DOJ v. Realtors: Back in the Ring

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The question is not “will” but “when” will antitrust enforcers challenge any new real estate broker association rules prescribing how the brokers compete. The U.S. Department of Justice (“DOJ”) antitrust lawsuit against the Consolidated Multiple Listing Service (“CMLS”) is just the latest in the long-running battle between the real estate broker industry and the DOJ and U.S. Federal Trade Commission (“FTC”) over what if any limitations the industry can impose on competition by new business models made possible by the Internet.

THE MLS MEETS THE INTERNET

The development of Multiple Listing Services (“MLSs”) may have been the most significant development in the residential real estate market in the twentieth century. A joint venture among brokers, an MLS allows brokers to communicate to other brokers their listing information on homes their clients want to sell, obtain information on homes their clients may want to buy, and cooperate in other ways, including making arrangements to share commissions. By providing a mechanism to pool their listings on all or nearly all homes in a locality, an MLS increases the quality and lowers the cost of

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the services brokers provide to buyers and sellers of houses. These joint ventures are largely procompetitive and so valuable that participation in the local MLS is necessary for a broker to compete in almost any local market.

As it has for so many other industries, the Internet has revolutionized how Americans shop for homes. Since the MLS was conceived, the Internet more than anything has improved communication of listing information among brokers—and now directly to home buyers. Obtaining listing information once required an in-person visit with a broker, who could search the MLS “book” or later a brokers’ electronic database. Today brokers and broker associations can make the MLS database available immediately and efficiently to their clients. Brokers’ websites have become known as Virtual Office Websites (“VOWs”) because they make available all the services once found only in a broker’s office. VOWs now are present in many real estate markets, although not all. Beginning in the late 1990s, the introduction of VOWs has changed how Americans shop for homes, just as the Internet has changed how they shop for books, music, clothing, and even cars, insurance, and other products and services.

VOWs lower the cost of some of the services brokers provide and make possible new broker business models, creating new competitive distinctions among brokers. At one end of the spectrum is a broker that continues to offer the full range of services historically provided by brokers—all of the listing, marketing, showing, and closing services that clients might desire—in exchange for the traditional 6 percent commission (which in practice is about 5 percent). At the other end of the spectrum, a VOW-based
broker could offer more limited services at lower cost and lower price, for home sellers and buyers that wanted to handle some of the effort themselves. At this end is the “referral model” broker that uses its VOW to attract and educate home buyers and then refers buyers to brokers that provide on-the-ground services, in exchange for a referral fee.

Incumbent brokers responded to VOW entry in various ways. Some incumbents immediately embraced the new technology themselves, to face off against the new entrants. Others advocated that there be less cooperation among traditional brokers and the web-based entrants. Their arguments have raised a number of antitrust law and policy issues that still are being addressed by local broker associations, government agencies, and the public—and are making their ways through the courts. Some broker associations have imposed rules that limit the ability of VOW-based brokers to be members of a local broker association and its MLS or to have access to the MLS listing information. There now have been numerous actions challenging these rules by government antitrust authorities: the DOJ’s Antitrust Division, the FTC, and some state attorneys general. The CMLS case is only the latest in a series of antitrust agency enforcement actions against broker associations that have limited VOWs’ use of MLSs.

UNITED STATES V. NATIONAL ASSOCIATION OF REALTORS

The DOJ’s 2005 action against the VOW policy adopted by the National Association of Realtors (“NAR”) may be the most significant challenge to efforts to restrict VOWs use of MLSs. NAR is the organization of realtor associations nationwide,
and it has authority to establish rules for adoption by local associations and their MLSs. In May 2003, NAR formulated new rules that had the potential to limit VOW participation in MLSs. Under NAR’s “opt out” rule, any broker could cause the local MLS to withhold that broker’s listings from being displayed on a VOW or all VOWs. Before then, all brokers that were members of the MLS could provide any relevant listing in the MLS to customers by any delivery method (e.g., by hand, mail, fax, e-mail, or Internet).

In *U.S. v. NAR*, the DOJ characterized the NAR rule as a tool to thwart competition by VOW-based brokers. The DOJ alleged that a broker must be able to offer access to virtually all of the listings in the area to compete effectively, which could be frustrated even by the “opt out” of an incumbent with a small market share. The DOJ pointed to a particular case in which all of the competitors of one VOW-operating broker exercised an opt out, forcing the broker to abandon his website. The DOJ action also challenged NAR’s “anti-referral rule,” which precluded certain uses of the referral model, and other provisions of NAR’s VOW policy. The DOJ claimed that NAR’s policies discouraged price and quality competition and raised entry barriers, in violation of Section 1 of the Sherman Act.¹ The NAR case signaled the government’s intention to respond aggressively when it believes that incumbent brokers are engaged in efforts to

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control the use of Internet technology in their industry and limit cooperation with new entrants.²

NAR settled the DOJ challenge just weeks before trial was scheduled to begin in July 2008. The consent decree to which NAR has agreed to abide for ten years

1. forbids use of the opt out rule (allowing only individual sellers to decline Internet display of their home information) and

2. eliminates the anti-referral rule, but

3. allows a reasonable membership restrictions (discussed below).³

The NAR lawsuit is only one of a long string of antitrust actions brought by the DOJ, FTC, and private plaintiffs, challenging broker association rules on MLS access and other industry practices.⁴

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² NAR’s motion to dismiss the DOJ action was denied. Memorandum Op. and Order Denying Defendant’s Motion to Dismiss, United States v. Nat’l Ass’n of Realtors, 2006 WL 3434263 (N.D. Ill. Nov. 27, 2006), 2006-2 Trade Cas. (CCH) ¶ 75,499.


GOVERNMENT AND INDUSTRY ARGUMENTS

The government has addressed the broker association rules in the context of traditional antitrust joint venture law and claimed that they are horizontal restraints on trade that violate Section 1 of the Sherman Act. A joint venture among competitors may be procompetitive, joining the complementary resources of otherwise competing firms to provide products or services of greater value than the individual competitors independently could offer. It seems everyone agrees that an MLS is a procompetitive joint venture. Incidental restrictions on competition agreed to by the joint venturers may be lawful, if they are no broader than necessary to achieve the venture’s procompetitive benefits, or unlawful if they unnecessarily and unreasonably restrain trade.

As a general rule, a competitor association that has acquired market power by becoming essential to competing may not exclude competitors unless justified by the procompetitive needs of the association. The government often has pointed to Associated Press v. United States, which challenged Associated Press’s by-laws that allowed any member to veto a local competitor from joining, and in which the Court held that it was a restraint on trade for the association of competitors with market power to give each individual member the power to exclude a competitor from that association. In any particular case, the antitrust outcome of course turns on the facts, and courts have reached


5 United States v. Realty-Multi-List, Inc., 629 F.2d 1351, 1370 (5th Cir. 1980) (stating that “where a broker is excluded from a[n MLS] with the requisite market power without an adequate justification in the needs of the service, both the broker and the public are clearly harmed”).

6 Associated Press v. United States, 326 U.S. 1, 12 (1945) [hereinafter Associated Press].
varying decisions in challenges to association membership restrictions and other rules on how members compete.\footnote{E.g., Northwest Wholesale Stationers, Inc. v. Pacific Stationery and Printing Co., 472 U.S. 284, 296-97 (1985) (expulsion from cooperative not unlawful without showing of market power or anticompetitive effect); Associated Press, \textit{id.} at 12 (affirming judgment for government); United States v. Realty-Multi-List, Inc., 629 F.2d 1351, 1370 (5th Cir. 1980) (reversing summary judgment for defendant in challenge to MLS membership restrictions); Santana Prods., Inc. v. Bobrick Washroom Equip., Inc., 401 F.3d 123, 132 (3d Cir. 2005) (rejecting antitrust challenge to marketing campaign about competing product, where customers not prevented from buying product); Consolidated Metal Prods., Inc. v. American Petroleum Inst., 846 F.2d 284, 292-93 (5th Cir. 1988) (approving trade association decision not to certify particular manufacturing design, where that did not bar customer access to the product and no anticompetitive effect shown).}

In response to VOW entry and to enforcement actions, brokers have offered legal and policy arguments that the enforcement agencies largely have rejected, but not all of which have been addressed by the courts. A few are discussed here.

1. Collective v. Unilateral

Industry advocates have argued that the challenged association rules actually are not Sherman Act violations. In the NAR case, for example, the defendant argued that its membership rules did not constitute a Section 1 “restraint” because exercising the opt out authorized by the NAR policy was the choice of the individual incumbent broker. More generally, some brokers have argued that it should be lawful for a broker independently to decide not to deal with a newcomer that that broker believes is not contributing to the joint venture. In contrast, the DOJ viewed the NAR policy as a restraint imposed by agreement among the competing members of the broker associations. Even if the opt-out decision was independent, it was effective only because the collective policy allowed the
opt out to cause the MLSs to withhold some of the MLS benefits from particular members.8

The DOJ did not claim that the NAR policy was per se illegal, and therefore the parties would have had to litigate the rule of reason question of whether the rule actually restrained trade. The DOJ may have argued that the policy itself was anticompetitive because of a predicted tendency to disadvantage one type of competition. Of course the government would have sought to prove actual anticompetitive effects in particular markets where the policy had been implemented.

2. Free Riding

Another argument made by incumbent brokers is that VOW entrants are free riding on the investments incumbents have made in making the local MLS a valuable source of information for brokers. This argument has been most pointedly directed against referral-model brokers and to VOW-based brokers that open the MLS database to home shoppers through an attractive website, expect a commission in the event a shopper buys a house, but do not bring sellers with homes for sale to help “fill” the MLS. Joint venture law recognizes that exclusion may be justified if admitting a free-riding competitor would undercut incentives to join the venture and thereby ultimately harm consumers.

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8 The district court rejected the “not a restraint” argument, noting that “a group of market participants cannot immunize ‘arrangements or combinations designed to stifle competition … by adopting a [group] membership device accomplishing that purpose.’” Memorandum Op. and Order Denying Defendant’s Motion to Dismiss, United States v. Nat’l Ass’n of Realtors, 2006 WL 3434263 (N.D. Ill. Nov. 27, 2006), at *13, 2006-2 Trade Cas. (CCH) ¶ 75,499 (quoting Associated Press, supra note 6, at 19; modifications in original). In its response to the motion to dismiss, the DOJ explained that a Section 1 “restraint of trade” refers to restraints on competition, not restraints on competitors. Memorandum of the United States in Opposition to Defendant’s Motion to Dismiss, United States v. Nat’l Ass’n of Realtors (Feb. 6, 2006), at 16, available at http://www.usdoj.gov/atr/cases/f214500/214501.pdf.
The incumbents have asserted that admitting VOWs unjustifiably imposes costs on them and will lead to traditional brokers leaving their MLSs. The government’s cases suggest prosecutors would draw the line elsewhere. Broker associations are not entitled to dictate what technology new entrants use to compete or how they might divide various broker functions among different providers. In the government’s view, allowing VOW-based brokers to have full use of MLSs and to introduce new business models has not undercut competition by traditional brokers, nor caused incumbents to abandon MLSs. Just the opposite, the Internet has lowered the cost and increased the variety and value to consumers of the services brokers provide. The merits of these opposing factual arguments have yet to be litigated.

However, the DOJ implicitly has recognized that free-rider concerns may be addressed with reasonable membership restrictions. In its NAR settlement, the DOJ allowed NAR to limit MLS participation to persons actively involved in the real estate brokerage business. This may exclude enterprises that only operate an Internet portal (e.g., Yahoo!) or a business distantly related to residential real estate (e.g., Home Depot) and that want to attract customers by offering access to the MLS but are not actually in the brokerage business. By agreeing to this requirement, DOJ has signaled it may find some such limitations appropriate.

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9 An MLS participant “actively endeavors during the operation of its real estate business to list real property of the type listed on the MLS and/or to accept offers of cooperation and compensation made by listing brokers or agents in the MLS.” Proposed Final Judgment, Exhibit B, United States v. Nat’l Ass’n of Realtors (N.D. Ill. May 27, 2005), at 2.
3. Value of New Models

Another argument made by some in the brokerage industry is that some of the new business models made possible by VOWs do not bring significant value to consumers, suggesting they therefore are only adding “middleman” or intermediary costs to the industry. For example, some have argued that referral-model brokers do not bring new home listings into the market, but only detour shoppers through their VOWs to extract a commission, leaving the real work to brokers in the field. Similarly, some have pointed to the fact that today many traditional brokers offer clients Internet access to MLSs, suggesting that admitting tech-savvy VOWs now does not bring new benefits to justify the disruption of VOW business models.

These fact-based arguments have not been addressed by the courts. However, antitrust enforcers are likely to reject them. Prosecutors would argue that industry associations are not entitled to exclude new business models even if they arguably might be less valuable than traditional approaches. If a new entrant actually adds no value, the market will weed it out. Some brokers independently may refuse to cooperate with true free riders, and industry self-regulation is not needed here and creates risk of anticompetitive collective action. The DOJ also may believe that the threat of VOW competition has contributed to the rapid adoption of Internet technology even by traditional incumbents.
**UNITED STATES V. CONSOLIDATED MULTIPLE LISTING SERVICE**

In its most recent action, the DOJ has challenged the association rules adopted by Consolidated Multiple Listing Service, the association of brokers in the several counties around Columbia, South Carolina. Unlike an opt-out rule that limits VOW use of MLS listings, the challenged CMLS rules directly preclude some alternative business models.

CMLS has required that brokers provide a specified set of services, foreclosing the option of offering customers limited services or a menu of services at various prices. As described in the DOJ complaint, CMLS’s rules require that its members have “active involvement” in all aspects of the transaction, including “in the marketing, sale, and closing of the property.” CMLS’s brokers must use the association’s pre-approved contract and cannot alter the terms of their engagement. CMLS also has unfettered discretion over the admission and expulsion of broker members.\(^{10}\)

CMLS may have intended for its rules to address the concern expressed by some in the industry about “limited” or “inferior” service being offered to consumers who agree to a lower price but are unaware that they will not receive the full range of services traditionally provided by brokers. In response, the DOJ may contend that an industry association may not regulate what it regards inferior competition: the market will eliminate undesirable service, and fraud and consumer protection laws are available to protect customers who are wrongfully misled. According to the DOJ, these rules prevent broker business models from competing to offer fewer services:

CMLS’s Rules prevent members from providing a set of brokerage services that includes less than the full array of services that brokers traditionally have

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provided—even if a consumer prefers to save money by purchasing less than all of such services.\textsuperscript{11}

CMLS already has amended its rules in response to the DOJ challenge,\textsuperscript{12} although as of the publication date of this article, the nature of the amendments has not been announced. Nevertheless, given the government’s prior actions, there seems little prospect of the DOJ agreeing to a settlement that does not require that CMLS abandon its rules that limit competition by new business models.

The battle lines are drawn between the antitrust enforcers and the real estate brokers, and the CMLS case is just the latest skirmish. The brokerage industry so far has not succeeded in convincing prosecutors that industry self-regulation of new technology uses and new business models should be allowed. It was inevitable that the DOJ would view CMLS’s rules as antitrust violations, and there seems little chance of a resolution that does not require that CMLS abandon these restrictions.

\textsuperscript{11} \textit{Id.} at ¶4. The complaint in particular alleges that the rules preclude competition by “fee for service” and “exclusive agency listing” models. \textit{Id.} at ¶22-23. The complaint also notes that CMLS requires that members be primarily in the real estate business and have an office in the Columbia, South Carolina area. \textit{Id.} at ¶26(c).

\textsuperscript{12} \textit{Id.} at ¶27.