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UNITED STATES OF AMERICA
FEDERAL TRADE COMMISSION
NEW YORK REGIONAL OFFICE

COMMISSION AUTHORIZED

July 6, 1990

Ms. Gail A. Bates, Director
Division of Licensing Services
N.Y.S. Department of State
162 Washington Avenue
Albany, New York 12231

Dear Ms. Bates:

The staff of the Federal Trade Commission¹ is pleased to respond to the request of the Department of State for comments on the preliminary "Codification of Rules and Regulations Affecting Real Estate Licensees" ("Proposed Regulations").² We understand that the Proposed Regulations are intended to reduce confusion and misunderstanding among consumers, real estate brokers and salespersons ("Licensees") and to promote better "operational standards."³

The Proposed Regulations would, among other things, require Licensees to make specified disclosures to home sellers and prospective buyers regarding, for example, Licensees' obligations to each; proscribe certain forms of representation, such as dual agency; and limit specified contract terms, such as the duration of listing agreements. We believe that disclosure requirements may benefit consumers in some circumstances, which we discuss subsequently. We note, however, that the Proposed Regulations'

¹ This letter presents the views of the staffs of the Los Angeles and New York Regional Offices and the Bureau of Competition of the Federal Trade Commission. They are not necessarily the views of the Commission or of any individual Commissioner.

² Our comments are limited to the potential effects of the Proposed Regulations' residential real estate brokerage provisions and, in particular, to those proposed regulations that most significantly may affect consumers. We express no opinion as to the Department of State's authority to promulgate the regulations.

³ Memorandum from Gail S. Shaffer, Secretary of State, State of New York, to Members of the Real Estate Industry (December 18, 1989).

limitation of certain real estate practices and contract terms unnecessarily may harm some consumers.

I. INTEREST AND EXPERIENCE OF THE STAFF OF THE FEDERAL TRADE COMMISSION

The Federal Trade Commission is charged with preventing unfair methods of competition and unfair or deceptive acts or practices in or affecting interstate commerce.⁴ Consistent with this mandate, the staff of the Federal Trade Commission often submits comments, upon request, to federal, state, and local governmental bodies to help them assess the competitive and consumer welfare implications of pending proposals.

The staff of the Commission has considered numerous issues relating to competition in real estate markets, including New York State real estate markets.⁵ In addition, the staff of the Commission's Los Angeles Regional Office conducted a study of the residential real estate industry. That study included a nationwide survey of consumer experiences with real estate brokers, some of the findings of which are noted below.⁶

II. PROPOSED DISCLOSURE REQUIREMENTS

Section 4 of the Proposed Regulations would impose on Licensees various disclosure obligations designed to ensure that all prospective parties to real estate transactions understand

⁴ 15 U.S.C. § 41 et seq.

⁵ See, e.g., Multiple Listing Service Mid County, Inc., 110 F.T.C. 482 (1988); Orange County Board of Realtors, Inc., 106 F.T.C. 88 (1985). Enforcement matters involving non-New York State real estate markets include Florence Multiple Listing Service, Inc., 110 F.T.C. 493 (1988); and Multiple Listing Service of Greater Michigan City Area, Inc., 106 F.T.C. 95 (1985).

⁶ The Residential Real Estate Brokerage Industry, Washington, D.C.: Los Angeles Regional Office of the Federal Trade Commission (1983) ("Staff Report"). See also Butters, Consumers' Experiences with Real Estate Brokers: A Report on the Consumer Survey of the Federal Trade Commission's Residential Real Estate Brokerage Investigation, Washington, D.C.: Federal Trade Commission (1983).

Licensees' agency status and obligations.⁷ In substantial part, the disclosure requirements appear to be a response to some prospective buyers' misunderstanding of the role and obligations of Licensees who are assisting them in "house hunting," but who may be acting as agents of sellers.⁸

Prospective buyers typically are introduced to properties by agents retained by home sellers or by cooperating brokers who seek to share in commissions paid by sellers and who may be sub-agents of sellers.⁹ The circumstances surrounding "the house

⁷ An agency may arise by express or implied agreement. An implied agreement may be inferred from facts and circumstances, especially the words and conduct of the parties. In general, unless an agreement to the contrary is established, a real estate broker is deemed to be an agent of the seller--typically because the seller is responsible for payment of the commission to be earned. However, seller responsibility for payment of a cooperating broker's commission ordinarily does not preclude the parties' agreeing that the broker will represent the purchaser. See, e.g., Currier, Finding the Broker's Place in the Typical Residential Real Estate Transaction, 33 U. Fla. L. Rev. 655, 660-65 (1981).

⁸ For example, Section 4(a) of the Proposed Regulations provides that "[a] licensee shall make his agency status and obligations clear to the clients, customers and other licensees with whom the licensee deals." Section 4(g) provides that "[w]hile representing a client, a licensee shall not, by words or conduct, cause a customer or customer's agent to believe that the licensee can or will represent the interests of the customer." And Section 4(j) states that "[w]henver the words or conduct of a customer indicate that the customer has misconstrued or misunderstood the relationship between the licensee and the customer, the licensee shall take prompt, unequivocal and affirmative action to clarify the true relationship between the licensee and customer."

⁹ The listing agreement used by members of at least one New York State multiple listing service, Rockland County Multiple Listing System, provides that the home seller engages every member of the multiple listing service as his or her authorized agent. The subagent designation is more often intended by cooperating brokers in New York State, the Handbook of Multiple Listing Policy (1980) of the National Association of Realtors ("NAR") providing, in Section 1.2:

A Multiple Listing Service is defined as a means by which one Participant makes a blanket unilateral offer of subagency to the other Participants and as a facility for the orderly correlation and dissemination

hunt"¹⁰ may lead some prospective buyers to assume that Licensees represent them, whether or not it is so. Prospective buyers who unknowingly treat sellers' agents as their own may be harmed in at least two ways. First, they may unintentionally reveal to sellers' agents--and through the agents to the sellers--"proprietary" bargaining-related information. Second, prospective buyers may unwittingly fail to secure fiduciary representation or assistance, such as the services of a buyer's broker or an appraiser. The Staff Report on the residential brokerage industry provides some support for the belief that a substantial number of prospective buyers believe themselves to be "represented" by the brokers who assist them.¹¹ Insofar as some of these brokers may see themselves as sellers' agents,¹² consumer injury may result.

Where, as may be true here, some consumers lack information necessary to protect and advance their interests, adoption of a regulation requiring the disclosure of pertinent information may be beneficial. Whether or not such a regulation will promote consumer well-being may depend on the utility of the information to be disclosed, the manner in which it is to be disclosed, and

of listing information among the Participants so that they may better serve their clients and the public.

Approximately 90% of the nation's multiple listing services are affiliated with the NAR. See Staff Report at 8.

¹⁰ For example, prospective buyers often initiate the contacts with Licensees. Thereafter, prospective buyers may share a great deal of personal information--about family needs, about personal preferences, and about economic circumstances, among other things--with Licensees. Prospective buyers and Licensees may spend a considerable portion of their time for several days in succession in one another's exclusive company. These circumstances also may bear on whether or not an agency between a Licensee and a prospective buyer will be implied. See note 7 supra.

¹¹ Nearly three quarters of the home sellers and of the home buyers who responded and who had participated in co-brokered transactions believed that the cooperating brokers were, in some sense, "representing" the buyers. Staff Report at 8, 14, and 180 et seq. Nearly three quarters of the home buyer-responders reportedly told the agents with whom they worked the highest price that they would pay for the property sought; and more than four fifths of these buyers believed that the agents would keep that information in confidence. Staff Report at 186.

¹² See note 9 supra.

the countervailing costs of making the mandated disclosure.¹³ Accordingly, if the State determines that the market is failing to provide prospective real estate buyers with adequate information regarding agency, it may wish to adopt a cost-effective disclosure regulation.

Section 4 of the Proposed Regulations further would require each Licensee to disclose to prospective listers of property all of its policies and procedures that "affect the marketing" of listers' properties. These policies and procedures expressly include, but are not limited to, refusals to deal with specific companies and refusals to offer commission splits of at least 50% to subagents, co-brokers, or buyers' brokers.¹⁴ It may be that in listing their homes some consumers are disadvantaged, and the efficient operation of the real estate market frustrated, because of Licensees' undisclosed in-house policies. For example, a policy of refusing to deal with off-price brokers and buyers' agents may reduce the exposure of listers' homes, possibly affecting listed homes' time-on-market and selling prices. The same may be said of a policy of severely restricting compensation offered to successful co-brokers.¹⁵ Timely disclosure of these and like policies would permit consumers to take their potential effects into account in deciding with whom to list properties. If the State determines that a substantial number of consumers is harmed by non-disclosure, it may wish to adopt cost-effective disclosure requirements.

We urge the State to consider with caution, however, the requirement in the Proposed Regulations that all in-house

¹³ See generally International Harvester Co., 104 F.T.C. 949 (1984).

¹⁴ See Proposed Regulations at 4(e). The reference to "subagents" apparently relates to non-residential listings.

¹⁵ The requirement in Section 4(e)(3) that a Licensee disclose to prospective listers any policy to refuse to offer to co-brokers and buyers' agents at least a 50% share of the commission may inappropriately discredit every split weighted in favor of the listing broker. It may be preferable to limit commission split-related rules to the disclosures contained in Sections 15(c) and 16(d) of the Proposed Regulations. Section 15(c) provides that listing brokers must explain to prospective listers "the client's right to determine and specify the amount of compensation and all other terms upon which listing broker may be authorized to offer compensation to subagents, co-brokers and/or buyer's [sic] agents." Section 16(d) provides that every agency agreement shall set forth, among other things, the commission split that the listing broker is authorized to offer to co-brokers and to buyers' agents.

policies and procedures that "affect the marketing" of listed properties be disclosed. A tremendous variety of policies and procedures could be deemed to "affect the marketing" of properties, and their disclosure could entail costs--including reduced consumer attention to the most significant aspects of the proposed brokerage arrangement--in excess of their benefits.

III. PROSCRIPTION OF CERTAIN FORMS OF REPRESENTATION

The Proposed Regulations may be construed to ban certain types of representation. For example, Section 5 of the Proposed Regulations, which specifies that "[a] licensee shall not represent adverse interests in the same real estate transaction," may be taken to ban so-called "dual agencies." We have been advised that the Secretary of State concludes that New York State law now bars dual agencies on the premise that one actor cannot satisfy fiduciary obligations to parties with adverse interests, and that Section 5 of Proposed Regulations merely restates the general law.¹⁶

Some limited forms of dual representation may not impose conflicting obligations on Licensees, however. For example,

[a]fter full disclosure of the representation alternatives, the buyer and the seller might agree that the broker will be a collector of information and a messenger of positions, rather than a broker who will investigate, disclose, advise, negotiate and fully protect a principal's best interests.

Part of the special arrangement could be that confidential information, such as the buyer's ultimate negotiating position, may not be revealed to the seller.¹⁷

¹⁶ We understand, however, that in some circumstances parties' informed consent to dual agency will constitute an affirmative defense in an action against the dual agent. This defense is not lightly established: "Informed consent is more than just knowing that one and the same agent represents both the buyer and the seller. The broker is obligated to disclose all facts relevant to the buyer's and the seller's decisions of whether or not to consent to the common representation." J. Reilly, Agency Relationships in Real Estate, Real Estate Education Co. 63-65 (1987) (emphasis in original).

¹⁷ Id.

The availability of such a representation alternative may enable some home sellers and home buyers to obtain wanted--and only wanted--Licensee services at prices less than the cost of separate and inclusive representation. As we understand it, the general law's bar does not necessarily extend to some limited forms of dual representation. Accordingly, the State may wish to modify the Proposed Regulations to clarify or recognize the appropriateness of dual representation consistent with the avoidance of Licensee conflicts-of-interest.

The Proposed Regulations also appear to prohibit a listing broker from offering subagencies to Licensees not affiliated with him or her. Such Licensees would be "cooperating brokers," as defined in the Proposed Regulations, and therefore would not operate as agents or subagents of homeowners.¹⁸ We understand that the intent underlying restriction of subagency offers is to avoid potential homeowner liability for wrongful acts and omissions of brokers with whom homeowners have no direct relationship. However, it is difficult to determine precisely how the proposed regulation would affect the rights and liabilities of homeowners and cooperating brokers, and whether the proposed regulation would impair the efficient delivery of brokerage services. Accordingly, the State may wish to further assess the likely effectiveness and costs of the ban on subagency,¹⁹ and to modify the proposed regulation if appropriate.²⁰

IV. LIMITATIONS OF CONTRACT TERMS

The Proposed Regulations also contain provisions that would restrict the terms of contract between Licensees and homeowners. Restrictions on terms of contract may, in some instances, advance

¹⁸ See, for example, Sections 1(a) and (e), 6, and 16(e). Section 1 contains applicable definitions. Section 6 precludes brokers' offering and accepting of offers of subagency from other brokers. And Section 16(e) prohibits brokers' use of agency agreements authorizing the making of subagency offers.

¹⁹ The comments of multiple listing services and trade associations regarding the Proposed Regulations may be of substantial assistance to the State in understanding the efficiency implications of the proscription of subagency offers.

²⁰ For example, the State may wish to permit informed homeowners to consent to their brokers' extending offers of subagency to prospective cooperating brokers. This is the approach adopted in the Proposed Regulations' application to non-residential real estate transactions. See Section 7 of the Proposed Regulations. See also Section 15, relating to disclosure of homeowners' rights to determine contractual options that limit personal liability.

public interests. However, restrictions on terms of contract also may impose unnecessary costs on consumers. Section 16(c) of Proposed Regulations, which limits listing agreements to not more than 90 days, may be an example of the latter.

The activity level in real estate markets may vary considerably from area to area and from time to time. In some instances, a 90-day listing period may provide more than enough time for a Licensee to promote the sale of a property. Under other market conditions, however, a 90-day listing period may be quite inadequate. When homeowners and Licensees are free to negotiate the duration of listing agreements, local market conditions can be considered and the interests of homeowners and Licensees accounted for. In contrast, administrative determination of "the appropriate" listing contract duration may lock homeowners and Licensees into contract terms that, at times, serve neither.

Listing brokers may provide a variety of useful services to homeowners.²¹ The availability of these services may depend on listing brokers' expectations that the costs of providing the services will be recouped from commissions on sales of properties listed by them.²² Limiting by regulation the duration of listing agreements may reduce the likelihood that homes will be sold during given listing periods, particularly in a "buyers' market." If listing brokers believe that they cannot recover their costs during the regulated listing period, they may reduce services provided and/or increase the price charged for those services.²³ In either event, homeowners' interests may suffer. Accordingly,

²¹ These services may include: the preparation of detailed market analyses to guide homeowners in establishing list prices; the holding of open houses to acquaint prospective cooperating brokers and prospective purchasers with listed properties; the preparation and publication of pictorial advertisements featuring listed properties and other promotional materials; the analysis of prospective purchaser traffic and feedback and the provision of related guidance to homeowners as to prospective purchaser objections (such as the market will not support the asking price, or the dirty kitchen cabinets are turning people off); and the provision of "house-sitting" services on behalf of listers that have relocated at a distance from listed properties.

²² Costs are not necessarily recouped in each transaction. Rather, each listing broker ordinarily expects to recoup costs over the course of several transactions.

²³ Some listing brokers might reduce their costs and increase their revenues by requiring home listers to separately contract and pay for services, such as "for sale" advertising, that now often are provided without additional charge pursuant to listing agreements.

the State may wish to explore less restrictive alternatives to the proposed Section 16(c), such as requiring Licensees to make a cautionary disclosure, or abandon it.

Section 16(f) also restricts the terms of contract between Licensees and homeowners. That section provides that "[a] real estate broker shall not use any agency agreement which authorizes the real estate broker to limit offers of compensation to members of any particular trade group or association." Homeowners typically may seek to list their properties in a manner that will ensure widespread cooperative brokerage efforts. Some homeowners, however, might prefer to restrict offers of compensation to members of a given organization, where membership in that organization attests to some quality of importance. For example, organizational membership may be limited to persons having extensive training and/or experience, or may certify compliance with a high-minded code of professional ethics. Thus, by agreeing to limit offers of compensation to members of such an organization, homeowners might increase the effectiveness of cooperative brokerage efforts, or reduce the risks of dealing with brokers and sales representatives who engage in ethically questionable practices. Accordingly, the State may wish to reconsider the advisability of adopting Section 16(f) of the Proposed Regulations.²⁴

V. CONCLUSION

We have limited our comments to matters substantially affecting competition and consumers in residential real estate markets. Within that context, we adhere to the view, in part reflected in the Proposed Regulations, that information failures that deprive consumers of the ability to act in their self-interest are best addressed by adoption of narrowly tailored disclosure requirements. Overly broad disclosure requirements may impose substantial and unnecessary consumer costs. Similarly, some proposed restrictions on forms of Licensee representation and on contract terms may frustrate some consumers' efforts efficiently to satisfy their wants. In those instances, careful identification of the public policies to be advanced may permit the adoption of less restrictive regulations, such as narrowly

²⁴ If the proposed Section 16(f) were withdrawn, Licensees would likely be obligated under Section 4 of the Proposed Regulations to disclose to prospective listers any in-house policies limiting offers of compensation to members of a particular trade group. See discussion at pages 5 and 6 supra.

tailored disclosure requirements, or the dropping of the proposed regulation.

Very truly yours,



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