broker is honesty and integrity. FTC Consumer Survey, Seller Question 20.

511/ Seventy-four percent of sellers felt that their agents represented them. FTC Consumer Survey, Seller Question 53.

512/ See, e.g., Hempel, Belkin, and McLeavey, supra, note 43, at 45; Case Report, supra, note 57, Part 2, at 9.

513/ FTC Consumer Survey, Seller Question 20.

514/ Id.

515/ FTC Consumer Survey, Seller Question 29.

516/ See, e.g., Gresham, supra, note 111, at 436 (1974).

517/ See, e.g., Case Report, supra note 57, Part 2, at 12. See also Real Estate Review (Summer 1979).

appraisal services.

(2) Self-Dealing

Undisclosed self-dealing, i.e., the undisclosed purchase of the home by the listing broker, is a flagrant violation of the broker's duty to disclose material facts to the principal. This practice violates both the state licensing law standards and the Realtors' Code of Ethics. Yet, it still is said to occur.[518]

(3) "Vest Pocket" Listing

Industry observers feel the listing broker's withholding of relatively low-priced, easy-to-sell listings from the MLS without the knowledge of the seller is a relatively common practice. Our surveys produced some results which are consistent with the occurrence of this practice.[519]

In smaller towns an MLS may be less necessary than in large communities. A buyer can obtain fairly complete knowledge of the inventory for sale by visiting a substantial percentage of the brokers in the area. In a small town, it might even be wise not to list on the MLS. An expensive home which warrants more individual selling effort may be better sold by the listing broker without the cooperation of others — the broker can invest in more advertising because he or she is more assured of receiving the full commission.

In larger cities, however, the MLS is more important for the average seller. In cities, the potential increase in selling price from using the MLS is sufficiently important that it is at least arguable that sellers should be specifically involved in any decision not to list on the MLS.

(4) Negotiations

Brokers play an important role in negotiations. Most sellers tell their brokers the lowest price they will accept. Most surveyed buyers reported that the broker told them how low the seller would go, even where there was only one broker in the transaction.[520]

This pattern is consistent with the broker's financial interests and with Realtor literature that characterizes negotiations as a process of "selling" both sides of the transaction in order to make a deal, as opposed to working solely towards the goal of obtaining the highest price for the seller.[521]

518/ See Ch. III, Part B.3. for further discussion of self-dealing.

519/ See Ch. III, Part B for a description of vest-pocket listing and a summary of survey results.

520/ See Ch. III, Part B.3.

521/ See, e.g., NAR, The Brokers Round Table, Letter No. 7 (August 1958); and J. Allen, Executive Sales Manager, Coldwell Banker & Co., "Time Management Fundamental of Successful Negotiations," California Real Estate (May 1973), at 6.

To the extent some brokers do compromise the interests of their principals in order to make a sale, this would seem to result largely from the contingent form of payment. On the other hand, this form of payment does encourage what the seller ultimately wants — a sale. Innovative fee arrangements which give the listing broker more incentive to sell the house for a higher price or less of an incentive to sell regardless of price might aid in addressing any perceived problem in this area. However, in the present industry environment, innovative fee arrangements involving advance-fee or fee-for-service arrangements do not account for any significant percentage of industry transactions.

3. Broker/Buyer

a. Formal Relationship

Buyers today generally have no contractual or agency relationships with the brokers or salespersons with whom they deal in the course of purchasing their homes.

The broker dealing with the buyer, whether he or she is the listing broker or a cooperating broker, receives his or her compensation pursuant to a contract with the seller. While it is generally the seller's intent that the broker be compensated from the proceeds of the transaction as a whole (i.e., from the sum received from the buyer), it is the seller alone who has the formal contractual relationship.

The traditional judicial view, following real estate brokerage industry practice, has been that the broker who is paid a commission by the seller, whether he or she is the listing broker or a cooperating broker, is only the seller's agent and owes no agency duties to the buyer.[522] In this context caveat emptor defines the relationship between broker and buyer.[523]

Many states are now beginning to relax this traditional doctrine. Statutes, regulations, and case law in many jurisdictions impose duties of fairness and honesty on brokers who deal with buyers, although the broker may be regarded as the seller's fiduciary.[524] However, some state courts are showing a greater

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522/ Brown and Green, supra, note 500, at 15; see also Huttig v. Nessy, 100 Fla. 1097, 130 So. 605 (1930); Linneman v. Summers, 95 N.J. Eq. 507, 123 A.2d 539 (1974).

523/ Brown and Green, supra, note 500, at 15-16; see also Caveat Emptor! The Doctrine's Stronghold, 1 Williamette L.J. 369 (1960); Comment, Real Estate Brokers' Duties to Prospective Purchasers, 1976 Brigham Young L. Rev. 513 (1976); Comment, A Reexamination of the Real Estate Broker-Buyer-Seller Relationship, 18 Wayne L. Rev. 1343, 1345 (1972) (hereinafter cited as "Broker-Buyer-Seller Relationship."

524/ Brown and Green, supra, note 500, at 16; see also Harper v. Adametz, 142 Conn. 218, 113 A.2d 136 (1955); Zichlin v. Dill, 157 Fla. 96, 25 So.2d 4 (1946); Comment, 1976 Brigham Young L. Rev., supra, note 523, at 514-15; Broker-Buyer-Seller Relationship, supra, note 523, at 1345-48, 1350-53.

tendency to let the question of agency go to the trier of fact for consideration in light of all the facts in the case.[525] In both the single and multiple broker contexts, courts are beginning to hold that a broker may be the agent of, and owe duties to, either or both buyer and seller, even though the broker's payment comes from only one of the parties.[526]

In some cases, where the prospective buyer has solicited a broker to find or show him or her the property, the broker finds property satisfactory to the buyer, and the buyer knows the broker will earn a commission from the owner, the law also implies a promise on the part of the buyer to complete the transaction. In that situation, failure to complete the transaction may make the buyer liable to the broker for breach of the implied promise.[527] This becomes, in effect, an implied promise to pay the broker's commission if he or she finds an appropriate property. That is, given appropriate facts, some jurisdictions will not only allow the trier of fact to find agency and fiduciary duties running from the broker to the buyer, but will also find implied promises running from the buyer to the broker.[528] While most of these cases involve developers, commercial property, or some special reliance, they are not limited to these situations.[529]

In sum, while the general rule in most jurisdictions is that both the listing and cooperating brokers are paid by, and therefore are agents of the seller and, as such, owe no fiduciary duties to the buyer, in a few jurisdictions, courts allow the question of agency be determined by the trier of fact.

b. Problem Areas

(1) Subagency — Industry View

In considering the relationships between brokers and buyers, one should distinguish between two different factual situations: (1) the non-cooperative situation, where the buyer deals with the listing broker directly; and (2) the cooperative situation, where the buyer deals with a broker who has searched the MLS or in-house list of homes in order to find a home listed by another broker that is suitable to the buyer.

525/ Brown and Green, supra, note 500, at 16; Brokaw v. Black-Foxe Military Institute, 37 Cal. 2d 274, 231 P.2d 816; Baskin v. Dam, 4 Conn. Cir. 702, 239 A.2d 549 (1967).

526/ Brown and Green, supra, note 500, at 16-17; see also Wolf v. Price, 244 Cal. App. 2d 165, 52 Cal. Rptr. 889, 894 (1966); Pepper v. Underwood, 48 Cal. App. 3d 698, 122 Cal. Rptr. 343 (1975); Miller & Starr, Current Law of California Real Estate, Section 4.6 (1975).

527/ See, e.g., Ellsworth Dobbs, Inc. v. Johnson, 50 N.J. 528, 236 A.2d 843 (1967).

528/ See, Brown and Green supra, note 500, at 20.

529/ Id.

While sixty-six percent of sales involving brokers now involve cooperating brokers,[530] the role of brokers as agents of sellers evolved before the MLS and complex markets made routine cooperation among brokers feasible and universal. In early times sellers might list with several brokers and buyers contact a number of brokers in their search for a house. Under such circumstances it was and is, quite natural to consider the broker who has a direct contractual relationship with the seller to be the agent of that seller.

Where the buyer is dealing with a cooperating broker who has found a house on the MLS for the buyer, it is much less obvious that the traditional view of agency to the seller should apply. The cooperating broker has not acted primarily as a salesperson for his or her listings but has searched the MLS for an appropriate home for the buyer. The view of the cooperating broker as a subagent of the seller is therefore the source of a number of anomalous results.

In a column carried in the journal of the California Association of Realtors, California State Commissioner David Fox was asked the following question: "What is wrong with a real estate agent suggesting to the prospective buyer of property that it can be purchased for less than the listed price or on better terms?" His answer was as follows:

> "The listing agent in a real estate transaction has a fiduciary duty to the owner of the property that agent has engaged to sell. In most real estate transactions, the cooperating agent is considered to be a subagent of the seller and therefore bound to the same fiduciary obligation to the seller. The fiduciary obligation carries with it a duty to act in the best interests of the seller in all respects and that of course includes negotiating a contract for the seller on the best terms and at the best price obtainable. Therefore, neither the listing nor the selling agent should suggest to a prospective purchaser terms less favorable to the seller than the terms set forth in the listing agreement unless the seller has given express approval to this tactic."[531]

Under this view, reiterated and reinforced even in the jurisdictions with the most modern real estate and agency law, a buyer can benefit fully from a broker's knowledge only if he or she separately hires an outside, non-cooperating broker.[532]

(2) Reliance of Consumers

While buyers may not be able to rely fully on the seller's broker, counsel for the National Association of Realtors readily agrees that, "Often a purchaser's only available source of expertise and information is his seller'

530/ FTC Consumer Survey, Seller Question 52.

531/ California Real Estate (March 1979).

532/ Brown and Green, supra, note 500, at 18.

broker."[533]

The problem of consumer dependence upon a broker with adverse interests is highlighted most obviously with respect to information relating to the appropriate price to offer for the house, because consumers have neither great expertise nor direct access to the MLS in order to determine the sales prices of comparable houses. Experts generally agree that the major source of information for buyers, specifically including price information, therefore, is the broker.[534]

In our Consumer Survey, buyers were asked to identify the single most influential source of information used to determine the price that they offered to the seller. The most influential source, identified as such by 21 percent of buyers, was the advice of their broker. Another 18 percent stated that comparable sales information provided by their broker was the most influential source.[535]

Buyer reliance on the broker involves more than pricing information. Almost 67 percent of buyers surveyed agreed that they "relied on [their] agent's advice a great deal when making decisions about purchasing [their] house."[536] In those transactions where an agent was involved, 90 percent of buyers worked with the agent to find the house.[537] Sixty-five percent of these buyers worked with only one agent during their search for a house.[538] The nature of this reliance was also indicated by the feeling of most buyers that the ability of the agent to discover defects or other problems in the house is a very important characteristic of the agent.[539] Further, slightly over 80 percent of buyers agreed that their agent played a major role in negotiating with the seller.[540]

In light of the heavy reliance that buyers must and do place on brokers, it is not surprising that most buyers apparently are confused as to whom the broker represents. Overall, 57 percent of buyers surveyed indicated that they thought that "the agent who handled the purchase of [their] house" was representing them.[541]

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[533] William D. North, "Identity Crisis Realtors Style," Real Estate Today (November/December 1973), at 53.

[534] See, e.g., Hempel, Belkin, McLeavey, supra, note 43, at 45.

[535] FTC Consumer Survey, Buyer Question 33. See also Ch. III, Part B.3.

[536] FTC Consumer Survey, Buyer Question 53.

[537] FTC Consumer Survey, Buyer Question 10.

[538] FTC Consumer Survey, Buyer Question 11.

[539] FTC Consumer Survey, Buyer Question 29. Of four levels of response from "very important" to "of little importance," 53.3% indicated this characteristic was "very important," 75.5% indicated it was "very important" or "important."

[540] FTC Consumer Survey, Buyer Question 53.

[541] Buyers were asked, "Who did you think the agent who handled the purchase of your home was representing?" The response was as follows: Respondent (Buyer) -- 56.6%; The Seller -- 18.7%; Buyer and Seller -- 9.6%; and Himself/Herself Broker -- 15.2%. FTC Consumer Survey, Buyer Question 31.

Looking at those buyers who dealt with a cooperating broker as opposed to those buyers who dealt with listing broker directly, the following results were obtained: 71 percent of those buyers dealing with a cooperative broker felt that the agent who handled the purchase of their home was representing them; 31 percent of buyers dealing directly with the listing broker felt that the agent was representing them.[542]

Buyers perhaps also expressed their perception of the role and function of the broker when they rated the relative importance of various characteristics of and services provided by brokers. A list of such characteristics and services was read to the consumers surveyed. They were asked to rate each characteristic and service by degree of importance varying from the top category of "very important" to the bottom category of "little importance."

The top three responses in the "very important" category were as follows:[543]

Characteristic/Service	Percentage of "Very Important" Responses
1. "Agents' honesty or integrity"	83%
2. "Agents' ability to understand buyer's needs"	68%
3. "Agents' ability to negotiate with potential seller"	63%

These responses appear to be more consistent with an expectation that the broker is going to represent the buyer than with an understanding that the broker is the seller's agent.

(3) Conduct of Brokers

Brokers do not always appear to be acting as representatives of sellers. Brokers regularly advertise that they will aid buyers. Many brokers believe that they can adequately represent both parties to the transaction. They believe that by bringing the parties together on mutually acceptable grounds they are in fact representing both parties.[544]

While some brokers believe that they adequately represent buyers, many also defend their right to engage in certain conduct which may be inconsistent with

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[542] FTC Consumer Survey, Buyer Cross Tabs, Questions 31 by 46.

[543] FTC Consumer Survey, Buyer Question 29.

[544] Case Report, supra, note 57, Part 2, at 8.

the best interests of the buyer. One is the not uncommon practice of "steering" buyers away from a home listed by a disfavored broker, even though such a home may be appropriate for the buyer. Many cooperating brokers believe they have a right not to show buyers such homes.[545] Legally, those brokers are correct, as long as they, first, act individually and not as part of a group; second, do not mislead the buyer about the nature of their services; and, third, do not engage in conduct which implies an agency on behalf of buyers. The deceptive image that may be created in the minds of buyers, and not necessarily the failure of any individual broker to pick up on all "unilateral offers of subagency," is what presents a problem. Of course, any concerted refusal by brokers to show homes of another broker would raise very serious antitrust concerns.

In sum, brokers are clearly not, in the eyes of buyers and by their own statements, acting as exclusive representatives of the sellers. As the industry literature and industry leaders indicate, the role and agency status of the broker dealing with the buyer are clouded by uncertainty and confusion.

c. Analysis

(1) Consumer Injury

(a) In General

It is impossible to quantify whatever consumer injury may result from the anomalous broker/buyer relationship. However, the lack of a formal relationship does have a direct bearing upon lackluster competition in commission rates, the possibility of overpayment for homes, and potential missed opportunities to purchase homes not shown to buyers.[546] This section is concerned with the latter two types of injury. For purposes of analysis, this kind of injury can result from: (1) non-disclosure to buyers; (2) under-representation of buyers; and (3) lack of legal responsibility to buyers.

While we concentrate in the following sections upon injury to buyers, it should be acknowledged that it is possible that when brokers fail to observe formal duties neither party may necessarily lose and both sometimes may even gain. For example, if brokers working with the buyer and for the seller disclose confidential information to each party, the net effect of the disclosures sometimes may be to speed up the negotiations to arrive at a price fully acceptable to both. In such circumstances the brokers act to arbitrate between the parties rather than act as arms-length "representatives."

545/ "[M]ust a Realtor show property of a price competitive broker which is listed at a rate less than the Realtor feels will achieve an acceptable split for him? As a general rule, probably not." C. Wallace, President, California Association of Realtors, "The Facts About Price Fixing," California Real Estate (April 1979), at 25, 48, 58.

546/ As discussed in Ch. II and Ch. IV, Part E., we hypothesize that steering by cooperating brokers away from listings of discount brokers may be a primary contributing factor to commission rate stability.

(b) Non-disclosure

Non-disclosure of the status of the broker's relationship to the seller ma result in the buyer inappropriately relying on an adverse party. The buyer oft is ignorant of the broker's agency to the seller, and of the broker's duties to inform the seller of all material facts and to sell the house for the highest price possible. Buyers often reveal information to such brokers which, if the buyer were aware of the brokers' duties to the sellers, buyers might otherwise not reveal.[547] In fact, 73 percent of buyers reportedly told the agent with whom they worked the highest price they would pay for the property.[548] Eighty three percent of buyers surveyed felt that the information that they had given the broker regarding how high a price they would pay would remain confidential.[549]

On the other side of the coin, 66 percent of sellers surveyed indicated th their broker told them how high he thought the buyer would go.[550]

There is some indication that this reliance on brokers is related to a lac of disclosure of their role. On our consumer survey, those buyers who thought the broker represented them were much more likely to "strongly agree" that what they told the broker "about how high [they were] willing to go for the house . . . would remain confidential."[551]

(c) Under-Representation

The present interpretation that all cooperating brokers are agents of the sellers may also lead to injurious under-representation of th buyers' interests.

State law evidences a general public policy to protect consumers in the re estate transaction. All 50 states license brokers and consider brokers to be agents and fiduciaries because of the reliance by consumers on brokers and the substantial risks involved in the transaction. In the residential real estate market there are complicated questions of price and fitness which may call for the unbiased expertise and advice of a broker. The present broker-consumer situation, however, is characterized by an asymmetry of information and negotiating power.[552] The seller is expert regarding his or her own house and has the financial incentive to sell the house for the highest price possible. The listing and cooperating brokers, who are experts regarding houses generally the specific neighborhood, and the transaction, in general, have financial incentives to close the deal as quickly as possible and formal duties to

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547/ See Brown and Green, supra, note 500, at 3.

548/ FTC Consumer Survey, Buyer Question 53.

549/ Id.

550/ FTC Consumer Survey, Seller Question 60.

551/ FTC Consumer Survey, Buyer Cross Tabs, Question 31 by Question 53.

552/ See Brown and Green, supra, note 500, at 4.

represent the seller. The brokers do not have incentives to uncover and disclose to the buyer facts concerning the property which may tend to show it in a less favorable light. Thus, a buyer not represented by a broker may be unable to fully evaluate the worth of a particular house. Such may be reflected in over-payment for the house.

Industry members and industry literature tend to agree that a broker who is an agent for the buyer is more likely to obtain a price and terms more favorable to the buyer than would a broker who is the seller's agent.553/

When comparing the prices at which houses were purchased with the sellers' initial asking prices, we might expect, all things being equal, well-represented buyers to have gotten a larger discount than those who were not well-represented. Analysis of survey results indicates that those buyers who felt that the broker represented the seller were, in fact, much less successful in negotiating the price of the house down from the initial asking price than those buyers who felt that the broker represented either the buyer alone or both the buyer and the seller.554/

Another aspect of under-representation involves the broker's potential failure to show and promote equally all homes which may be appropriate for the buyer. Brokers, we hypothesize, may often feel that, because they are agents of sellers and not of buyers, they are not obliged to show the buyers, for example, those homes listed by discounters.555/

Forty percent of the buyers surveyed indicated that the most important reasons buyers use brokers relate to market access.556/ MLSs generally do not allow buyers to have direct access to that pool of housing information.557/ While consumers may find homes through direct advertising and "for sale" signs, the vast majority of sellers choose to use brokers, and close to 60 percent of buyers surveyed became aware of the home they purchased through a broker or the MLS.558/

Buyers expect brokers to show all appropriate homes. Eighty- nine percent of buyers surveyed expected their broker to inform them about "all homes that would probably be suitable for [them]."559/

With the broker being the primary source of information regarding houses for sale, his or her choosing not to show homes which might be appropriate to the buyer might effectively deny that buyer such information, thereby denying

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553/ See, e.g., Real Estate Review Volume II, No. 2 (Summer 1972), at 29.

554/ FTC Consumer Survey, Buyer Cross Tabs, Question 31 by "Buyer Price/Ask Price."

555/ See note 545, supra. Some industry commentators, however, feel that brokers who represent buyers may have a duty to advise their clients when another broker has a listing which better meets the client's needs. R. Goodman, "Practice and Malpractice," California Real Estate (June 1977), at 4.

556/ FTC Consumer Survey, Buyer Question 18.

557/ FTC MLS Survey, Question J1.

558/ FTC Consumer Survey, Buyer Question 28.

559/ FTC Consumer Survey, Buyer Question 53.

the buyer the opportunity to maximize his or her satisfaction by purchasing most appropriate home.

(d) Lack of Legal Liability or Remedy

In addition to the problems of non-disclosure and under-representation, the prevailing view that both listing and cooperating brokers owe duties to the seller may leave the buyer without remedies or at a legal disadvantage in the event something goes wrong with the purchase. The law attaches great significance to the presence of a fiduciary relationship in determining a person's liability to another.

For example, housing defects may be a source of post-purchase dispute among buyers, sellers, and brokers. The issue is often whether the seller or broker(s owed any duties to the buyer and, if so, what level of disclosure or affirmative conduct those duties required. While recent developments in some jurisdictions impose a duty on the seller and the seller's agents to disclose material facts concerning the property of which the buyer is unaware or which are not observable, many jurisdictions apply this rule only to concealed defects. Many courts still deny compensation to a buyer aggrieved by "his" or "her" broker's acts amounting to less than fraudulent misrepresentation, on the ground that no fiduciary relationship existed.[560]

Similarly, state real estate licensing agencies place great significance on the existence or non-existence of an agency relationship in analyzing consum complaints concerning a broker. Where a buyer alleges that the broker faile disclose housing defects, for example, there often can be no violation of the licensing standards because there was no agency relationship between such buyer and broker. Licensing officials, like most courts, generally look to the listin agreement to find agency and find there an agency that runs to the seller only.[561]

560/ See Brown and Green, supra, note 500, at 4-5; Broker-Buyer-Seller Relationship, supra, note 523, at 1351-52; Gresham, supra note 111, at 437. Consumers Union, concerned that brokers may have no obligation to disclose housing defects, asked William North, General Counsel of the NAR, what obligation to the buyer an agent would have if he or she discovered a leaking basement in the house. C.U. reported the following response: "If the real-estate broker is not asked the question and does not induce the buyer to rely on his evaluation of the quality of the home, the real-estate broker has no legal obligation to disclose the defect." Consumer Reports (September 1980) at 573.

561/ See, e.g., Report of Interview with R. Arnold and F. Carasko, California Department of Real Estate (March 29, 1979).

(2) State Agency Law

The conclusion reached after an extensive survey of the agency laws of all 50 states conducted for us under the supervision of Professors Barry Brown and Eric D. Green, was as follows:

> [W]hile the law is strongly inclined towards finding no broker-buyer fiduciary relationship in the absence of an agreement to the contrary, there are no significant legal barriers that prevent the parties to a residential real estate transaction from reordering their relationships to provide that the broker or brokers involved may represent and owe fiduciary responsibility to the buyer. 562/

Specifically, with respect to cooperating brokers operating within the MLS, there is nothing in the law of agency in any state which prevents the cooperating broker from representing only the buyer, even in price negotiation and even where the commission is to be paid by seller. To avoid the risks of a court finding dual agency and breach of fiduciary duties to the seller, such a buyer's representative would probably have to disclose his or her position, and, in some jurisdictions, obtain the formal consent of the seller. Such disclosure and consent can be recorded anywhere; one possible location would be on the deposit receipt.563/

(3) The Possibility of Buyer's Representation

If representation of buyers is a legal possibility, why do so few brokers today provide such a service?

One possible answer to this question might be that industry educational and training programs may influence brokers to believe that buyer representation is improper when they are acting as cooperating brokers.

Cooperating brokers wishing to act as buyers' representatives face far fewer problems than their industry education and literature may lead them to believe. While some industry members and real estate attorneys have regularly reiterated that cooperating brokers face unavoidable conflicts of interest if they try to act as buyers' representatives,564/ such conflicts are avoided when appropriate

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562/ Brown and Green, supra, note 500, at 7. Emphasis in original. Appendix A to their report contains a summary of the real estate brokerage and agency law of each state as it affects the possibility of buyer's representation. Section III of that report also contains model listing agreements.

563/ Brown and Green, supra, note 500, at 21.

564/ See, e.g., H. Miller, M. Starr, Current Law of California Real Estate (1975), at 49; Commissioner David Fox, California Real Estate (March 1979).

forms informing the parties and providing for consent are used.

Some Realtors' associations have taken positions which facilitate the opportunity for the cooperating broker to act solely as a buyer's representative. The legal staff of the California Association of Realtors, for example, now defines a "buyer's broker" as a "cooperating broker solicited by the buyer."[565]

Realtor positions have also, apparently, provided that a buyer's representative can usually qualify as "procuring cause" and receive the offered commission split. While perhaps not aimed at this precise issue, the National Association of Realtors has adopted a rule which appears to cover it. In May 1973, the National Association adopted Interpretation No. 31, Official Interpretations of Article I, Section 2, By Laws of the National Association. This Interpretation deals with MLS rules which tend to limit the brokers in their relationships with buyers. The Interpretation reads as follows:

> A Board rule or a rule of a Multiple Listing Service (MLS) owned by, operated by or affiliated with a Board, which establishes, limits or restricts the Realtor in his relations with a potential purchaser, affecting recognition periods, is an inequitable limitation on its membership.[566]

The Realtors have also interpreted Article 22 of their Code of Ethics to allow buyer representation. Article 22 states, in relevant part, as follows:

> In the sale of property which is exclusively listed with a Realtor, the Realtor shall utilize the services of other brokers upon mutually agreed-upon terms when it is in the best interest of the client. . . .[567]

NAR Interpretive Case No. 22-5 deals with cooperation where the purchaser has designated another broker to be his advisor. The case concluded that a listing broker who had refused to cooperate with such a pruchaser-adviser was in violation of Article 22.[568]

The National Association of Realtors' Handbook on Multiple Listing Policy also takes the position that the MLS cannot restrict the brokers in their relationships with consumers. The purpose of the MLS is strictly limited to the orderly dissemination and correlation of listing information.[569] It is the

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565/ Legal Staff Q's and A's, California Real Estate (April 1979), at 10.

566/ California Real Estate (October 1978), at 54.

567/ Interpretations of the Code of Ethics, 6th Edition (1976), at 171.

568/ Id. at 175.

569/ Handbook on Multiple Listing Policy (1975) (hereinafter cited as "Handbook"), at 7.

stated policy of the National Association of Realtors, as noted in the Handbook, to avoid interference in their members' business unless it deals with ethical practice.[570]

While the agent who uses the MLS may be considered to have effectively appointed all other members of the MLS as his or her other subagents on a blanket basis, the MLS is "fundamentally a clearing-house of listing information and has no interest in establishing the terms under which the listing broker offers subagency to other MLS participants. . . ."[571]

Even if the use of the MLS is considered an offer of subagency for limited purposes (special subagencies), there is no reason for it to be considered in all cases a grant of agency which includes the full range of fiduciary duties of the listing broker. The existence of an agency relationship is a question of fact and brokers and consumers are free to structure their agency relationships as they see fit.[572]

Sellers believe that, where a cooperating broker is involved, whether in a different firm or in the same firm, that broker represents the buyer.[573] In fact, most sellers might be rather surprised to know that under the law of agency they may be vicariously liable for the misrepresentations of cooperating brokers if such brokers are, in fact, their subagents.[574] If a cooperating broker were clearly the buyer's agent, the seller would be relieved from such exposure. In this regard, Professors Brown and Green concluded as follows:

570/ "No restriction or limitation may be placed on a Realtor as to the manner in which he conducts his business unless it concerns ethical practice." Id. at 50-51.

571/ Id. at 48, 51.

572/ See Brown and Green, supra, note 500, at 21. See also Wise v. Dawson, 535 A.2d 207 (1975), holding that the usual MLS arrangement does not create an agency relationship between listing broker and selling broker. The purpose of the multiple listing service is an information exchange. Because there is no control by the listing broker over the selling broker, the mere fact of the split commission does not create an agency relationship. For this reason the court rejected a suit against the listing broker attempting to hold the listing broker liable for the selling broker's misrepresentations.

573/ Where the cooperating broker was with the same firm as the listing broker, 77% of sellers surveyed believed that the cooperating broker represented the buyer. Where the cooperating broker was with a different firm, 74% of sellers surveyed believed that the cooperating broker represented the buyer. FTC Consumer Survey, Seller Cross Tabs, Questions 50 by 52.

574/ See, e.g., Johnson v. Seargeants, 152 C.A.2d 180, 313 P.2d 41 (1957); Granberg v. Turnham, 166 C.A.2d 390, 333 P.2d 423 (1958); Restatement (Second) of Agency, Sections 142, 255, 264, and 283.

> The consequences appear significant enough in themselves to require disclosure to sellers in listing agreements, so that sellers may intelligently decide whether they want the cooperating broker to be their agent.575/

An even more important reason than brokers' ignorance about their own right to act as a buyer's broker, however, may be that most buyers believe they are n adequately "represented."576/

The belief among buyers surveyed that the broker was a representative of t buyer correlated with high buyer satisfaction.577/ Those buyers who worked wit only one, as opposed to many, brokers, were more likely to feel that that broke was their representative.578/ Furthermore, they were more likely to be satisfied, use the broker again, and recommend that broker to a friend.579/ These buyers, who believed that the broker was their representative, also expected that broker to show all homes which were suitable to them.580/

Cooperating brokers have at least some long-term financial incentives to b buyers' representatives. A very high percentage of brokerage business comes fr referrals.581/ Sellers often leave the community. Buyers, however, are future sellers in that community. A satisfied customer or client is much more likely be the source of referrals and return business.

(4) Dual Agency

Theoretically, a broker may act as a dual agent, representing both the buy and seller, if there is knowledge and consent of all parties. However, because the agent for the seller has a duty to sell the house for the highest price on the best terms posible for the seller, and the agent for the buyer would a duty to purchase the house for the lowest price and on the best terms possibl for the buyer, it might be virtually impossible for a dual agent to negotiate a advise both parties with respect to price and terms. Attorneys who have commented on this area have concluded that such dual representation involves unavoidable conflicts of interest.582/

575/ Brown and Green, supra, note 500, at 22.

576/ Seventy-one percent of buyers surveyed who were working with a cooperating broker believe that the broker represented them. FTC Consumer Survey. Buyer Cross Tabs, Questions 31 by 46.

577/ FTC Consumer Survey, Buyer Cross Tabs, Questions 31 by 16.

578/ FTC Consumer Survey, Buyer Cross Tabs, Questions 31 at 11.

579/ FTC Consumer Survey, Buyer Cross Tabs, Question 11 by Questions 16, 45 and 53.

580/ FTC Consumer Survey, Buyers Cross Tabs, Questions 31 by 53.

581/ See Ch. IV, Part D.

582/ See, e.g., Brown and Green, supra, note 500, at 17-18; W. Milligan, "The Legalities of Broker Cooperation," California Real Estate (August 1976), at 43, 45; H. Miller and M. Starr, Current Law of California Real Estate (1975), Section 4.16, at 49.

There is, however, a potential role for a broker as a "middleman." A middleman is not an agent. Unlike an agent, he or she has "no independent initiative and is employed only to introduce the parties to each other. . . ."[583] He or she has no power to negotiate, and is akin to the "finder" in commercial transactions.[584] A middleman, therefore, is what we might call a "pure broker" who does no more than match buyers and sellers. He or she does not become involved in advisory functions or functions which involve an exercise of professional discretion.[585]

However, a real estate broker in a residential transaction is rarely a true middleman. Consumers put considerable reliance in brokers, and brokers conduct themselves in a manner which is often interpreted by consumers as representation.[586]

Given the problems of attempting to act as a dual agent, there seems to be little reason why a cooperating broker would want to absorb that risk. Where, however, a listing broker is dealing directly with a buyer, the buyer and/or seller may wish to consent to something less than full representation by that broker.

(5) Brokerage versus Representation

Over the years, brokers have carried on the business of brokerage by dealing with both parties without much concern about the technical legal requirements of agency law and fiduciary relationships. Brokers, paid on a contingency basis, are strongly oriented toward making a successful match of buyer and seller. Brokers' compensation depends upon their ability to sell to and deal with both sides of the transaction.[587] Some brokers appear to view negotiation more in

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583/ Restatement (Second) of Agency, Section 391(d).

584/ See Annotation, 63 A.L.R.3d 1211, 1224.

585/ Under California law even an unlicensed person can act as a middleman and collect a fee from a broker or principal. The public policy requiring a license in order to protect consumers does not apply in such circumstances. See, e.g., Opinion of the Legal Division, California Association of Realtors, California Real Estate (October 1979), at 32.

586/ See, e.g., Wiston v. David Mayer Bldg. Corp., 337 Ill. App. 67, 84 N.E.2d 858, 860 (1949) ("Middleman situations are exceptional").

587/ "You have two jobs in every real estate transaction. (1) Selling the buyer; and (2) selling the seller." NAR, Broker's Roundtable, Letter No. 7 (August 1985), at 4. See also California Continuing Education of the Bar, Real Estate Sales Transactions, Section 1.19. In Britian, ethical codes require that a buyer's representative be compensated on a fee-for-service basis as opposed to a contingency basis. Monopolies Commission, Estate Agents (1969) at 20.

terms of closing a transaction than representing a client. In an article entitled "The Art of Negotiation," appearing in the National Association's publication Real Estate Today, for example, Realtors were instructed on how to influence the buyers' and sellers' decisions. The article discussed emotional and non-rational factors that influence transactions. While the article stres ethical conduct, it concluded with the following: "Real estate negotiating is probably one of the few areas in life where ends can justify means. . . . It r be necessary to 'handle' the seller as well as the buyer."588/

A lack of concern by many brokers about issues that seem important to lawyers may, in part, be due to a basically different view of the role of the broker. While brokers may be primarily interested in making a sale or facilitating a transaction, which is what they are essentially hired to do, lawyers tend to see brokers as "representatives" who are to be guided by the requirements of agency law in using their expertise to their clients' best advantage. Perhaps because of these differing views, brokers often may see lawyers as being unjustifiably negative toward transactions.589/ Lawyers, because they tend to point out potential problems, may make it more difficult brokers to successfully make a sale, and this can raise transaction costs.

Some commentators believe that the conflicts in the brokers' role, and especially the ill-defined nature of the relationship between the broker and t buyer, are directly related to the industry's goal of achieving professionalism. A statement by former NAR president Joseph Doherty summarize one view of this dilemma:

> I would think that professionalism would come when we represent one party for a fee. We have been living with the most difficult situation where we are the agent for the owner only. He pays us, and we have a fiduciary responsibility toward him and still we have to be very careful that we represent the best interests of the other party to the transaction in terms that will be absolutely fair, ethical, and so on. I can't think of another profession that would operate that way, unless it be a marriage counselor.590/

588/ "Art of Negotiation," Real Estate Today (April 1970).

589/ See, for example, California Continuing Education of the Bar, Real Estate Sales Transactions, § 1.30.

590/ California Real Estate (June 1974), at 5.

G. FEE STABILIZATION

1. Introduction

A principal subject of this report is why brokerage fees today are highly uniform within markets. Some observers claim the market is in equilibrium. Others, citing historical evidence, conclude that the principal cause has been efforts by brokers to stabilize or raise their fees. We conclude that the structure of the brokerage industry nationally is, today, more important than either vigorous competition or overt price-fixing in maintaining fee uniformity.591/

However, historic efforts by brokers to stabilize and raise their fees have certainly contributed to rate uniformity and may be responsible, in part, for the current level of fees. This section reviews those efforts and assesses their overall significance.

We have identified two types of efforts at formal fee stabilization: the use and enforcement of fee schedules and covert price-fixing conspiracies. The two methods are quite different. Fee schedules were openly applied in the past; covert price conspiracies are furtive and have been of concern largely since the demise of official fee schedules.

2. Fee Schedules

a. History of Fee Schedules

Many local associations of brokers bound their members to use fee schedules from their inception. For example, in 1923 the Chairman of the NAREB Committee on Commissions claimed that the Chicago brokers' association had used a schedule for more than 40 years.592/

Efforts to raise rates through the use of schedules met with greater success in cities than in small towns. "It has not always been easy," one state Association official noted in 1927, "especially in some of the smaller towns, to

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591/ See generally Ch. II and Ch. IV, Parts B, C, and E.

592/ Proceedings of the Brokers Division, NAREB Annual Convention, June 27-30, 1923, Cleveland, Ohio, at 15-19. In comparing fee schedule levels, it is important to distinguish between open and exclusive listings. Historically in the U.S. (and to this day in Great Britain), exclusive listings have been associated with lower commission rates, probably because of the greater assurance of return offered to brokers by those listings. For example, in 1923 the rate in Chicago tapered from 6% down to 3%, depending on the value of the home. By contrast, at that same time in New York the accepted rate was only 1%. National Association officials praised the rate level in Chicago, and considered it illustrative of the power of the Board in Chicago. However, the officials considered New York not directly comparable, since, unlike Chicago, listings in New York were generally exclusive.

raise old established rates, but if the brokers will stand by their guns, it will unquestionably work out in the end."[593]

The success of the early schedules is reflected in the trade literature of the period. Articles relating to multiple listing services indicate that, by th 1930's, commission rates were relatively stable in most areas, especially in those localities where an MLS was successful.[594] "There are exceptions, it is true, generally in communities where brokers are not organized and where educational programs have been neglected."[595] Thus, despite the widespread apparent success of the schedules, in some areas compliance was viewed as in fac marginal.[596]

As late as 1938, fees varied considerably among different cities in the U.S. Both 4 and 5 percent were common rates, but brokers in some areas still used tapered scales going down to 2-1/2 percent.[597]

Returning from a meeting of the National Association, CREA Commission Committee Chairman Paul Bomberger reported in a 1939 article entitled "Fine Work on Schedules Aids Brokers Make More Money": "It is the intention of the Nationa Association to work out a guide to be used as a model for Boards throughout the United States."[598]

In 1940, Mr. Bomberger was both Chairman of the CREA Uniform Commission Committee and Chairman of the NAREB Committee on Rates, Rules and Customs. In a report to the CREA membership regarding the national progress made by these committees, Bomberger noted: "The trend seems to be for various states to adopt uniform schedules for the individual states, and some of the adjoining states ar working together to have the uniform schedules over more than one state."[600]

By the 1950's the 5 percent commission rate was quite uniform across the U.S. In 1958 there began a general increase from 5 percent to 6 percent throughout the country.[601] It appears that this increase, as before, began first in the cities.

A reflection of the widespread fee schedules movement is found in the ethic codes of the periods. Prior to 1950, the National Association of Real Estate Boards' Code of Ethics included an article stating that fee schedules, established by local Boards, were fair and should be observed by every Realtor. The National Association By-Laws further provided that each member Board shall

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593/ E. Graham, Chairman, Uniform Rate Committee, "Report of the State Uniform Commission Rate," California Real Estate (January 1927), at 47.

594/ J. Westrom, Chairman, CREA Appraisal Division, "Ethics and Real Estate Brokers," California Real Estate (April 1937), at 51.

595/ Id.

596/ See also California Real Estate (January 1936), at 28.

597/ California Real Estate (October 1938), at 52.

598/ California Real Estate (July 1939), at 16.

600/ "Uniform Schedules of Commissions Add to Earning Power," California Real Estate (June 1940), at 54.

601/ NAR, "Brokers Roundtable, Letter No. 7" (August 1958), at 3.

adopt the Code of Ethics. As a result, local Boards of Realtors adopted standard commission rates for their members. Usually the Boards' Codes of Ethics provided that "brokers should maintain the standard rates of commission adopted by the Board and no business should be solicited at lower rates." Members agreed to abide by this Code, with the effects on rate uniformity documented above. There was nothing secret or covert about the use of the fee schedules.602/

In the late 1940's, the Department of Justice brought its first antitrust suit involving the fixing of real estate commission rates. The government charged that the National Association and the members of the Washington (District of Columbia) Real Estate Board had combined and conspired, in violation of the Sherman Act, to fix commission rates for their brokerage services by adopting a schedule of rates to which members consented. The Supreme Court held that the adoption of standard rates of commissions constituted a conspiracy in restraint of trade in violation of the Sherman Act, even though the Association imposed no penalties on brokers for deviations from the rate schedules.603/

Soon after the NAREB decision, the National Association terminated the practices of formally adopting rate schedules and encouraging local Boards to require adherence. Boards and their MLSs began instead the practice of "recommending" or "suggesting" commission rates. Because local Boards had a long history of established schedules, this new approach resulted in little change in practice. For example, in 1960 the California Association, with the support of 103 local Boards, openly voted to raise the commission rate to 6 percent.604/

In 1962, the state of California challenged the California Real Estate Association's "recommended" fee schedule in People v. California Real Estate Association.605/ This action resulted in a consent judgment against the state Association and 17 local Boards in southern California. The resulting order prohibited price fixing in any form, including any use of schedules.

Later, a Justice Department investigation of recommended fee schedules resulted in the NAR's adoption in 1971 of its "Fourteen Points," one of which prohibits the use of recommended fees.606/ The Justice Department investigations also resulted in at least 15 actions alleging price fixing by local Boards and member firms.607/ All the cases alleged, among other practices, the use of

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602/ See also Ch. IV, Part A.

603/ U.S. v. National Association of Real Estate Boards, et al., 399 U.S. 485 (1950).

604/ California Real Estate (February 1960), at 7.

605/ 1962 Trade Cas. (CCH) ¶ 70,446. (Sup. Ct., L.A. 1962).

606/ See Ch. IV, Part C, "Multiple Listing Services," for a complete discussion.

607/ See discussion of U.S. v. Prince George's County Board of Realtors, U.S. v. Jack Foley, and U.S. v. Greater Syracuse Board, infra. See also, e.g., U.S. v. Atlanta Real Estate Board, 1972 Trade Cas. (CCH) ¶ 73,825 (N.D. Ga. 1971); U.S. v. Cleveland Real Estate Board, 1972 Trade Cas. (CCH) ¶ 74,020 (N.D. Ohio 1972); U.S. v. Greater Pittsburgh Board of Realtors, 1973 Trade Cas. (CCH) ¶ 74,454 (W.D. Pa. 1973); U.S. v. Long Island Board of Realtors, Inc., 1972 Trade Cas. (CCH) ¶ 74,068 (E.D.N.Y. 1972); U.S. v. Los Angeles Realty Board,

(Continued)

suggested commission rates and commission splits.608/ Most of the cases resulted in consent decrees whereby the local Boards were prohibited from fixing or suggesting commission rates.

b. Importance of Fee Schedules

During the time when formal efforts at fee stabilization were an accepted practice, the National Association President expressed his opinion that first on the list of services provided by the local and state Associations was: "Commissions, a uniform schedule of fees and commissions so there is no opportunity for misunderstanding between [the Realtor] and his clients as to the value of his services."609/

An early chairman of the National Association's Committee on Commissions, in an article entitled "Bases for Establishing Commission Rates," stressed the importance of uniformity of rates. Commission-cutting was considered unethical. In addition, in order to ensure a good return for good services, it was considered essential that buyers and sellers accept rates as fixed.610/

Commission-cutting, often associated with new entrants, undermined the ability of the others to secure the higher rates. The Chairman of the California Uniform Commission Committee noted: "There are many brokers who are operating under lower commission charges than provided by the schedule. They are injuring themselves very definitely, and making it harder for the others to receive adequate compensation for their services."611/

The same official added: "We have found it a great help to be working under this schedule. . . . Wherever our charges were questioned, we showed them the schedule, and have never lost a client for that reason."612/ One of the reasons for the success of fee schedules was the lack of resistance by sellers. A National Association spokesman, commenting on the increase of rates from 5 to 6

1973 Trade Cas. (CCH) ¶ 74,366 (C.D. Cal. 1973); U.S. v. Memphis Board of Realtors, 1972 Trade Cas. (CCH) ¶ 74,056 (W.D. Tenn. 1972); U.S. v. Metro MLS, Inc., 1974-2 Trade Cas. (CCH) ¶ 75,137 (E.D. Va. 1974); U.S. v. Multiple Listing Service, 1973 Trade Cas. (CCH) ¶ 74,515 (O. Or. 1973); U.S. v. Real Estate Board of Metropolitan St. Louis, 1973-2 Trade Cas. (CCH) ¶ 74,744 (E.D. Mo. 1973); U.S. v. Real Estate Board of New York, Inc., 1974-2 Trade Cas. (CCH) ¶ 75,350 (S.D.N.Y. 1974); U.S. v. Real Estate Board of Rochester, New York, Inc., 1975 Trade Cas. (CCH) ¶ 60,192 (W.D.N.Y. 1975).

608/ Access to the MLS and the appropriateness of MLS fees were also at issue in many of these cases.

609/ California Real Estate (June 1940), at 74.

610/ Proceedings of the Brokers Division, NAREB Annual Convention, June 27-30, 1923, Cleveland, Ohio, Real Estate Brokerage, at 16.

611/ P. Bomberger, Chairman, Uniform Commissions Committee, CREA, California Real Estate (January 1936), at 28.

612/ Id.

percent in 1958, noted: "Increasing the rate from 5 to 6 percent is catching fire all over the country, and about the only reason the increased rate has not become more generalized is the fear some brokers have of owner resistance. Such fears are unfounded."[613] The average seller, not having sold in years, had no idea of what a commission rate ought to be, according to this spokesman.[614]

c. Current Status of Fee Schedules

Numerous government antitrust suits in the 1970's challenging "suggested" rate schedules indicate that the use of schedules continued to be relatively common until very recently.[615] In the course of this investigation, we found that Realtor Boards and most MLSs studied now appear to have abandoned the overt use of required or suggested fee schedules.[616] The only related practice for which we have current evidence is the use of suggested or required commission split rates. A small number of non-Realtor MLSs appear to follow this practice.[617]

3. Covert Price-Fixing Conspiracies

In addition to the open and at one time widely accepted use of fee schedules, brokers have at times also engaged in covert conspiracies to fix or raise commission rates or splits. No precise measure of the historical or current prevalence of these conspiracies is, of course, possible.

The frequency of price-fixing litigation, however, increased in the era following the demise of fee schedules. Many antitrust actions were initiated during the 1970's. This frequency is attributed by some to a more vigorous effort by prosecutors and private plaintiffs. Others believe it may also be due to an increased use by brokers of covert methods to achieve the results fee schedules once achieved openly.

Separate efforts in the 1970's by brokers in Maryland to fix or raise commission rates from 6 to 7 percent resulted in two Department of Justice lawsuits. In 1971 the Prince George's County Board of Realtors settled Justice Department charges of price fixing by agreeing to a consent order prohibiting the fixing of fees, the use of fee schedules, and other practices.[618] In a second

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613/ NAR, "Brokers Roundtable, Letter No. 7," California Real Estate (August 1957), at 3.

614/ Id.

615/ See cases cited above in note 607.

616/ See FTC MLS Survey, Question D5; see also, City Summaries of five U.S. cities (Los Angeles, Seattle, Boston, Minneapolis-St. Paul, Jacksonville).

617/ While a small number of non-Realtor MLSs have used commission split schedules, some of these have now abolished these schedules. See FTC MLS Survey, Question D11. See also Seattle City Summary.

case, efforts by Maryland brokers in the mid-1970's to raise commissions fr[illegible]6 to 7 percent resulted in the first felony conviction under the revised Sher[illegible] Act. Defendants received sentences involving large fines and suspended jail terms for their roles in the conspiracy.[619]

In upstate New York, a federal grand jury indicted ten corporations on charges of conspiring to fix commission rates during the period 1972 to 1974. All defendants pleaded "no contest" to the criminal charges and paid fines totalling $156,000.[620] In the companion civil action, the Syracuse Board of Realtors and nine brokerage firms settled the price fixing charges by agreeing an order prohibiting, among other practices, the fixing or recommending of commission rates.[621]

A significant number of state antitrust actions also has occurred in recen years. During the 1970's at least eight states brought actions against Boards Realtors or other groups of brokers alleging forms of price fixing, in addition to other practices.[622] Investigations are underway in several other states.[623] And local prosecutors have also identified and challenged alleged price-fixing activities.[624]

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[618] U.S. v. Prince George's County Bd. of Realtors, 1971 Trade Cas. (CCH) ¶ 73,393 (D. Md. 1970).

[619] U.S. v. Jack Foley Realty, Inc., et al., 598 F.2d 1323 (4th Cir. 1979), cert. denied, 100 S. Ct. 727 (1980).

[620] U.S. v. Greater Syracuse Bd. of Realtors, et al., Crim. No. 77 CRM 57, 1978-1 Trade Cas. (CCH) ¶ 62,008 (N.D.N.Y. 1980).

[621] U.S. v. Greater Syracuse Bd. of Realtors, et. al., Civil Action No. 77 Civ. 159 (N.D.N.Y., 5/3/79).

[622] Colorado v. Colorado Springs Board of Realtors, Civ. No. 78-0658, (Dist. Ct., 4th Dist., filed Sept. 16, 1978, case pending); Illinois v. Baird & Warner, Inc., No. 76CH970 (McHenry County Cir. Ct., consent filed May 15, 1977); Maine v. Greater Bangor MLS, (Super. Ct., Penobscot County, August 22, 1977, case pending); Massachusetts v. Jones, Civ. No. 16835 (Super. Ct. Hampshire Co., filed Sept. 28, 1978, case pending); Vermont v. Heritage Realty of Vermont, 1979-2 Trade Cas. (CCH) ¶ 62,897 (Vermont Supreme Ct., 1979. No. 49-79); Vermont v. Rutland County Board of Realtors, No. 5223-78-RC, (Rutland Super. Ct., 7/17/79); Washington v. MLS of Spokane, Inc., 1974-2 Trade Cas. (CCH) ¶ 75,439 (Wa. Super. Ct., Spokane County, 1974); Iowa v. Carroll Multiple Listing Service Inc., No. 26069 (Dist. Ct. Carroll Co., filed May 24, 1979, case pending).

[623] See Appendix B, Section 3.c.

[624] People of the State of California v. National Association of Realtors; People of the State of California v. California Association of Realtors; People of the State of California v. San Diego Board of Realtors; San Diego County Super. Ct. Civ. No. 375 827 (1978), Fourth District Court of Appeals, Division One, Case No. Civ. 18380. California v. Glendale

(Continued)

In addition, numerous private antitrust actions were filed in the 1970's, alleging brokerage price-fixing activities of various types.625/

Of course only litigated cases (such as Jack Foley above), or to some extent "no contest" pleas (such as Greater Syracuse Board above), offer unequivocal proof of brokerage price-fixing activities. However, the nationwide pattern of investigations, antitrust cases, and settlements suggests that in recent years local price fixing conspiracies may to a certain extent have been a continuing phenomenon in real estate brokerage.

4. Conclusions

Given the complexity of the brokerage industry, the significance of fee stabilization efforts can be easily misunderstood. Efforts to stabilize or raise brokerage commissions have been and still are, to some extent, an aspect of the brokerage industry. These efforts, however, do not appear to be the primary cause of current rate uniformity.

Formal fee schedules have now been largely abandoned by broker groups. Nevertheless, some residual effects can reasonably be inferred, since in many areas suggested schedules were in effect less than 10 years ago. These effects include both a stigma that seems to attach to price competition and the current pattern of fees in most communities. If, however, the use of fee schedules were the principal cause of uniformity within local markets, we would expect to have seen a pattern of shifting away from uniformity within each local market since the time of the abandonment of the schedules. Yet our rate data indicates no such shift.626/ Causes other than fee schedules, therefore, must be at work today to account for the observed pattern of uniformity.

It is logical to assume that covert price-fixing conspiracies may still contribute in some limited degree to rate uniformity. This may, for example, be evidenced by a sudden local increase in the level of commission rates by numerous

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Board of Realtors, Inc., (Sup. Ct. C 138761) and California v. Hawthorne-Lawndale Board of Realtors, Inc., No. C. 148828, L. A. Cty, Sup. Ct., (1/22/76).

625/ See, e.g., Penne v. Greater Minneapolis Area Bd. of Realtors, 604 F.2d 1143 (8th Cir. 1979), 1979-2 Trade Cas. (CCH) ¶ 62,820 (8th Cir. Ct. reversed the District Court and remanded the case); Forbes v. Greater Minneapolis Bd. of Realtors, 1973-2 Trade Cas. (CCH) ¶ 74,696 (D. Minn. 1973) Fourth Division, No. 4-72 Civ. 569 (1975); Butowsky v. Prince George's County Board of Realtors, Inc., Civ. Action No. 71-1086K, (D. Maryland, settled Jan. 1976); Hill v. Art Rice Realty Co., 1974-2 Trade Cas. (CCH) ¶ 75,364 (N.D. Ala. 1974); James v. Phoenix Real Estate Board, Civ. No. 73-559, (D. Arizona, settled May 1975); Mazur v. Behrens, 1974 Trade Cas. (CCH) ¶ 75,070 (N.D. Ill. 1972); Nichols v. Mobile County Board of Realtors, Inc., 1978-2 Trade Cas. (CCH) ¶ 62,200 (S.D. Ala. 1978); McKerall v. Huntsville Real Estate Board, 1976-1 Trade Cas. (CCH) ¶ 60,709 (N.D. Ala. 1976); Ogelsby and Barclift, Inc., v. Metro MLS, Inc., 1976-2 Trade Cas. (CCH) ¶ 61,064 (E.D. Va. 1976).

626/ See Ch. III, Part A.

or all firms. The costs of adopting a policy of uniform increases in price may be reduced by broker interdependence: brokers share the same organization usually share vital data through the cooperative service of the MLS, and rely heavily on referrals and cooperation with competitors. It, therefore, might be less difficult to organize price collusion and to detect and sanction violators. Once a new rate level is established it might be maintained by the structure of the industry.

Antitrust actions undoubtedly reduce the frequency of covert conspiracies that contribute to price uniformity. However, we have no evidence that efforts at stopping these per se unlawful conspiracies produce significant change in rates. Observation of areas where price fixing cases have been successful reveal no pattern of significant rate reduction.627/ Overt collusion has generally not been necessary to maintain uniform prices because the brokerage system is, by very nature, self-enforcing.

Price fixing activities of today, whatever their precise extent, are essentially related to larger structural issues in the brokerage industry, and although plainly illegal, are not fundamental causes of price stability.

627/ Los Angeles, St. Louis, New York City, Pittsburgh, Atlanta, Syracuse, Minneapolis-St. Paul, Rochester, Washington, D.C. and a number of other cities have been the locales of actions by the Justice Department alone. We have no evidence that any of these cities has experienced significant rate reduction, and at least in the cases of Los Angeles, St. Louis, Atlanta, and Minneapolis-St. Paul, we have statistical evidence that no significant reduction has occurred. See Ch. III, Part A.