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PARTICIPATION IN PRIVATE MLSs/MLS CLUBS: Beware of the Legal Risks and Code of Ethics and MLS Rules Obligations

Background

In the age of the Internet and social networking, many REALTORS® have noticed the development of online private MLS groups. These are MLS-like clubs on Facebook or elsewhere that operate in the shadow of organized real estate's existing MLSs. Essentially, they establish a forum for "pocket listings." The private groups set up certain rules for membership and participation such as requiring that the listings submitted through the club be marketed exclusively to the club and kept off MLSs, that only select individuals can participate and that offers of compensation meet certain minimums. For the most part, the members of these private groups are simultaneously members of established MLSs who are also governed by their MLS's rules. They may also be REALTORS® governed by the Code of Ethics (COE). This paper will discuss the various MLS and COE rules implicated by participation in these private MLSs, as well as the legal concerns and risks.

Discussion

MLS Listing Requirements

In accordance with the C.A.R. Model MLS Rules, a broker participant is required to submit new listings located within the MLS service area into the MLS within 2 days after all necessary signatures of the seller have been obtained on the listing agreement or at the start date of the listing, whichever is later. (*Note: some local MLSs may have established different time frames). The mandate applies to exclusive right to sell or exclusive agency listings on one to four unit residential property and vacant lots.

The MLS Rules make an exception to mandatory submission only in the event the seller refuses to permit the listing to be disseminated by the service and signs a certification to that effect. Since any decision to forego the marketing opportunities of the MLS is supposed to be driven by the seller, the MLS takes the extra step of requiring the listing broker to provide evidence of the seller's instruction to keep the listing off the service. In instances where the seller refuses to allow the listing to be submitted, to avoid sanction by the MLS, a listing broker is required to submit a seller-signed exemption to the MLS within the same time period listing broker would otherwise be required to submit the listing. C.A.R. has drafted the SEL standard form to be used by sellers for this purpose. The SEL explains to sellers that an MLS exposes a seller's property to a broad audience of real estate brokers, agents and potential buyers so that a seller

has an opportunity to learn about the marketing potential the property will be missing by keeping the listing off the MLS.

If a seller opts to keep her property off the service, and the listing broker timely submits a C.A.R. SEL form or other certification signed by the seller stating that the seller does not authorize the listing to be disseminated by the MLS, listing broker can “pocket the listing” without violating MLS rules.

The MLS Mandatory Submission and related rules are set forth below:

7.5 Mandatory Submission. Broker Participants shall input exclusive right to sell or exclusive agency listings on one to four unit residential property and vacant lots located within the service area of the MLS within 2 days after all necessary signatures of the seller(s) have been obtained on the listing or at the start date of the listing, whichever is later. Only those listings that are within the service area of the MLS must be input. Open listings or listings of property located outside the MLS's service area (see section 7.7) are not required by the service, but may be input at the Broker Participant's option.

7.6 Exempted Listings. If the seller refuses to permit the listing to be disseminated by the service, the listing broker shall submit to the service a certification signed by the seller that the seller does not authorize the listing to be disseminated by the service.

7.7 Service Area. The MLS's service area shall be determined by the MLS Committee, subject to approval by the Board of Directors. If the A.O.R. has entered into regional MLS agreements or a regional MLS corporation with other MLSs and has enlarged the service area as part of the agreement or corporation, submission of the type of listings specified in section 7.5 is mandatory for the area covered by the combined service areas of the Associations signatory to the regional MLS agreement or part of the regional MLS corporation.

While a listing agent following the MLS rules set forth above can submit perfunctory seller exemptions to the service to be in technical compliance with MLS rules, analysis does not end there. Other problems persist.

Code of Ethics Requirements

Has a listing agent “pocketing” a listing truly obtained *informed* seller consent to market solely to a small, closed group of agents? MLS exposure offers a seller great benefits and maximum exposure to potential buyers. A listing agent desiring a pocket listing should be upfront about this tactic, and some sellers will still be fine with the limited listing exposure such a choice provides. Brokers who only place listings on a small, private MLS need to notify the seller that there will be limited exposure for their property because the private MLS only has a limited number of members. If the REALTOR® fails to make this full disclosure, he or she could be in violation of Article 1 that imposes a fiduciary duty on the REALTOR® to put their clients'

interests ahead of their own. Article 12 also requires a REALTOR® to provide a true picture in their “real estate communications” including marketing.

Legal Issues

The law imposes on an agent the overall fiduciary duty to act in the best interest of one’s client, in this case, the seller. Usually, a greater exposure to the market increases the likelihood of getting the highest price on the best terms for the seller because more prospects will know of the property’s availability and therefore more people will express an interest in or make an offer on the property. Theoretically, narrowing the band of buyer prospects by only marketing through a “private MLS” negatively affects the seller by reducing the pool of potential purchasers. Again, listing agents who will only be submitting the listing to a small, private MLS must provide full disclosure and get consent for this tactic. Not only is this duty owed to the client, it is crucial to remember that under the Business & Professions Code, sections 10176 and 10177, a licensee is subject to censure by the DRE and can lose his or her license for any fraud or dishonest dealing or even demonstrated negligence or incompetence in performing an act for which he or she is required to hold a license.

Participation in closed membership groups on the Internet or Facebook may also present additional legal problems. Depending on how they are structured and operate, private MLSs may pose antitrust concerns. The rules of some private MLS clubs require that that offers of compensation meet certain minimums. Fixing commission rates in this fashion is per se unlawful. A group of competitors assembling to fix commission rates acts in violation of antitrust laws, and those who participate are deemed complicit in the scheme. Additionally, depending on the make-up of any given market and the strength of the collective market share of those participating, a closed, exclusionary MLS which monopolizes a market area could potentially create other restraint of trade issues.

Take Aways

REALTORS® contemplating “pocket listings” or participation in private MLSs must honor their obligations and duties under MLS Rules, the Code of Ethics and the law. Make sure you have obtained informed consent from a seller after full disclosure of any marketing plan which will limit a listing’s exposure on the market. If not prepared to be transparent with a seller about such a plan, then don’t risk obtaining an ill-informed “consent.” Instead, submit the listing to the MLS.

Because many REALTORS® have expressed concern that it may be too easy to “pocket” a listing without sufficient measures in place to promote informed seller consent, a local MLSs so inclined may wish to engage in a public relations campaign, touting to sellers the benefits of having their listings submitted to the Service. This could be done in any number of mediums (ex: local newspaper, radio advertising, etc). Keep in mind that any measures in this regard should be clear of overreaching or disparagement.

Finally, avoid participation in exclusionary, private MLSs which fixes or regulates commission.