



UNITED STATES OF AMERICA



FEDERAL TRADE COMMISSION  
Washington, DC 20580

DEPARTMENT OF JUSTICE  
Washington, DC 20530

April 20, 2005

Loretta R. DeHay  
General Counsel  
Texas Real Estate Commission  
P.O. Box 12188  
Austin, TX 78711-2188

Re: **Proposed Amendments to 22 TEX. ADMIN. CODE § 535.2**

Dear Ms. DeHay:

On February 22, 2005 the Texas Real Estate Commission ("TREC") proposed a revision to its current rules concerning a real estate broker's responsibilities.<sup>1</sup> According to TREC, the revisions are necessary to clarify an ambiguity in the current rules governing real estate brokerage that create some uncertainty for buyers' agents and home-sellers with respect to the role of buyers' agents and limited-service brokers ("LSBs") in real estate transactions involving limited-service brokerage.

The Federal Trade Commission ("FTC" or "Commission") and the United States Department of Justice believe that by prohibiting core limited-service brokerage options and therefore requiring some home-sellers to purchase services that they otherwise would choose to perform themselves, TREC's proposed amendments to 22 TEX. ADMIN. CODE § 535.2 are likely to harm Texas consumers by reducing their choices and likely raising prices without providing any countervailing benefits. Competition between full-service brokers ("FSBs") and LSBs is likely to provide benefits to Texas consumers and there is no evidence that LSBs have caused any consumer harm. If TREC nevertheless is concerned about potential confusion with regard to the services LSBs provide to their clients or LSBs imposing additional costs on buyers' agents, it should consider less restrictive alternatives to protect consumers than the current proposal, which would deprive Texas consumers of core limited-service brokerage options. Accordingly, we urge TREC not to adopt the proposed amendments.

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<sup>1</sup>See Broker's Responsibility, 30 Tex. Reg. 1400 (proposed Mar. 11, 2005).

## I. Interest and Experience of the FTC and the Department of Justice

Congress has charged the FTC with enforcing laws prohibiting unfair methods of competition and unfair or deceptive acts or practices in or affecting commerce.<sup>2</sup> Pursuant to this statutory mandate, the Commission encourages competition in the licensed professions, including real estate brokerage, to the maximum extent compatible with state and federal goals. The FTC has experience in analyzing aspects of the real estate transaction. For example, the FTC and the Department of Justice have commented on numerous occasions in support of allowing non-attorneys to compete with attorneys in the provision of certain real estate settlement tasks.<sup>3</sup> Further, in 2002 the Commission held a public workshop on barriers to electronic commerce in many industries, and gathered testimony on state restrictions that may impede competition from online real estate service providers.<sup>4</sup>

The Department of Justice is also entrusted with enforcing this nation's antitrust laws. For more than 100 years, since the passage of the Sherman Antitrust Act, the Department of Justice has worked to promote free and unfettered competition in all sectors of the American economy through its civil and criminal enforcement programs. In particular, the Justice Department has a long history of enforcement efforts in the real estate area that includes several cases involving restrictions on access to multiple listing services and other restraints limiting competition among real estate brokers. Recently, for example, the Justice Department filed a civil antitrust lawsuit against the Kentucky Real Estate Commission.<sup>5</sup> The suit alleges that the Kentucky Real Estate Commission violated Section 1 of the Sherman Act by promulgating and enforcing a regulation that prohibits Kentucky real estate brokers and sales associates from offering rebates and other inducements to attract customers. The Department also recently sent a

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<sup>2</sup>Federal Trade Commission Act, 15 U.S.C. § 45.

<sup>3</sup>Letter from FTC and the Justice Department to Massachusetts State Representative Paul Kujawski (Oct. 6, 2004); letter from FTC and the Justice Department to Standing Committee on the Unlicensed Practice of Law, State Bar of Georgia (Mar. 20, 2003); letters from the FTC and the Justice Department to Speaker of the Rhode Island House of Representatives and to the President of the Rhode Island Senate, *et al.* (June 30, 2003 and Mar. 28, 2003); letter from the FTC and the Justice Department to President of the North Carolina State Bar (July 11, 2002); letter from the FTC and the Justice Department to Speaker of the Rhode Island House of Representatives, *et al.* (Mar. 29, 2002); letter from the FTC and the Justice Department to the Ethics Committee of the North Carolina State Bar (Dec. 14, 2001); letter from the FTC and the Justice Department to the Supreme Court of Virginia (Jan. 3, 1997); letter from the FTC and the Justice Department to the Virginia State Bar (Sept. 20, 1996). These letters can be found at <http://www.ftc.gov/be/advofile.htm>. See also Brief *Amicus Curiae* of the United States of America and the Federal Trade Commission in *Lorrie McMahon v. Advanced Title Services Company of West Virginia*, 607 S.E. 2d 519 (W. Va. 2004) (filed May 25, 2004), at <http://www.ftc.gov/be/V040017.pdf>; Brief *Amicus Curiae* of the Federal Trade Commission and the United States of America in On Review of ULP Advisory Opinion 2003-2 (filed July 28, 2003), at <http://www.ftc.gov/os/2003/07/georgiabrief.pdf>.

<sup>4</sup>FTC Workshop, POSSIBLE ANTICOMPETITIVE EFFORTS TO RESTRICT COMPETITION ON THE INTERNET (Oct. 10, 2002), written statements and transcript available at, <http://www.ftc.gov/opp/e-commerce/anticompetitive/agenda.htm>.

<sup>5</sup>See Complaint, *United States v. Kentucky Real Estate Comm'n*, Civ. Act. No. 3:05CV188-H (filed Mar. 31, 2005), at <http://www.usdoj.gov/atr/cases/f208300/208393.htm>.

letter to the Oklahoma State Legislature opposing pending legislation in Oklahoma that is similar to the proposed amendment at issue here.<sup>6</sup>

## II. Background

Broadly, the tasks involved with selling a house include marketing it and negotiating with buyers. Traditional FSBs bundle these tasks together; for a fixed commission – typically split with the buyer’s agent – an FSB will list a house in the local MLS, place advertisements for it in the local paper and on the Internet, conduct open houses, and coordinate other showings. Additionally, an FSB provides advice on pricing and assists the seller in negotiating and closing the transaction.

Some consumers may want to sell their house without the assistance of a broker but desire the additional exposure of listing their home in the local MLS. Such consumers, however, cannot list their house in the MLS on their own; only a licensed real estate agent who is a member of the local MLS can list a house in the local MLS.<sup>7</sup> LSBs serve these consumers by unbundling MLS listing from the menu of tasks an FSB typically performs, thus providing their clients with fewer services at lower prices. A seller contracting with an LSB typically pays a flat fee in exchange for the LSB listing the house in the local MLS and providing additional selling aids, such as yard signs, online advertisements, and a lock-box to allow buyers’ agents to show the home when the seller is not present. Limited-service brokerage contracts also typically require the seller to agree to pay a commission to a buyer’s broker who supplies the ultimate buyer of the home.<sup>8</sup> A seller who finds a buyer without the help of a buyer’s broker does not incur this fee. Importantly, a seller might elect not to use an LSB in marketing the house or in

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<sup>6</sup>See Letter from R. Hewitt Pate, Assistant Att’y Gen. to Oklahoma State Representative Todd Heitt (Apr. 8, 2005), at [http://www.usdoj.gov/atr/public/press\\_releases/2005/208486.htm#letter](http://www.usdoj.gov/atr/public/press_releases/2005/208486.htm#letter).

<sup>7</sup>See, e.g., *Rules and Regulations of North Texas Real Estate Information Systems, Inc.* §§ 5.01-5.02 (Feb. 18, 2004) (“NTREIS”), at <http://www.ntreis.net/FormsAndDocs/rulesregs.htm>.

<sup>8</sup>See, e.g., American Home Market.com (3 percent commission for a broker that finds a buyer), at <http://www.mlslistingnetwork.com/Nav.aspx/Page=http://MLSListingNetwork.com/PageManager/Default.aspx?PageID=241757>; ForSaleByOwner.com (allowing consumers to offer buyers’ agents any commission rate, but noting that “owners should consider that offering less than the traditional 3% could affect these Buyers Agent Realtors [sic] ‘degree’ of interest in showing your property to their customers”), at <http://www.forsalebyowner.com/perl-bin/showPage.cgi?szNextPage=placead.html&szAction=NEW&szURL=MLS;FSBOAdvertisingService.com> ( 2-3 percent commission for broker that finds a buyer), at <http://www.fsboadvertisingservice.com/flat-fee-mls-MLSTX3.asp>; ifoundahome.net (allowing home-sellers to offer “a 3% commission or more” to buyers’ brokers), at <http://www.ifoundahome.net/Listingwork/SBasicListing.htm>; Texas Discount Realty (3 percent commission for a broker that finds a buyer), at <http://www.texasdiscountrealty.com/flatfee.htm>. See also Roy T. Black & Hugh O. Nourse, *The Effect of Different Brokerage Modes on Closing Costs and Housing Prices*, 10 J. RES. REAL ESTATE 87, 91 (1995) (reporting that for a sample of real estate transactions in Atlanta, when the transaction involved only a buyer’s broker, the buyer’s broker received between 3 - 3.5 percent commission).

negotiating with buyers; under a limited-service brokerage contract, the seller often agrees to negotiate directly with buyers or their agents.<sup>9</sup>

### III. The Proposed Rule

Section 535.2 of the Texas Administrative Code sets forth a real estate broker's responsibilities. The pertinent portion of these rules currently reads:

A real estate broker acting as an agent owes the very highest fiduciary obligation to the agent's principal and is obligated to convey to the principal all information of which the agent has knowledge and which may affect the principal's decision. A broker is obligated under a listing contract *to negotiate* the best possible transaction for the principal, the person the broker has agreed to represent.<sup>10</sup>

Although the current rule obligates both FSBs and LSBs to "negotiate" for their clients, it does not set out what "negotiation" requires. TREC's proposal would set forth the "minimum level of service" that "negotiation" entails. Specifically, the proposal states:

In negotiating for his or her principal the broker shall provide the following services:

- (1) accept and present to the principal offers and counter-offers to buy, sell, or lease the principal's property or property the principal seeks to buy or lease;
- (2) assist the principal in developing, communicating, and presenting offers, counter-offers, and notices that relate to the offers and counter-offers; and
- (3) answer the principal's questions relating to offers, counter-offers, and notices.<sup>11</sup>

The proposal also would make it a violation of TEX. OCC. CODE ANN. § § 1101.652(b)(22), (27) for a "broker who represents a principal under a listing contract that grants an exclusive agency to the broker . . . [to] instruct or authorize another broker who

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<sup>9</sup>As TREC noted in its 2002 proposal of almost identical amendments to those currently under consideration:

In many cases under [a limited-service brokerage contract], a real estate broker may provide no service to the seller except to place the listing in a Multiple Listing Service. Typically, the listing broker instructs the cooperating broker to contact the seller directly for all purposes (showings, presentations of offers, and negotiations.)

Broker's Responsibility, 27 Tex. Reg. 9255, 9256 (proposed Oct. 4, 2002).

<sup>10</sup>22 TEX. ADMIN. CODE § 535.2(b) (emphasis added).

<sup>11</sup>30 Tex. Reg. at 1401 (proposed 22 TEX. ADMIN. CODE §§ 535.2(d)(1)-(3)).

represents another party in the transaction to negotiate directly with the principal.”<sup>12</sup> Because a local MLS will not accept “non-agency” listings,<sup>13</sup> LSBs must enter into “exclusive agency” relationships with their clients.<sup>14</sup> Thus, the proposed amendments would require LSBs to provide home-sellers with certain services in addition to MLS listing, and would prohibit LSBs from instructing buyers’ agents to negotiate directly with their clients.<sup>15</sup>

Finally, the proposal also would add the following exception:

When a broker delivers an offer or counter-offer to another broker, the broker is not negotiating or attempting to negotiate with a principal he or she does not represent by delivering a copy of the offer or counter-offer to the principal he or she does not represent so long as the broker representing the principal consents to the delivery and the broker who makes the delivery does not discuss or attempt to discuss the terms or conditions of the offer or counter-offer with the principal he or she does not represent.<sup>16</sup>

Because the proposed rule states that brokers “shall provide” the enumerated services, we interpret the proposed rule to prohibit a broker from contracting to provide less than those enumerated services – for example, contracting solely to list a property in the multiple listing service (“MLS”). TREC now has told us that it believes that the proposed rule would not prohibit brokers from contracting to provide fewer than the enumerated services. Specifically, TREC has stated that the proposal would allow an LSB to enter into a contract to provide only MLS listing as long as the agreement contained a proviso allowing the home-seller to request the LSB to provide the additional enumerated services. As discussed below, if that is the case, then we urge it to revise the proposed rule to allow explicitly these types of limited service agreements. We caution, however, that while this revision would reduce our concerns about the

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<sup>12</sup>*Id.* (proposed 22 TEX. ADMIN. CODE § 535.2(e)).

<sup>13</sup>*See* NTREIS, *supra* note 7, at § 7.01 (“Each property listing filed with the MLS must be ‘an exclusive right-to-sell (or lease)’ or an ‘exclusive agency’ listing. . . . Open listings, net listings, and non-agency listings will not be accepted for filing with the MLS.”).

<sup>14</sup>*See* Letter from Greg Abbott, Attorney General of Texas, to Wayne Thornburn, Administrator, TREC, at 3 (Dec. 14, 2004) (“Abbott Opinion”) (citing North Texas Real Estate Information System, Inc., MLS Listing Rule § 7.01 & West Texas Regional MLS, art. 5 Listing Procedures), at <http://www.oag.state.tx.us/opinions/ga/ga0282.pdf>. An “exclusive agency” relationship preserves the right of an owner “to sell the property on an unlimited or restrictive basis.” *See* NTREIS, *supra* note 7, at § 7.01. A home-seller also may enter into an “exclusive right-to-sell” relationship, which is an agency relationship that does not preserve the right of the home-seller to find buyers on his or her own. *Id.*

<sup>15</sup>Although TREC’s general counsel notes that those brokers “whose business models are inconsistent with the proposed amendments” may avoid the rule by establishing a “non-agency relationship,” it appears that given MLS rules, an LSB could not enter into a non-agency relationship and still be able to offer a service that included listing in the local MLS. *See* 30 Tex. Reg. at 1401.

<sup>16</sup>*Id.* (proposed 22 TEX. ADMIN. CODE § 535.2(f)).

rule's restrictions on competition, it would not alleviate them completely. As we understand it, such a revised rule still would eliminate competition from LSBs who provide only MLS listing.

#### **IV. Competitive Effects of the Proposed Rule**

Competition provides substantial benefits to consumers. As the Supreme Court has observed, “ultimately competition will produce not only lower prices, but also better goods and services.”<sup>17</sup> Indeed,

[t]he assumption that competition is the best method of allocating resources in a free market recognizes that all elements of a bargain – quality, service, safety, and durability – and not just the immediate cost, are favorably affected by the free opportunity to select among alternative offers.<sup>18</sup>

Regulations that limit forms of competition may be useful when they address specific market failures that have been shown to harm consumers.<sup>19</sup> In these instances, however, restraints on competition should be drawn narrowly to avoid depriving consumers of the benefits of competition beyond the level necessary to achieve the regulatory goal.

TREC’s proposal is likely to deprive Texas consumers of the benefits of robust competition between LSBs and FSBs without providing any countervailing benefits.

##### **A. The Proposal is Likely to Reduce Competition**

By mandating that all brokers provide home-sellers with a level of service beyond that provided by LSBs, and by prohibiting a seller who has entered into a limited-service brokerage contract from agreeing to negotiate a real estate transaction on his or her own behalf, TREC’s proposal will eliminate certain limited-service brokerage arrangements as an option for Texas

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<sup>17</sup>*Nat’l Soc’y of Prof’l Eng’rs v. United States*, 435 U.S. 679, 695 (1978) (citation omitted).

<sup>18</sup>*Id.*; accord *FTC v. Superior Court Trial Lawyers Ass’n*, 493 U.S. 411, 423 (1990).

<sup>19</sup>Importantly, this proposal is not the product of a TREC study, but rather appears to have originated with the Texas Association of Realtors (“TAR”), whose members stand to gain from the elimination of competition from limited-service brokers. See Letter from George Stephens, Chairman of the Board, TAR to The Hon. Mike Brodie, Chairman, TREC (Sept. 11, 2003) (“TAR Letter”) (asking TREC to consider amending 22 TEX. ADMIN. CODE § 535.2 to include minimum service requirements by including a definition of “to negotiate” that includes the same provisions that appear in the current proposal). Although TAR noted that it had “studied and debated the issue,” neither in that letter nor in its comments on the current proposal does TAR note any instances of consumer harm associated with LSBs.

consumers.<sup>20</sup> By limiting competition from LSBs, TREC's proposal likely will cause both consumers who prefer LSBs and those who prefer FSBs to pay higher prices.

First, TREC's proposal will harm those consumers who prefer the combination of price and service offered by LSBs. The proposed rule would force home-sellers who prefer to market their house and to negotiate a transaction on their own in exchange for lower brokerage fees to purchase extra services, which necessarily raises the price of brokerage.<sup>21</sup> Clearly, some brokers in Texas think that there is a demand for a product that combines fewer brokerage services with a correspondingly lower price. Whether they are right or wrong ordinarily is a question that is left for competition to determine. By preventing consumers from having the option of certain, important limited-service brokerage arrangements, TREC is substituting its own judgment for the competitive process.

Consumer preferences are heterogeneous. Accordingly, although some home-sellers may prefer to pay lower prices for limited-service brokerage, others may prefer to pay higher prices for full service brokerage. But this does not justify the complete elimination of these important limited-service brokerage options for consumers. Consumers are better off when they are able to evaluate all elements of the bargain and to choose whether to hire an FSB or LSB. For example, an informal sample of Web sites offering limited-service brokerage in Texas suggests that a home-seller may pay from \$325 to \$699 for a limited-service brokerage contract that would include listing his or her house in the MLS but would leave marketing and negotiating to the home-seller.<sup>22</sup> If a buyer pays \$136,000 for the seller's house, a seller who contracted with an LSB for \$699 and agreed to pay a three-percent commission to a buyer's agent would pay a total

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<sup>20</sup>As TREC's general counsel noted in the Texas Register notice for the proposed amendments, "Those licensees whose business models are inconsistent with the proposed amendments . . . will need to include the three services, at a minimum, in their menu of services if the licensee will be acting pursuant to an agency relationship." 30 Tex. Reg. at 1401.

<sup>21</sup>As TREC admits in its Texas Register notice, "[a]ny additional costs of providing the services [required under the proposal] may be offset by charging the individual client for the services provided." 30 Tex. Reg. at 1401.

<sup>22</sup>*See, e.g.*, American HomeMarket.com (MLS listing for \$499), at <http://www.mlslistingnetwork.com/Nav.aspx/Page=http://MLSListingNetwork.com/PageManager/Default.aspx?PageID=24175>; ForSaleByOwner.com (offering MLS listing for \$699), at [http://www.forsalebyowner.com/perl-bin/showPage.cgi?szNextPage=placead.html&szAction=NEW&szURL=MLS](http://www.forsalebyowner.com/perl-bin/showPage.cgi?szNextPage=placead.html&szAction=NEW&szURL=MLS;); FSBOAdvertisingService.com (offering MLS listing for \$398), at <http://www.fsboadvertisingservice.com/flat-fee-mls-MLSTX3.asp>; ifoundahome.net (offering MLS listing for \$325), at <http://www.ifoundahome.net/Listingwork/SBasicListing.htm>; MyCastle.com (offering MLS listing for \$498), at [http://www.mycastle.com/selling/selling\\_plans.aspx](http://www.mycastle.com/selling/selling_plans.aspx); Texas Discount Realty (offering MSL listing for \$495), at <http://www.texasdiscountrealty.com/flatfee.htm>. These services also offer various additional services beyond listing in the MLS (e.g., listing on Realtor.com, posting an advertisement on the LSB's Web site, providing yard signs and a lock box for keys so that buyers' agents can show the home when it is unattended). Further, many of these services also provide full-service brokerage options in exchange for a commission.

of \$4,779 in brokerage fees to sell his or her home.<sup>23</sup> The same seller who agreed to pay an FSB a six-percent commission would pay a total of \$8,160 to sell the house. If the TREC proposal is adopted, this limited-service option would be eliminated and many consumers would feel compelled to purchase \$3,381 in additional services that they would have preferred to perform on their own. Clearly, such consumers are worse off because they are unable to choose their preferred combination of price and services.<sup>24</sup>

A second form of consumer harm from TREC's proposal arises because LSBs are likely to provide a competitive constraint on FSBs' pricing. An FSB who wants the business of a consumer who might otherwise consider limited-service brokerage will need to offer lower commissions and/or increased quality to induce the consumer to choose to purchase the additional services offered by an FSB. If LSBs are eliminated as a choice for consumers, some consumers who prefer FSBs are likely to pay higher prices for real estate brokerage.<sup>25</sup> Indeed, in the similar case of real estate settlement services, both the New Jersey and the Kentucky Supreme Courts have observed that non-attorneys, which charged less for settlement services, put competitive pressure on attorney pricing.<sup>26</sup>

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<sup>23</sup>2004 data from the National Association of Realtors shows the median sales price of existing single family homes in the Houston Metropolitan Area to be \$136,000. See National Association of REALTORS, Median Sales Price of Existing Single-Family Homes for Metropolitan Areas (2005), at [http://www.realtor.org/Research.nsf/files/REL04Q4T.pdf/\\$FILE/REL04Q4T.pdf](http://www.realtor.org/Research.nsf/files/REL04Q4T.pdf/$FILE/REL04Q4T.pdf). Assuming that a seller paid \$699 for limited-service brokerage and paid a three-percent commission to a buyer's agent, total brokerage fees associated with selling the home would be \$4,779  $[(.03 \times \$136,000) + \$699]$ .

<sup>24</sup>Consumers would suffer further harm because the proposed rule disables clients from negotiating directly with brokers on the other side of the transaction. Even where clients engage a broker to advise them on negotiations, some prefer to conduct the actual negotiations themselves.

<sup>25</sup>An FSB that is unable to offer different prices to different home-sellers will base its pricing decisions on those home-sellers who are indifferent between hiring an FSB and an LSB. The degree to which LSB pricing constrains FSB pricing increases as the proportion of consumers who are indifferent between LSBs and FSBs at current prices becomes greater. If an FSB is able to offer different prices to different home-sellers, an FSB is likely to offer lower prices only to those home-sellers who are indifferent between FSBs and LSBs and those who prefer LSBs at current prices. If LSBs similarly are able to target price discounts to home-sellers who prefer full service brokerage at current prices, however, this could lead FSBs to lower the prices they charge to these home-sellers as well. This sort of "competitive price discrimination" by differentiated home-sellers can lead to lower prices for all consumers compared to a uniform price equilibrium. See Kenneth S. Corts, *Third-Degree Price Discrimination in Oligopoly: All-out Competition and Strategic Commitment*, 29 RAND J. ECON. 306 (1998).

<sup>26</sup>For example, the New Jersey Supreme Court found that real estate closing fees were much lower in southern New Jersey, where lay settlements were commonplace, than in northern New Jersey, where lawyers conducted almost all settlements. Specifically, southern New Jersey buyers unrepresented by counsel paid no legal fees as a part of closing costs, while unrepresented sellers paid about \$90; southern New Jersey buyers represented by counsel throughout the entire transaction – including closing – paid on average \$650, while sellers paid \$350. This was in sharp contrast to northern New Jersey, where buyers and sellers represented by counsel paid on average \$1,000 and \$750, respectively. See *In re Op. No. 26 of the Comm. on the Unauthorized Practice of Law*, 654 A.2d 1344, 1349 (N.J. 1995). Additionally, in the course of rejecting a Kentucky Bar opinion that would have greatly restricted the ability of title companies to perform settlement services, the Supreme Court of Kentucky noted that

(continued...)



Finally, even if TREC's proposal were read in the manner stated by TREC – to allow LSBs to contract to provide only MLS listing as long as they were prepared to offer the required additional services – the proposed rule likely would have adverse competitive effects. The proposal would require LSBs who wish only to provide MLS listing services to incur additional costs associated with adding the capacity to provide the enumerated minimum services, thus eliminating as a viable business model limited-service brokerage that provided only MLS listing.

## **B. The Proposal is Unnecessary to Prevent Consumer Harm**

Given the benefits that consumers enjoy from competition, it is important to tailor regulations narrowly so that they restrain competition no more than is necessary to achieve their stated goal. Regulations that limit forms of competition may be beneficial when they address specific market failures that have been shown to harm consumers. Thus, in principle, a regulation could create net benefits for consumers if it were to result in an increase in the quality of brokerage not assured through competition and if consumers were willing to pay more for that increase in quality than they actually would pay in higher prices.

TREC's mission is "to assist and protect consumers of real estate services."<sup>27</sup> There is no evidence, however, that limited-service brokerage harms consumers. To the contrary, as explained above, competition between FSBs and LSBs is likely to benefit consumers. None of the reasons TREC provides to support the alleged need to adopt the proposed amendments appears to involve consumer harm, let alone require the reduction of competition from LSBs. Instead, less-restrictive measures that would preserve robust competition between FSBs and LSBs would likely be sufficient to ameliorate any of TREC's concerns.

TREC explained the need for mandating a minimum level of service for real estate brokerage in 2002 when it previously proposed nearly identical amendments:

[Limited-service brokerage] raises several concerns for brokers who represent buyers interested in properties listed under limited service agreements. Often times the seller does not understand the complexities of the transaction and relies upon the cooperating broker for assistance and advice. The seller is reluctant to approach the limited service broker for assistance at the risk of incurring significant additional fees; in some cases the

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<sup>26</sup>(...continued)

"before title companies emerged on the scene, [the Kentucky Bar Association's] members' rates for such services were significantly higher – in some areas as much as 1% of the loan amount plus additional fees." *Countrywide Home Loans, Inc. v. Kentucky Bar Ass'n*, 113 S.W.3d 105, 120 (Ky. 2003). Further, the court noted that "the presence of title companies encourages attorneys to work more cost-effectively." *Id.* Similarly, studies examining the economic effects of licensing requirements have shown them to increase the prices that consumers pay for services that are restricted to licensed individuals. See, e.g., Morris Kleiner & Robert Kurdrlle, *Does Regulation Affect Economic Outcomes? The Case of Dentistry*, 43 J.L. & ECON. 547 (2000); CAROLYN COX & SUSAN FOSTER, *THE COSTS AND BENEFITS OF OCCUPATIONAL REGULATION*, Federal Trade Commission (1990).

<sup>27</sup>See Mission Statement of the Texas Real Estate Commission, at <http://www.trec.state.tx.us/mission.asp>.

limited service broker will not provide the additional services. When the cooperating broker represents the buyer, the cooperating broker is uncomfortable about providing assistance or advice to the seller. Cooperating brokers also understand, however, that failing to provide the requested services to the seller may jeopardize the transaction or increase risks associated with the transaction.<sup>28</sup>

First, we are unaware of any instance where an LSB's conduct has caused consumer harm.<sup>29</sup> Indeed, a TREC commissioner has noted a concern with a "lack of complaints filed with the commission to justify promulgating a rule that would effectively put 'fee for service' brokers out of business."<sup>30</sup>

Second, competition between FSBs and LSBs should be sufficient to solve any problems that arise from LSBs imposing additional costs on buyers' agents. If clients of LSBs attempt to shift costs onto buyers' brokers or if transactions with clients of LSBs are more risky, buyers' brokers will be reluctant to show houses listed by LSBs.<sup>31</sup> Accordingly, LSBs' clients will have to offer buyers' brokers sufficient additional compensation to induce them to show their buyers houses subject to a limited-service listing.

Third, if TREC is concerned that home-sellers who have contracted with an LSB may mistakenly expect assistance from the buyer's broker, there appear to be less-restrictive measures to alleviate the perceived problem than reducing brokerage options for consumers. For example, TREC could require LSBs to disclose to their customers that buyers' brokers do not represent them and instead owe a fiduciary duty to the buyer. If, as TAR asserted when it first requested that TREC promulgate the current proposal, "[t]he rule is necessary to help avoid any confusion as to the services that a consumer may expect to receive from his or her broker and to help avoid any confusion between brokers who represent the parties in the transaction," requiring disclosure and consent appears sufficient to avoid "any confusion" on the part of a consumer or a buyer's

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<sup>28</sup>27 Tex. Reg. at 9256.

<sup>29</sup>We requested from TREC all complaints involving limited-service brokerage. We received three complaints arising from two transactions. Importantly, these complaints were filed *by an LSB against buyers' agents*. Further, the complaints concern the same LSB and buyers' agents, and in both cases are related to almost identical allegations of fraud on the seller surrounding the negotiation of the buyer's agent's commission. We also note that although the TAR Letter, *supra* note 19, stated that a "task force within the Texas Association of REALTORS has studied and debated issues related to this proposal and recommends clarification under the existing rule," nowhere in that letter nor in its comments to TREC on the current proposal does TAR cite to a single instance of consumer harm. *See* TAR Letter at 2.

<sup>30</sup>*See* Memorandum from Paul Jordan, TREC Commissioner to TREC Commission members (Nov. 21, 2003) ("Jordan Memorandum").

<sup>31</sup>Indeed, houses listed under a limited-service contract receive special designation in the MLS "as such listings can present special risks with regard to representation." *See* NTERIS, *supra* note 7, at § 7.01.

agent regarding what services an LSB will perform.<sup>32</sup> Indeed, the National Association of Realtors' Code of Ethics allows buyers' agents to deal directly with clients that are parties to exclusive agreements "with the consent of the client's agent or broker" or when "such dealings are initiated by the client."<sup>33</sup> As TREC Commissioner Paul Jordan has observed, "industry practice has long supported the 'contact the seller directly' model" as long as the buyer's agent has "consent of the seller's broker."<sup>34</sup>

Fourth, TREC also argues that the proposal is necessary to clarify an ambiguity in the existing regulatory scheme.<sup>35</sup> Specifically, under TEX. OCC. CODE ANN. § 1101.652(b)(22), TREC "may suspend or revoke" a broker's license or "take other disciplinary action" if a broker

negotiates or attempts to negotiate the sale, exchange, or lease of real property with an owner, landlord, buyer, or tenant with knowledge that the person is a party to an outstanding written contract that grants exclusive agency to another broker in connection with the transaction.<sup>36</sup>

Further, section 1101.652(b)(27) subjects a broker to the same penalties if he or she "aids, abets, or conspires with another person," to violate *inter alia* section 1101.652(b)(22).<sup>37</sup> In a limited-service contract, the LSB is likely to instruct other agents who represent potential buyers to negotiate the transaction directly with the seller.<sup>38</sup> TREC, however, contends that section 1101.652(b)(22) imposes a duty "to negotiate" on any broker who is a party to an exclusive agency relationship, which would mean that a buyer's agent who has any direct contact that is considered a "negotiation" with a seller who is party to a limited-service brokerage contract would be in violation of the statute. Further, LSBs who instruct buyers' agents to initiate contact with their clients that is considered a "negotiation" would be "aiding and abetting" such a

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<sup>32</sup>See TAR Letter at 1.

<sup>33</sup>CODE OF ETHICS AND STANDARDS OF PRACTICE OF THE NATIONAL ASSOCIATION OF REALTORS, Standard of Practice 16-13 (Jan. 1, 2005), at [http://www.realtor.org/mempolweb.nsf/214c1520b27c9ee286256b2600557d81/697f087a12502ea186256f710074e071/\\$FILE/2005%20Code%20of%20Ethics.pdf](http://www.realtor.org/mempolweb.nsf/214c1520b27c9ee286256b2600557d81/697f087a12502ea186256f710074e071/$FILE/2005%20Code%20of%20Ethics.pdf). The TREC proposal rejects this code provision and prohibits such direct dealings.

<sup>34</sup>Jordan Memorandum, *supra* note 30, at 2.

<sup>35</sup>See 30 Tex. Reg. at 1400-1401; Letter from Wayne Thornburn, TREC Administrator to Greg Abbott, Attorney General of Texas at 3-4 (June 8, 2004) ("Request Letter"), at [http://www.oag.state.tx.us/opinions/requests\\_ga/RQ0224GA.pdf](http://www.oag.state.tx.us/opinions/requests_ga/RQ0224GA.pdf); Abbott Opinion, *supra* note 14, at 3.

<sup>36</sup>TEX. OCC. CODE ANN. § 1101.652(b)(22).

<sup>37</sup>*Id.* at § 1101.652(b)(27).

<sup>38</sup>See 27 Tex. Reg. at 9256 (typically, LSBs "instruct[] the cooperating broker to contact the seller directly for all purposes (showings, presentations of offers, and negotiations)").

violation. Therefore, according to TREC, the proposed amendments are necessary to clarify exactly what the duty “to negotiate” entails.<sup>39</sup>

Clearing up any ambiguity that may exist in the current regulatory structure, however, does not require TREC to adopt a rule that would eliminate core limited-service brokerage arrangements in Texas. By using the term “may” in TEX. OCC. CODE ANN. § 1101.652(b), the Texas Legislature gave TREC discretion as to when a broker violates the terms of sections 1101.652(b)(22) or 1101.652(b)(27) and as to whether to take any action when a violation occurs.<sup>40</sup> Just as TREC’s proposal explicitly excludes delivering offers and counter-offers to a represented principal from the definition of “negotiate,” TREC also explicitly could exclude contact between a broker and a principal who has consented to deal directly with brokers from the definition of “negotiate.” Alternatively, in light of the discretion given it by the Texas legislature, TREC could clarify that a broker does not violate sections 1101.652(b)(22) or 1101.652(b)(27) when the principal in an exclusive agency contract has consented to deal directly with buyers’ brokers.

Finally, it is important to note that under TREC’s proposal, consumers who sell their houses on their own without listing them in the MLS will continue to be allowed to negotiate directly with buyers’ agents. TREC’s proposal would forbid only those consumers who wish to sell their houses on their own, but with the aid of an MLS listing, from negotiating directly with buyers’ agents. There appears to be no reasoned justification for a rule that treats these two classes of home-sellers differently. Both prefer to negotiate the sale of their houses on their own; those home-sellers who enter into “exclusive agency relationships” with LSBs do so because MLS rules require that such a relationship exist for a broker to list a house in the MLS.<sup>41</sup> An interpretation of 22 TEX. ADMIN. CODE § 535.2 and TEX. OCC. CODE ANN. § § 1101.652(b)(22), (27) based on duties owed under an agency relationship that prevents consumers from contracting with an LSB only to be listed on the MLS ignores the true nature of limited-service brokerage contracts. Given TREC’s discretion in determining when a broker violates sections 1101.652(b)(22) or 1101.652(b)(27), there is an alternative to the current proposal that would

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<sup>39</sup>As TREC notes, proponents of the rule argue that “because a licensee may not negotiate with a represented party under section 1101.652(b)(22), TREC rules should clarify what services the represented party may expect from their broker, and when the opposite side broker may deal directly with the represented party.” Request letter, *supra* note 35, at 3.

<sup>40</sup>*See Womack v. Berry*, 156 Tex. 44, 51 (Tex. 1956) (“The use of the permissive word ‘may’ imports the exercise of discretion”); *see also Wright v. Ector County Independent School*, 867 S.W.2d 863, 868 (Tex. App. El Paso 1993) (“The ordinary meaning of ‘shall’ or ‘must’ is of mandatory effect, while the ordinary meaning of ‘may’ is permissive.”). That the Texas Legislature chose to use “shall” in some sections of the TEX. OCC. CODE (e.g., section 1101.654, which requires action against a real estate broker engaged in the unauthorized practice of law) and “may” in others (e.g., TEX. OCC. CODE ANN. § 1101.652(b)) clearly demonstrates that the legislature intended TREC to have discretion with regard to whether to take action against a broker violating the terms of sections 1101.652(b)(22) or 1101.652(b)(27). *See Tri-Star Petroleum Company v. Tipperary Corporation*, 107 S.W.3d 607, 615 (Tex. App. El Paso 2003) (“We infer from the use of ‘shall’ in some sections of the TAA and ‘may’ in others that the Legislature intended different meanings to attach to these words.”).

<sup>41</sup>*See* note 14 and accompanying text, *supra*.

avoid an unnecessarily formalistic distinction between two identical classes of home-sellers and that would preserve competition from LSBs. That alternative is to clarify that when the principal in an exclusive agency contract has consented to deal directly with buyers' brokers, brokerage contracts do not trigger a duty "to negotiate," and do not implicate sections 1101.652(b)(22) or 1101.652(b)(27).

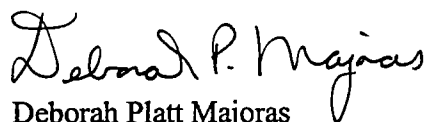
These suggested modifications to the proposal are not meant to be exhaustive but serve only to demonstrate that TREC can provide clarification to brokers as to whether they are in violation of sections 1101.652(b)(22) or 1101.652(b)(27) in a far less restrictive manner than currently is proposed. Such an approach would allow TREC to accomplish its goals and to spare Texas consumers the harm associated with the complete elimination of limited-service brokerage.


### Conclusion

Adopting the proposed changes to 22 TEX. ADMIN. CODE § 535.2 is likely to harm consumers by reducing competition between LSBs and FSBs without providing any countervailing benefits. Accordingly, we urge TREC not to adopt the proposed rule. If TREC nevertheless decides that it should take action to avoid confusion with regard to the role of buyers' agents or to clear up any ambiguity in the current regulatory scheme, we suggest that requiring disclosure to home-sellers or exempting LSBs from an obligation to negotiate in instances where a home-seller has consented to deal directly with buyers' agents are far less restrictive means to accomplish the same goals than completely eliminating certain limited-service brokerage options for Texas consumers.

Respectfully submitted,

By direction of the  
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