Kansas Association of REALTORS® Presents

Required Salesperson & Broker Core: Misrepresentation & Agency

REALTOR® Continuing Education

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KANSAS ASSOCIATION

OF

REALTORS®

3644 SW Burlingame Road

Topeka KS 66611-2098

Phone: 800-366-0069

ext. 2129 or ext. 2131

Locally: 785-267-3610

ext. 2129 or ext. 2131

Fax: 785-267-1867

www.KansasRealtorEducation.com

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Misrepresentation & Agency

This course has been approved by the Kansas Real Estate Commission for 4 hours of continuing education credit. This course also meets the common mandatory core requirements for both Salespersons and Brokers that began on January 1, 2000. Brokers have an additional 4-hour mandatory core requirement that may be selected.

This course counts as required hours for Brokers and Salespersons under Kansas law.

The Author – Vernon L. Jarboe has over 30 years' experience in real estate matters handling development issues, land use, zoning and financing of small and major projects. Vernon also represents many local boards of REALTORS® through form review, advising on legal issues, including antitrust and ethics issues. Litigation experience includes representing landowners and condemning authorities in eminent domain matters, real estate brokers and salespersons in liability matters and collecting commissions. Vernon has continually manned the Real Estate Legal Hotline since its inception in 1998. The Legal Hotline serves participating REALTORS® statewide.

Vern can be contacted at:

Vernon L. Jarboe, Attorney
Sloan Law Firm
534 Kansas Avenue, Suite 1000
Topeka, Kansas 66603

vjarboe@sloanlawfirm.com
Office: 785-357-6311
Mobile: 785-640-0970
sloanlawfirm.com

This course is provided by the Kansas Association of REALTORS® and they offer the continuing education credit.

This course is composed of four (4) components:

1. A narrative discussion of agency under current Kansas law in the real estate business. You need to read the narrative before proceeding.
2. Class discussion over an expanded version the materials covered by the narrative, including questions over the quiz responses.
3. Resolution of fact patterns in small group and class discussion.
4. You will receive an email from KEYNOTE PROFESSIONAL DEVELOPMENT SERIES that will contain the link to the online exam for each class after all the classes have completed. This exam will need to be completed within 48 hours of the class. Upon successful completion of the online exam, be sure to click the "finish" button and that will take you to the screen to fill out the information for your certificate. Once you create the certificate, the system will email it to you, KREC and KAR.

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TOPICAL OUTLINE OF PART 1 -- THE NARRATIVE PORTION:

I. BROKERAGE RELATIONSHIPS IN REAL ESTATE TRANSACTIONS ACT (BRRETA)

A. AGENCY

1. **How to start and end the relationship**
2. **What responsibilities do you have as an agent**
3. **What do you need in your written agreement**
4. **What is a transaction broker – its duties and differences**

II. MISREPRESENTATION

A. FRAUD

1. **Active fraud**
2. **Passive fraud**

B. NEGLIGENT MISREPRESENTATION

C. BROKER LIABILITY AND AVOIDANCE

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BROKERAGE RELATIONSHIPS IN REAL ESTATE TRANSACTIONS ACT (BRRETA)

This law was passed in 1997, after extensive study by the Kansas Real Estate Commission (KREC) through a committee of brokers, large and small, urban and rural, commercial, residential and agricultural, along with one citizen not in the business and one real estate attorney.

Why was this study done?

Prior to the study a national survey revealed that more than half of all buyers and sellers believed that the real estate licensee involved in their transaction worked for the buyer. This is despite the fact that almost all the real estate licensees believed they worked for the seller. As a matter of law the licensees were correct and the consumers wrong. This disconnect led to the need for clarification of the relationship.

Prior to this study Kansas, among other states, had court decisions that were inconsistent with licensee expectations. A late 1970's decision in Kansas resulted in the court deciding a licensee had become a buyer agent by agreeing to help a buyer (unsuccessfully) acquire a property that had not even been on the market. Some months later when the licensee listed that same property and sold it immediately, but not to the buyer who originally called, the court found it to be a breach of buyer agency duties. The licensee was incensed – he had not had a written agreement with the buyer and the buyer had never agreed to pay him – but he lost, none the less. The court found common law agency rules to prevail in the real estate business and under the common law - agency relations can arise by implication and do not need a written agreement.

The common law is case based legal precedent originating in British law. It basically provides that agency arises when one person retains another to do a job, may include an implied obligation to pay for services and does not always require a written agreement.

BRRETA, therefore, was a response to the lack of understanding among consumers, gave licensees a road map to legal activities and was an effort to better define the relationship with consumers for licensees.

AGENCY

Buyer and seller agency under BRRETA requires a written agreement. Absent a written agreement the law implies a transaction brokerage relationship to exist. Therefore, if you are working with a consumer as a buyer or seller and have not yet entered into a written agreement you are working as a transaction broker. It is also possible to be a transaction broker by entering into an agreement with a buyer or seller that defines your role as that of transaction broker. Finally, one also becomes a transaction broker by specific agreement, in writing, where a conflict has arisen and the broker/salesperson has an existing agency relation with both buyer and seller in the same transaction.

How to start and end the relationship?

Agency begins with a written agreement between the licensee and a consumer who is referred to as a "*client.*" Transaction brokerage may begin simply by providing real estate services without a written agreement or it may begin with a written agreement with the consumer who is referred to as a "*customer.*" These relationships end when they expire due to passing an end date defined in the written agreement, when a transaction closes or when the parties, that means the licensee and consumer, reach a written agreement to terminate the relationship. The duties of accounting for money and confidentiality survive termination of the relationship.

What responsibilities do you have as an agent?

Your first duty is to perform the terms of your written agreement. Obviously, that necessarily means you must know the terms and conditions of your agreement with your client. It is important to know the description of duties in your agreement. The second duty is to promote the interest of your client with the utmost good faith, loyalty and fidelity. It is therefore important to remember that the interests of your client come before the interests of third parties and, in fact, before your own interests.

What are the duties of a broker or salesperson regardless of agency relationship?

Whether acting as an agent of either buyer or seller or simply working as a transaction broker with any consumer, brokers and salespeople have the duty to:

- Present all offers in a timely manner
- Disclose all adverse material facts known about a property
- Advise consumers to get qualified third party opinions
- Account for consumer money and property in your possession
- Comply with other federal and state laws
- Keep confidential information confidential

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These duties are collectively the duties described by law.

The duty to present offers in a timely manner leaves a lot to interpretation. However, if you provide enough definition to the circumstances most people can agree on what "timely" means. The result is different if you or your consumer are incommunicado due to illness or physical inaccessibility. The result is different if you and your client have electronic communication and are "in range."

The duty of accounting means that when consumer property is in your possession you have a duty to reasonably protect it and to turn it over to the consumer. This may be as simple as protecting them from theft at an open house, depositing earnest money as required or making them aware of information you have that makes their real estate worth more than they realize.

The duty to disclose known adverse material facts is significantly different from the old rule of disclosing all you "knew or should have known," but it definitely does not permit you to keep defects in the property a secret whether you learn them from the seller, observation, a previous inspection, neighbor or any other means. This includes a duty to disclose omission or inconsistencies in qualified third party inspections – but that does not mean you should substitute your judgment for theirs.

The duty to suggest the use of a qualified third party does not mean picking the inspector but does not prohibit you from suggesting one or more options. It basically means you need to tell the consumer there are significant property condition situations that neither they nor you are expert enough to judge and they should consult with someone you reasonably believe competent for the services for which they are retained.

Compliance with federal and state law refers to the myriad of other regulatory laws impacting real estate. These include federal, state and local fair housing rules, City Ordinances, Real Estate Settlement and Procedures Act (RESPA), Truth in Lending, Americans with Disabilities Act (ADA), etc.

Confidential information by definition means information made confidential by some law or rule or personal information about a consumer that is private and if disclosed to the other consumer in the transaction would place the one about whom the information relates at a disadvantage.

What do you need in your written agreement?

By law the agency agreement needs to "set forth the terms and conditions of the relationship." Specifically required are a fixed expiration date, any limitations on duties of confidentiality, compensation terms as well as all duties described by law. (above-described)

What is Transaction Brokerage?

Sometimes one consumer lists their home with a company and another consumer thinking of buying a property works with that same company. It may be true that both the buyer and seller have selected the same licensee with that one company. If both consumers are working with their respective licensee as transaction brokers then there is no conflict.

If, however, one or both of them are working with their respective licensees as an agent then a conflict arises. Kansas law does not (some other states do) allow dual agency – the same licensee or company representing both sides to the same transaction.

What is Designated Agency?

Kansas law does allow something that will permit two licensees within the same company to represent both sides of one transaction. This is called designated agency. Designated buyer agency means that one licensee in the company represents the buyer to the exclusion of all other licensees (including the broker) in the company. The other licensees then are transaction brokers as to the consumer (buyer in this case) unless they have a competing agreement. If another licensee in the same company has a designated seller agency agreement (also meaning that licensee represents the interests of the seller to exclusion of all other licensees in the company) on the property the consumer is interested in then that is permitted – ***IF*** *both the listing agreement and buyer agency agreement indicate this possibility (designated agency on both sides) may arise.*

Designated agency is created by agreement with the consumer and appointment by the broker or broker designee – all in writing. There can be only one designated agent (or team) for a single consumer. When agents work together as a "team" obligations on one designated agent apply equally to all who are so listed as designated agents. It is possible to become a designated agent mid-transaction, if that becomes in the interest of the consumers and the proper written documentation for the relationship exists.

Many companies in Kansas take all listing and buyer agreements as designated agency to facilitate this arrangement. In these circumstances it is very important to remember the duty of "utmost good faith, loyalty and fidelity" to your client and the duty to preserve confidences – even at the water cooler.

What is a transaction broker – its duties and differences?

By definition, a transaction broker is a licensee who assists a consumer with a real estate transaction without being an agent or advocate for the interests of any consumer in the transaction. It is often then referred to as a position of neutrality – working for the transaction but not for either buyer or seller's interests.

Note: all the duties "described by law" apply equally to buyer agency, seller agency, designated buyer and seller agency and to transaction brokerage.

What duties are not owed by real estate licensees?

The law specifically says there is no duty to do an independent inspection of the property. Therefore, you need to avoid becoming an "expert" by opining on subjects that qualified third parties should be hired to opine on. You also have no duty to go behind what the qualified third party offers for an opinion – again do not second guess the expert.

What things are allowed to both agents and to transaction brokers?

It would be difficult to make a living in real estate one listing or one buyer at a time. Therefore, the law specifically says it is not a violation of the duty of "utmost good faith, loyalty and fidelity" to work with more than one seller or more than one buyer at a time – even if their interests directly conflict – so long as it is not on opposite sides of the same transaction.

The law permits compensation to and cooperation with other brokers even if they are on the opposite side of the transaction. The law also carves out a list of "ministerial acts" – such things as attending an open house, answering phone inquiries and making referrals without implying any form of agency or transaction brokerage relation.

MISREPRESENTATION

This means a licensee either discloses false information about a property or fails to disclose accurate information known to the licensee. It is one of the most common causes of litigation against licensees and one of the most common complaints to KREC about licensees. Historically, 75% of all litigation against licensees was based on misrepresentation. Among the things you can do wrong in the eyes of KREC, only stealing your client's money or lying in advertising hold a candle to their opinion of licensees who lie to their customers or clients.

FRAUD – if you are lying and you know it – clap your hands. That would be active fraud.

What is Active Fraud?

Active fraud is the act of knowing the truth and telling something else. It is very commonly believed that this is what all licensees do to sell houses. Consumers usually start off believing that the licensee knew the truth and lied. The good news is not many cases are proven. The bad news is active fraud can lead to not only paying to fix the problem but punitive damages. When the jury assesses punitive damages they can look at financial statements and tax returns to see how much pain should be applied to "teach the lesson".

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What is Passive Fraud?

Passive fraud is the affirmative act of knowing the truth but simply not telling. The best Kansas example is a case where there were two termite inspections. One says "yes, there are" and the other "no, there aren't" termites. The broker and seller decided to reveal only the "no, there aren't" version and of course the "yes, there are " report was correct. The intentional nondisclosure of something you know the buyer would want to know is passive fraud.

NEGLIGENT MISREPRESENTATION

Negligent misrepresentation is the act of lying but not knowing it when you should have known better. Negligence occurs whenever you are performing some duty in a way that impinges on the rights of others. Following too closely in your car and rear ending someone is an example of negligent driving. Not driving as well as you should and causing loss to someone else. In its simplest form negligent misrepresentation then is making a disclosure without enough information to have made the disclosure. If you are following the law – disclosing what you know and suggesting the use of qualified third parties for inspection you will not likely be guilty of this offense.

BROKER LIABILITY AND AVOIDANCE

Good notes and records

Keep in mind each transaction is for you (hopefully) one of many each year but for the consumer is the only one for years. Therefore, they hang on everything you say and every inference from what you say. It is important to develop strategies to make sure you give the same good service every time and document that you do. Think about how to record what you say when showing, when suggesting the use of a qualified third party or explaining the terms of a contract. Do it the same way every time – use an outline if you need to – or let written materials do your talking.

How do you document the unusual question or fact that comes up in a transaction? How do you prove you told someone something or that you gave them some piece of information? Remember if you are on the witness stand, for you it will be one of the dozen transactions from two years ago, but for the consumer the only one. If you want to be persuasive have notes on what you said and did – on the cover of the file, an email to yourself, an email to the consumer, a fax to the other licensee in the transaction, etc. The jury is more likely to believe the witness who says, "I have no memory of what happened two years ago but let me refresh my recollection by looking at my notes." than the one who says, " I recall perfectly what was said (or not said) two years ago."

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Seller and buyer expectations can be controlled with education. Few transactions or properties are perfect. In fact, no properties are perfect – some transactions may be. If you help the consumer understand the issues that may come up, you will look all the more expert, even when warning them of "bad stuff." Most homes will eventually have termites and no inspection known can always find them. Don't lull the consumer into false reassurance with "Don't worry about them -- we will get an inspection." when you know the inspector will at best say, "I did not see any – in the places I looked -- and oh by the way, I did not look everywhere."

Possible default issues by either side can be described, planned for and minimized with education. The consumer needs to know delays sometimes happen due to things outside anyone's control, and sometimes the other side does not do what they agreed in writing to do. That IS why we have contracts, but contracts do not assure we can MAKE anyone do anything.

Available inspections and what they do and do not prove should be explained. Almost anything a consumer might be concerned about and many things they did not know to be concerned about can be inspected for. On the other hand, every professional inspection has its limits. You know what they are – inform the consumer so their expectations match reality.

What are the pros and cons of seller disclosure statements and what they do and do not prove? These forms are not required in Kansas – although they are in many other states. They are not a perfect device because a seller may have owned a property for such a short time that the specific problem may never have arisen. The forms are good for buyers, sellers and licensees to preserve in writing what was disclosed at the time of contract negotiation.

It is important to hire an attorney when you are outside the scope of your experience in counseling the consumer. Classic situations include:

- *The other side is in default – what now?*
- *What risk is there if I do not do what I promised to do?*
- *Some contract language is needed for the weird deal.*

You need to watch out for red flags. These are conditions that do not look correct. It may be something the seller shows or tells you that doesn't sound or look right, something an inspector says in a report that you have never seen written up that way or just a condition at the property that would bother you if you owned it. These are the conditions that come back to bite you later if you do not point them out to the consumers.

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Errors and Omissions (E&O), aka malpractice insurance is not required in Kansas, although it is for many other states. In those states you cannot get or renew a real estate license without first proving you have insurance. It is generally acquired by the broker to cover the broker, the business and all licensees affiliated with that firm.

Most E&O insurance is written on a Claims made vs. occurrence basis. Your car insurance coverage is occurrence based – you have to have insurance in force on the date of the loss to have coverage. Claims made insurance covers you for claims made during the period of the coverage. Therefore, if you mess up while you have insurance but drop your coverage (nonpayment, retire or change to a company without coverage) before the claim is filed you may have no coverage. There are solutions but you need to talk to your insurance professional.

Deductibles for E&O policies may not cover attorney fees. This means that you have to pay the attorney who defends you even if there is ultimately no loss. It is important to let the carrier know of a pending claim as soon as you know about it. Failure to notify the carrier and let them try to defend the case may invalidate your coverage for the loss that otherwise would have been covered. If you are going to settle a claim that seems small compared with your deductible, invest a few dollars getting a properly prepared release so you don't have a consumer asking for a small sum you pay only to come back later for a little more and then later for a little more – you get the idea. If you are going to settle – get it resolved—in writing.

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