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The DOJ Asks: Does the Landmark Real-Estate Settlement Go Far Enough?

Justice Department might pursue additional changes to the costs associated with buying and selling a home

By Nicole Friedman Follow *and Laura Kusisto* Follow

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With the real-estate industry poised to abandon its longstanding commission structure next month, the Justice Department is signaling it isn't done scrutinizing how real-estate agents get paid.

The industry has battled many lawsuits alleging that the system for compensating agents keeps costs artificially high. It largely resolved these lawsuits in March with a sweeping settlement that will make it easier for home buyers to negotiate fees with their own agents and could lead more buyers to forgo agents altogether.

But federal enforcers' recent actions indicate they are still weighing whether the settlement goes far enough. If they decide it doesn't, they could pursue more substantial changes to the costs associated with buying and selling a home.

The Justice Department has intervened in two industry lawsuits and sent a formal inquiry to the California Association of Realtors, a large state trade association, about some legal forms it provides for agents to use during the home-sale process. It has also asked some real-estate companies about their rules governing listings.

The Justice Department has a long history of investigating the residential real-estate business. PHOTO: DAVID PAUL MORRIS/BLOOMBERG NEWS

At a meeting with the National Association of Realtors in late June, the department raised concerns that agents will attempt to circumvent the new rules, NAR President Kevin Sears said in a letter to the group's members.

“Clearly the DOJ is still very much involved in this,” said Gary Acosta, chief executive of the National Association of Hispanic Real Estate Professionals, who attended the meeting.

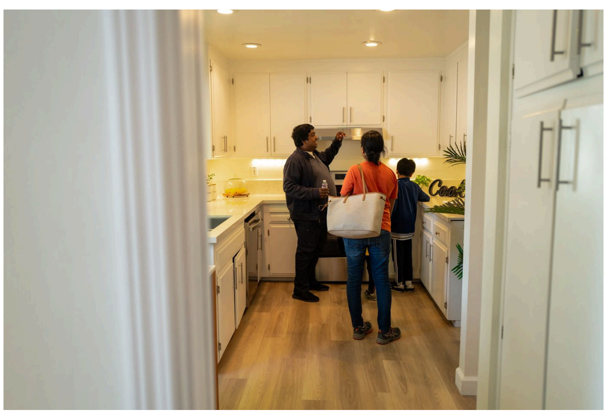
The new industry rules included in the NAR class-action settlement go into effect on Aug. 17, but the full settlement is not scheduled to receive final approval from a federal judge until November. That means the Justice Department has months to decide if it wants to formally object to the settlement and argue it won’t bring commissions down enough. That wouldn’t automatically negate the agreement, but a judge could tell the parties to go back to the negotiating table.

An attorney for the Justice Department said at a court hearing in another case in May that the department hadn’t yet decided whether to intervene in NAR’s settlement.

The Justice Department has a history of investigating the residential real-estate business dating to the 1940s, when a department lawsuit led the Supreme Court to declare that local real-estate associations’ mandatory fees were illegal.

A court order last year prevented the Justice Department from doing much to investigate the industry. Then in October, private plaintiffs received a historic $1.8 billion jury verdict in Kansas City, which empowered the plaintiffs’ attorneys to negotiate a nationwide settlement.

The agreement reached in March with NAR is expected to lead to the biggest upheaval in the process of buying and selling homes since the 1990s, when the current system was enacted.



The changes could lead to a 30% reduction in what Americans pay in real-estate commissions, analysts say. PHOTO: MANUEL ORBEGOZO FOR WSJ

The Justice Department got the green light in April to resume investigating NAR after a federal appeals court ruled that the department wasn’t bound by a previous settlement with the trade group. Now it has to decide whether to let the private plaintiffs’ settlement go into effect and see how the industry adapts or try to push for changes before then.

Roger Alford, a law professor at the University of Notre Dame who previously served at the Justice Department, said he thinks the department will likely want to take further action before the election in November.

"They want to lay down a marker that, 'This is a real concern for us,'" said Alford, who also testified as an expert witness for the plaintiffs.

Analysts at Keefe, Bruyette & Woods have predicted that the changes could lead to a 30% reduction in the $100 billion that Americans pay in real-estate commissions every year. The typical commission—5% to 6% of the purchase price, split between the seller's agent and the buyer's agent—is among the highest in the world.

Starting next month, many sellers will no longer include offers to compensate buyers' agents when listing homes in local databases known as multiple-listing services. Buyers will also be required to sign contracts with their agents, which plaintiffs' attorneys and consumer advocates expect will lead to more negotiation between buyers and agents and reduce the 2.5% to 3% buyer's agent commission that is now common.

Consumer advocates and some industry participants, however, have raised alarms that some agents will try to preserve the current commission system.

For example, while sellers won't be able to make offers to compensate buyers' agents in multiple-listing services, they could still make those offers on social media or elsewhere. Critics of the settlement warn that sellers' agents could still pressure sellers to offer similar rates to before by warning that buyers will avoid their properties if they don't.

The full settlement is not scheduled to receive final approval until November. PHOTO: DAVID RYDER/BLOOMBERG NEWS

NAR's president urged the group's 1.5 million members to avoid exploiting any potential loopholes.

"NAR—and I personally—oppose any attempts to circumvent the settlement," Sears said in a letter to members. "We expect the DOJ to continue making inquiries into industry practices."

Agents could also seek workarounds by using confusing or misleading legal forms, said Stephen Brobeck, a senior fellow at the Consumer Federation of America. State Realtor associations often provide forms for formalizing client relationships or managing home sales that are widely used by agents.

The Justice Department sent an inquiry to the California Association of Realtors about proposed changes to its forms, the association said last month. The Consumer Federation had previously sent the Justice Department an analysis critiquing some of the forms, Brobeck said.

“I am not optimistic that the state associations are going to come out with any form that is fair to consumers,” Brobeck said.

The California Association of Realtors said that the Consumer Federation’s critiques are misguided and based on early drafts of its forms. The association released revised forms last week.

The Justice Department has opposed a proposed settlement in a separate lawsuit against a multiple-listing service in Massachusetts. The judge has paused the case until a final decision is made on NAR’s national settlement.

In a hearing in that lawsuit in May, a Justice Department attorney said the NAR settlement was an improvement from the current system but doesn’t go as far as the department would like.

The Justice Department also filed a brief in recent weeks in a continuing lawsuit involving Rex, a low-cost startup, over an industry rule that made it difficult for home buyers to find the firm’s listings on Zillow. The rule is optional but had been adopted in many markets, and the Justice Department said in its filing that it appeared to have had suppressed competition.

Rex lost at trial, but the case is on appeal. The Justice Department encouraged the appellate judges to order a new trial.

The department has sent inquiries in recent months to multiple-listing services about this rule, according to people familiar with the matter.

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