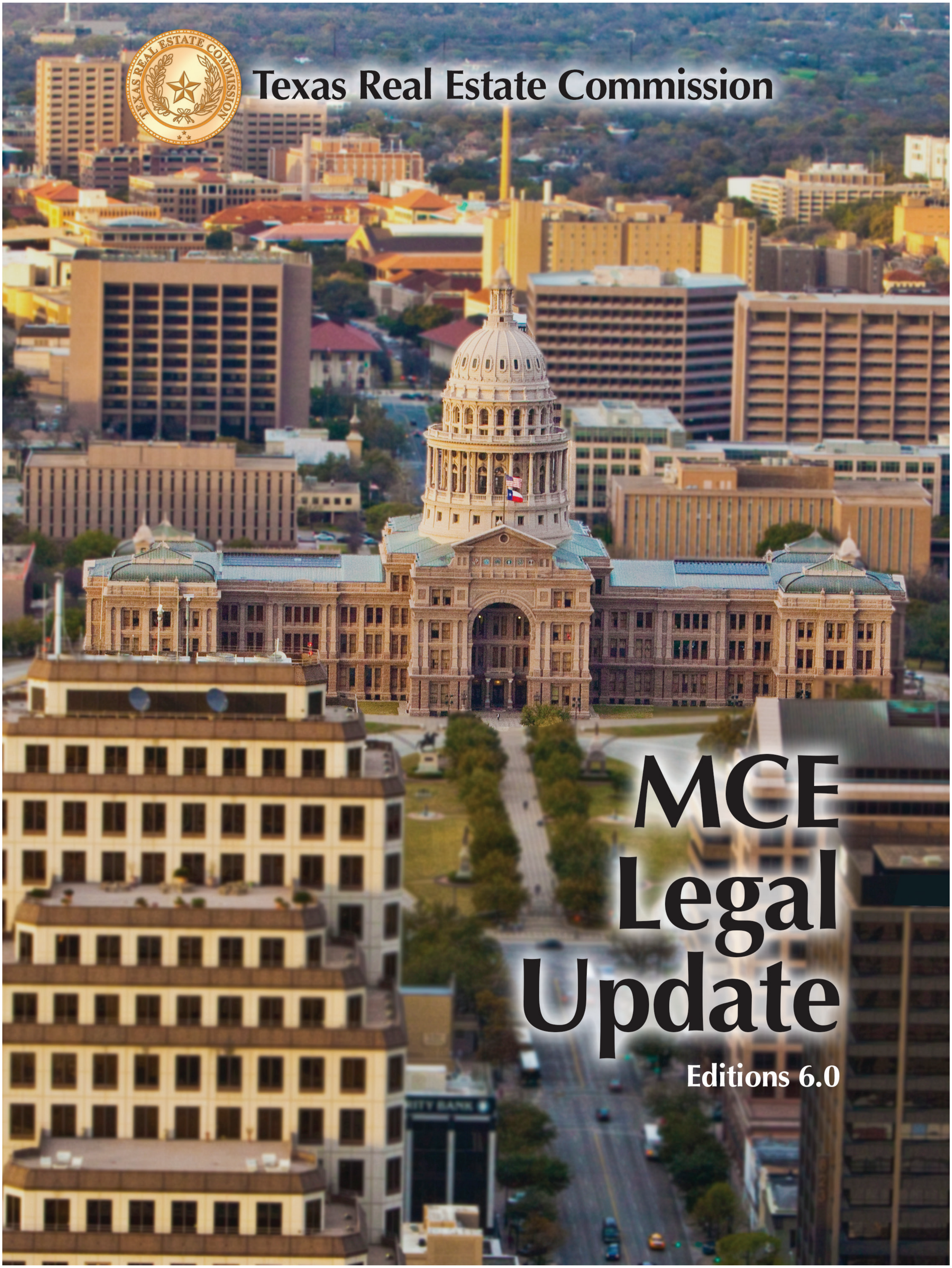

Texas Real Estate Commission

MCE Legal Update

Editions 6.0

Acknowledgments

Real Estate Center Staff

Gary W. Maler, Director
David S. Jones, Communications Director
Robert P. Beals II, Art Director
Denise Whisenant, Education Coordinator

MCE Writing Group

Loretta Dehay
Kerrie Lewis
Lori Levy
Charles Jacobus
Philip Schoewe
Justin Switzer
Ron Walker
Avis Wukasch

Texas Real Estate Commission

Douglas Oldmixon, Administrator
Avis Wukasch, Chair
Bill Jones, Vice Chair
Joanne Justice, Secretary
Troy C. Alley, Jr.
Adrian A. Arriaga
Jaime Blevins Hensley
Weston Martinez
Thomas (TJ) Turner
Chart H. Westcott

Real Estate Center Advisory Committee

Mario A. Arriaga, Chair
Kimberly A. Shambley, Vice Chair
James M. Boyd
Russell L. Cain
Jacquelyn K. Hawkins
Walter F. (Ted) Nelson
Stephen D. (Doug) Roberts
Ronald C. Wakefield
C. Clark Welder
Avis Wukasch, Ex-officio

Foreword

In cooperation with the Texas Real Estate Commission, the Real Estate Center at Texas A&M University developed this real estate legal update curriculum with the assistance of an advisory committee of active licensees, attorneys and education providers. Real estate licensees are encouraged to acquire additional information and to take courses in specific, applicable topics.

This curriculum has been developed using information from publications, presentations and general research. The information is believed to be reliable, but it cannot be guaranteed insofar as it is applied to any particular individual or situation. The laws discussed in this curriculum have been excerpted, summarized or abbreviated. For a complete understanding and discussion, consult a full version of any pertinent law. This curriculum contains information that can change periodically. This curriculum is presented with the understanding that the authors and instructors are not engaged in rendering legal, accounting or other professional advice. The services of a competent professional with suitable expertise should be sought.

The authors, presenters, advisory committee, Real Estate Center and Texas Real Estate Commission disclaim any liability, loss or risk personal or otherwise, incurred as a consequence directly or indirectly from the use and application of any of the information contained in these materials or the teaching lectures and media presentations given in connection with these materials.

When using this course for three hours of Legal Update MCE credit as required by the Texas Real Estate Commission, this textbook must be reproduced and used in its entirety, without omission or alteration.

Contents


EQUAL JUSTICE UNDER LAW

Chapter 1

Legislative Changes

SB 985 – Authorizing Broker Agreements for the Sale of Real Property by Certain Municipalities

Senate Bill 985 adds §253.014 to the Local Government Code to permit a home rule city to contract with a licensed broker to sell real property owned by the city. Generally speaking, a home rule city is one with a population exceeding 5,000, which has adopted a home rule charter. Prior to this change, these cities were required to sell property under an open bid or auction process. The city may now list the property with the broker who will place the listing in a multiple listing service for at least 30 days.

HB 3038 – Auctioning Real Estate

House Bill 3038 amends Chapter 1802 of the Texas Occupations Code Chapter regarding the licensing of auctioneers. The purpose of the bill was to update Chapter 1802, especially with respect to consumer protections against unscrupulous practices in sales made through auction transactions, including sealed bids.

One of the provisions (Sec. 1802.051(a)) was amended to state that a person may not act as an auctioneer of real or personal property in this state unless the person holds an auctioneer's license. The Real Estate License Act (TRELA) has, for many decades, provided that a real estate broker may auction real estate. Longstanding interpretations harmonizing this provision of TRELA with the licensing requirement in Chapter 1802 recognize that while an auctioneer's license under Chapter 1802 is required for a person to call an auction, a broker or salesperson license is required for a person who handles other facets of the transaction such as negotiating the contract, showing the property, or other activity which typically requires a real estate license. This harmony should remain unchanged as both Acts permit their respective licensees to sell real property under an action (oral or by sealed bid). Both Acts provide for enforcement action in the event of unscrupulous activity.

Previously, Chapter 1802 provided that individuals licensed as auctioneers could act only for an entity that was owned by a licensed auctioneer or that held a dealer number under the Transportation Code. The bill now permits the individual auctioneer to also act for an entity that is a real estate brokerage firm under TRELA. This change permits the broker and auctioneer to provide the full complement of services related to selling and auctioning real property.

It is possible that the Texas Real Estate Commission (TREC) and the Texas Department of Licensing and Regulation (TDLR) may need to adopt clarifying rules in light of the statutory changes.

HB 2075 – Texas Uniform Condominium Act (Chapter 82 Property Code

Borrowing Money

There were a number of changes made to the Texas Uniform Condominium Act. One authorizes the condominium association, by resolution of the board of directors, to borrow money and assign as collateral for the loan

- the association's right to future income, including the right to receive assessments; and
- the association's lien rights.

If the declaration requires a vote of members of the association to borrow money, the loan must be approved as provided for in the declaration. If a lower percentage is not provided by the dedicatory instrument, approval requires the consent of owners holding 67 percent of all the voting interests.

Insurance Coverage

A condominium association's insurance policies may provide for commercially reasonable deductibles as the board determines appropriate or necessary. If any portion of the condominium for which insurance is required is damaged or destroyed, it shall be promptly repaired or replaced by the association unless the condominium is terminated or 80 percent of the unit owners vote not to rebuild. Each unit owner may vote, regardless of whether the owner's unit or limited common elements have been damaged or destroyed. The board may levy an assessment to pay for the expenses in accordance with each owner's common expense liability.

If the cost to repair damage to a unit or common elements covered by the association's insurance is less than the amount of the applicable insurance deductible, the party who would be responsible for the repair in the absence of the insurance shall pay the cost of the repair of the unit or common elements.

If the association's insurance provides coverage for the loss, and the cost to repair the damage is more than the applicable deductible, the dedicatory instruments determine who pays the deductible. If the dedicatory instruments are silent as to who pays, the board of directors of the association, by resolution, shall determine the payment of those costs. If the board does not approve a resolution, the costs are a common expense. If the damage is due wholly or partly to a unit owner or a guest of the unit owner, the association may assess the deductible and other expenses in excess of the insurance proceeds against the owner and the owner's unit.

New Foreclosure Sale Rules

If the association's lien for assessments is foreclosed, the unit owner has the right to repurchase (redeem) the unit within 90 days of the foreclosure sale. If the association is the purchaser, the owner must pay all amounts due to the association at the time of the foreclosure sale in order to redeem, including

- interest from the date of the foreclosure sale to the date of redemption, as provided in the declaration for delinquent assessments; and
- reasonable attorney fees and costs incurred by the association in foreclosing the lien.

If a party other than the association is the purchaser, the redeeming owner must pay to that purchaser of the unit,

- the amount equal to the amount bid at the foreclosure sale,
- interest on that amount at the rate of six percent,
- any assessments paid to the purchaser after the date of the foreclosure, and
- any reasonable costs incurred by the purchaser as the owner of the unit including the cost of maintenance and leasing.

The redeeming owner must also pay to the association all assessments that are due as of the date of the redemption, including reasonable attorney fees incurred by the association in foreclosing the lien.

Property Owner Associations

HB 35 – Use of Adjacent Lot (effective immediately)

House Bill 35 adds §209.015 to the Property Code. A home owners associations (HOA) cannot prohibit or restrict an owner's use of a lot that, if it is for residential purposes, is adjacent to the lot where the owner's residence is located. Any rule doing so is void. The HOA may place reasonable restrictions on architectural or aesthetic criteria, which would require the owner to obtain HOA approval before the owner begins construction.

If an owner elects to use an adjacent lot for residential purposes, the lot must be included as part of the property or as sale of the adjacent residence, or it must be restored to its original state so that a new residence can be built. An owner can sell the adjacent lot separately only for the purpose of constructing a new residence in compliance with existing HOA requirements unless the lot has been restored to its original state.

"Adjacent lot" is essentially defined as a contiguous lot. "Residential purposes" is generally defined as a building or structure "customarily appurtenant to a residence" and includes a garage, driveway, water well, utility line, children's playscape, fence, swimming pool, etc., that is contiguous to the lot either on the side property line or the back property line.

HB 680 – Flagpoles (effective immediately)

House Bill 680 amends §§202.001 and 202.011 of the Property Code. An HOA may regulate the size, number and location of flags. The regulation does not prevent the installation of at least one flagpole per property that is

- no more than 20 feet in height and is in the front yard (subject to zoning, easements and setbacks); or
- is attached to the residential structure.

SB 198 – Drought-Resistant Landscaping (effective September 1, 2013)

Senate Bill 198 amends §202.007 of the Property Code. An HOA cannot prohibit or restrict (through a dedicatory instrument) a property owner from using drought-resistant landscaping or water-conserving turf. It does not prohibit an HOA from requiring an owner to submit a detailed plan for the landscaping to the HOA for review and approval. The HOA may not unreasonably deny or withhold approval of the plan or unreasonably determine that the plan does not have "aesthetic compatibility." The terms "drought resistant" and "water-conserving turf" are not defined in this bill.

SB 1372 – Timeshare Act Amendments

Senate Bill 1372 establishes the Timeshare Owners Association Act under chapter 221 of the Property Code. Timeshare owners associations are exempt from the provisions mandated by the Homeowners Association Act found in Chapter 209 of the Texas Property Code. This bill provides a parallel set of applicable provisions to the governance of timeshare owners associations.

SB 2911 – Real Estate Inspectors

House Bill 2911 amends Chapter 1102 of the Texas Occupations Code (TOC). The bill contains provisions related to the professionalism of Texas real estate inspectors and adopts practices related to inspectors to match those used by other TREC licensees. The bill requires inspectors to undergo fingerprinting and a criminal history check. It also adopts a late renewal provision for inspectors, grants applicants a year to complete the application process, and contains language that enables TREC to better communicate with inspectors. The bill also clarifies that an inspector seeking to reinstate a license under §1102.110 must complete the current continuing education requirements before reinstatement and requires some hands-on training before an inspector may begin actual field inspections. Finally, the bill allows TREC to accept a bond as an alternative to E&O coverage for the licensing of inspectors. This alternative will allow inspectors to lawfully continue to work if the market ceases to provide E&O coverage for inspectors.

HB 585 – Appraiser Disclosure Requirements Before an ARB

House Bill 585 amends current law relating to ad valorem taxation, especially the provisions of the Tax Code dealing with tax protests before an Appraisal Review Board (ARB). While the majority of the bill has no impact on the regulation of real estate appraisers, one section of the bill requires that a licensed or certified appraiser appearing before the ARB must state the capacity under which he or she is appearing.

HB 2532 – Propane Distribution Retailer Disclosure

House Bill 2532 amends the Utilities Code to establish standards for propane distribution system retailers. In relevant part, the bill requires distribution system retailers to provide certain disclosures and to record certain documents in the county real property records in which the distribution system retailer owns or operates a propane gas system. The bill also establishes notice requirements for a homeowner who proposes to sell or convey real property located in a propane gas system service area owned by such a retailer. The notice required by the bill is required to be provided by a seller "at or before the execution of a binding contract for the purchase of the real property described in the notice or at closing of purchase of the real property." While the effective date of the bill is September 1, 2013, the recording required of a distribution system retailer must be completed not later January 1, 2014, or the 90th day after the date a distribution system retailer completes construction of a new propane gas system in the county.

Chapter 2

Regulatory Changes

New Broker License Requirements

In addition to the new four-year experience requirement, TREC recently enacted new rules to establish experience requirements to qualify for a broker's license. For a broker's license application filed after January 1, 2012, active experience is measured by a combination of active licensure and transactional experience over the four-year period. An applicant must accrue a total of 3,600 points for transactional experience for four out of five years, using a point system detailed in the rule, or be able to complete the time and transaction requirements within the one-year period after the broker's application is filed. The application must have the signature of the applicant's sponsoring broker or brokers for the relevant time periods. The applicant must complete

- one transaction in each year of the four years in which the applicant is claiming experience, and
- accrue a total of 3,600 points
  - the sale of single-family residential home = 300 points
  - a closed purchase or sale of an apartment complex of five or more units = 450 points
  - listing or buyer representation agreements = 10 points each
  - an executed lease for a residential or commercial property = 50 points

Transaction Document Verification

While the applicant is not required to include copies of the transaction documents with the broker application, the documents must be provided to TREC upon request. An applicant who is a member of a team may not claim experience for the transaction work done by the team unless the applicant is listed in the documentation as an agent for one of the parties.

Affidavit in Lieu of Documentation

If an applicant is unable to obtain the appropriate documentation or signature of the sponsoring broker, the applicant must submit the following:

- a TREC Affidavit in Lieu of Documentation and/or Signature to describe the applicant's efforts to obtain the signatures, and
- two TREC Affidavits in Support of Claimed Experience.

Each Affidavit must be signed by a different person familiar with the applicant's circumstances and attest to the applicant's efforts to obtain the documents or signature.

Licensees Buying, Selling and Leasing Property for Themselves

Under TRELA §1101.652(a)(3), licensees may not engage in misrepresentation, dishonesty or fraud when buying, selling or leasing property in their own name or in the name of a spouse, parent, or child. Recent amendments to §535.144 of the TREC Rules clarify that under §1101.652(a)(3), a licensee acting in his or her own name or in the name of spouse, parent, or child also includes a licensee acting in the name of a trust of which the licensee is the trustee or of which the licensee or the licensee's spouse, parent, or child is a beneficiary. The Rules now clarify that TREC has jurisdiction under §1101.652(a)(3) to take disciplinary action against a licensee engaging in a real estate transaction in the name of

- the licensee;
- a business entity in which the licensee is more than a 10 percent owner;
- the licensee's spouse, parent or child; or
- a trust for which the licensee is the trustee or of which the licensee or the licensee's spouse, parent, or child is a beneficiary.

Further, the amendments clarify that a licensee engaging in a real estate transaction in the name of a trust is obligated to provide the same written disclosure regarding licensure that is required when the license holder is acting in the name of a family member or a business entity in which the licensee is more than a 10 percent owner.

Broker Price Opinions or Comparative Market Analyses

The TREC Housekeeping Bill in 2011, SB 747, amended TRELA to remove "appraisal of real property" from the definition of real estate brokerage. The bill also added a new definition of real estate brokerage to include providing "a written analysis, opinion, or conclusion relating to the estimated price of real property if the analysis, opinion, or conclusion is

- not referred to as an appraisal;
- provided in the ordinary course of the person's business; and
- related to the actual or potential management, acquisition, disposition or encumbrance of an interest in real property.

The Texas Appraiser Licensing and Certification Board (TALCB) Housekeeping Bill, HB 2375, removed the exemption for appraiser licensing for a real estate licensee and added new definition of a "Broker Price Opinion" (BPO) to mirror the definition in TRELA added by SB 747 as described above. Thus, real estate licensees may no longer conduct an "appraisal" or "opinion of value" of real property. They may continue to do BPOs or Comparative Market Analyses (CMA) as long as they comply with the requirements added by SB 747 (not referred to as an appraisal) and the BPOs and CMAs are

- provided in the ordinary course of business; and
- related to the actual or potential management, acquisition, disposition or encumbrance of an interest in real property.

To clarify the new TRELA requirements, TREC amended §535.16 (Listings; Net Listings) and §535.17 (Broker Price Opinion or Comparative Market Analysis) to replace any references to "opinion of value" with "broker price opinion" or "comparative market analysis." Section 535.16, which has been in place for at least 15 years, requires real estate licensees to provide a broker price opinion or comparative market analysis on a property when negotiating a listing or when purchasing property for their own account that they learned of while acting as an agent. In addition, the recent amendments clarify that a real estate licensee may not perform an appraisal of real property unless the licensee is licensed or certified under Texas Occupations Code, Chapter 1103. The amendments to §535.17 require real estate licensees to give a USPAP disclosure in all cases where a BPO or CMA is provided. The previous version of the rule only required licensees to give the disclosure if the BPO was provided for a separate fee.

To summarize, the term "appraisal" and phrase "opinion of value" was removed from wherever they were referenced in the TREC rules. Real estate licensees may no long "appraise" real property (or give an opinion of value) if they are not licensed under Chapter 1103 of the Texas Occupations Code, and real estate licensees must give a written USPAP disclosure whenever they complete a BPO or CMA.

Final Mortgage Rules/CFPB

The Dodd-Frank Wall Street Reform and Consumer Protection Act of 2010 established the Consumer Financial Protection Bureau (CFPB) whose stated mission is to make markets for consumer financial products and services work for Americans, whether they are applying for a mortgage, choosing among credit cards, or using a number of other consumer financial products. Congress established the CFPB to protect the consumer by writing rules, supervising companies, taking consumer complaints, and monitoring financial markets for new risks to consumers.

On January 10, 2013, the CFPB issued three final rules setting out significant new standards for mortgage underwriting and escrow requirements. The final rules address

- standards on "ability-to-repay" and "qualified mortgages" (QM Rule),
- changes in Home Ownership and Equity Protection Act (HOEPA), and
- escrow account requirements for higher-priced mortgage loans.

The QM Rule applies to consumer credit transactions, which are secured by a dwelling and are other than

- home equity lines of credit,
- mortgages secured by timeshare plan interests,
- reverse mortgages, or
- temporary or bridge loans with terms of 12 months or less.

A residential mortgage lender is prohibited from making mortgage loans unless it has made a reasonable, good faith determination that the borrower has a reasonable ability to repay. The lender must take into account

- the borrower's income and assets,
- current employment status,
- loan payments,
- payments for mortgage-related obligations (insurance, tax, etc.) and other debt obligations,
- alimony and child support,
- monthly debt-to-income ratio or residual income, and
- the applicant's credit history.

If the lenders do not comply with all these rules, they are subject to fines.

The standard mortgages must have terms of 30 or fewer years, a fixed-rate interest rate for at least five years after consummation; points and fees are generally kept at three percent. They must also have periodic payments that do not result in an increase to the principle balance, deferral of principal repayments or billing payments. Borrowers may have no more than one payment that is 30 days delinquent in the 12 months before applying for the standard loan (and none in the six months before applying).

The borrower's income, assets, debt obligations, alimony and child support must be verified, and the borrower's debt-to-income ratio cannot exceed 43 percent at the time of consummation of the mortgage.

Another issue is compliance. Some smaller banks and smaller lending institutions might not be able to afford the compliance requirements, and they could very well be out of the home mortgage business altogether. This could increase the cost of mortgages over the long term.

New Appraisal Requirements

Six federal financial regulatory agencies issued their final rule that establishes new appraisal requirements for "higher-priced mortgage loans." They include amendments to the Truth and Lending Act made by the Dodd-Frank Wall Street Reform and the Consumer Protection Act of 2010. Mortgage loans are "higher-priced" if they are secured by a consumer's home and have interest rates above certain thresholds. The rule requires creditors to use a licensed or certified appraiser who prepares a written appraisal report based on a physical inspection of the interior of the property. The rule also requires the creditor to disclose to applicants information and the purpose of the appraisal and to provide them a free copy of the appraisal report.

If the seller acquired the property at a lower price within six months prior to the sale, creditors must obtain a second appraisal at no cost to the buyer.

Capital Gains Tax Rule Changes

Long term capital gain tax rates for real estate assets generally stay at 15 percent for taxpayers whose adjusted taxable income does not exceed $400,000 (individual) and $450,000 (joint). For taxpayers with an adjusted taxable income exceeding those amounts, the capital gain tax rate rose to 20 percent.

The exclusion that applies to the gain resulting from the sale of one's residence remains unchanged; $250,000 exclusion for a single filer and $500,000 for joint filers.

3.8 Percent Investment Income Tax & 0.9 Percent Medicare Tax

In addition to the capital gains tax, a new Net Investment Income Tax of 3.8 percent and a Medicare Tax of 0.9 percent may apply to a taxable capital gain. Effective January 1, 2013, these two taxes are imposed on taxpayers with adjusted taxable income that exceed $200,000 (individual) or $250,000 (joint).

Altogether, the tax rate on a taxable gain resulting from the sale of a property could be as high as 24.7 percent depending the tax bracket of the owner.

Appraisal Management Companies

In January 2012, the Texas Appraiser Licensing and Certification Board (TALCB) adopted additional rules marking the final step towards implementing House Bill 1146, which passed during the 82nd legislative session and gave TALCB jurisdiction over Appraisal Management Companies (AMCs). Together with measures adopted previously, these rules define the process for registering and operating as an AMC in Texas. The rules took effect on March 5, 2012, and require AMCs to become registered with TALCB no later than July 2, 2012.

One of the most significant clarifications in the new rules deals with appraiser compensation. AMCs are required to adopt a written compensation policy that complies with federal law and to pay appraisers a fee that is "customary and reasonable" for the requested report. They are also banned from requiring an appraiser to sign a statement conceding that the fee to be paid for an assignment is "customary and reasonable," as was often required in previous standard fee agreements between the AMC and all appraisers on its panel.

AMCs must also ensure appraisers are competent to perform the requested services and review at least five percent of all appraisal reports ordered by the AMC, including one of the first five appraisals performed by each new appraiser on its panel. While most AMCs review every appraisal for "administrative compliance," the required review sets out applicable standards and the scope of work of the review to ensure the appraisal is in compliance with the Uniform Standards of Professional Appraisal Practice (USPAP).

HB 1146 established an AMC Advisory Committee with its members appointed by the governor. It imposed a high standard, consistent with the consumer protection provisions in the federal Dodd-Frank bill. TALCB hired additional staff necessary to meet requirements and must collect fees needed to meet operating expenses.

Rules for Business Entities

Owning Less Than 10 Percent of an Entity

Several new statutory provisions and rules affect the way business entities licensed as brokers do business in Texas. Under amendments to TRELA, enacted in 2011 under Senate Bill 747, a business entity licensed as a broker is required to obtain errors and omissions insurance of at least $1 million if the designated broker of the entity owns less than 10 percent of the entity. A business entity obtaining or renewing a license or changing its designated broker must provide proof

- that the designated broker directly owns at least 10 percent of the business entity when obtaining or renewing the broker's license, and
- that the new designated broker is an officer, manager or general partner of the entity.

If the designated broker does not directly own at least 10 percent of the business entity, the business entity must show proof that the entity maintains E&O insurance of at least $1 million as required by TRELA. TREC has approved a Certificate of Insurance form for the broker to provide the required information regarding E&O coverage.

Compensation

In addition, SB 747 clarified that a business entity that receives compensation on behalf of a licensee is required to be licensed as a broker.

Partnerships and LLCs

Finally, SB 747 in 2011 eliminated the exception for licensure for a partnership or limited liability partnership acting through a partner who is a licensed broker.

Education Standard Advisory Committee

The Education Standard Advisory Committee (ESAC) is a new statutory committee created by amendments to TRELA, enacted in 2011, under Senate Bill 747. The function of ESAC is to regularly review and revise curriculum standards, course content requirements, and instructor certification requirements for core and MCE courses.

The committee consists of 12 members appointed by TREC. A non-voting TREC staff member may also be appointed. The committee consists of

- seven members who have been engaged in the practice of real estate for at least five years before appointment and who are actively engaged in that practice,
- four members who are real estate instructors or owners of real estate schools accredited by TREC that provide core or continuing education, and
- one member who represents the public.

ESAC is in the process of revising curriculum for all required core courses. As of this writing, it has recommended a curriculum for Principles of Real Estate I and II, consisting of two 30-hour courses and a 30-hour Law of Agency curriculum. ESAC is in the process of formulating curricula for two 30-hour courses in Promulgated Contracts and Law of Contracts.

In addition, ESAC is working on ways to improve correspondence and alternative delivery courses. Currently pending before TREC is an ESAC-recommended rule change to require that core course completion certificates issued by TREC-accredited schools must include the starting and ending date of the course to show compliance with the requirement that the course presentation did not exceed 10 hours per day.

The long term goals for ESAC include reviewing

- all core curriculum content;
- course fees and approval processes;
- the acceptability of the various course delivery methodologies (such as classroom, correspondence, alternative delivery, and combination delivery courses);
- alternative evaluation methods of student mastery (other than examinations);
- provider qualifications; and
- instructor qualification standards, including both delivery and mastery.

Justice Court Rule Changes for Evictions

With the passage of House Bill 79 in 2011, the Texas Legislature directed the Texas Supreme Court to create rules for eviction proceedings to accommodate the consolidation of small claims courts with justice courts and to comply with other legislative changes. After months of holding hearings and gathering input, the Texas Supreme Court finalized a new set of rules for justice-court cases, which can affect timelines, mediation and formality.

Timelines

The new rules alter some of the timelines currently required after an eviction suit is filed. The old rules stated that the trial must occur sometime between six and 10 days from the date of service of the citation. The new rules state that the trial must occur between 10 and 21 days from the date the petition (complaint) is filed, but it may not occur fewer than six days after service of citation has been obtained.

Mediation

Parties in an eviction proceeding could be required to mediate unless it would delay the trial.

Formality

The Texas Rules of Evidence and other Texas Rules of Civil Procedure no longer apply to eviction proceedings, making them less formal. There are limited exceptions, such as when the judge determines a rule must be followed to ensure fairness to all parties or when applicable law specifically provides.

Chapter 3

Hot Topics

Choice of Title Company

Section 9 of the Real Estate Settlement and Procedures Act (RESPA), provides that no seller of property that will be purchased with the assistance of a federally related mortgage shall require, directly or indirectly, as a condition to selling the property, that title insurance be purchased by the buyer from any particular title company.

In most residential transactions in Texas, the seller typically pays for the owner's policy for insurance and the buyer typically pays for the lender's policy. Additionally, title companies in Texas not only provide or place the title insurance but also offer escrow and settlement services.

A debate has lingered as to whether the buyer has the absolute right under Section 9 to choose the title company in a residential transaction. In most transactions in Texas, the choice of the title company is negotiable between the parties because

- most sellers in Texas do not require the purchase of title insurance as a condition to sell and, instead, buyers seek to obtain the insurance;
- the owner's policy is not purchased by the buyer in most transactions;
- the buyer is not prohibited from purchasing title insurance directly if the buyer pays for the policy; and
- the services of the title company can be severed into parts other than the issuance of a title policy.

Although licensees may suggest particular title companies to their clients, they should not insist on the use of a particular title company due to their own preferences and any such preferences should not hinder negotiations.

If a seller (especially, an institutional seller) insists on using a particular title company and such insistence creates a problem during negotiations, the licensees should only communicate each party's preference and advise their principals to seek the advice of counsel.

Form 36-7 – Addendum for Property Subject to Mandatory Membership in a Property Owners Association

In 2011, the Texas legislature passed amendments to Chapter 207 of the Property Code, which is the part of the code that deals with resale certificates and other information that property owners associations (POAs) are required to provide to buyers and sellers upon request. The Broker/Lawyer Committee then revised TREC Form 36-7 to include newly added options available under the revised statute. When a property is subject to a mandatory POA, the parties may wish to review the form to see if it should be negotiated as part of the transaction.

(SEE FORM ON PAGE 14)

Paragraph A of the form defines four items the POA is to provide:

- the resale certificate,
- the POA's bylaws,
- any rules the POA maintains, and
- the subdivision's restrictions.

All four items should be provided when a person requests what is known as the "subdivision information" from the POA.

Before the 2011 changes, only the seller (or seller's representative) could request the subdivision information; however, now the buyer, seller, title company or the brokers may obtain the subdivision information. Therefore, Form 36-7 allows the parties to check either Paragraph A(1) or A(2) depending on which party will request the subdivision information. Both paragraphs contain termination rights if the subdivision information is not delivered timely to the buyer. Assuming the buyer timely receives the subdivision information, both paragraphs give the buyer three days to review the subdivision information and terminate the contract (presumably but not necessarily, on the basis of an item in the subdivision information). In

EQUAL HOUSING OPPORTUNITY

ADDENDUM FOR PROPERTY SUBJECT TO MANDATORY MEMBERSHIP IN A PROPERTY OWNERS ASSOCIATION

(NOT FOR USE WITH CONDOMINIUMS)

ADDENDUM TO CONTRACT CONCERNING THE PROPERTY AT

____
(Street Address and City)

____
(Name of Property Owners Association, (Association) and Phone Number)

A. SUBDIVISION INFORMATION: "Subdivision Information" means: (i) a current copy of the restrictions applying to the subdivision and bylaws and rules of the Association, and (ii) a resale certificate, all of which are described by Section 207.003 of the Texas Property Code.

(Check only one box):

❑ 1. Within ____________ days after the effective date of the contract, Seller shall obtain, pay for, and deliver the Subdivision Information to the Buyer. If Seller delivers the Subdivision Information, Buyer may terminate the contract within 3 days after Buyer receives the Subdivision Information or prior to closing, whichever occurs first, and the earnest money will be refunded to Buyer. If Buyer does not receive the Subdivision Information, Buyer, as Buyer's sole remedy, may terminate the contract at any time prior to closing and the earnest money will be refunded to Buyer.

❑ 2. Within ____________ days after the effective date of the contract, Buyer shall obtain, pay for, and deliver a copy of the Subdivision Information to the Seller. If Buyer obtains the Subdivision Information within the time required, Buyer may terminate the contract within 3 days after Buyer receives the Subdivision Information or prior to closing, whichever occurs first, and the earnest money will be refunded to Buyer. If Buyer, due to factors beyond Buyer's control, is not able to obtain the Subdivision Information within the time required, Buyer may, as Buyer's sole remedy, terminate the contract within 3 days after the time required or prior to closing, whichever occurs first, and the earnest money will be refunded to Buyer.

❑ 3.Buyer has received and approved the Subdivision Information before signing the contract. Buyer ❑ does ❑ does not require an updated resale certificate. If Buyer requires an updated resale certificate, Seller, at Buyer's expense, shall deliver it to Buyer within 10 days after receiving payment for the updated resale certificate from Buyer. Buyer may terminate this contract and the earnest money will be refunded to Buyer if Seller fails to deliver the updated resale certificate within the time required.

❑ 4.Buyer does not require delivery of the Subdivision Information.

The title company or its agent is authorized to act on behalf of the parties to obtain the Subdivision Information ONLY upon receipt of the required fee for the Subdivision Information from the party obligated to pay.

B. MATERIAL CHANGES. If Seller becomes aware of any material changes in the Subdivision Information, Seller shall promptly give notice to Buyer. Buyer may terminate the contract prior to closing by giving written notice to Seller if: (i) any of the Subdivision Information provided was not true; or (ii) any material adverse change in the Subdivision Information occurs prior to closing, and the earnest money will be refunded to Buyer.

C FEES: Except as provided by Paragraphs A and D , Buyer shall pay any and all Association fees or other charges associated with the transfer of the Property not to exceed $_______________ and Seller shall pay any excess.

D. DEPOSITS FOR RESERVES: Buyer shall pay any deposits for reserves required at closing by the Association.

E. AUTHORIZATION: Seller authorizes the Association to release and provide the Subdivision Information and any updated resale certificate if requested by the Buyer, the Title Company, or any broker to this sale. If Buyer does not require the Subdivision Information or an updated resale certificate, and the Title Company requires information from the Association (such as the status of dues, special assessments, violations of covenants and restrictions, and a waiver of any right of first refusal), ❑ Buyer ❑ Seller shall pay the Title Company the cost of obtaining the information prior to the Title Company ordering the information.

NOTICE TO BUYER REGARDING REPAIRS BY THE ASSOCIATION: The Association may have the sole responsibility to make certain repairs to the Property. If you are concerned about the condition of any part of the Property which the Association is required to repair, you should not sign the contract unless you are satisfied that the Association will make the desired repairs.

______________________ Buyer	______________________ Seller
______________________ Buyer	______________________ Seller

those transactions where the buyer does not require the subdivision information, the parties may check Paragraph A(4).

If the seller has, before entering into a contract, obtained and provided the subdivision information to the buyer, Paragraph A(3) may apply. It states that the buyer has received and approved the subdivision information. It also addresses whether the buyer will want or require an updated resale certificate. Because the statute expressly states only that a seller may request an updated resale certificate, Paragraph A(3) provides that the seller will request it and deliver it to the buyer. Paragraph A(3) provides that the buyer will pay the seller in advance for the cost of obtaining the updated resale certificate.

Occasionally, a party may ask the title company to request and obtain the subdivision information for them. A title company is not a party to the contract and is not required to request or obtain the information. Therefore, a bold notice in the form states that the title company may only perform that service (if the title company agrees to do so) upon receipt of the fee to obtain the subdivision information.

Occasionally, a POA may change something that was previously reported in the subdivision information. The seller should notify the buyer (as required by Paragraph B) when the seller becomes aware of a material change. The buyer may continue or terminate the contract if the change is material and adverse.

Paragraph C allows the parties to negotiate which party or parties will pay any transfer fees or other fees that the Association imposes because there has been a change of ownership.

Paragraph D provides that a "deposit" or "reserve" is not a fee; therefore, the buyer is responsible for deposits or reserves the POA requires from the property owner.

Paragraph E is the seller's authorization that permits the POA to provide any updated information to the buyer, the title company or a broker. Again, because the statute does not specifically provide that the buyer may obtain "updated" information, this authorization was added to the form to eliminate any concerns a POA may have about releasing updates. There are times when only the title company requires updated information, in which case Paragraph E will address which party will pay the title company for any cost the POA may charge the title company for the updated information.

The amount a POA may charge for the subdivision information varies greatly throughout the state. The statute provides that the POA may charge a reasonable fee for the subdivision information. The statute does not define how a reasonable fee for the subdivision information may be determined. One may argue that the fee is what a reasonable person would pay for such information in similar circumstances. Alternatively, one may argue that it is an estimate of the actual cost the POA incurs in assembling and delivering the information. Nonetheless, the parties may wish to inquire about the price when negotiating Form 36-7 and determine if the POA maintains some or most of the information on its website.

Mutual Termination of Contract Form

Recently TREC proposed a new form, "Mutual Termination of Contract," which will likely be adopted in February of 2014. The form is used only when both the buyer and seller agree that the contract is terminated. It does not replace Form No. 38-4, Notice of Buyer's Termination of Contract, which is used when the buyer has a right to terminate under the contract without regard to the seller's consent (for example, terminating under the option or under the financing addendum for credit approval).

The Mutual Termination of Contract form contains two parts. The first part is used when both parties agree that the contract is terminated, and they also agree on how the earnest money will be released. The form contains an instruction to the escrow agent on how to disburse the earnest money. The first part of the form looks similar to other earnest money release forms, including the Texas Association of Realtors® (TAR) release of earnest money form that has been in common use and which TAR will likely cease to publish when TREC adopts its new form.

The second part of the form is used when the parties agree that the contract is terminated but have not yet agreed as to how the earnest money will be disbursed. In this case, the parties are only agreeing not to enforce specific performance of the contract against the other so the property may be placed back on the market.

E-mail Negotiations and the Creation of Contracts

Can an exchange of e-mails between parties to a real estate transaction, either directly between the parties or through their brokers, constitute a binding contract?

The question has been the subject of some debate as more cases involving the Uniform Electronic Transactions Act (UETA) are being litigated. To definitively answer the question, a review of the specific facts involved in a particular situation must be reviewed. Generally, there are 5 principles that courts will review and discuss.

UETA's Purpose

The purpose of UETA is to provide that a record or signature cannot be denied legal effect or enforceability simply because it is in electronic form (§322.007, B&CC). A contract is enforceable if it is in electronic form. If the law requires a signature on the contract to be enforceable, a contract that contains the signatures in electronic form is enforceable, absent any showing that a party has opted out under UETA.

UETA's Effect on the Law of Contracts

UETA does not change the elements necessary to create a contract and does not change the elements necessary to establish a signature except to allow the electronic version to substitute for "paper and ink." It does not change the Statute of Frauds, which requires certain contracts, such as the contract for the sale of real estate, to be in writing, and signed by the party against whom the contract is to be enforced.

Using an Electronic Signature

UETA defines an electronic signature to include "an electronic sound, symbol, or process attached to or logically associated with a record and executed or adopted by a person with the intent to sign the record." (§322.002(8), B&CC). UETA also provides that an electronic signature is attributable to a person if it was the act of the person (§322.009, B&CC) of whom the signature is attributed.

Satisfaction of Contract Elements

The elements for the creation of an enforceable contract are

- an offer,
- acceptance that mirrors the terms of the offer,
- consideration,
- meeting of the minds,
- communication that each party has consented to the terms of the agreement, and
- execution or delivery of the contract with the intent that it be mutually binding.

A contract for the sale of real property must meet certain elements and must additionally satisfy the statute of frauds (a writing and a signature).

The Authority of the Broker

A real estate broker is typically a special agent and not a general agent. A special agent does not have the authority to bind his principal to transactions. The special agent is engaged to conduct a specific act for the principal. The general agent is authorized to conduct all of the principal's business in a particular area. The general agent usually has the authority to bind the principal. Listing agreements and buyer representation agreements commonly used in Texas are specific with respect to the fact that the broker and agent do not have authority to bind the principal.

Historically, electronic communications from one broker to another in a real estate transaction have not generally been found to bind the brokers' principal because

- the evidence establishes that the broker did not have the authority to bind the principal;
- the e-mail communications are not found to be the contract between the parties;
- the elements of the creation of a contract, as noted above, were not present;
- the statute of frauds is not satisfied; or
- the broker's name in the e-mail is not attributable to the principal as an act of the principal.

Clarifying E-mail

A broker who wants to make it clear that his or her e-mail may not bind the principal, may wish to disavow such authority by written statement in the e-mail. For example,

- "The broker's statements in this e-mail do not create an agreement for the broker's clients."
- "My typed name in this e-mail is not my electronic signature nor is it the electronic signature of any of my clients," or
- "I, the named broker, do not have the authority to bind my clients to a contract."

Case Study

Dittman V. Cerone, No. 13—11—00196—Cv, Court Of Appeals of Texas, Corpus Christi -Edinburg, March 7, 2013

A recent Texas case (Dittman v. Cerone) ruled, under the facts of that particular case, that a broker's e-mail did, in fact, bind the broker's principal.

The Dittmans owned a 3.78-acre property in Seabrook known as the "Stable Property." They also owned an adjoining 17-acre tract. Adjoining their property was another 17-acre tract owned by a neighbor. The Dittmans and the neighbor decided to market both 17-acre properties as a single parcel (34 acres), which was known as the "Pasture Property." They listed the Pasture Property with a broker.

A buyer expressed interest in the Pasture Property and had several e-mail communications and phone conversations with the broker. The buyer expressed *interest in the Stable Property, although it was not for sale. The buyer and sellers signed a contract for the Pasture Property for $2.65 per square foot. After signing the contract, the buyer asked the broker about the Stable Property again. The broker responded by e-mail that the Dittmans were not interested in selling the Stable Property at the time but could offer him a "right of first refusal."*

After reviewing the title commitment on the Pasture Property, the buyer learned that there were several oil and gas leases affecting the Pasture Property. The parties then began negotiating a reduction in the sales price to $2.50 per square foot, a two-year lease-back of the Pasture Property, as well as a possible option to buy the Stable Property. There were three critical e-mails sent during negotiations:

E-mail 1

The broker sent an e-mail message to the buyer stating "...I was able to confirm... that they will agree to a 2 year option at $2.75 s.f. on the 3.78 acre tract. As-is. This is subject to you closing on the 35 acre tract tomorrow. ...In addition, he is prepared to lease the 35 acre tract for that same period for $300 per month plus he will carry necessary insurance." The broker typed his own name to the e-mail.

E-mail 2

The broker sent a second e-mail to the buyer stating, "...throughout the late afternoon and early evening my client's [sic] debated and considered the totality of the deal on the table. They have decided they will not revise the price from the agreed $2.50 s.f. number.... We can work immediately thereafter to prepare the necessary material to reflect the agreement reached in principal [sic] yesterday concerning the 2 year option on the 3.7 +/- acre stable property at $2.75 s.f..." Again the broker typed his own name to the e-mail.

E-mail 3

The Dittmans then sent the broker an e-mail stating "...I wanted to let you know that we are working on getting the following agreements ready for Mr. Cerone's review. The first will be the Lease Agreement for the 34.59 acres. The term is to be a twenty-four (24) month period at the rate of $300.00 per month. The second will be the twenty-four (24) month option to purchase the 3.78 acre tract of ours in Seabrook at $2.75 p.s.f. We will keep you posted on the progress of both items." Ms. Dittman typed her name to the e-mail.

The buyer accepted, by e-mail, the Dittmans' offer of a two-year option to buy the Stable Property for $2.75 per square foot, agreed not to terminate the Pasture Property contract, and closed on the purchase of the Pasture Property.

Later, the buyer attempted to exercise the option to buy the Stable Property. The Dittmans, through an attorney, informed the buyer that they never gave him an option contract. They argued that they had offered him a "right of first refusal." The buyer sued for specific performance on the option contract.

The trial court issued a detailed order and concluded that the three e-mails constituted a valid option contract and ordered the Dittmans to sell the Stable Property to the buyer. The Dittmans appealed.

The Dittmans first argued that the e-mails were separate documents and could not, together, constitute one contract to enforce. But the appellate court noted that instruments pertaining to the same transaction may be read together to ascertain the parties' intent. The court ruled that the essential terms of a contract were present in the three e-mails.

The sellers then argued that the three e-mails did not comply with the Statute of Frauds:

- *They did not agree to grant an option, but only agreed that they would be willing to grant an option in the future. The court held that if the essential elements of a contract were present in the writing (the e-mails), the agreement to do something in the future may be enforced as a contract.*
- *The e-mails did not sufficiently describe the property to be conveyed. The court ruled that references in the emails were sufficient enough to identify the land with reasonable certainty.*
- *They did not agree to conduct the transaction by electronic means, and they did not agree to be bound by an electronic signature. The court noted that "whether the parties agree to conduct a transaction by electronic means is determined from the context and surrounding circumstances, including the parties conduct." The court noted that the Dittmans agreed they had authorized the broker to send the e-mail, were copied on the e-mail, and did not communicate to anyone that the e-mail was incorrect. The evidence showed that the buyer had, by e-mail, communicated his acceptance of the terms in the broker's e-mail.*
- *The Dittmans also argued that the broker did not have the authority to bind them. The court held that the Dittmans did instruct the broker to inform the buyer that they would give him a two-year option, and they authorized the broker to send the e-mail.*
- *The trial court also held that the Dittmans*

committed fraud. The appellate court upheld the fraud finding noting that there was evidence that they told the broker to tell the buyer that they would give the buyer a two-year option on the Stable Property if he would close the purchase of the 34.59 acre property, but they had no intention of fulfilling that agreement.

Handling Trust and Property Management Funds

About 25 percent of TREC's disciplinary orders involve licensees' failure to properly account for, maintain, or refund money the licensees hold in trust for others, most commonly when acting as a property manager. These cases are some of the most serious and concerning disciplinary actions, because they strike at the core fiduciary responsibilities of all licensees, namely, to be faithful and observant to the trust placed in the licensees. They also strike at the characteristics of honesty and trustworthiness, which are required to obtain a license.

When TREC issues this type of a disciplinary order, it often cites in the order that the licensee has violated TRELA §652(b)(9) and (10) that

- require a licensee to properly account for or remit money, within a reasonable time, that the licensee receives and that belongs to another; and
- prohibits a licensee from commingling money that belongs to another with the licensee's own money.

To add clarification and interpretation of these two sections, TREC has adopted specific rules under 22 TAC 535.146, 535.159 and 535.160 for licensees to follow. The term "trust account" below includes an account that holds any other person's funds, such as a property management account or escrow account.

- If a broker holds money belonging to another, he or she must use a separate trust account or an escrow agent to hold the funds. If a broker does not accept money belonging to others, a trust account is not required.
- A salesperson may not maintain a trust account, but a broker may designate a salesperson as a signatory of the broker's trust account. The broker is solely responsible and accountable for all funds received, deposited or disbursed to or from the account.
- A broker's trust account must be specifically identified as a trust account (for example, "trust account," "escrow account," or "property management account").
- Upon receipt of funds belonging to another person, a salesperson must immediately deliver the funds to the broker.
- If a licensee receives money belonging to another that is to be deposited with a named escrow agent, the licensee must deposit the money with the escrow agent by the close of business of the second working day after execution of the contract or, if all the parties agree, by the time required by the agreement.
- A broker may not compel the parties to use the broker as an escrow agent in a transaction. It is up to the parties to choose the escrow agent.
- A broker who maintains a trust account must retain
records of each deposit and withdrawal on the account for at least four years.
- A licensee may not commingle money belonging to others with the licensee's own funds or other non trust funds. Such funds must be deposited in the broker's trust account or with the named escrow agent in the contract. Placing money belonging to others in a licensee's personal or business accounts is prima facie evidence of commingling.
- Licensees who hold money belonging to others hold the money as fiduciaries. The broker holding money belonging to another acts as a trustee for the person making the deposit and the party for whose benefit the broker holds the money.
- If money belonging to another person is properly deposited in the broker's trust account, and if any party to the transaction makes demand for the money, the broker must, in a reasonable period of time (defined as 30 days), properly account for or remit the money. To "properly account," the licensee should:
  - disburse the money to the appropriate party, if the licensee can determine which party is entitled to the money;
  - pay the money into the registry of a court and interplead the parties if the licensee cannot make a determination as to which party is entitled to the return of the money; or
  - if the written agreement in the transaction authorizes the broker to require a release and authorization before disbursing the money, give each party a written statement requesting the signed releases along with a detail of the amount of money and the place of custody, and then pay the money to the appropriate party or

parties in accordance with the releases when received or, if the parties cannot agree, pay the money into the registry of a court and interplead the parties.

- If a licensee acquires ownership of money in the broker's trust account (for example, earned fees or commissions) the licensee must remove such money from the trust account within a reasonable time (defined as 30 days after the licensee acquires ownership).
- The balance of a broker's trust account must, at all times, equal the total of the trust funds received except that the broker may deposit and maintain a reasonable amount in the account for service fees, including fees charged for insufficient funds. The broker must keep detailed records of any funds deposited under this exception.
- Using money from a trust account other than to disburse the money to the parties, expending the money for the benefit of a party in accordance with the party's written instructions, deducting the broker's earned fees or commissions in accordance with written authorization to do so, or paying service fees (as described in the previous paragraph) is prima facie evidence of commingling.
- A broker's trust account may be an interest bearing account as long as the broker may withdraw the funds and disburse the funds at the appropriate time. Unless the broker has an agreement with the person who deposited the funds providing otherwise, any interest earned on the account must be distributed to the person or persons who are the equitable owners of the funds during the time the interest is earned. If a broker deposits trust funds in a noninterest bearing account, the broker is not liable for the interest or for charges on the funds unless there is an agreement to the contrary.
- A broker may, but is not required, to maintain separate trust accounts for earnest monies, security deposits, and for other trust funds.
- If a broker accepts a check as an escrow agent and later finds that such check has been dishonored, the broker must immediately notify, in writing, all parties to the transaction.

What Should Happen When an Agent Changes Broker?

Changing broker sponsorship affects consumer relationships, and brokerage responsibilities and can be performed on paper or online.

Sponsorship Change on Paper

For a paper sponsorship change, Salesperson Sponsorship Form-1 is required. It is for "Use When Changing Brokers or going from Inactive to Active." This document is available on the TREC website (www.trec.gov). This form requires the salesperson's signature to certify that the former sponsoring broker has been given written notice of the termination as required by the TREC Rules. The form also requires the new sponsoring broker's signature indicating the broker's agreement to serve as a sponsor and to be responsible for the real estate brokerage activities of the newly sponsored salesperson. The paper sponsorship change takes longer to complete and is more costly than an online sponsorship change.

Sponsorship Change Online

For an online sponsorship change, TREC's Online Relationship Management Tool (RMT) is available. RMT has been positive for TREC, licensees and consumers. RMT allows brokers or salespersons to manage their sponsor relationships online quickly and easily. Whoever initiates the request for sponsorship is the party who pays. This method is designed to be faster and less expensive than a paper application. The Rules state that a sponsorship is not active until the recipient accepts the invitation. This means that even when a salesperson has paid, and the RMT has sent an invitation to a new broker, the salesperson cannot practice real estate until the sponsorship becomes active, which occurs when the recipient accepts the sponsor invitation.

Check the TREC Rules First

TREC Rules have procedures for the circumstances relating to all activity regarding licensure. Reference to the Rules prior to an action is a best practice.

Notifying TREC of Sponsorship

When a salesperson whose license status is active enters the sponsorship of a broker, the salesperson and broker whose sponsorship the salesperson has entered shall notify TREC within 10 days, submit the appropriate fee, and request issuance of a new license reflecting the new association. The salesperson may act as the broker's salesperson from the date the notice and fee are mailed or delivered to TREC.

Termination of Salesperson's Association with Sponsoring Broker

TREC will no longer consider the broker to sponsor the salesperson upon receipt of the license or upon receipt of a written request from a new sponsoring broker to sponsor the salesperson, whichever occurs first. If the sponsorship has ended, because the salesperson has left the sponsorship, the salesperson shall immediately send written notification to the broker. If the sponsorship has ended because the salesperson has left the sponsorship, the salesperson shall immediately notify the broker in writing. If TREC receives a request from a broker to sponsor a salesperson shown in TREC's records as sponsored by another broker, TREC shall notify the former broker of the change in sponsorship.

When the sponsorship of a salesperson ends, the broker shall immediately return the salesperson's license or copy to TREC or otherwise notify TREC in writing that the sponsorship has ended.

If a salesperson's license becomes inactive during an attempt to change brokers, the procedure is different to reactivate the salesperson's license with the new broker.

Craigslist Leasing Scams

The Better Business Bureau, the FBI, and the Federal Trade Commission are just a few of the institutions warning consumers to be wary of Craigslist advertisements and other similar Internet services when searching for a rental home. Because of the high number of people using the Internet when searching for rental property, scammers have found a new way to steal money from the unsuspecting. Craigslist seems to be at the center of this activity because of its convenience and popularity.

Prospective renters respond to an online advertisement for a rental property being offered at below-market rental rates. The "landlord," the scammer who holds no ownership interest in the property, replies that the renter will need to wire money for a deposit or rent, typically outside the United States, in order to receive keys to the property. If the potential tenant asks to view the property first, the landlord replies that he or she is out of the country and cannot show the house. Many times the scammers have obtained photographs online from legitimate websites that list homes for sale. Scam victims are shocked when they show up to the property ready to move in, only to find it is occupied by the homeowner who is just as bewildered as they are. The homeowner may have listed his or her property for sale, but not for rent.

The Federal Trade Commission offers tips on what to watch for to avoid falling victim to this scam:

- They tell you to wire money. This is the surest sign of a scam. There's never a good reason to wire money to pay a security deposit, application fee, first month's rent, or vacation rental fee. That's true even if they send a prospective renter a contract first. Wiring money is the same as sending cash — once you send it, you have no way to get it back.
- They want a security deposit or first month's rent before you've met or signed a lease. It's never a good idea to send money to someone a prospective renter has never met in person for a rental property the prospective renter hasn't seen. In addition to setting up a meeting, a prospective renter should do a search on the owner and listing. If the same ad is listed under a different name, that's a clue it may be a scam.
- They say they're out of the country. But they have a plan to get the keys into a prospective renter's hands. It might involve a lawyer or an "agent" working on their behalf. Some scammers even create fake keys. Don't send money to them overseas. If prospective renters cannot meet the landlord in person, see the rental property, or sign a lease before the renter pays, they should keep looking.

Forms Changes

TREC No. 20-12, One to Four Family Residential Contract (Resale)

- The definition of "Property" is moved from the end of Paragraph 2 to the beginning of the paragraph.
- Paragraph 6.A.(8) is amended to provide that, at buyers' expense, the exception shall be amended to read "shortages in area" unless the buyer instructs the title company otherwise.
- The third sentence in Paragraph 6.B regarding delivery of Commitment and Exception Documents is amended to read "…the time for delivery will be automatically extended up to 15 days or 3 days before the Closing Date, whichever is earlier" to foreclose the delivery of such documents at closing.
- Paragraph 7.D is amended to define "As Is" as "the present condition of the Property with any and all defects and without warranty except for the warranties of title and the warranties in this contract."
- The notice after paragraph 7.D is moved to the body of the paragraph after the definition of "As

Is" and the defined term "As Is" is added to that sentence and subparagraphs (1) and (2) to replace "in its present condition."

- The parenthetical at the end of paragraph 7.D is changed to add "and treatments" at the end of the sentence.
- The second sentence in Paragraph 7.F is amended to clarify that, if no license is required by law to perform a repair or treatment, all repairs and treatments must be performed by persons "who are commercially engaged in the trade of providing such repairs or treatments" rather than "authorized by law to provide such repairs or treatments."
- Paragraph 7.F is amended to change the number of days in the last sentence from 15 to 5 days regarding the Buyer's option to extend the Closing Date if Seller fails to complete agreed repairs and treatments prior to closing.
- Paragraph 9 is amended by adding a new Paragraph 9B regarding leases wherein the Seller (1) agrees not to execute any lease or convey any interest in the Property after the effective date without the Buyer's written consent, and (2) incorporates existing Paragraph 9.B(5) and renumbers existing Paragraph 9B to 9C to contain 9B(1)-(4).
- Paragraph 14 is amended to add the clause "or cause to be restored" in the first sentence.
- Paragraph 16 is amended to remove the mediation check boxes to require mediation to resolve disputes between Buyer and Seller related to the contract.
- Paragraph 23 is amended to provide that the Seller or Listing Broker must receive the option fee within 3 days after the effective date of the contract rather than Buyer paying Seller the option fee within 2 days after the effective date of the contract to make it clear that it is not enough that the Buyer puts the option fee in the mail within 2 days after the effective date; the Seller or Listing Broker must receive the option fee within 3 days after the effective date.
- The last page is amended to clarify that the agents should not sign on the blank lines; they should insert their names only.

TREC No. 9-11, Unimproved Property Contract

Amendments to TREC No. 9-11, Unimproved Property Contract are the same as those proposed for TREC Form No. 20-12 except as follows:

- The definition of "Property" in Paragraph 2 is not changed.
- Paragraph 7.E(1) is amended to be the same as Paragraph 7.H(1) in Form 25-10, Farm and Ranch Contract.
- Paragraph 7.E(3) regarding environmental hazards is amended to change "any environmental hazards or conditions affecting" to "any environmental hazards that materially and adversely affect" the property.

TREC No. 23-13, New Home Contract (Incomplete Construction)

Amendments to TREC No. 23-13, New Home Contract (Incomplete Construction) are the same as those proposed for TREC Form No. 20-12, except as follows:

- The definition of "Property" in Paragraph 2 is not changed. There are no amendments to paragraph 7 except to insert missing parentheses.
- Paragraph 7.I(3) regarding seller's disclosure of environmental hazards is amended to change "any environmental hazards or conditions materially affecting" to "any environmental hazards that materially and adversely affect" the property.
- Paragraph 9 is amended by adding a new Paragraph 9.B regarding leases wherein the Seller agrees not to execute any lease or convey any interest in the Property after the effective date without the Buyer's written consent.

TREC No. 24-13, New Home Contract (Completed Construction)

Amendments to TREC No. 24-13, New Home Contract (Completed Construction) are the same as those proposed for TREC Form No. 20-12 except as follows:

- Paragraph 7.H(3) regarding seller's disclosure of environmental hazards is amended to change "any environmental hazards or conditions materially affecting" to "any environmental hazards that materially and adversely affect" the property.
- Paragraph 9 is amended by adding a new Paragraph 9.B regarding leases wherein the Seller

agrees not to execute any lease or convey any interest in the Property after the effective date without the Buyer's written consent.

TREC No. 25-10, Farm and Ranch Contract

Amendments to TREC No. 25-10, Farm and Ranch Contract are the same as those proposed for TREC Form No. 20-12, except as follows:

- Paragraph 2 is amended to refer to addenda or specific provisions for exclusions and reservations.
- The last page is not amended.

TREC No. 30-11, Residential Condominium Contract

Amendments to TREC No. 30-11, Residential Condominium Contract. The proposed revisions are the same as those proposed for TREC Form No. 20-12 except as follows:

- Paragraph 2.B(3) is deleted as a typographical error.
- No changes were made to paragraph 6.A.(8).

TREC No. 37-5, Subdivision Information, Including Resale Certificate

Amendment to TREC No. 37-5, Subdivision Information, Including Resale Certificate for Property Subject to Mandatory Membership in a Property Owners' Association is amended as follows:

- Amend Paragraph H to more closely track statutory changes to Chapter 207, Property Code.

TREC No. 40-5, Third Party Financing Addendum

Amendment to §537.47 proposed to adopt by reference Standard Contract Form TREC No. 40-5, Third Party Financing Addendum for Credit Approval:

- New paragraph E is added to reference USDA Guaranteed Financing.

Contract Forms

When negotiating contracts for the sale or lease of any interest in real property, licensees may only use forms that are authorized by Section 537.11 of the TREC Rules. Those forms include

- forms adopted by TREC for the type of transaction for which the form is used,
- forms required by the property owner (prepared by the owner or an attorney),
- forms required by an agency of the United States government,
- forms prepared by an attorney licensed in Texas and approved by the attorney for the type of transaction involved if TREC has not promulgated a form for that kind of transaction.

The contract forms adopted by the Texas Real Estate Commission are available to any person, because they are public records. However, **TREC contract forms are intended for use only by licensed real estate brokers or salespersons who are trained in their correct use.** Mistakes in the use of a form may result in financial loss or an unenforceable contract. Licensees should not distribute these forms to clients or customers to fill out by themselves.

TREC does not promulgate listing or buyer representation agreements, property management contracts, forms for commercial property, or residential leases (other than temporary residential leases used in connection with a sale). These forms can be obtained from an attorney or a trade association.

The forms provided by associations are often copyrighted and available only to their members. Use of those forms by non-members is a copyright violation. Sharing of the forms by members with non-members is an abuse of their association membership benefit.

Chapter 4
Case Studies

"As Is" vs. Seller's Disclosure

RITCHEY V. PINNELL, 357 S.W.3D 410 (TEX. APP.—TEXARKANA 2012, NO PET.)

Ritchey purchased a house in Winnsboro, Texas, from the Pinnells pursuant to a sales agreement that provided that Ritchey accept the property "as is." Prior to the sale, Mr. Pinnell (not licensed as a plumber nor an electrician) had remodeled the house, doing most of the electrical work and all of the plumbing work himself without obtaining permits from the City of Winnsboro. After the sale had been completed, Ritchey was unable to obtain a certificate of occupancy from the city because the electrical and plumbing work failed to comply with building code requirements. Without a certificate of occupancy, Ritchey was barred by municipal authorities from occupying the house. Ritchey filed suit against the Pinnells for real estate fraud, alleging that the Pinnells' failure to disclose in the seller's disclosure notice that the repairs to the house violated building code requirements amounted to misrepresentation or concealment of a material fact. The Pinnells moved for summary judgment, arguing that the "as is" clause in the purchase agreement defeated the reliance element of statutory real estate fraud. The trial court held in favor of the Pinnells.

The court of appeals reversed the trial court's decision. Ritchey argued that the trial court erred by granting the summary judgment because there is evidence of fraud, in that the Pinnells made material misrepresentations in the seller's disclosure notice, and Ritchey relied on those misrepresentations in entering into the "as is" sales agreement. In other words, Ritchey maintains that she was fraudulently induced to enter into the purchase agreement that contained the "as is" clause.

The Pinnells' disclosure statement to Ritchey stated that they were unaware of, "[r]oom additions, structural modifications, or other alterations or repairs made without necessary permits or not in compliance with building codes in effect at the time."

The "As Is" clause in contracts does not defeat the reliance element of statutory real estate fraud for information or omissions in a Seller's Disclosure Notice.

Splitting Commission with Buyer

WU V. RHEE, (WL 5198336, BKRTCY. S.D. TEX. 2012)

Wu engaged the services of Rhee, a family friend and a real estate licensee. At the time, Rhee was initially hired, Wu had already identified a property and negotiated a sales price. If Wu purchased the property, Rhee's broker's duties would have been limited, and he was to keep only $10,000 of the commission and rebate the remainder of it to Wu. The first deal did not close. Later that year, Rhee negotiated a purchase price on behalf of Wu. Once again, Wu and Rhee agreed to split the $60,000 commission. After closing, Rhee explained that his sponsoring broker would have to be paid the commission, and then Rhee would share that commission with Wu. Wu never received any money, then Rhee filed for bankruptcy protection in an effort to discharge the obligation.

Multiple e-mails were exchanged between Rhee and Wu in attempt to negotiate a settlement. The e-mails were amicable and indicated that both sides sought a mutually beneficial and amicable settlement.

In analyzing the fraud issue, the court concluded that Rhee engaged in fraud in a real estate transaction by promising to pay $20,000 to Wu and held that Rhee was responsible for actual damages as well as $5,000 in exemplary damages, because he was aware of the falsity of the promise he made. The court then awarded an additional $25,235.92 in attorney fees. The court also held that Rhee was liable for fraudulent inducement and found that he also violated the Texas Deceptive Trade Practices Act.

While commission agreements have to be in writing for a broker to pursue a commission, the same standard does not apply to principals. The court noted that Wu was not a licensed real estate broker and therefore not familiar with the requirements on commission agreements imposed by TRELA. More importantly, Rhee owed a fiduciary duty to Wu.

The court also found that there was a breach of contract, a cause of action for common law fraud and conversion and ultimately awarded Wu $50,235.92 in damages. The court further noted:

"A fiduciary duty imposes special obligations on a real estate agent. The real estate agent must 'be faithful and observant to trust placed in the agent, and be scrupulous and meticulous in performing the agent's functions.' Additionally, the real estate agent [must] place no personal interest above that of the client."

The court held that Rhee violated both of these aspects of his fiduciary duty to Wu.

Ultimately, TREC paid $50,000 from the Real Estate Recovery Fund on this case.

Not paying a client a promised split of a licensee's commission (rebate) is a breach of the fiduciary duty of a real estate licensee.

Buyer Representation/ Misrepresentation

DEFTERIOS V. DALLAS BAYOU BEND, LTD., 350 S.W.3D 659 (TEX.APP.-DALLAS 2011, PET. DENIED)

A developer, Nussbaum, received a call from Defterios, a broker, stating that his client, Flaven, was interested in purchasing the developer's portfolio of properties. Defterios told the developer that Flaven was the beneficiary of a multimillion dollar trust fund and wanted to use those trust funds to purchase the properties. Flaven eventually signed contracts to buy nine of the properties. The contracts initially called for an August 2004 closing, but the closings were rescheduled a number of times. Defterios told the developer that the reason for the delays was that the trust fund was not releasing the funds.

On many occasions, Defterios told Nussbaum that he had verified the existence of the funds and that the closings were imminent. Over a year after the contracts were signed, however, the deals still had not closed. At that time, Nussbaum came to believe that Flaven did not have the financial resources to close on the properties and that all of Defterios' representations about Flaven and the trust fund had been false. As it turned out, Flaven was a Massachusetts truck driver and was not the beneficiary of a multimillion dollar trust fund; he never closed on the contracts.

Eventually, some of the properties were deeded to the lender banks in lieu of foreclosure and others were sold for a loss. Many of the individual investors in the properties lost all the savings they had invested in the properties. The jury found no direct benefit-of-the-bargain damages, but awarded over $12 million in consequential damages to the developer and investors for fraud and negligent misrepresentation.

On appeal, Defterios did not challenge the finding of liability, but argued that the evidence did not support the damages and the types of damages awarded.

The court reviewed the evidence and held that the jury could have reasonably found that Defterios' misrepresentations were a cause-in-fact of damages to Nussbaum and investors. The evidence showed that Nussbaum did not cancel the contracts with Flaven, because Defterios continually represented that the trust funds had been verified and that Flaven was going to purchase the properties. The evidence showed that if Defterios had not represented that he had verified the existence of the trust funds and that the closings were imminent, the developer would not have extended the closing date and would have put the properties back on the market on September 9, 2004. The evidence also showed that the developer deferred maintenance on the properties because of the contracts with Flaven. By the time the developer realized that Flaven would not purchase the properties, the market had declined, and the properties needed repairs. Nussbaum had to take the properties off the market and make the repairs before he could place the properties back on the market. Additionally, the evidence showed that the properties had to be taken off the market because they were "shop worn" and prospective buyers had lost interest in them. The jury could have reasonably found from the evidence that the broker's representations caused the developer to incur expenditures for capital improvements, operating losses, and a loss in market value that they would not otherwise have incurred if the properties had closed according to the contracts.

Again, having reviewed the evidence and the parties' respective arguments, the court concluded that the jury could have reasonably found that the types of damages incurred by the developer were foreseeable to Defterios. The evidence showed that Defterios was a real estate broker and, as such, was familiar with the market. The jury could have reasonably inferred that a person in Defterios' position could have contemplated that the types of losses awarded here would be incurred if his representations were false.

A broker can be held liable for ancillary losses to a party that could reasonably have been contemplated due to misrepresentations made by the broker.

Reversionary Interests are Compensable in a Takings Case

EL DORADO LAND COMPANY, L.P. V. CITY OF MCKINNEY, 395 S.W.3D 798, TEX., MARCH 29, 2013

In 1999, El Dorado Land Company sold several acres to the City of McKinney for use as a park. The deed provided that the conveyance was "subject to the requirement and restriction that the property shall be used only as a community park." If the City decided not to use the property for that purpose, the deed further granted El Dorado the right to purchase the property. The deed labeled this right an option and set the option's price at the amount the City paid or the property's current market value, whichever was less.

Ten years after acquiring the property, the City built a public library on part of the land. The City did not offer to sell the property to El Dorado or otherwise give notice before building the library. After learning about the library, El Dorado notified the City by letter that it intended to exercise its option to purchase.

After the City failed to acknowledge El Dorado's rights under the deed, El Dorado sued for inverse condemnation.

The City claimed that this case did not involve a compensable taking of property but a mere breach of contract for which the City's governmental immunity applied. The trial court agreed and dismissed the lawsuit. The court of appeals upheld the trial court's decision. The matter was appealed to the Texas Supreme Court.

This case focuses on the nature of El Dorado's interest in the land. El Dorado argued that its right to purchase is a real property interest because it is a reversionary interest and, more particularly, a right of reentry. The City, on the other hand, contended that El Dorado's option was not a real property interest but a mere contract right.

El Dorado characterized its reversionary interest as a right of reentry. A right of reentry is a future interest created in the grantor that may allow the grantor to possess the property when the grantee's fee simple estate terminates because of a condition that subsequently occurs. El Dorado's right to possess was contingent on the property's use. If the City violated the deed restriction, El Dorado had the power to terminate the City's estate. The deed referred to this power or right as an option, but it effectively functioned as a power of termination, or as El Dorado labels it, a right of reentry. The Supreme Court noted that it has equated this right to an estate or interest in land.

Because a right of reentry requires its holder to make an election does not make it any less a property right, particularly when the holder has made the required election.

The Supreme Court then turned to the issue of whether El Dorado's reversionary interest could support a takings claim under the Texas Constitution. In other cases, the court has held that reversionary interests similar (but slightly different) from the one in this case are compensable if taken by the state. The court saw no reason to distinguish between the reversionary interest in those cases and in this case. Under Texas law, the possibility of reverter and the right of reentry are both freely assignable like other property interests. Simply put, both the possibility of reverter and the right of reentry are future interests in real estate.

When private property is taken for a public purpose, the Texas constitution requires that the government compensate the owner. When the government takes private property without paying for it, the owner may bring suit for inverse condemnation.

In summary, the Supreme Court ruled that the reversionary interest retained by El Dorado in its deed to the City is a property interest capable of being taken by condemnation. It expressed no opinion on whether a taking occurred in this case. It reversed and remanded to the trial court for it to determine whether the City violated its deed restrictions by building a public library on a part of the land dedicated for use as a community park and, if so, to what extent the City had taken El Dorado's interest in the restricted property.

A reversionary provision in a deed creates a property interest that is compensable if taken by the state.

Attempt to Convert Separate Property to Community Property

ESTATE OF CUNNINGHAM, 390 S.W.3D 685, TEX.APP.–DALLAS, 2012

Cunningham and his first wife divorced in 1978. They had 6 children. He married his second wife on March 15, 1985, and they remained married until his death on November 28, 2008.

During his life, Cunningham owned three tracts of land:

- 5 acres he acquired in 1967 from his parents where he built his home;
- 24 acres he inherited from his parents in 1975 (contiguous to the 5-acre tract); and
- 54 acres he inherited from his parents (not contiguous to the others).

After the second marriage, Cunningham conveyed to his second wife an undivided one-half interest in the 5-acre tract and an undivided one-half interest in 34–acre tract out of the 54-acre tract. He later conveyed 5.710 acres of the 54-acre tract to his daughter.

On September 25, 2008, about two months before he died, Cunningham and his second wife executed a document entitled "Agreement to Establish Right of Survivorship to Community Property between Spouses." Shortly after his death, his second wife filed an application to adjudicate the agreement. The trial court approved the application stating that all the "real and personal property" of Cunningham and his second wife, owned at the time of his death, was community property and the agreement created a right of survivorship in their community property in favor of the second wife.

Four months later, one of the children from the first marriage filed a bill of review asserting Cunningham's real property had been acquired by inheritance and was his separate property and that the trial court was in error in finding that the agreement converted it to community property. The trial court denied the bill of review and an appeal ensued.

The appellate court found that the agreement did not comply with §4.203 of the Family Code and did not convert Cunningham's separate property into community property.

The court noted that the Family Code provides that spouses may agree to convert all or part of their separate property to community property. An agreement to convert separate property to community property must be in writing, signed by the spouses, identify the property being converted, and "specify that the property is being converted to the spouses' community property." A mere transfer of a spouse's separate property to the name of the other spouse or to the name of both spouses is insufficient to convert separate property to community property. An agreement to convert separate property to community property is not enforceable if the spouse against whom enforcement is sought did not receive a fair and reasonable disclosure of the legal effect of converting separate property to community property.

The document in this case was a fill-in-the-blank form. It was completed by the second wife's son and Cunningham's brother. The form stated in relevant part:

"The parties agree that the following is held as their community property: Home and other real property locate[d] at: 15375 County Road 342 Wills Point TX including all inheritance property."

"It is agreed that title to all community property of Husband and Wife, specifically identified herein or held as community property shall pass to the surviving spouse upon the death of the first of us to die, without the necessity of probate court proceedings or other legal action other than the recording of this Agreement in the records of the County Clerk of Kaufman County."

The court found that the agreement did not state the spouses agree to convert all or a part of one spouse's separate property into community property. The agreement identified only the five-acre tract and did not identify the other two tracts. There was no evidence presented that either Cunningham or his second wife received a fair and reasonable disclosure of the legal effect of converting separate property to community property. The second wife testified they did not discuss the effect of converting Mr. Cunningham's separate property to community property, nor did they have any documentation explaining the conversion. Therefore, the appellate court found that the agreement did not convert the separate property to community property. The court rendered judgment that the bill of review be granted and remanded the case for further proceedings.

Spouses who want to convert separate property to community property must comply with all of the requirements of §4.203 of the Family Code including a specific agreement to convert one spouse's separate property to community and there must be evidence that the spouses received a fair and reasonable disclosure of the legal effect of the conversion.

The Risk Caused by Certain Pets

HARRIS V. EBBY HALLIDAY REAL ESTATE, INC., 345 S.W.3D 756, TEX. APP. – EL PASO, JULY 20, 2011

In May 2007, the Harrises signed a listing agreement with Ebby Halliday to sell their residence in Dallas. At that time, the Harrises owned two pit-bull type dogs, which spent most of their time in the backyard. The backyard is fenced on all sides and closed off with three gates. Two of the gates are secured with combination locks. To access the backyard from the front, one must go through at least one of the locked gates.

On May 3, 2008, the listing agent scheduled an appointment to show the property to a potential buyer. The Harrises' son removed the dogs from the property prior to the showing. After the showing, Mrs. Harris returned home, and the dogs were returned to the backyard. Sometime later in the afternoon, the dogs escaped through an unsecured gate and attacked a neighbor who was walking his own dog.

After retrieving the dogs, the Harrises went to the backyard to try and determine how the dogs escaped. According to Mrs. Harris, a padlock on one of the gates had been unlocked and left in a position which prevented the gate from latching securely. The Harrises concluded that the listing agent failed to secure the gate after showing the property. According to the listing agent and the buyer's agent, none of the visitors used the gate as the showing was done exclusively through the front of the house.

The Harrises filed suit against Ebby Halliday alleging that the listing agent was negligent by failing to properly secure the gate after the showing. The Harrises also claimed that Ebby Halliday breached the listing agreement by failing to secure the property after a showing. The trial court granted a summary judgment for Ebby Halliday. The Harrises appealed.

The Harrises did not appeal the ruling as to the breach of contract claim and, therefore, considered the appeal only for the negligence claim.

To prevail in a negligence claim, the Harrises would have had to establish a duty, a breach of that duty, and damages that were proximately caused by the breach. Whether or not a breach of a duty has occurred is determined by comparison to the applicable standard of care. The Harrises contended that Ebby Halliday breached the standard of care by failing to, "adequately and properly secure" the property after a showing. The "ordinary care" standard is generally defined as that which an ordinarily prudent person, exercising ordinary care, would have done under the same circumstances.

The court noted that although the Harrises' response included extensive arguments regarding the existence of a duty, and evidence of breach, their response failed to address the standard of care ground at all, either at trial or on appeal, and ruled that the summary judgment was affirmed on that ground alone.

Agents must exercise a standard of care that a prudent person would ordinarily exercise in securing property following a show, or they could be found negligent for subsequent events resulting from failing to meet that standard.

Mutual Mistake/Scrivener's Error

SIMPSON V. CURTIS, 351 S.W.3D 374 (TEX. APP.-TYLER 2010, NO PET.)

The Curtises agreed to sell 85 acres to the Simpsons. The earnest money contract provided that the seller reserve the minerals and timber; however, the reservations were not included in the deed delivered at closing. When the Curtises asked the Simpsons to execute a correction deed, the Simpsons refused, so the Curtises sued.

The trial court held that the failure to include the reservation in the deed was a scrivener's error and that the Curtises were entitled to reformation of the deed.

The underlying objective of reformation is to correct a mutual mistake made in preparing a written instrument, so that the instrument truly reflects the original agreement of the parties. By implication, reformation requires two elements: an original agreement and a mutual mistake, made after the original agreement, in reducing the original agreement to writing. A mutual mistake is one common to both or all parties, wherein each labors under the same misconception respecting a material fact, the terms of the agreement, or the provision of a written agreement designed to embody such an agreement. Moreover, if a mistake has been made by a scrivener or typist, an instrument may be reformed and modified by a court to reflect the true agreement of the parties.

The court held that there was sufficient evidence to support the finding that the failure to include the reservation was a scrivener's error and a mutual mistake. The Simpsons contend, however, that the merger clause in the deed precluded the trial court from considering the variance between the terms of the earnest money contract and the deed in determining the existence of a mutual mistake. The court disagreed. The merger doctrine applies to deeds only in the absence of fraud, accident, or mistake. In an equitable action to reform an instrument that fails to express the real agreement due to mutual mistake, parol evidence is admissible to show the true agreement. Further, the statute of frauds is not an impediment to the introduction of parol evidence to establish an agreement for a mineral interest in an action for reformation based on mutual mistake. Because the court determined that there was a mutual mistake in the signing of the deed, the merger doctrine is inapplicable.

The merger clause in a deed does not apply to parol evidence to establish that the failure to convey mineral interests in the deed when agreed to in the contract was a scrivener's error and a mutual mistake. A party is entitled to reformation of a deed to correct a mutual mistake made when reducing the terms of an original contract to writing to convey the property.

Real Estate License Required for a Business Broker to Sell Real Estate

SMITH SALES V. METAL SYSTEMS, 397 S.W.3D 305, TEX. APP. – DALLAS, MARCH 5, 2013

The parties entered into a listing agreement in July 2008. Dean, as broker, was granted the exclusive right to sell Metal's business. The contract lists the sales price as $4,580,000 and notes real estate is included in the sale. The business broker was to receive four percent on the sale.

The business broker later sued the seller for nonpayment of his commission claiming that the seller breached the listing agreement. The seller claimed the business broker could not sue to collect any compensation, because the listing agreement includes real estate and there is no evidence the business broker held a real estate license when he entered into the listing as required by TRELA. TRELA provides a party may not maintain an action to collect compensation for an act as a broker or salesperson unless the party alleges and proves it was a licensed real estate broker. The trial court granted a summary judgment in favor of the seller on this basis. The business broker appealed.

On appeal, the business broker argued that TRELA did not apply, because the listing did not contemplate real estate to be part of the sale for which he was to be paid. He argued that the sale was to be either the sale of the seller's stock or the sale of the seller's assets and, if a sale of assets occurred, a real estate broker would be engaged to handle the sale of the real estate assets. However, the agreement contained a check box that asked if real estate was included in the sale, and the box was checked "yes." The appellate court stated that the business broker's testimony that real estate was not contemplated by the listing was parol evidence, which must be excluded as the written agreement was not ambiguous. Therefore, since the listing stated that the sale included real estate, a real estate broker license was required. The appellate court affirmed the summary judgment granted by the trial court.

If real estate is included in the listing agreement for the sale of business assets, a business broker who is not licensed by TREC may not maintain an action against the seller for commission.

Stigma Damage May be Awarded for Remediated Property

HOUSTON UNLIMITED, INC. V. MEL ACRES RANCH, 389 S.W.3D 583, TEX. APP. – HOUSTON (14TH DISTRICT), NOVEMBER 15, 2012

Houston Unlimited (HUI) operated a metal-processing facility. Mel Acres' property is undeveloped ranchland located across the highway from HUI's facility. A culvert flows downhill from HUI's facility, under the highway, and into a stock tank ("the large pond") on Mel Acres' property.

In late 2007, Mel Acres' lessee, a cattle rancher, complained that a number of its calves had died or experienced various defects. Someone associated with the lessee had observed an HUI employee "dumping" the contents of a large drum into the culvert and that pipes were discharging materials from HUI's process building. Mel Acres retained an environmental consultant, who found arsenic, chromium, copper, nickel and zinc exceeding state action levels in the culvert and copper exceeding state action levels in a large pond.

In December 2007, Mel Acres lodged a complaint with Texas Commission on Environmental Quality (TCEQ). HUI was a "registered large quantity generator," meaning it was permitted to generate hazardous waste in amounts greater than 1,000 kilograms per month. A TCEQ inspector found that HUI did not have the proper permits, plans or employee training. The investigators found that HUI was illegally discharging industrial waste into and adjacent to state waters and instructed HUI to immediately cease. There was no berm or other structure, as required, to prevent water containing spent blast media and other processing materials from flowing off-site during rain events. Soil and water sampling from the pond revealed chromium, copper, aluminum, and zinc exceeded state action levels. TCEQ concluded that an unauthorized discharge of industrial hazardous waste occurred at the HUI facility and affected Mel Acres' property. HUI paid a find assessed by TCEQ. TCEQ concluded HUI was either negligent or intentional in its violation of TCEQ rules.

Within a week after the TCEQ visit, HUI began to make corrections to resolve the violations. Both HUI and Mel Acres hired their own experts to determine the extent of the damage and whether the contaminant levels on the Mel Acres property had decreased. The experts found and testified to conflicting findings. HUI's expert found that the levels had decreased to acceptable levels and that there was not continuing damage. Mel Acres' expert testified that the damage to the Mel Acres' property was devastating and that many of the contaminant levels still exceeded acceptable limits.

Mel Acres sued HUI for trespass, nuisance and negligence. Mel Acres alleged that it suffered permanent damage, measured by loss in market value of the property. The jury found that HUI did not create a permanent nuisance on the property or commit trespass, but found that HUI's negligence proximately caused "the occurrence or injury in question" and assessed $349,312.50 as the difference in market value of the property before and after "the occurrence." The trial court signed a final judgment awarding Mel Acres $349,312.50 in actual damages, pre-judgment interest of $42,965.45, court costs of $14,711.65, and post-judgment interest. HUI appealed.

HUI contended that the evidence was insufficient to prove that HUI caused permanent injury to Mel Acres' property or any reduction in Mel Acres' property value.

Mel Acres had disavowed any claim for temporary damages and sought only permanent damages—measured by diminution in market value as a result of contamination. When property is permanently damaged, the appropriate measure of damages is lost market value.

HUI claimed that it caused, at most, temporary injury to the large pond on Mel Acres property, which was alleviated within weeks of its occurrence. It argued that Mel Acres presented no evidence HUI caused permanent injury.

According to Mel Acres, it proved that HUI permanently injured the large pond. Alternatively, Mel Acres suggested that, even if the contamination were temporary, it nevertheless suffered permanent damage because even the temporary contamination created a permanent stigma on the property, resulting in lost market value.

The appellate court agreed that Mel Acres did not have to prove permanent damage, because it was able to prove lost market value by virtue of a permanent stigma created by the temporary contamination.

HUI argued that such stigma damage is precluded under Texas law. However, HUI did not cite any Texas authority precluding recovery of lost market value due to stigma.

The appellate court relied on non-environmental contamination damage cases to hold that it is allowable to recover stigma damages from a remediated physical injury to real estate (for example, property that suffered a flood, a property that was defectively constructed, or a repaired foundation). It also relied on non-Texas cases that awarded permanent stigma damages caused by remediated damage. It reasoned that if recovery were precluded even when lost market value results from a stigma remaining after remediation of physical contamination, Mel Acres would have no recourse for such a loss. Accordingly, Mel Acres could recover lost market value due to stigma, as a form of permanent damage, when the evidence shows the stigma resulted from a physical injury.

The appellate court reviewed the appraisal expert testimony of the parties related to the amount of the stigma. Both parties' appraisers confirmed that a remediated contaminated property may suffer a permanent stigma. The court concluded that the evidence was sufficient to support a finding that Mel Acres suffered permanent damage in the form of stigma from temporary contamination. The jury's figure reflected a 15 percent reduction in value due to a permanent stigma. The appellate court affirmed the trial court's judgment.

One judge dissented on the basis that he found the expert appraisal testimony did not support the jury's award and was not reliable to determine the extent of the stigma.

Cured damage can still create stigma, which can result in permanent damage due to lost market value.

Listing Agreement/Protection Period

839 E. 19TH STREET, L.P. V. FRIEDSON, 373 S.W.3D 674 (TEX.APP.-HOUSTON [14TH DIST.] 2012, NO PET. HISTORY TO DATE)

Friedson, a licensed broker and doing business as National Property Income LLC, entered into a listing agreement with an owner of an apartment complex. The listing agreement ended on April 30, 2006, with a "protection period" covering the 90 days after the ending date. Borenstein of 839 E. 19th Street found the Mesa Ridge property in an Internet search and contacted Friedson about the property. Friedson delivered a copy of a title insurance policy, financial information, rent rolls and other due diligence materials to Borenstein. Friedson brokered an offer from 839 E. 19th Street dated April 7, 2006, to purchase the property for $5,800,000. The seller rejected this offer.

After the primary term of the listing agreement with the seller expired, Borenstein contacted Friedson. Friedson entered into a buyer representation agreement with 839 E. 19th Street, covering only the one property owned by the seller. The term of the buyer representation agreement ran from May 9, 2006, through September 29, 2006, with a "protection period" extending for 120 days after the termination of the agreement.

Friedson brokered a second offer from 839 E. 19th Street dated May 30, 2006, to purchase the property for $6,250,000. This offer expired for lack of acceptance by the seller. After the second offer expired, the seller told Friedson that it had decided not to sell the property. Borenstein represented to Friedson that he was no longer interested in purchasing the property or dealing with its owner.

Friedson did not list the prospects to be protected under the buyer representation agreement during the 120-day "protection period." 839 E. 19th Street placed the property under contract with the seller on November 6, 2006, which was during the 120-day "protection period." The seller sold the property to 839 E. 19th Street for $6,350,000.00.

Friedson did not receive a commission. He fixed a broker lien on the property and filed suit. The trial court awarded judgment to Friedson based on a breach of the buyer representation agreement.

The Court of Appeals reversed. It noted that the buyer representation agreement began on May 9, 2006 and that the protection period applied only to property called to the client's attention during the agreement, namely, between May 9 and September 9 of that year.

Friedson had called the property to the client's attention in April 2006, so the broker had not satisfied the terms of the protection period for it to apply in this case.

Brokers should specifically list any prospects known (clients or properties, as applicable) under protection period provisions of listing or buyer representative agreements, especially if there has been contact prior to the date the listing or buyer representative agreement is signed.

Mold!

ARLINGTON HOME INC. V. PEEK ENVIRONMENTAL CONSULTANTS, INC., 361 S.W.3D 773 (TEX. APP. –HOUSTON [14TH DIST.] 2012)

A buyer brought a cause of action against a real estate broker and a mold assessment consultant for negligence, negligent misrepresentation, and deceptive trade practices. He also brought action against the broker for breach of fiduciary duty after discovering the home contained mold.

The broker, acting on behalf of the buyer, hired a licensed mold assessor to evaluate the property prior to the acquisition. The property was reported to have previous water damage and mold. The licensed mold inspector found no mold on the property at all. There were parts of the property that mold inspector could not access. The buyer subsequently acquired the property, and several months later filed suit because they found a significant presence of mold on the property when the buyer started to remodel the house.

At the time he was hired, the inspector set out the scope of his work in his contract for his services. The house was much bigger than the inspector originally anticipated, but the inspector continued to inspect the property in accordance with the scope he had set out in the contract for his services.

The buyer sued the inspector and the broker for DTPA violations and negligence. The buyer did not sue the inspector for breach of contract.

The jury found that the broker had not breached his fiduciary duty, noting that it was uncontroverted that the mold assessor's lab results showed no evidence of mold whatsoever, and the broker merely transmitted the report to the buyer and therefore had no responsibility for the contents of the report, nor the veracity thereof. The jury found the inspector was 60% negligent in causing the damage and that the owner was 40% negligent.

The trial judge reversed the jury verdict against the mold assessor by granting a judgment notwithstanding the verdict, holding that the mold assessor's lab results spoke for themselves (the house had no mold at the time it was inspected), and the jury erred in finding damages against the mold assessor.

It may be important to note that during the trial, the mold assessor testified that the mold must have been brought in by the buyers in their furniture, clothing, rugs, etc., because there was clearly no evidence of mold during the inspection period.

On appeal, the court held that the JNOV was proper even though the seller had some experts who testified that mold must had been present in the house at the time of the inspection because of the extent of the mold. Given the scope of work, the court said that the evidence was not sufficient to show that the inspector's report was wrong. Under the facts of this case, the court held that the buyer could not ignore its breach of contract claims and try to pursue a negligence or DTPA claim.

A broker who merely transmits a mold report to a buyer is not responsible for the truth of the contents of the report.

Inspectors are Professional for Purposes of DTPA

RETHERFORD V. CASTRO, TEX. APP. – WACO, JAN. 4, 2012

In March 2008, an inspector licensed by TREC inspected a home for buyers who were under contract to buy the home. The inspector noted in the "Roof Structure and Attic" section of the inspection report that it was "Not Functioning or in Need of Repair," because there was water damage in the attic, and he observed that there was water damage in two rooms of the house. He believed that the water damage was caused by condensation from the metal roof resulting from a lack of ventilation. He indicated that the water damage was not a serious issue. In the report, he gave advice on how to fix the ventilation issues in the attic.

He noted that the roof covering was inspected but stated "No problems were noted." The buyers closed on the purchase of the house "as is."

During a rainstorm in October 2008 water started running down the wall of the home in the same place where the water damage was noted on the inspection report. After investigating the matter, the buyers found problems with the roof. A few months later, they repaired the roof but could not afford to replace the roof as was recommended by the roofer. Before making the roof repairs, the buyers engaged who found a number of problems with the roof and opined that the leaks would have been discovered if the first inspector had the necessary experience and knowledge to properly inspect the roof, although he did not know the first inspector or anything about his qualifications.

The person who repaired the roof testified that the black discoloration he observed in the wooden beams in the attic had to have been there for longer than 12 months and that he found approximately 200 screws of varying degrees of looseness on the roof out of approximately 1,500 on the entire roof when his company repaired the roof.

The buyers sued the inspector and alleged violations of the DTPA and a claim for negligent misrepresentation. The trial court entered judgment for the buyers for the cost of the repairs and attorney fees holding that the DTPA applied. The inspector appealed.

The appellate court noted that the DTPA has an exemption for those who render professional services when the essence of that service is based on providing advice, judgment or opinion. A professional service is one that arises "out of acts particular to the individual's specialized vocation. An act is not a professional service merely because it is performed by a professional; rather, it must be necessary for the professional to use his specialized knowledge or training." Not every act of a professional qualifies for an exemption under the DPTA (for example, a misrepresentation of fact, a failure to disclose information, an unconscionable act, or breaches of an expressed warranty are not advice, judgment or opinion).

The appellate court also noted that the professions falling under the DTPA's professional services exemption is not statutorily defined. Generally, lawyers, accountants, and doctors are professionals under this exemption when rendering judgments or opinions. There was no reported case history on the question as to whether a real estate inspector fell under the DTPA's professional services exemption. The court looked at other vocations that have been classified as professions and looked at the history of law that requires home inspectors to be licensed. The court noted that the inspector licensing statute:

- defines a real estate inspection as "a written or oral opinion as to the condition of the improv3-ments to real property…;"
- uses the term "professional inspector;"
- contains a tiered licensing system with specific experience and education requirements, including an apprenticeship; and
- requires the sponsorship of entry level inspectors by professional inspectors.

After looking at the foregoing and other matters generally related to various professions, the court ruled that a professional real estate inspector fits the definition of a professional and qualifies for the exemption under the DTPA when rendering an opinion, judgment or advice.

The court then reviewed whether the conduct in this case involved services that were providing advice, judgment or an opinion. It found that an inspection report is the inspector's opinion as to the condition of the house, as it has been statutorily defined as such.

The court then looked to whether any of the exceptions to the DTPA's professional services exemption applied in this case. The court noted that the buyers complained the inspector was unqualified to inspect a metal roof, that he did not perform the inspection according to TREC rules, he did not inspect the screws on the roof, and he went beyond the scope of the inspection when he gave his opinion as to the cause of the water damage in the attic. The court concluded that this case did not involve a claim under the DTPA but, instead, involved claims for breach of contract and negligence.

The appellate court noted that the trial court's judgment did not refer to the negligent misrepresentation cause of action or contain any conclusions of law regarding the elements to establish recovery on the basis of negligent misrepresentation. Therefore, the court reversed the judgment of the trial court and remanded the case for a new trial on the issue of negligent misrepresentation.

A professional real estate inspector qualifies for exemption under the DTPA when rendering an opinion, judgment or advice. Therefore claims on such matters cannot be brought under the DTPA but must be pursued on grounds of negligence or breach of contract.

Failure to Disclose Prior Termite Infestation and Damage

LAWRENCE V. KINSER, TEX.-APP. – DALLAS, DECEMBER 15, 2011

In the summer of 2006, the Kinsers bought a home from the Lawrences after seeing that the house was for sale when driving through a neighborhood. When the Lawrences showed the Kinsers the home, the sellers discussed the remodeling they had done to the house. The contract price was $125,000. The Kinsers had home and termite inspections completed before the closing. Both the Kinsers and the Lawrences were present at the time of the inspections. The Lawrences disclosed in the seller's disclosure notice that the house had been "sprayed and treated in spring for termite[s]. Outside only." The Lawrences told the broker that it was "for maintenance purposes only." The Kinsers expressed concern and asked the Lawrences if there were any termites or if there had ever been any termites. The Lawrences responded that there had been no termites.

Nine days after closing, the Kinsers found termites. The interior of the home appeared freshly painted. The Kinsers hired a licensed exterminator and termite inspector to perform another inspection. The inspector identified an area where the termites had already eaten the wood. The inspector took pictures, which were admitted at trial. The Kinsers obtained estimates on repairing the termite damage, but they could not afford to make the repairs and decided to move. They rented a place to live and sold the house approximately eight months later for $74,000, a thousand dollars less than they owed on the mortgage.

The Kinsers sued the Lawrences and the first termite inspector. They settled their claim against the inspector. The trial court (bench trial) entered judgment in favor of the Kinsers. The trial court found that the Kinsers were entitled to benefit of the bargain damages, out-of-pocket expenses, mental anguish damages, additional damages permitted by the DTPA, and attorney fees.

On appeal the Lawrences contended that the evidence was insufficient to show they made false material representations or that their acts were a substantial factor in bringing about an injury to the Kinsers. The appellate courted noted that the trial court found the Lawrences committed fraud. It noted that the Lawrences testified that, at the time they filled out the seller's disclosure form, they knew that in 2004 live and dead termites had been found. The Lawrences called a termite company, which advised them to treat the entire house for termites. The termites came back in 2005, and the home was treated again. In 2006, a few months before the sale to the Kinsers, termites appeared again, and the house was treated again. The Lawrences did not disclose any of these treatments. Instead, the seller's disclosure notice stated that the house had been "sprayed and treated in spring for termite[s]. Outside only." It noted that the Lawrences responded "no" to the Kinsers' question as to whether there were any termites or if there had been any termites at the property. The Kinsers testified they would not have closed on the house if they had known the Lawrences

- had seen a swarm of termites outside the house in the spring of 2004,
- hired a to professional treat the house for termites in 2004, and
- experienced a recurrence of termites in 2005 and had a professional come out and treat the house.

The appellate court found this evidence was factually sufficient to support the trial court's determination.

The Lawrences argued that the Kinsers relied on their own professional inspection, which negated any reliance on their misrepresentations or failure to disclose. The appellate court noted that a buyer's independent inspection precludes a showing of causation and reliance if it reveals to the buyer the same information that the seller allegedly failed to disclose.

In this case, there was no evidence that the buyers relied solely on the opinion of their inspector in making their decision to purchase the house. The testimony showed that the Kinsers' decision to buy the property would have been materially affected if the Lawrences had told them about the prior termites. Although it may be true that their inspector's failure to discover the termites inside the house was a producing cause of their damages, there may be more than one producing cause of damages in a case. Had the Lawrences disclosed the termites, the buyers could have had their inspector look more deeply for signs of termite damage. The evidence also showed the Lawrences actively concealed the presence of the termites, making it more difficult for the inspector to discover them. Therefore, the buyer's procurement of an independent inspection did not supersede the seller's actions as a producing cause of damages.

The Lawrences argued the Kinsers failed to present competent evidence to support any damages. The appellate court reviewed the evidence presented at trial related to the damages and the testimony of the parties and others related to the damages, including the evidence related to the Kinsers' damages for mental anguish and attorney fees. It found that the record contained competent evidence of out-of-pocket expenses, loss of fair market value, mental anguish damages and attorney fees. The court affirmed the trial court's judgment.

A buyer's procurement of an independent inspection does not supersede a seller's failure to disclose a condition of the property as a producing cause for damages.