Kansas Association of REALTORS® Presents

Legal Environment of the Real Estate Professional

REALTOR® Continuing Education

By Vernon L. Jarboe

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OF

REALTORS®

3644 SW Burlingame Road

Topeka KS 66611-2098

Phone: 800-366-0069

ext. 2129 or 2120

Locally: 785-267-3610

ext. 2129 or 2120

Fax: 785-267-1867

www.KansasRealtorEducation.com

Home Study

QUICK STUDY

E-Mail Material

The content of this class includes questions about the law and applies law to fact patterns. Neither the printed material nor discussion should be mistaken for **THE LAW,** which often turns on very narrow points and slim factual distinctions. Actual problems and remedies require the expertise of a **REAL ESTATE ATTORNEY.** It is important to know the difference between your problem and a client or customer problem. Customer and client legal problems must be referred to competent counsel. You should not provide answers to these problems. **Legal Hotline** members should call the Hotline and non-members should consider signing up.

This course was approved by the Kansas Real Estate Commission for four elective hours.

Quick Study Legal Environment for Real Estate: Part 1

This course counts as an elective class for Brokers Salespersons under Kansas law

About the Author – **Vernon L. Jarboe**, **J.D,; L.L.M.; REALTOR® ; Broker**
has over 35 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® with form review, advising on legal issues, including antitrust and ethics issues. His litigation experience includes representing landowners and condemning authorities in eminent domain matters, real estate brokers and salespersons in liability matters and collecting commissions. He also represents REALTORS® in defense of regulatory complaints before the Kansas Real Estate Commission (KREC). Vern has continually manned the Real Estate Hotline since its inception in 1998. The Hotline serves participating REALTORS® statewide.

Vern can be contacted at:
Vernon L. Jarboe, Attorney vjarboe@sloanlawfirm.com
Sloan Law Firm Office: 785-357-6311
534 Kansas Avenue, Suite 1000 Mobile: 785-640-0970
Topeka, Kansas 66603 sloanlawfirm.com

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

This course is composed of four (4) components:

1. A narrative discussion of issues impacting licensees under current Kansas law in the real estate business. You need to read the narrative before proceeding.
2. Class discussion over an expanded version of the materials covered by the narrative, including questions over the quiz responses.
3. Resolution of fact patterns in small group and class discussion.
4. There is an open book quiz over the narrative material in Part 1 and 2. This can be completed at the end of the group discussions or taken with you and faxed to KAR at 785- 267-1867 within 10 days of the class.

COURSE OUTLINE

- Introduction to Fair Housing
- Contract issues
- Land use regulation
- Zoning
- Antitrust

Legal Disclaimer:
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- Introduction to Fair Housing

One could argue that the first fair housing act was passed in the aftermath of the Civil War. The Civil Rights act of 1866 forbid discrimination in contracts on the basis of Race. However, the effectiveness of that law was dissipated by court interpretations that lessened its impact and created segregated housing, schools, restrooms, lunch counters, etc. The country changed and the law changed with it, especially as people of all kinds participated in the great European wars in the first half of the 20th Century.

Brown vs. Topeka Board of Education

This Supreme Court decision in 1954 created a complete reversal in the law from decisions made in the latter part of the 19th Century with the judicial pronouncement that "separate cannot be equal". Not all parts of the US were ready for this change. Peaceful and not so peaceful reactions to this decision over the ensuing decade ultimately led to the Civil Rights act of 1964 and Fair Housing Act of 1966. The Fair Housing act forbids discrimination on the basis of race, color, religion and national origin. The act was amended in 1974 to forbid housing discrimination on the basis of sex and again in 1988 to forbid discrimination on the basis of handicap and familial status.

The "protected class" designation means that discrimination between people when based on membership in one of these classes violates the law. This does not make all discrimination illegal. For example – discrimination on the basis of profession would be legal and a REALTOR® could, therefore, refuse to show houses to an attorney.

PROHIBITIONS - IF DISCRIMINATION IS BASED ON MEMBERSHIP IN PROTECTED CLASS

- Refusal to sell, deal or negotiate with a person on the basis of their membership in a protected class violates the law. So refusing to show a buyer homes because they are of a particular race is illegal but refusing because they have a personality you don't like is fine. Obviously, if all the people you don't like are of a different race that could be a problem.
- Offering different terms in sale or lease to different persons that are members of different classes is illegal. For example: charging someone to repaint an apartment when the walls are marked up by their children is fine if you also do that when you have adults that mark up the walls with picture hanging, posters stuck to the wall and the like.
- Advertising property available only to certain groups – would be illegal even if you could get the newspaper to run the ad. This will only become more problematic as more advertising goes to online sources where there is no editor in charge of the "publisher".
- Denying housing available when it is available is one of the more common violations. It is viewed as the classic dodge to violations of law by those who think they will not be discovered. A person who advertises property as available suddenly says it is not available when the mixed race couple applies is likely to be viewed as committing this violation.
- Lending institutions violate fair housing law by denying or making different loan terms based on an applicant's membership in a protected class.
- A broker or group of brokers violate fair housing law by refusing real estate services to persons based on their membership in a protected class. This could be a broker denying agency services to an individual or a group of brokers denying membership in the board to another licensee if those denials were based on membership in a protected class.
- Steering is the affirmative act of directing buyers to or away from a property or neighborhood based on their membership in a protected class. This could

include taking someone to an ethnic neighborhood because the licensee "assumes" the buyer will want to live with their own "kind" or responding to a request from a buyer to take them to an ethnic neighborhood that they want. It is ok to take a buyer to a particular neighborhood where the buyer selects the neighborhood even if you suspect the buyer is "steering" themselves just not ok for you to steer them.

- Blockbusting is the act of trying to encourage sales in a neighborhood through fear of changes to come with a new ethnic group moving in.

PENALTIES FOR VIOLATING FAIR HOUSING LAW

- Actual damages

You are sued for the losses the discriminated against person suffers as a result of your actions. This might include a more expensive choice they must take by virtue of your actions, but even more expensive, if you lose, are the payments you could owe the person for emotional pain and suffering.

- Civil penalty

This is a penalty that is imposed by the government and the money goes to the government. Unlike traffic fines the numbers are larger – starting at $10,000 for first offenses.

- Punitive damages

These damages are assessed where the actions are deemed so bad that a lesson to both the wrongdoer and others who know of the violation needs to be taught. The penalty is measured by the ability of the wrongdoer to pay so a jury might get your tax return and financial statement to figure out how much money it will take to teach you the lesson you need to learn.

- Injunctive relief

Judicial relief that includes an order to do or stop doing something is referred to as an injunction. In this instance the court order might include a requirement that an entire real estate firm take classes from HUD on fair housing issues or mandate advertising in a particular ethnic newspaper.

- Licensee discipline

The Kansas Real Estate Commission has the right to impose discipline for fair housing violations. This could include a fine, suspension or revocation of a license.

- State fair housing law

Kansas has fair housing laws. The protected classes, prohibitions and violations will look much like the federal law. If you violate state law, you will likely violate federal law, and vice versa.

EQUAL PROFESSIONAL SERVICE

- Use a systematic procedure
- Ask yourself if you have objective information
- Ask yourself if your customer has set the limits
- Then offer a variety of choices

CONTRACT ISSUES

- Making a contract

Understanding when you have a contract and when you don't is important even though the ultimate decision on that issue is not yours and should be referred to independent legal counsel. Selling the same house to a second buyer when the first buyer has a contract or thinks she has a contract is among the worst things you can do. Sometimes parties have created contract expectations where the seller doesn't think a contract exists, or believe they know they created a condition which has failed to the point of voiding the contract. Make sure you counsel the seller appropriately and where there is risk refer them to their attorney or at least suggest they go and – remember to create a record of that suggestion.

  - Offer – where one party makes an offer in sufficient completeness that it can be accepted by the other. In real estate that includes at least knowing the parties, property, price, closing date and a signature. Today this all may have occurred by email.

  - Acceptance – where the receiving party indicates all the important terms are agreed to. Remember to accept - it is "yes" and not "yes but . . ." or "yes and . . .", or "yes except . . ." – all of which imply a counter offer. A counter offer is really a different form of "no".

- Consideration – means there is something of value flowing each way in the deal. In real estate this means money from the buyer and property from the seller.

- In writing – statute of frauds – this is a piece of old English Common Law codified by legislative enactment in Kansas indicating that when it comes to real estate then parties are bound only by written agreement. However, that written agreement requirement can be pretty loose if there is some type of writing, partial performance by the parties or other action deemed to override this need.

- One interesting, but as yet unanswered question, may be "can we make a contract by email" – not a scanned document emailed but simply emails between buyer and seller that have parties, price, property, closing and "signed?".

EARNEST MONEY

Earnest money is designed to be a statement of the buyer's good faith and bona fides. In the typical Kansas house transaction it really does very little toward that end because it is so nominal in the context of either the buyer's ability to pay or the seller's risk of loss in the event of default.

- Earnest money is not required to make a contract binding. The lack of earnest money is often felt to be a lack of commitment by the buyer simply because it is so common. The oft stated "all contracts require consideration," while a true statement, does not have anything to do with the earnest money – which is just part of the overall price to be paid and hence part of the "consideration" paid by the buyer for the seller's deed.
- In some cases the buyer makes a deposit of earnest money prior to contract acceptance in order to prove bona fides either where they are leaving town before acceptance or the offer is low or otherwise not one the seller is likely to approve. This can be done and does not create a problem if the seller never approves the contract because the prohibition on release of earnest money without the approval of both parties only comes into existence "after contract acceptance" so in the event seller does not agree to the contract – then the buyer's earnest money can be released on demand by the buyer.

- Promissory notes and non-cash deposits are acceptable forms of earnest money so long as the contract clearly indicates to the seller that the buyer is not providing cash (a check that is dated currently is cash but a postdated check is really a form of a promissory note).
- Some contracts provide that the earnest money is to be held by the seller. It is relatively common where a new custom home is being built by the seller and the builder is concerned about the buyer bailing out on closing where the house is not particularly marketable to other buyers due to peculiar tastes in design or finish work of the custom buyer. This practice is acceptable – again so long as the contract says so – buyer has some risks. What if the deal fails and buyer should get the money back and the seller doesn't have the money or refuses to pay? What if the seller/builder files bankruptcy?
- Withdrawal of earnest money that has been deposited with an escrow agent, including a broker's trust account, requires some formality:
  - Closing will result in release either to the closer as part of the proceeds or sometimes to the listing broker as part of the commission.
  - Consent of both parties to release earnest money to one of them or to be split or to be applied to transactional expenses - where the contract has been cancelled due to default by buyer or seller will result in release of earnest money.
  - Court orders may be obtained to instruct the escrow agent to release the money to one of the parties after the court determines a default and to whom the money should pass. Small claims court can be used where the amount of money is small enough to fit under the small claims limit. In small claims court the party wanting the money sues the other party and the escrow agent.
  - Kansas has a statute to allow release of earnest money held by a broker if there is a demand by one party for the money and certified mail notice of intent to release the money is sent. K.S.A. 58-3061(h):

> "Notwithstanding any other terms of this contract providing for forfeiture or refund of the earnest money deposit, the parties understand that the applicable Kansas real estate laws prohibit the escrow agent from distributing the earnest money, once deposited, without the consent of all parties to his agreement. Buyer and seller agree that failure by either to respond in writing to a certified letter from broker within seven days of receipt thereof or failure to make written demand for return or

> forfeiture of an earnest money deposit within 30 days of notice of cancellation of this agreement shall constitute consent to distribution of the earnest money as suggested in any such certified letter or as demanded by the other party herto."

SPECIAL KINDS OF CONTRACTS

Options – are contracts that give a buyer the right to acquire a seller's property if the buyer chooses to buy but does not require them to buy. Options are commonly used in development deals where the buyer does not want to buy unless neighboring property is acquired, where a buyer has purchased part of what a seller owns or buyer is trying to get a particular tenant signed up but the buyer needs a commitment from the seller to sell if the buyer wants or needs to close.

First right of refusal – do not commit the seller to selling but obligate the seller to ask the buyer before selling property to any one else. These, too, are commonly used where a seller has acquired part of what a seller owns and wants to buy more but seller does not want to sell more land at the current time. These are sometimes used by tenants who want the landlord to offer property to the tenant before selling it to anyone else.

Seller financed transactions – which are sometimes known as contract for deed, purchasing under contract or installment sale transactions are all forms of the same thing. Another variety of this transaction includes the lease option agreement where buyer is tenant and part of the payment applies to purchase. In some instances the seller actually deeds the property to buyer and takes a mortgage for the unpaid portion of the price but in most cases the deed to buyer is held in escrow and an escrow agent keeps track of the buyer's attentiveness to making payments, paying taxes, keeping the property insured and delivers a deed on final payment. Sellers in these forms need to know that the escrow agent is really serving only an accounting function and not a collection agent function – the escrow agent has no duty to pester the buyer, sue the buyer or even decide the seller should sue the buyer. The seller is acting as a banker and needs to do those things for themselves. In the event of default – no matter what type of default it is – failure to pay, failure to pay taxes, keep the place insured or maintain the property will all require the seller to hire an attorney and to foreclose – unless the buyer just gives a quitclaim deed and walks.

LAND USE REGULATIONS

- Zoning refers to Public (state, local, city and or county) rules, regulating the use of land. There are regulations dealing with use of land near airports, in flood zones, that has had lead paint applied, or where there has been other environmental contamination all of which are outside what is normally considered zoning.
- Where a local government wishes to regulate land uses one thing they do is adopt a zoning map. Typically this map is available online and depicts each parcel of land in the governmental jurisdiction by color, cross hatch or otherwise segregates each use type with some designation.

Zoning regulations are the rules that apply to each use type. The regulations show what uses are allowed in each district, provides height, mass, parking, and minimum setbacks from front, side and back yard that are required. Interpretation of these regulations is very technical and when customers or clients have questions it is best if they are referred to the local government for interpretation. If REALTORS® attempt to interpret or even serves as intermediary between consumer and the government there is much risk of misinterpretation or bad message handling.

- If someone owns a piece of land and finds the zoning regulations applicable do not match the owner's desire then the owner can file for an amendment to the zoning map. It is the application of the regulations to the map which create the restriction. Sometimes buyers make closing contingent on such a zoning change being approved before closing to ensure they get to what they want after closing.

- Variances can also be requested from the application of the rules. Variances are normally granted only where the owner did not intentionally create a violation but where technical application of the rules imposes an unfair hardship on the owner. Typical situations for a variance are where the lot is oddly shaped and it becomes difficult to build on the lot. It is more difficult if the owner builds something first and asks for permission later.

- Conditional use permits are granted where a use is limited in time or restricted to the current owner. These are often used to allow an industrial uses like rock quarries in an otherwise agricultural area for a limited period

of time and subject to restrictions such as: where trucks exit the property, when blasting operations can occur and reclamation requirements.

- Grandfathered uses arise when zoning rules change and there was a use already in place. Because zoning rules arose mostly after 1940 in Kansas there were many cases where a use existed before zoning. The old neighborhood grocery is the best example. This has also occurred where zoning rules were extended out into the county after land use rules had been in existence inside a city for a long time and then get extended out into the country. The idea is that the existing use should not be outlawed when it was there first.

- Declarations of restrictions, covenants and deed restrictions are private as opposed to public rules regulating the use of land. Because they are private the government does not enforce these rules, rather, they are enforced by private law suits between parties based on the contract. These are typically imposed by someone who owns a larger tract and sells part off. It may be as simple as the owner of 80 acres selling 40 and wanting to control how the part being sold is used or as complicated as the developer of a condominium complex selling "cubes of airspace" and obligating the purchasers of a cube to help pay the expenses of operating all the cubes and dictating how to be a nice neighbor in the use of common and partly common spaces. Evaluating how neighborhood restrictions apply, if they apply, whether they are enforceable or whether a buyer can do what they want to do should be referred to an attorney.

- Antitrust

The Sherman Antitrust Act was passed in the late 1800's to restrict conglomerations of businesses to the point where competition was not occurring and consumers damaged.

Sherman prohibits contracts, combination or conspiracy in restraint of trade. This means that a single business cannot violate Sherman because it requires two or more actors to create a contract, a combination or conspiracy. A single broker can set prices, policies and contract requirements for his firm.
Price agreements between two or more brokers who should be competing with each other on price would violate Sherman. Sherman also prohibits an allocation

of customers or territory such as where brokers in neighboring counties agree not to compete with each other. Also prohibited are boycotts or refusal to deal where two brokers agree not to show the listings of a third broker that they don't like.

- Risks in the real estate industry with respect to Sherman Act violations include alleged price fixing and attempts to interfere with competition by agreements between brokers.
- In what other industry do you sell your competitors inventory? This forces brokers who are also competitors to talk to each other and gives opportunity for violations.
- Negotiation over price and terms for listings should be with clients not competitors. An agreement not to charge less than a certain amount or not to take listings for less than ___ days would violate Sherman.
- The penalties for violation of Sherman include treble damages (in other words the loss created by the violation times 3 and jail. So in addition to getting sued and losing your license it adds the risk of going to prison.

DEFENSES

- Avoid incriminating situations – like a board meeting where commissions are being discussed.
- Do not make disparaging comments about competitors that sound like there is some agreement that the competitor is not abiding by.
- Do not defend commission rates as standard when we know they are not all the same. It is tempting to say "the board has a rule" when negotiating commission with a seller rather than just saying "I am worth it".
- As always the best defense is to understand and follow the law.