



**Texas Real Estate Commission**

# **MCE Ethics**

**Edition 6.0**



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# Foreword

In cooperation with the Texas Real Estate Commission, the Real Estate Center at Texas A&M University developed this real estate ethics 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.

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When using this course for three hours of Ethics 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

---

The Canons of Professional Ethics — Chapter 1.....	1
The Five Canons.....	1
1. Fidelity (22 TAC §531.1) .....	1
2. Integrity (22 TAC §531.2) .....	1
3. Competence (22 TAC §531.3) .....	1
4. Consumer Information Form 1-1 (22 TAC §531.18) .....	2
5. Discriminatory Practices (22 TAC §531.19).....	2
TREC Complaints .....	2
Complaint Priorities .....	3
Refund to Consumer.....	3
TREC Advisory Letters.....	3
Informal Proceedings .....	3
Temporary Suspension .....	3
Association Complaints.....	3
Citation Program .....	4
Agency Relationships — Chapter 2.....	5
Fiduciary Duties .....	6
Information About Brokerage Services and Agency Disclosure.....	6
Disclosure of Representation .....	6
Intermediary .....	6
Working both sides of one transaction .....	10
Contract Issues — Chapter 3 .....	12
Effective Date.....	12
Paragraph 11 — Special Provisions .....	13
As-Is Clause .....	13
Brokerage Fees.....	13
Poorly Drafted Clauses.....	13
Factual Statements and Business Details .....	14
Multiple Offers .....	14
Deal With Multiple Offers Before You Receive Them .....	14
Don't Let A Little Bird Tell Them.....	14
Defect Disclosure — Chapter 4 .....	15
Seller's Disclosure of Property Condition.....	15
Property Defects.....	15
Disclosure.....	15
Exceptions to the Seller's Disclosure Notice .....	15
Defect Disclosure FAQ .....	16

Advertising — Chapter 5 .....	18
Definition.....	18
Including the Broker’s Name .....	18
Teams .....	18
Assumed Names.....	19
Corporations .....	19
Trade Names.....	19
Signs.....	19
Intellectual Property — Chapter 6 .....	20
Copyright Laws .....	20
Private Industry Association Forms .....	20
Photographs and Music .....	20
Software .....	20
Dispute Resolution — Chapter 7 .....	21
Mediation .....	21
Arbitration .....	21
Unlicensed Assistants — Chapter 8.....	22
Determining Brokerage Activity .....	22
Direct and Indirect Activities .....	23
TREC Cases — Chapter 9 .....	25
Misidentifying a Trust Account.....	25
Not-So-Timely Condominium Documents .....	25
False Promises.....	26
Roof Repairs.....	27
Missing Rent Payments.....	27
Ignoring the Client .....	27





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# The Canons of Professional Ethics

# Chapter 1

Title 22 of the Texas Administrative Code (TAC) Chapter 531 includes five canons of professional ethics and conduct. The canons apply to real estate licensees and are included in the rules of the Texas Real Estate Commission (TREC). Acting as a fiduciary, the real estate licensee must exercise a standard of duty and care when representing a client in a real estate transaction. The licensee must subordinate his or her own interest to the client's interest. The canons also support the Federal Fair Housing Act in forbidding discrimination in real estate activities. These canons are similar in content to general business ethics and common law agency principles from a variety of sources including case law, statutory law and codes of ethics of many professional and trade associations.

## The Five Canons

### 1. Fidelity (22 TAC §531.1)

A licensee represents the interest of his or her client. In performing duties to the client, the licensee must

- make his or her position clear to all parties concerned in a real estate transaction,
- treat other parties to a transaction fairly,
- be faithful and observant to the trust placed in the licensee,
- perform duties scrupulously and meticulously, and
- place no personal interest above the client's interest.

#### Case Study

*The case of Wu v. Rhee, which is summarized in the Legal Update materials, is an example of a case in which the court held the licensee violated his fidelity duties to the client.*

### 2. Integrity (22 TAC §531.2)

A licensee

- has a special obligation to perform his or her responsibilities, and
- must use caution to avoid misrepresentation by acts of commission or omission.

#### CASE STUDY

*The case of Deftenus V. Dallas Bayue Bend, LTD, which is summarized in the Legal Update materials, is an example of a case where a licensee failed to avoid alleged misrepresentations.*

### 3. Competence (22 TAC §531.3)

A licensee

- is knowledgeable as a real estate practitioner,
- is informed on market conditions that affect the real estate business,
- continues his or her education in the intricacies involved in marketing real estate for others,
- stays informed about national, state and local issues and developments in the real estate industry, and
- exercises judgment and skill in the performance of his or her work.

A licensee might ask the following:

- What are my strengths and deficiencies?
- Do I attend classes to improve my services to my clients or customers? How often?
- Which resources are available to help me maintain my competence?
- Do I keep abreast of market conditions in the area in which I practice? How?
- Am I aware of trends in real estate practices? How do I usually find out about these trends?
- Do I read TREC and trade publications? Which ones? How do they help me maintain my competence?

- Can I identify local, state and national issues that are currently under development or consideration?

#### **CASE STUDY**

*The owner of a residential property entered into a property management agreement with a broker. The broker advised the owner to accept a prospective tenant with a City of Houston Section 8 voucher that was less than the rental amount listed for the property. The broker also advised the owner to accept a payment of additional money outside the written lease agreement. The broker then prepared, and the owner signed a lease, which lowered the rent to the voucher amount but increased the security deposit. In addition, the broker prepared a lease addendum cited "past due" although the rents were not past due. Finally, the broker advised the owner in an e-mail to leave her belongings in the house and let the Section 8 inspector mistakenly think that the personal property belonged to the prospective tenant. Although the owner eventually terminated the listing agreement with the broker and found a new tenant, the owner filed a complaint with TREC.*

*Result: The broker entered into an agreed order with TREC admitting that she failed to be knowledgeable as a real estate brokerage practitioner in violation of §531.3 of the TREC Rules, and acted negligently or incompetently in her role as an agent for the owner in violation of Tex. Occ. Code §1101.652(b)(1). TREC reprimanded the broker, assessed an administrative penalty of \$500, and ordered the broker to take 30 classroom hours in a property management course.*

#### **4. Consumer Information Form 1-1 (22 TAC §531.18)**

Each active real estate broker or real estate inspector licensed by TREC must display Consumer Information Form 1-1 prominently in each place of business that the broker or inspector maintains.

#### **5. Discriminatory Practices (22 TAC §531.19)**

No real estate licensee shall inquire about, respond to or facilitate inquiries about or make a disclosure, which indicates or is intended to indicate any preference, limitation or discrimination based on protected classes. Protected classes include race, color, religion, sex, national origin, ancestry, and familial status. Protected classes also include handicap of an owner, previous or current occupant, potential purchaser, lessor or potential lessee of real property. A handicapped individual includes a person

who had, may have had, has or may have AIDS, HIV-related illnesses or HIV infection as defined by the Centers for Disease Control of the U.S. Public Health Service.

## **TREC Complaints**

A person may file a complaint with TREC against a real estate licensee if the person believes the licensee violated The Real Estate License Act (TRELA). If TREC has jurisdiction over the complaint, it will typically investigate the allegations by interviewing the parties and witnesses and gathering relevant information. After review, TREC's Standards & Enforcement Services (SES) will notify the licensee if it intends to initiate disciplinary proceedings. After a hearing or other settlement procedure, a decision or agreed order will be entered. If the evidence establishes a violation, TREC may impose a reprimand, an administrative penalty, suspension or revocation of the license (either of which may be probated), or any combination of the above.

TREC's SES division received nearly 1,000 complaints related to brokers and salespersons in Fiscal Year 2012 (September 2011 through August 2012). Based on staff impressions, the following is a list of the most frequent issues:

- Leasing/Property Management - Misappropriation, includes misappropriation, commingling, and failure to properly account for money
- Leasing/Property Management - Other, includes general negligence, false promises and referrals
- Broker Supervision - broker's failure to supervise sponsored salespersons
- Salespersons - general negligence, false promises, rebates, improper referrals and earnest money issues.
- Intermediary/IABS - includes failure to disclose, obtain written consent, or provide a form.

In addition, payments made from the Real Estate Recovery Trust Account were at an all-time high in the last fiscal year. Typical trust account payments involve general negligence related to property management, mortgage fraud, and sham investment schemes. There has been a gradual increase in size of the payments made from the fund with more payments reaching the statutory caps of \$50,000 for a single transaction, and \$100,000 for multiple transactions. Pursuant to §1101.655 of TRELA, if TREC makes a payment from the Real Estate Recovery Trust Account to satisfy all or part of a judgment against a licensee, TREC may revoke that license.

## Complaint Priorities

TREC is required to maintain a system to act promptly and efficiently on complaints and must maintain a file on each complaint. TREC gives priority to the investigation of complaints filed by a consumer and an enforcement case resulting from the consumer complaint. TREL A requires that TREC assign priorities and investigate complaints using a risk-based approach based on the

- degree of potential harm to the consumer,
- potential for immediate harm to the consumer,
- overall severity of the allegations and the complaint,
- number of license holders potentially involved in the complaint,
- previous complaint history of the license holder, and
- number of potential violations in the complaint [TREL A §1101.204(h)].

## Refund to Consumer

TREC may order a licensee to pay a refund to a consumer as provided by an agreement resulting from an informal settlement conference or an enforcement order in addition to imposing an administrative penalty, suspension, revocation or other sanction (TREL A §1101.659).

## TREC Advisory Letters

When appropriate, TREC may close a complaint file by issuing an advisory letter to a licensee. This is generally appropriate in more technical matters, when the provision that was violated is new, or when evidentiary or procedural problems exist, such as the unavailability of witnesses. An advisory letter is not formal disciplinary action. Instead, the advisory letter is a notification that there were items revealed in the investigation that do not warrant disciplinary action but, if not corrected, could lead to further complaints and, ultimately, disciplinary action.

## Informal Proceedings

In some cases, once the SES staff establishes that TREC has jurisdiction to open a complaint for an investigation, the Deputy Director of SES may offer a complainant and respondent an opportunity to participate in an alternative dispute resolution process (ADR). This process offers the parties an opportunity to create a satisfactory solution in lieu of an investigation and possibility of a contested case hearing. The

Deputy Director does not have authority to compel a complainant or respondent to participate in the process or to accept a specific agreement to resolve the complaint matter. If an agreement can be reached, it may bring some satisfaction and a voice in the outcome for the complainant. For a respondent, it may save time and allow input into the final result.

If the parties cannot reach an agreement, or if SES does not pursue the ADR process at the outset, the complaint is investigated and reviewed by other staff in SES to determine if there is sufficient evidence to proceed with a contested case hearing against the licensee. TREC is required to adopt procedures governing informal disposition of contested cases. An informal disposition at the contested case level must provide the complainant and the licensee the opportunity to be heard, which is very similar to the ADR process offered in lieu of an investigation. However, the contested case ADR requires the presence of a public member of TREC for a case involving a consumer complaint and at least two TREC staff members with experience in the regulatory area that is the subject of the proceeding (TREL A §1101.660).

## Temporary Suspension

TREC's presiding officer for a case involving a consumer is required to appoint a disciplinary panel, consisting of three TREC members, to determine whether a person's license to practice should be suspended temporarily. If the disciplinary panel determines that the licensee constitutes a threat to the public by continuing to practice, or the licensee constitutes a continuing threat to the public welfare, the panel will temporarily suspend the person's license (TREL A §1101.662).

## Association Complaints

The Associations of Realtors®, the National Association of Real Estate Brokers (NAREB®, Realtists), and other trade associations receive complaints alleging ethics violations against their members. Such complaints can be directed to the local association to which the member belongs. Typically, a grievance panel will conduct an initial review to determine if the complaint alleges a violation of the organization's code of ethics. If there is an alleged ethics violation, a hearing panel will convene to hear testimony and presentation of evidence, decide whether a violation of the association's code of ethics occurred, and order any warranted disciplinary action. Disciplinary action could include

- a reprimand,
- a fine,
- probation,
- suspension of membership,
- revocation of membership, or
- any combination of the above actions.

The panel will advise the parties of any rights to appeal the decision.

## **Citation Program**

The Texas Association of Realtors® (TAR) began a citation policy in January, 2011, to provide an option for faster resolution of ethics complaints. Only complaints related to certain articles (NAR Code of Ethics) qualify for the program. A model citation schedule

lists conduct that is subject to citation. A grievance tribunal determines whether a complaint is subject to citation. If a citation is issued, the respondent is advised that he or she has the right to request a full due process hearing rather than pay the citation fine. Sanctions for an agreed-to citation include fines and education.



# Agency Relationships

## Chapter 2

It is important to keep in mind the difference between a customer and a client.

**Customer:** a person(s) who is not represented by an agent but can receive information and assistance from a licensee. Example: a seller's broker who assists an unrepresented buyer

**Client:** a person(s) whom the licensee has agreed to represent

The example below shows how a seller's agent would treat a buyer — a customer, not a client.

A buyer (customer) might expect some or all of the following services:

- providing the customer information about and showing the customer available properties, disclosing any known property defects,
- preparing any offers for submission,
- assisting in coordination of inspections or surveys, etc.,
- assisting the customer in locating and obtaining

financing, and

- working with all parties to solve problems and facilitate the closing.

The seller's agent is **unable** to provide the following to a buyer (customer):

- advising on how much to offer on a property, if less than the asking price;
- disclosing the amount the seller will take, if less than the asking price;
- informing the customer about the seller's motivation or deadline to sell;
- informing the customer about previous offers;
- advising the customer regarding positions to take during negotiations; or
- disclosing information to the customer that would be detrimental to the seller's negotiating position or that is confidential, unless required by law to disclose.

*If the seller grants specific permission to disclose the foregoing information, the seller's agent may do so. Such permission should be documented!*

## **Fiduciary Duties**

A fiduciary is a person who has a high duty of care for another person, the client. The law requires the fiduciary to place the client's interest ahead of his or her own interest. When a licensee begins to provide agency services to a party, or a party believes that such services are being provided, the fiduciary relationship begins. Fiduciary relationships are common and can involve attorneys, trustees, investment brokers and real estate agents, among others. The principal, or client, is the person with whom the licensee has a fiduciary relationship. Although the licensee's duty is to act in the principal's interest, the licensee owes a duty of honesty and fairness to all parties in the transaction.

## **Information About Brokerage Services and Agency Disclosure**

At the first substantive dialogue with a client or prospect, always provide the Information About Brokerage Services (IABS) statement, which contains the statutory information relating to brokerage services. The statement may appear in any format as long as it is in at least 10-point type [TRELA §1101.558(d)]. TREC publishes a form entitled *Information About Brokerage Services* that most licensees use to comply with the statute.

A substantive dialogue is a meeting or written communication that involves a substantive discussion relating to specific real property. A substantive dialogue does not include a dialogue at an open house or a meeting after the time of the contract. For example, a face-to-face meeting with a prospective client in which you are discussing properties is a substantive dialogue. Written correspondence (including e-mail or other electronic means) about specific properties constitutes a substantive dialogue. A telephone conversation by itself might or might not constitute a meeting that would require providing the form. If a telephone conversation constitutes a substantive dialogue, a prompt delivery of the form should follow.

The *Information About Brokerage Services* statement is not required if the licensee is meeting with a party represented by another licensee. For example, if you are the listing broker and happen to meet a represented buyer, you do not need to provide the form. The Information About Brokerage Services statement also is not required if the transaction is a residential lease

for one year or less and a sale is not being considered. The IABS form published by TREC provides for signatures. The signatures are not required by statute; however, it is prudent to request acknowledgment of the consumer's receipt of the form.

The statute requires that a licensee provide a written disclosure of the IABS. Some licensees attempt to comply with the statutory requirement by providing a link to the disclosure form on the TREC website in e-mail and written correspondence from the licensee to the client or prospect. While there is no case law or disciplinary case that gives safe harbor guidance on whether providing the disclosure by linking to the form is sufficient, the question is whether the licensee can prove that the client or prospect received the disclosure at the appropriate time. As indicated above, while the statute does not require signatures, the purpose of the signature lines on the IABS form approved by TREC is merely to acknowledge that the consumer received the form. Providing a link to the form in and of itself may not be sufficient proof that the consumer actually received the disclosure.

## **Disclosure of Representation**

The Information About Brokerage Services form informs parties only to potential representation and does not disclose the licensee's agency or representation. A licensee representing a party is required to disclose such representation at the first contact with another party to the transaction or another licensee who represents another party to the transaction. Agency disclosure may be oral or in writing. For example, when making an appointment with a listing agent or seller to show a property, a buyer's agent must disclose that he or she represents the buyer. Another example is when the listing agent meets a prospect at an open house or listed property.

## **Intermediary**

Intermediary status was created by statute in 1996 to acknowledge that a broker could be in the position of assisting two principals involved in the same transaction. An intermediary is a broker who is employed to negotiate a transaction between parties and acts as an agent of the parties. A broker who represents the buyer and the seller in the same transaction must act as an intermediary. For a broker to negotiate a transaction for two principals as an intermediary, the broker first must obtain written permission from the parties to act in such capacity, and the agreement must state the source of any expected compensation. When entering

into an agreement with a principal, the agreement may address whether the intermediary relationship is a possibility. To authorize the possibility of an intermediary relationship in a listing agreement or buyer representation agreement, the statute requires that the agreement be in writing and that the following be in bold print (TRELA §1101.651):

- intermediary may not disclose that the seller will accept a price less than the asking price, unless authorized in writing to do so by the seller;
- intermediary may not disclose that the buyer will pay a price greater than the price submitted in a written offer, unless authorized in writing to do so by the buyer;
- intermediary may not disclose confidential information, unless authorized in writing to disclose the information or required to do so by TRELA, a court order, or if the information materially relates to the condition of the property;
- intermediary may not treat a party dishonestly; and
- intermediary may not violate TRELA.

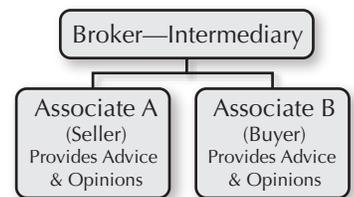
The intermediary may appoint different associated licensees to communicate with and carry out instructions of the respective parties. The appointment of associated licensees requires the written consent of the parties and written notification of appointments to the parties. The appointed licensees must still comply with the requirements listed above. Each appointed licensee may provide opinions and advice to his or her respective party. The intermediary is required to treat both parties fairly and impartially. The appointed licensees are not subject to the intermediary's duty of impartiality. An intermediary is not required to make appointments in every transaction. If no appointments are made, the broker, or any associated licensees, may not provide opinions or advice during negotiations to the party(s). There should be clear company policies regarding appointments. The issue of compensation is a matter of the brokerage's policy and is an internal concern. If appointments are made

- there must be a written authorization from both parties for the broker to act as an intermediary (this could be included in the written buyer representation agreement and the written listing agreement),
- the intermediary may not appoint himself or herself to either party,
- the intermediary cannot make appointments to one party without also making appointments to the other party,

- the intermediary must give written notice to each principal that appointments have been made and identify the respective appointees to the principals, and
- the appointees must keep confidential information confidential.

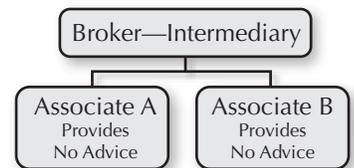
### Example 1

Agent A lists a shopping center. Agent B, working for the same company, comes in with a buyer (client). In this example, the broker's policy in such a situation is to appoint Associate A to the seller and Associate B to the buyer. The intermediary (broker) does not provide any opinions or advice to either party during negotiations. Each associate may provide opinions and advice during negotiations to the parties to whom each is appointed. The intermediary (broker) and the appointed associates remain obligated to comply with the items under TRELA §1101.651(d). All associates in a brokerage act in the role of an intermediary except for those associates who are appointed to the parties.



### Example 2

Assume the same facts as Example 1 except now the broker's policy is not to make appointments. In this example, the associates may not provide opinions or advice during negotiations to the party(s) each is serving. The associates may facilitate the transaction and assist the parties as neutral service providers.

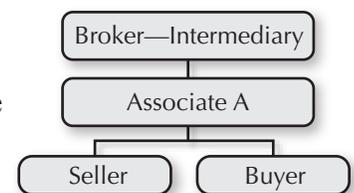


### Example 3

In a multi-agent brokerage, Associate A brings in both the buyer and seller. TRELA permits the broker to select an appropriate course of action in this example.

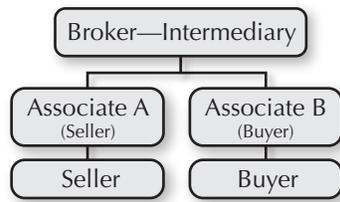
### Alternative 1

The intermediary may choose to make no appointments, in which case the intermediary (broker) and Associate A may not provide opinions or advice to either party during negotiations and remains obligated to comply with the items under TRELA §1101.651(d). Associate A and the intermediary may process or facilitate the transaction.



## Alternative 2

The intermediary may choose to reassign one or both of the parties to another agent. In the following example, the buyer is reassigned to Associate B.



The intermediary (broker) does not provide any opinions or advice to either party during negotiations. Each associate may provide opinions and advice during negotiations to the parties to whom each is appointed. The intermediary (broker) and the appointed associates remain obligated to comply with the items under TRELA §1101.651(d). The broker must have written consent for appointment.

### Example 4

What if the broker is a solo practitioner? May the solo practitioner act as an intermediary?

Yes, but the solo practitioner cannot make appointments of associated licensees. The intermediary (broker) does not provide any opinions or advice to either party during negotiations and remains obligated to comply with the items under TRELA §1101.651(d). No appointments are possible. The intermediary may process or facilitate the transaction.

### Example 5

When a broker owns a small brokerage and actively lists and sells property, may the broker appoint himself or herself to one of the parties? No. The broker shall not appoint himself or herself to one of the parties because the broker would be in two different roles. The broker may choose to make no appointments, and the broker and Associate B would not provide opinions or advice during negotiations. Each could process or facilitate the transaction. Alternatively, the broker could reassign the seller to another agent in the example above and make appointments.

### Example 6

A broker orally agrees to represent a buyer. The buyer now wants to buy one of the broker's listings. The broker must get a written consent from both buyer and seller to act as an intermediary before proceeding, and the written consent must comply with statutory requirements (TRELA §1101.559). One practical solution is to have the broker seek a written buyer representation agreement containing the consent for the broker to act as an intermediary. If the buyer does not agree to give written consent, the broker must advise the buyer that he or she is no longer represented and

that fiduciary duties are owed to the seller under the listing agreement.

I have a listing, and an unrepresented buyer wants to make an offer. Must I act as an intermediary?

No. A broker representing one party (client) to a transaction in which the other party is unrepresented (customer) is not an intermediary. One may assist the buyer and represent the seller in this example. Agents should check with their brokers about this situation as many companies have policies addressing this and other situations.

## Conflicts Arising in Early Termination of Agency Representation

The agency relationship is highly personal. It requires continuing consent of the principal and the agent. At any time, the agency relationship may be terminated by either party; however, an early termination without cause might expose the terminating party to liability under the representation agreement. If an agent continues to offer the property for sale after termination without the consent of the principal, it constitutes a violation of TRELA. Upon receipt of a notice of termination from a principal, the agent should cease acting as the principal's agent. A listing agent should cease all advertising. For example, remove signs, remove MLS listing, remove information from web site, etc.

### Case Study

*In November 2004, the Kims signed an exclusive listing agreement with Ahn, a broker, to sell their gas station (for one year, at \$1.3 million). The listing stated that Ahn would "make reasonable efforts and act diligently to sell the Property." Ahn told the Kims that she would place advertisements about the property in Korean and Chinese weekly newspapers and place the listing on LoopNet.*

*About three or four months before the end of the listing, the Kims informed Ahn that they wanted to terminate the listing. The Kims testified that Ahn agreed and that she would send written confirmation. The Kims called Ahn again and asked for the written confirmation. Ahn informed the Kims that she had told them that she would think about terminating the listing.*

*One of the Kims sent a fax to the broker stating, "I'm terminating our contract which we signed 11-01-04. Even though we signed for one year you agreed to terminate our contract." Ahn did not respond to the fax, but continued to advertise the property although a LoopNet page from September 15, 2005, identified the property as "off the market." Ahn*

*stopped calling the Kims after receiving the fax.*

*On November 15, 2005, the Kims entered into a contract to sell the gas station to buyers who were referred to them by a friend. When Ahn discovered the sale, she filed suit against the Kims for breach of the listing and sought recovery for her broker's fee. The Kims contended that Ahn waived her right to collect a fee and that she had breached the listing by failing to use reasonable efforts in marketing the property.*

*The jury found that Ahn waived the remaining term of the listing. It also found that Ahn failed to comply with a material obligation of the listing. The jury awarded the Kims \$16,500 in attorney's fees, which the trial court reduced to \$14,800.*

*The broker argued that, as a broker, she had the "exclusive authority to determine the best means to market the listing," which would give her discretion to determine the reasonable efforts to market the property. The court noted that whether a party has used "reasonable efforts" to fulfill its contractual duties is usually a question of fact for the jury. In this case, it was not disputed that part of the broker's reasonable efforts obligation was to market the property in newspapers and other media sources. Because the evidence demonstrated that the broker marketed the gas station inaccurately and inconsistently, there was sufficient evidence to support the jury's finding that Ahn failed to use reasonable efforts to market the property. Kim v. Ahn, Court of Appeals of Texas, Houston (1st Dist.), No. 01-11-00231-CV, Oct. 11, 2012*

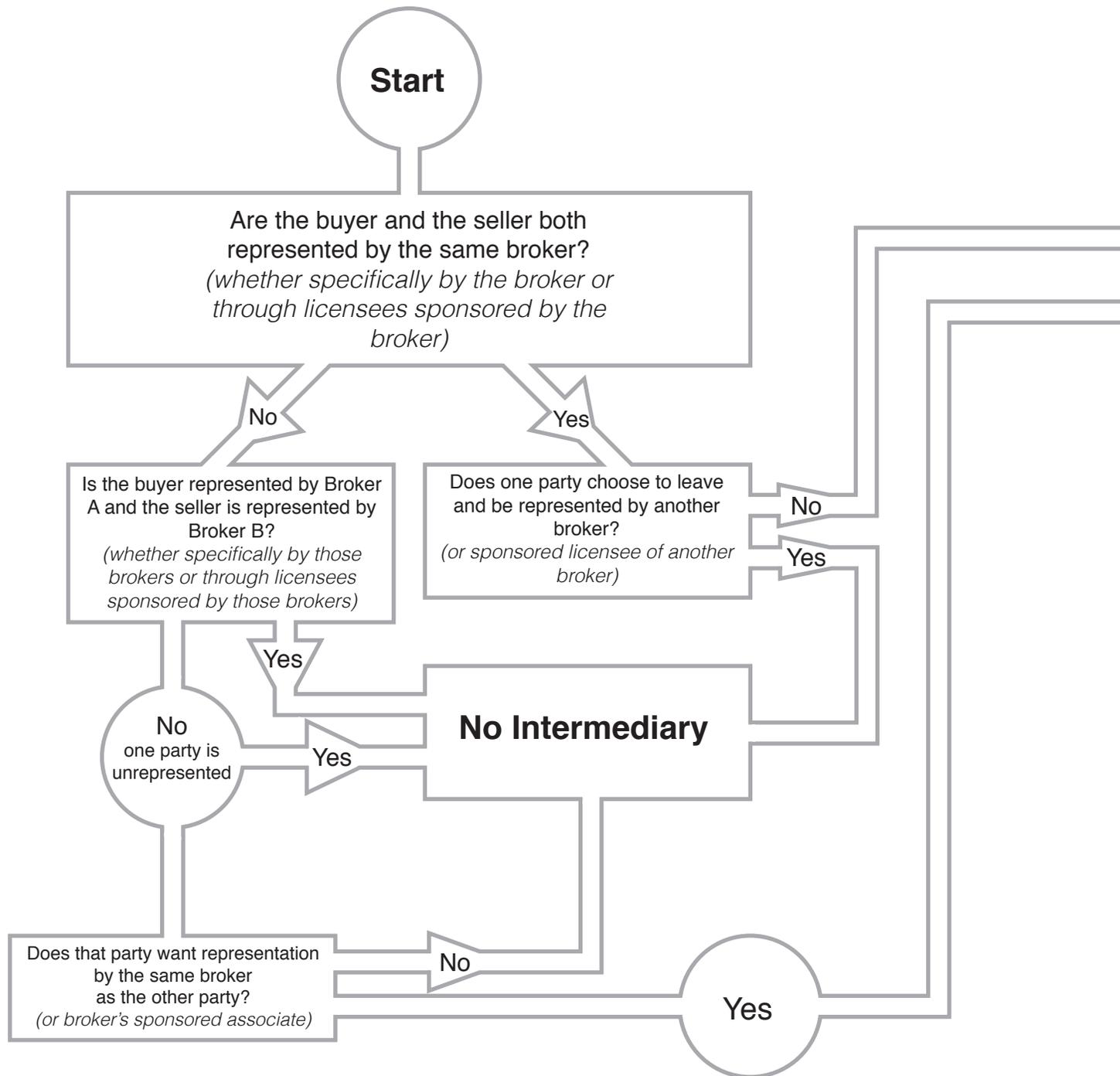
## **Compensation and Release of Contractual Obligation**

Upon early termination of an agency relationship, a broker might be due compensation. At the time of termination, the broker and the principal should resolve the amount of compensation, if any, that might be due. However, the broker may not take actions that, in effect, prohibit the principal from engaging the services of another broker or otherwise buying, selling or leasing the property after termination

## **Parties Subject to Prior Agency Relationship**

If a principal approaches a licensee and informs the licensee that the principal is subject to an existing exclusive agency relationship with another broker, the licensee should not provide any services until confirmation that the prior agency relationship has been terminated. The licensee should not interfere with an existing exclusive agency relationship under any circumstances [TRELA §1101.652 (b)(22)]. For example, the licensee should not suggest to the principal how the existing agency relationship should be terminated.

# Working both sides of one transaction



## Broker is an intermediary

*(represents seller and buyer)*

- Written consent from all parties required
- Written consent must state source of compensation and in **bold** or underlined print, the broker's obligations as intermediary under The Real Estate License Act.

Is the broker a solo practitioner, or does the broker sponsor only one other license?

Yes

No

Does the broker choose to make appointments?

No

Yes

Broker makes no appointments. A sponsored licensee of the broker could act on behalf of the broker as intermediary with no appointments.

**No advice or opinions to the parties allowed.**

Broker appoints sponsored licensees to buyer and seller. Broker may not appoint himself. If broker appoints a sponsored licensee for the seller, he must appoint a different licensee for the buyer and vice versa.

Requires consent of the parties and written notification of the appointments to the parties.

Only appointed licensee can provide advice and opinions to parties.



## Chapter 3

# Contract Issues

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### Effective Date

The effective date is the most crucial date in the contract. It is the date from which most, if not all, performance periods are measured. One of the most significant complaints that many escrow agents make about real estate licensees is that licensees often fail to insert the effective date into the contract.

#### *Who determines the effective date?*

The promulgated contract forms instruct the broker to fill in the final date of acceptance as the effective date. The broker may be either the seller's broker or buyer's broker. It may be prudent for both brokers to confirm the effective date between themselves when communicating final acceptance.

#### *How does a broker determine the effective date?*

The final date of acceptance is the date on which the contract becomes binding between the parties. It is the date that both buyer and seller have agreed to all terms of the contract and have executed the contract.

Four elements must be satisfied for final acceptance to take place. The effective date is the date when the last element (communication back) is made after the other three elements are satisfied.

1. The final contract must be in writing (typically satisfied when negotiations are made using promulgated forms).
2. Both buyer and seller must sign the final contract (including the initialing of any handwritten changes to the initially drafted offer, if applicable).
3. Acceptance must be unequivocal.
4. The last party to accept must communicate acceptance back to the other party (or the other party's agent).

#### *If the effective date is not filled in, does that mean that there is no contract?*

No. By signing the promulgated forms, the parties have mutually instructed the broker to fill in the final date of acceptance as the effective date. He or she may be placed in the precarious position of later

having to determine the effective date of the contract. The final date of acceptance must be resolved by the parties with the assistance of the brokers or, ultimately, a court of law.

### ***When calculating the time for performance, is the effective date included as the first day?***

No. Here is an example. The buyer has the right to terminate the contract within five days after the effective date, and the effective date is January 1. The buyer may terminate the contract at any time until 11:59 p.m. on January 6. Note that January 2 is the first day after the effective date.

### ***Is the effective date Saturday or Monday?***

On Saturday evening, the listing agent notifies the buyer's agent that the seller accepted the offer from the buyer. The seller accepted the offer unequivocally and signed the contract. The buyer's agent informs the listing agent that he will not be able to notify the buyer of the acceptance until Monday. Should the brokers insert Monday as the effective date? No. Under these facts, the elements of final acceptance are satisfied on Saturday.

## **Paragraph 11 — Special Provisions**

TREC contract forms and rules provide that the licensee may insert only factual statements and business details into the contract forms, including special provisions. Inserting a provision that materially affects the legal rights or duties of the parties may move the licensee into the unauthorized practice of law. In the past, licensees might typically insert statements such as “the big screen television and round sofa in the family room is to convey to the buyer.” Recently, TREC adopted (for voluntary use) the Non-Realty Items Addendum. This form is voluntary (because of lender-related issues); however, using the addendum eliminates the need to draft a special provision dealing with personal property items.

### ***Case Study***

*A broker wrote in special provisions, “Both Seller and Purchaser agree that there are items of Personal Property which will be removed from the Property and that all fixtures which are attached to the Property will remain with the Property, said fixtures including, but not limited to fences, working pens, gates, chutes, water well fixtures, and tanks.” The buyer argued that the seller defaulted when the seller failed to remove all the personal property (having left a few items). The seller prevailed because the court noted that the seller substantially complied with the provision and the word*

*“all” did not apply to “personal property” in the special provision [Lewis v. Foxworth, 170 S.W. 3d900 (2005)].*

### ***Case Study***

*In another case, a broker inserted a provision in the Farm and Ranch Contract form, with respect to minerals, that stated, “None of the above are available to be conveyed.” The seller thought he was retaining the minerals. The court concluded that the provision did not reserve the minerals and held for the buyer [Johnson v. Conner; 260 S.W. 3d 575 (2008)]. The Addendum for Oil, Gas and Other Minerals is now promulgated and licensees should provide this form to the parties who wish to negotiate mineral reservations.*

## **As-Is Clause**

The TREC contract forms have an as-is clause; therefore, licensees do not need to attempt to negotiate as-is provisions in the special provisions. More detailed or different as-is clauses should be negotiated through the parties' attorneys.

## **Brokerage Fees**

Paragraph 8 of the contract forms provides that agreements to pay brokers are contained in separate written agreements; therefore, it is prudent for the licensee to address the payment of brokerage fees outside the contract and not in special provisions.

## **Poorly Drafted Clauses**

The following clauses have been inserted into special provisions and should not have originated with licensees. These clauses are vague, incomplete, border on the unauthorized practice of law or are addressed by other promulgated addenda.

- “This contract is subject to a satisfactory appraisal report.” (or inspection report)
- “This contract is subject to the buyer selling buyer's existing home.”
- “Buyer agrees not to require seller to complete any repairs.”
- “Buyer may begin to move-in 3 days before closing.”(or seller to stay after closing)
- “If for some reason buyer cannot obtain financing, the parties will renegotiate owner financing at that time.”
- “Buyer requests seller to paint all exterior doors.”
- “Seller shall provide buyer with an allowance at closing in the amount of \$1,000.00.”
- “Buyer has the right to do inspections and

negotiate repairs, if any, through August 4, 2011 or as soon as the property is vacated. If such negotiations do not result in mutual agreement of the parties, buyer may terminate this contract and his earnest money will be refunded.” (This provision was drafted because the seller did not intend to vacate until about 10 days after the option period expired. The house was full of boxes and other items that blocked many of the walls and floors. The buyer wanted the right to review and terminate after he saw the house vacant.)

## Factual Statements and Business Details

A factual statement is a statement that can be verified as true. It is not a provision under which the parties agree to perform some obligations. A business detail is more of an accounting term that is used to provide more information helpful to an audit or transaction. Business details are, in essence, footnotes to help the reader to better understand a report. Similarly, the business detail in special provisions of the TREC contract forms should only provide information about the existing obligations of the parties found in other provisions of the contract form. Generally, it is not a place to insert additional provisions without the assistance of an attorney. Matters that may be appropriate for special provisions include, but are not limited to the following:

- disclosure that the licensee is related to one of the parties;
- disclosure that one of the parties is a licensee;
- certain instructions to the title company, such as the buyer purchasing the boundary deletion; or
- provisions that cannot fit into the limited space or line of another provision (for example, if four persons are the sellers).

## Multiple Offers

There are many misconceptions about what a seller must do with an offer. In Texas, the seller usually does not have to do anything. Licensees might argue that

- “...the seller must answer my buyer’s offer first...it came in first...”
- “...the seller must respond to my buyer’s offer, since we presented it in writing...”
- “...the seller must take my buyer’s offer. It was full price...”

Instead, the seller has several choices, which

include

- accept one offer and ignore the others,
- reject all offers, or
- reject one offer and make a counteroffer to that buyer.

## Deal With Multiple Offers Before You Receive Them

As the listing agent, a licensee should discuss multiple offers with the seller before they are received. The licensee and the seller can then decide to take one of the following actions:

- tell *no* other agent there are multiple offers, or
- tell *all* other agents there are multiple offers.

Some sellers and seller’s agents want to propose counteroffers, in writing with initials and signatures, to more than one buyer. This is not good practice. Remember, a counteroffer to a buyer remains open until the buyer rejects it (in writing) or it is withdrawn (in writing) by the person who made it.

Some listing agents want to tell one buyer’s agent (often a friend) in a multiple-offer situation the price and terms it would take so that the buyer’s agent can “get the deal.” Under TREC rules, a duty of fairness is owed to all buyers in the transaction. TREC interprets this to mean that the listing agent in a multiple-offer situation must not place one prospective buyer in a significant negotiating advantage over another buyer.

## Don’t Let A Little Bird Tell Them

Keep in mind that tweeting the exciting news of multiple offers (or posting it to Facebook or similar websites) may have the effect of notifying some agents without informing all agents.



# Defect Disclosure Chapter 4

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## **Seller's Disclosure of Property Condition**

### **Property Defects**

A defect is some irregularity in a surface or a structure of the property that mars its appearance or causes some aspect of the property to weaken or fail. It involves tangible aspects of the property, whether physical appearance or physical structure. A property surface or structure is defective when it is blemished, broken, deficient or imperfect in some physical sense (Coldwell Banker Whiteside v. Ryan Equity, 181 S.W. 3d 879).

### **Disclosure**

A seller of real property in Texas and a real estate broker must disclose to a prospective buyer any known defect in the property. The broker's duty to disclose known defects is the same regardless of whom the broker represents. This duty applies to all types

of property (residential and commercial) [TRELA §1101.652(b)(4)]. The Texas Property Code (§5.008) provides that a seller of residential property consisting of not more than one dwelling unit is to complete a seller's disclosure notice and deliver it to the buyer on or before the effective date of a contract.

### **Exceptions to the Seller's Disclosure Notice**

The requirement to provide the Seller's Disclosure Form does not apply to any transfers

- pursuant to a court order;
- by a trustee in bankruptcy;
- to a mortgagee by a mortgagor or successor in interest;
- by a mortgagee or beneficiary under a deed of trust who has acquired the real property;
- by sale conducted to a power of sale under a deed of trust or a sale pursuant to a court ordered foreclosure or has acquired the real property by deed in lieu of foreclosure;
- by a fiduciary in the course of the administration

- of a decedent's estate, guardianship, conservatorship or trust;
- from one co-owner to one or more co-owners;
- made to a spouse or a person or persons in the initial line of consanguinity of one or more of the transferors;
- between spouses resulting from a decree of dissolution of marriage or a decree of legal separation or from a property settlement agreement incident to such a decree;
- to or from a governmental entity;
- of new residences of not more than one dwelling unit that have not been occupied previously for essential purposes; or
- of real property where the value of any dwelling does not exceed five percent of the value of the property.

## Defect Disclosure FAQ

### ***What if, as a licensee, I learn that there is a defect, but the seller does not want it disclosed?***

Inform the seller that you are obligated by statute to make the disclosure and that an attorney should be consulted if the seller chooses not to disclose the defect.

### ***Why do multiple variations of the seller's disclosure notice exist?***

The seller's disclosure notice statute requires that the seller use the form set out in the statute or a form that is substantially similar containing all of the items in the statutory form. The TREC Seller's Disclosure of Property Condition form is identical to the statutory form. TREC publishes the form as a convenience for brokers, sellers and buyers. Some professional associations also publish seller's disclosure notice forms that comply with the statute and contain additional disclosures that those groups have determined are relevant. Whichever form the seller uses, it must contain all items in and be substantially similar to the statutory form.

### ***Must every seller deliver the seller's disclosure notice to a prospective buyer?***

The seller's disclosure notice statute contains 11 narrow exemptions that most real estate brokers typically will not encounter on a regular basis. The most common exemption is the new home exemption or builder exemption. The next two most common exemptions are the trustee or executor exemption and the foreclosure exemption. Under these exemptions, the following are not required to complete the seller's disclosure notice:

- a builder of a new home,
- a trustee or executor of an estate, and
- a lender after it has foreclosed on a property.

Keep in mind, however, that while these sellers are exempt under Texas Property Code §5.008, they are still required under common law and other statutes to disclose any known defect. It is the mechanism of disclosure, namely the seller's disclosure notice, which is not mandated.

### ***Is a relocation company required to deliver a seller's disclosure notice?***

If the relocation company is the seller, it must deliver the seller's disclosure notice.

### ***Must a seller disclose a previous death at a property?***

The statute provides that neither a seller nor a broker must disclose deaths that occurred by natural causes, suicide, or accidents unrelated to the condition of the property [Texas Property Code §5.008(c)].

### ***Must a seller disclose prior water penetration in a property?***

If the prior water penetration has been cured and any ensuing damage from the prior water penetration has been cured, there is no longer a defect, and the seller would not be obligated to disclose the prior water penetration. However, if the prior water penetration has not been cured or the ensuing damage has not been cured, then such items would be considered defects.

### ***Must a seller or broker disclose to a prospective buyer the fact that a registered sex offender resides in the neighborhood?***

The Code of Criminal Procedures §62.056 provides that neither the owner of a single-family residential property nor real estate agents have a duty to disclose that a nearby resident is a registered sex offender. Texas Government Code §411.088 requires that DPS information about sex offender registrants be made available to the public at no cost over the Internet.

### ***Is an off-site condition considered a defect (for example, roadways, landfills, feed lots, etc.)?***

Generally, an off-site condition is not a defect with the property in question. However, the off-site condition might affect the property. If it affects the property in a physical way, it is possible that the off-site condition could be the source of a defect that has moved onto the property. For example, if a neighboring property contains underground tanks that leak, the contaminant might leak onto the property in question.

***Must the listing broker or the seller provide a copy of a prior inspection report that they may have in their possession?***

The seller and broker have a duty to disclose any known material defects. Possession of a prior inspection report may be evidence of the seller's or broker's knowledge of a known defect. There is no statute or other law that specifically states the prior inspection report must be provided. The question is whether the known material defect, which may be noted in the prior inspection report, has been disclosed. Most risk managers and defense attorneys suggest that the broker or seller provide the prior inspection report to avoid allegations of nondisclosure or mischaracterization of a purported defect.

***May a listing agent instruct a buyer or buyer's agent not to provide a copy of the inspection report the buyer may obtain?***

Yes. However, the instruction is simply a request. If the seller or seller's agent receives a copy of the inspection report, it will be unlikely that they may later disavow any knowledge of the inspection report.

***Case Study***

*A buyer sued a seller for fraud and fraudulent inducement relating to the purchase of a store. Part of the letter of intent required the seller to produce all information in its possession to the buyer; however, the buyer alleged that the seller failed to disclose the declining credit status of the store. The purchase price was \$7,667,000.00 for the property based on the*

*absolute reported net income of \$805,040.00 per year.*

*The seller claimed there was an "as is" provision and a merger clause, which prohibited the lawsuit, because the buyer agreed to take the property "as is," and the contract for sale specifically provided that there were no other agreements outside the contract.*

*The jury found that the seller committed fraud against the buyer and awarded damages in the amount of \$3,961,524.60 and additional exemplary damages of \$667,000.00. The judge overruled the jury's verdict.*

*The appellate court defined fraudulent inducement as "a species of fraud that arises only in the context of a contract and requires existence of a contract as part of its proof." A contract is subject to avoidance on the ground that it was induced by fraud (citing Italian Cowboy Partners, Ltd. vs. Prudential Ins. Co. of Am., 341 S.W.3d 323 (Tex. 2011)). In this circumstance, failure to disclose information does not constitute fraud unless there is a duty to disclose the information. The court concluded that the seller had a common law and contractual duty to provide the economic information that was concealed because of the agreement under the letter of intent.*

*The court of appeals sustained the jury's findings on fraud, including the award of the damages, and remanded the case to the trial court with an order to render judgment on the verdict and pay the buyer's attorney fees. Fazio vs. Cypress/GR Houston I, L.P., \_\_\_ S.W.3d \_\_\_ (Tex.App.–Houston [1st Dist.] 2012)*



## Chapter 5

# Advertising

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TRELA §1101.652(b)(23) prohibits a licensee from publishing an advertisement that

- misleads or is likely to deceive the public, tends to create a misleading impression, or
- fails to identify the person causing the advertisement to be published as a licensed broker or agent.

This provision prohibits misleading advertising, and it requires licensees to identify themselves in advertising as a broker or agent.

### Definition

Section 535.154 of the TREC rules clarifies the statutory provision relating to advertisements. The definition of “advertisement” was updated to encompass a broad variety of electronic communications including social networking websites, such as Twitter or Facebook. Real estate information (including a listing), that is on a licensee’s website and behind a firewall or software requiring a password or registration to access the information, is not considered an advertisement.

### Including the Broker’s Name

The rule requires brokers and salespersons to clearly and conspicuously include the broker’s name in all advertising and permits the use of a broker’s assumed name if it has been filed with TREC. A broker must notify TREC within 30 days of starting or stopping the use of an assumed name. Although the rule does not specifically define “clear and conspicuous,” TREC adopted a safe harbor policy statement that it considers the broker’s name to be clear and conspicuous if it is no less than half the font size of the largest telephone number or other contact information in the advertisement.

### Teams

What are the advertising implications when a team or group of licensees in a brokerage firm work together and wish to advertise under a team name? First, the broker must register the team name as the broker’s “assumed name” with TREC. If the team name does

style with a Park, Pavilion, Footbal Athletic Field.  
s of 220 on FM 110 on Stoneland Rd . 512-111-1111

For sale, 100 acre tract with large barn and 4 outbuildings,  
good pasture, fenced crossfenced Call The Duke Team, **Incorrect**  
512-000-000.

10 acres heavily wooded, off Somewhere Rd. \$40,000;  
List C: 2771111111 DR 7987 A

style with a Park, Pavilion, Footbal Athletic Field.  
s of 220 on FM 110 on Stoneland Rd . 512-111-1111

**Correct** For sale, 100 acre tract with large barn and 4 outbuildings,  
good pasture, fenced crossfenced Call The Duke Team,  
512-000-000, Chisum Realty.

10 acres heavily wooded, off Somewhere Rd. \$40,000;  
List C: 2771111111 DR 7987 A

not include the name of a salesperson, the team can advertise using that name. The broker's name does not need to be included in the advertisement, since the assumed name belongs to the broker.

In addition, the advertisement must include the additional designation of "agent," "broker," or trade association name. The "agent" designation is not required after each licensee's name if the advertisement includes more than one name. As always, the sponsoring broker remains responsible for a team's advertising. If the team name includes the name of a salesperson, the rules against implying that the salesperson is responsible for the operations of a brokerage must be considered.

TREC has determined that using names such as the "Sally Salesperson Team" or the "Sam Salesperson Group" do not imply that the salesperson is responsible for operation of a brokerage so long as the advertisement also includes the name or another assumed name of the broker. However, some names such as "Sally Salesperson and Associates" or "Sam Salesperson and Company" do imply that the salesperson is responsible for the operation of a brokerage, even when the broker's name is included in the advertising. Thus, including the broker's name in the advertising does not cure the potential for misleading the public, and so the use of such names is not allowed.

## Assumed Names

Under Section 535.154(e) of the TREC Rules, a broker, individually or as the designated broker of a business entity licensed as a broker, is required to notify TREC in writing within 30 days after the broker or a sponsored salesperson starts or stops using an assumed name in business other than the name in which the person is licensed.

## Corporations

If the salesperson's name is part of the name of a corporation or limited liability company that is registered with the Secretary of State and licensed as a broker, the corporation or LLC may use the salesperson's name in advertising. The name of the designated broker must also be included, because the designated broker is the person responsible for the entity's actions. An unlicensed person's name may be used in advertising only if the name is properly filed as a business, trade or assumed name of a broker with TREC. The advertisement may not suggest the unlicensed person is authorized to engage in real estate brokerage.

## Trade Names

A licensee is prohibited from using a copyrighted trade name in advertising, such as "Realtist" or "Realtor" unless he or she has the authority to use the name. A licensee may use such terms only if he or she is a member of the trade association.

## Signs

The rule requires road signs to include the designation "agent" or "broker" (or a trade association name if a member) in a clear and conspicuous manner. Although proposed at one time, a minimum font size for this designation was not enacted. Instead, TREC adopted a policy stating that it considers the print to be clear and conspicuous if it is no less than half the font size of the largest phone number or other contact information on the road sign. The requirement to include a designation as a broker or agent does not apply to directional signs.

has the right place for you...  
home, land, commercial, lot  
whatever you need - we can help you

**CLICK HERE : CURRENT LISTINGS**

**CLICK HERE : DUKE and his TEAM**

links to the Heart of Texas

- how to sell
- weather
- how to buy
- schools
- why use DUKE
- government
- TREC

the **Duke** TEAM  
512.555.9504  
Deep in the Heart of Texas

***Duke is not the broker for this company.  
What is missing on this website?***



## Chapter 6

# Intellectual Property

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Numerous lawsuits have been filed over copyright infringement against real estate licensees. Brokers and agents, often without malicious intent, use articles from newspapers or magazine to post on their blog or website only to find themselves involved in a lawsuit over protected works. The answer a licensee might give is, “I gave credit to the newspaper for this material in my blog.” This is NOT good enough for copyrighted material. The licensee must have expressed written permission from the creator of the work in order to reproduce the work. The licensee should keep these simple things in mind: any copying of work, whether from a news source, software, photos, music or print material is prohibited without the express written permission from the creator of the work.

### Copyright Laws

Copyright laws apply to blogs, websites and social media postings, as well as printed materials. For example, a licensee wishing to give an opinion about a newspaper article in his or her blog may simply refer to the article by date and placement. The licensee should NOT include the entire article. With regard to

copying only parts of an article, there are some fair use rules in the copyright law. However, there are no specific rules about how many words constitute fair use. These rules depend on the circumstances of use. Copyright FAQs are available at [www.copyright.gov](http://www.copyright.gov).

### Private Industry Association Forms

In general, forms created by private industry associations, such as TAR, may be used only by association members.

### Photographs and Music

Many times photographs and music are copyright protected, also. The licensee should be certain to read all the fine print on websites before downloading files regarding the guarantee that the music or photographs are not copyright protected.

### Software

Use licensed software. A copyright infringement lawsuit will eliminate the money saved by not purchasing a software license.



## Chapter 7

# Dispute Resolution

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### Mediation

In 1987, mediation became one of the statutorily recognized types of Alternative Dispute Resolution (ADR). Texas statutes define a mediation resolution procedure as a forum before an impartial person (the mediator) used to facilitate communication between parties and to promote reconciliation, settlement or understanding. Mediators do not make decisions or give awards. In a successful mediation, the parties agree on a settlement in writing, which becomes binding on both parties. Mediators follow ADR procedures that are included in Chapter 154 of the Texas Civil Practices and Remedies Code. Researchers at the Real Estate Center at Texas A&M University surveyed practitioners and found that mediation has been used to settle a high percentage of disputes. Many Texas judges require court-ordered mediation before hearing a case.

Mediators are neither judges nor arbitrators. They are neutral facilitators in establishing dialogue among the parties to reach a settlement. Mediators do not need to be attorneys or hold special licenses

or credentials. There are numerous mediation service providers, such as county supported mediation services, private mediators, university law schools, and professional and trade associations. County or district court clerks usually maintain lists of mediators for their area.

Mediators should possess some knowledge of the subject matter, the outcome of prior cases involving the controversy, recoveries for similar matters in local courts, and ADR procedures. Although mediators should remain neutral, their expertise can provide valuable guidelines for settlement. Mediators may not impose their judgment on the issues.

### Arbitration

Texas statutes define arbitration as a forum where parties and counsel present their positions before an impartial third party who renders a specific award. The parties must agree in writing to arbitrate a dispute. There are numerous arbitration providers, such as the American Arbitration Association, private

attorneys, private arbitrators, and professional and trade associations. Typically, the arbitration procedure calls for a complaint or petition to be filed describing the dispute. The respondent will be given the opportunity to respond. A hearing is convened at which the parties present evidence and make arguments.

The arbitrator(s) renders an award. The prevailing party may seek to enforce the award as a judgment by requesting that a court of law do so. Arbitration awards may be appealed on procedural or due process grounds.



## Chapter 8

# Unlicensed Assistants

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Brokers and salespersons often hire assistants to do the more mundane work related to running a business or to assist with property management activities. Sometimes the assistants are licensed, but often they are not. This chapter addresses the kinds of activities that may and may not be conducted legally by unlicensed assistants.

### **Determining Brokerage Activity**

The first thing to determine is whether the activity is considered “real estate brokerage” and whether it is done “for another” person with the intention of collecting a fee or something of value. An unlicensed person whose neighbor has been transferred out of state may find a tenant and collect rent for the neighbor’s house so long as the person does not get paid for help-

ing out. On the other hand, if an unlicensed neighbor helps find a tenant, collects rent and then pays himself a “finder’s fee” before sending the rent to the owner, the neighbor needs to be licensed. If the activity is considered real estate brokerage and the person earns anything of value for doing it, a license is required.

## **Direct and Indirect Activities**

The types of activities requiring a license may be placed into two categories. The first category includes those activities in which a person directly helps another buy, sell or lease real property. These activities, such as negotiating a listing agreement with a property owner, spending the afternoon with a couple showing houses for sale, or negotiating a contract to buy real property, obviously require licensure. These “direct” activities are seldom called into question.

The second category of activities includes what might be referred to as “indirect” activities. Indirect activities are more difficult to classify as to whether a license is required. TREL A requires licensure of those persons who procure or assist in procuring prospects to buy, sell, or lease property, or procuring property to be bought, sold, or leased. While there are many day-to-day activities conducted at a real estate brokerage that do not require a license, it can sometimes be very difficult to decide whether an unlicensed assistant or other employees need to be licensed. The following questions and answers, based on real cases, may help licensees determine where to draw the line.

May an unlicensed person, identified as such, make calls to determine whether persons are interested in buying or selling property, and if so, make an appointment for a licensed agent to talk to them?

No. Often referred to as “telemarketing,” any such activities conducted in Texas must be conducted by a licensee. Section 535.4(e) of the TREC Rules clarifies that all solicitation work must be conducted by licensees.

### ***May an unlicensed person host an open house?***

Yes, but care must be taken that the unlicensed person does not “show” the house to prospective buyers. While §535.4(c) of the Rules makes clear that only licensed salespersons and brokers may show properties, under §535.5(h) a broker may hire an unlicensed assistant to serve as a “host or hostess” at a home offered for sale by the broker. While the Rules do not define “host or hostess,” that person’s role should be limited to greeting or registering visitors, and referring inquiries about the property to a licensee. Clearly, the person should not point out features of the home or

neighborhood to visitors; however, they may distribute flyers or brochures that describe the property.

### ***May unlicensed assistants set appointments to show a listing?***

Yes. Under the same rules stated above, an unlicensed assistant may call a homeowner and schedule an appointment for the broker to bring a potential buyer to see the home.

### ***May an unlicensed assistant drive a buyer to a listing and let the buyer into the home?***

Yes, but care must be taken that the assistant does not “show” the property. The assistant should identify himself or herself as an unlicensed assistant and explain his or her limited role. Any questions that arise regarding the property or the purchase of the property must be directed to a licensee.

### ***May an unlicensed assistant answer the telephone; place “for sale” signs; open a property, accompany inspectors, or place newspaper advertisements as directed by the broker?***

Yes. Section 535.5(g) of the Rules provides that answering the telephone and taking messages do not require a license. Further, §535.5(g) states that an unlicensed assistant, identified to callers as such, may confirm information concerning the size, price and terms of property advertised. The unlicensed person should not give information about properties other than that inquired about, and should refer any requests for information regarding other properties to a licensed agent. For example, the assistant might confirm that a particular property called about has three bedrooms and one bath, as previously advertised; however, the assistant may not attempt to direct the caller to other properties, which instead have two baths. Such questions must be referred to a licensee. The assistant should never attempt to “qualify” the caller in any respect.

General administrative duties such as placing “for sale” signs, unlocking doors, and placing advertisements, which are written by a licensee, can be considered indirect activities for which a person does not need a license to be paid to perform.

### ***Which functions may an unlicensed office manager perform?***

Unlicensed office managers may perform administrative tasks such as training or motivating personnel or any other tasks dealing with office administration and personnel matters. On the other hand, §535.4(d) of the Rules states that an unlicensed person may not direct or supervise agents doing work that requires a license. Therefore, an unlicensed person may not supervise licensed agents in helping others buy, sell or

lease property. They may not review contracts, supervise transactions, or help get contracts to the closing table. These tasks are properly conducted only by licensees.

***Does a bookkeeper for a brokerage firm need to be licensed?***

It depends on the bookkeeper's authority to handle trust funds held by the firm on behalf of clients. TRELA §1101.002(1)(A)(x) requires licensure for a person who controls the acceptance or deposit of rent from a resident of a single-family residential real property unit. Section 535.4(g) of the TREC Rules provides that a person controls the acceptance or deposit of rent if the person has the authority to use the rent to pay for services related to management of the property or has the authority to deposit the rent into a trust account and sign checks or withdraw money from the account. A single family residential property unit includes a single family home or a unit in a condominium, cooperative row-home or townhome. It does not include a duplex, triplex or fourplex unless each unit is individually owned. Thus, if the firm engages in property management of single family units and the bookkeeper can sign checks on the firm's trust accounts or use rent to pay for property management related services, the bookkeeper will need to have a real estate salesperson or broker license.

***May unlicensed assistants assist in arranging financing?***

Mortgage brokers, loan officers, and loan originators are licensed by the Texas Department of Savings and Mortgage Lending (SML), and any questions regarding the requirements for licensure for persons dealing with financing issues should be directed to that agency. According to the SML website, "Individuals previously exempt from licensure may need to be licensed under the Texas SAFE Act."

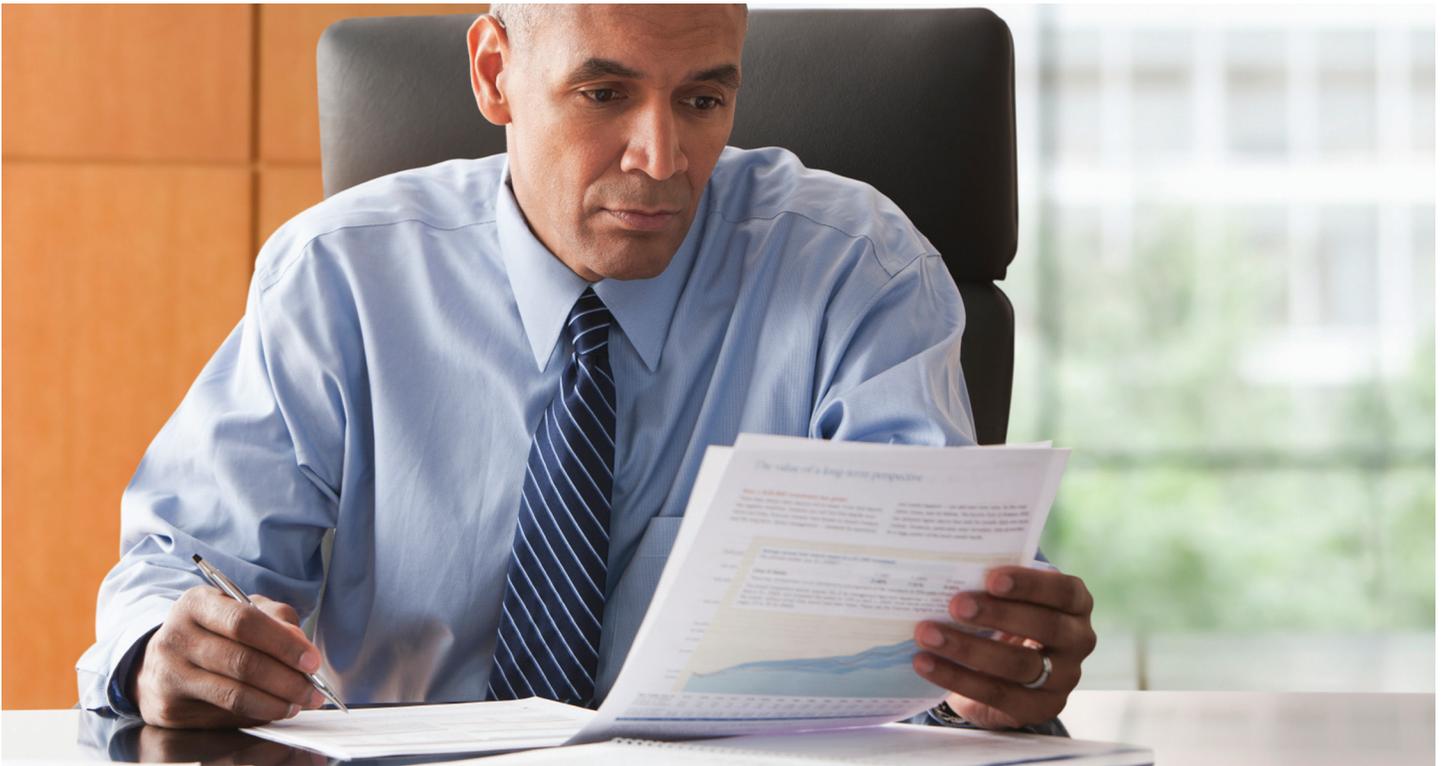
***May unlicensed persons serve as property managers for rental properties?***

Those who manage property for others and for compensation must be licensed if the management activity includes renting or leasing the property for the owner. In addition, TRELA §1101.002(1)(A)(x) requires licensure for a person who "controls" the acceptance or deposit of rent from a resident of a single-family residential real property unit as described above under the question about bookkeepers. Day-to-day upkeep of the property such as arranging for repairs, ongoing maintenance, and rent collection wherein the property manager is merely passing the rent payments on to the owner, does not generally require a license.

Persons acting as on-site managers at apartment complexes are exempt from licensure under TRELA §1101.005(7). Note, however, that this exemption does not apply to onsite management of condominiums or commercial properties if the management activity includes renting or leasing units.

***What can a licensee do to avoid criminal or disciplinary actions?***

The licensee employing the unlicensed assistant should analyze the assistant's job duties to determine whether the assistant is acting with discretion, and whether and to what degree the assistant is "directly" assisting others in buying, selling, or leasing property. Managing brokers might gain some protection from disciplinary action by establishing written guidelines and training for both licensed agents and unlicensed employees.



## Chapter 9

# TREC Cases

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### **Misidentifying a Trust Account**

A broker negotiated a lease between landlord and tenants. The tenants paid the security deposit by check payable to the broker. The broker and his staff failed to deposit the check into the broker's property management security deposit account.

The broker did not discover that the security deposit check had not been deposited until about a year later. The broker maintained two banking accounts for his property management activities, one for security deposits and one for receipt of day-to-day rental payments and disbursements. Neither account, however, was officially labeled as a property management or trust account. Both accounts were styled only in the broker's name. A complaint was filed with TREC related to the broker's handling of the trust account.

Result: The broker entered into an agreed order with TREC admitting that he acted negligently or incompetently, in violation of Tex. Occ. Code §1101.652(b)(1); and failed to clearly identify a trust account as such in

violation of §535.159(h) of the TREC Rules. TREC reprimanded the broker and assessed an administrative penalty of \$1,500.

### **Not-So-Timely Condominium Documents**

A seller listed a condominium unit in MLS with his agent, sponsored by Broker A. The monthly condominium owners' association fee was listed as \$195. The buyers agent, sponsored by Broker B, represented the buyer who was looking for a condominium unit to purchase, with the understanding that the buyer could not afford more than \$200 per month for the condominium owners association fees.

The agents negotiated a sales contract between the seller and the buyer for the property. The contract required the seller to provide the buyer with certain condominium documents and the condominium owners association Resale Certificate within five days after the effective date of the contract. After receipt of the

condominium documents, the buyer had six days to determine if he wanted to proceed with or cancel the contract.

Both agents failed to read or understand the contract terms, particularly those regarding the condominium documents, and both agents failed to ensure that those contract terms were properly addressed in their representation of their respective clients. The buyer never received the condominium documents and did not receive the Resale Certificate until the day of closing. It was not until after closing that the buyer learned that the monthly condominium owners association fee was actually \$323.

While the buyer's agent understood that the seller and seller's agent were responsible for providing the condominium documents and the Resale Certificate, she failed to ensure that the seller and the seller's agent provided these documents timely or sought an extension to the contract for the documents to be provided.

Although the buyer's agent attended closing with the buyer, she failed to review the Settlement Statement and Resale Certificate with the buyer. Had she done so, they would have discovered that the monthly condominium owners associate fee was more than the buyer could afford to pay.

In the transaction, the seller's agent required the buyer to sign a Hold Harmless document or the transaction would not proceed. The Hold Harmless Agreement was not provided or required by the seller.

Result: All four licensees entered into individual agreed orders with TREC admitting that they acted negligently or incompetently, in violation of Tex. Occ. Code §1101.652(b)(1) for the following:

- the brokers for failing to properly supervise the agents with little to no experience handling a condominium transaction,
- the seller's agent for requiring the buyer to sign a Hold Harmless Agreement and failure to timely provide the condominium documents and resale certificate, and
- the buyer's agent for failing to ensure that the buyer timely received the condominium documents and resale certificate and failing to review the documentation with the buyer at closing.

TREC reprimanded all four licensees and assessed administrative penalties against them. The licensees have also settled a related civil suit with the payment of civil damages to the buyer.

## False Promises

The sellers, through Broker A, listed their property in MLS with remarks indicating that the property was approved for a short sale. The potential buyer requested that his own agent, in his capacity as "loss mitigation negotiator," accompany him to a meeting with the seller. The buyer's agent claimed that he did not intend to list the sellers' property for sale by suggesting they terminate their current listing agreement with Broker A. However, both the buyer's agent and the buyer admitted to TREC that the buyer would only make an offer to the sellers if buyer's agent acted as the only agent in the transaction. Apparently the buyer made a verbal offer to purchase the property at the meeting. The buyer's agent and the sellers also executed a Short Sale Negotiation Agreement.

The buyer's agent never listed the property for sale, the buyer never made a written offer to purchase the property, and the sellers eventually removed their property from MLS and did not sell it. The company for which the buyer's agent acted as a loss mitigation negotiator placed a lien on the sellers' property for payment of a fee owed under the Short Sale Negotiation Agreement.

Result: TREC issued an advisory Letter to the buyer's agent regarding the meeting between him, the buyer and the sellers. In the letter, TREC made clear that although short sale negotiators are not subject to TREC's jurisdiction and the agency cannot review the conduct of the buyer's agent related to that matter, TREC was troubled about certain aspects of the meeting.

As the sellers had already obtained short sale approval from the sellers' lender, it is not clear why the sellers would sign the Short Sale Agreement except for the buyer's verbal offer to purchase the property made at the meeting. Any discussion with the sellers should have clearly delineated the purpose or capacity of the buyer's agent in attending the meeting. This may have helped the sellers avoid signing a Short Sale Negotiation Agreement in apparent reliance on the buyer's verbal offer to purchase the property.

The advisory letter advised the buyer's agent that Tex. Occ. Code §1101.652(b)(5) prohibits him from making false promises and §1101.652(b)(6) prohibits him from pursuing a course of misrepresentation through other agents, advertisements or otherwise. In this case, buyer's statements could be attributable to the buyer's agent.

## Roof Repairs

A broker represented a buyer in a condominium purchase. The contract included a seven-day option period. A property inspection was performed the day after the contract was executed. Although the roof was not failing, the report noted that the “roof is aging and will need to be replaced sooner rather than later. Inquire with the HOA (Homeowners’ Association) if there are sufficient funds to provide for replacement costs when the time comes.”

Five days later, the broker submitted to the seller a contract amendment, which included the statement: “Completely replace roof including removing all old shingles and felt and replace any damaged decking.”

The seller agreed to the amendment, although only the HOA and not seller had the authority to perform the repairs. By the time the HOA confirmed that it did not intend to repair the roof before closing, the buyer’s option period had expired, and it cost the buyer \$1449.20 to cancel the contract.

The buyer’s broker and the seller’s agent offered to reduce their commissions by \$3,000 each to defray the cost of the buyer’s reserve when the HOA replaced the roof in the future. The buyer, however, refused to accept the offer.

Result: The buyer’s broker entered into an agreed order with TREC, admitting that she acted negligently or incompetently, in violation of Tex. Occ. Code §1101.652(b)(1). The buyer’s broker was formally reprimanded and paid TREC an administrative penalty of \$1,000. She also agreed to take a 30-hour agency law course.

## Missing Rent Payments

A broker represented a seller under a listing agreement. In the listing agreement, the seller consented to the broker’s acting as an intermediary in the transaction. The broker found a buyer who entered into a sales contract with the seller. The contract provided for \$500 in earnest money. The broker was aware that the buyer did not deposit the earnest money with the title company as agreed in the Sales Contract, and the broker failed to inform the seller of this fact.

The Sales Contract indicated that the broker represented the seller and the buyer as an intermediary, although the broker failed to obtain written consent to act as an intermediary from the buyer.

The Sales Contract provided that closing would occur on a date certain. Due to a financing problem, the parties amended the contract to extend the closing date to several weeks later. The closing did not occur,

and on multiple occasions, the broker continued to request that the seller extend the closing date, citing the buyer’s financing issues. No other amendments were executed, and the sales transaction closed more than two months later.

Without the seller’s knowledge, the broker and the buyer entered a property management agreement for the property two months prior to closing. On the same date and without the seller’s knowledge or consent, the broker leased the property to tenants in the seller’s name. The broker collected money on behalf of the seller; however, he did not account for or remit the rent money to the seller. Shortly after the house was rented, someone told the seller that there appeared to be people living in the house, and the seller received information from the utility company that her account had been closed and re-opened in someone else’s name. The seller came back to Texas, and the broker remitted the rent to the seller at that time.

Result: The broker entered into an agreed order with TREC admitting that he

- acted negligently or incompetently,
- offered to sell or lease real property without the knowledge and consent and of the owner and on terms other than those authorized by the owner, and
- failed to keep the seller informed at all times of significant information applicable to the transaction.

The broker agreed to a probated suspension of his license for a one-year period; he agreed to take a 30-hour agency law course and paid an administrative penalty of \$5,500.

## Ignoring the Client

A broker entered into a Property Management Agreement (PMA) with the property owners, for a one-year term, to lease and manage the property on terms authorized by the owner. There was no rental rate inserted into the PMA. The PMA authorized the broker to collect and deposit rents, security deposits and other funds in a trust account on the owner’s behalf. The broker would receive seven percent of gross monthly rents collected and 30 percent or \$300, whichever is greater, for each new tenant.

Under the PMA, the owner was obligated to confirm ownership of the property and to notify the broker if delinquent on the mortgage, property taxes, insurance or owners association fees. If either party defaulted under the PMA, the other party could make demand with 10 days to cure, then proceed with prescribed legal remedies.

About one month after entering into the PMA with the owner, the broker leased the property to a tenant for \$1550 monthly rent and \$1550 security deposit beginning on the first of the next month. The tenant wanted to move in early, so the broker allowed the tenant to move in around mid-month and collected one half of the month's rent. The broker notified the owner that the property had been leased, but he failed to forward to the owner a copy of the tenant's application, credit report and executed lease.

A few days into the first full month, the owner requested a copy of the lease and requested to be notified by e-mail each month when rents were paid to the broker so that the owner would know when payment could be expected. The broker e-mailed the owner a copy of the executed lease a few days later and indicated the rent check for that month was in the mail.

A week into the second full month, the owner e-mailed the broker to ask why no rent check had been received for that month. The broker informed the owner that tenants said they would be paying toward the end of the month and would include late fees. The owner quickly replied that was not acceptable.

Having lost the copy of the lease e-mailed to him, the owner asked for another copy and instructed the broker to proceed with evicting the tenant for nonpayment of rent. Instead of proceeding, the broker told the owner that the tenant wanted to meet the following week to discuss a few things, so he would not proceed with eviction until after the meeting. As justification, the broker said there was no specific time to begin an eviction and the tenant had previously agreed to incur late fees.

The broker then asked the owner if he had anything to tell the broker before meeting with the tenant, to which the owner said, "no," but then explained he was proceeding with a loan modification on the property and was behind on his association fees.

Halfway into the second full month, with no rent yet received for that month, the owner e-mailed the broker indicating that he would send the eviction notice in three days if no funds were received by then. The broker claimed he would have an answer and a plan by that time. Three days later, the broker met with the tenant and learned that he had inadvertently opened mail addressed to the owner's ex-wife, which notified the owner of the lender's intent to accelerate the debt on the property and foreclose. The broker scanned and e-mailed the letter to the owner. Two days later, the broker notified the owner that the owner was in breach of the PMA since the owner was obligated

to inform him of being behind on the mortgage. The broker then demanded \$910 as the money due the broker from the owner for this breach and further told the owner that until the owner provided proof of paying the debt, the broker would allow the tenant to stay in the property without paying further rent until they could find another place to rent.

The following day, the owner again e-mailed the broker requesting a copy of the lease, noting the broker leased the property at a price not agreed to. The tenant opened a letter not addressed to him and again confirmed that the owner was attempting a loan modification. The owner then noted the tenant had stayed in the property rent free for 25 days and demanded the broker forward the tenant's security deposit and rent along with lease documentation to determine what amount would be due.

With no payment received, the owner delivered a Landlord's Notice to Tenant to Vacate by the end of the second full month. The broker replied by e-mail, accusing the owner of, among other things, losing the lease, not caring who opened the mail, failing to provide information about his debt, and stealing money from the tenant in violation of the law.

Following receipt of this e-mail from the broker, the owner e-mailed the broker to immediately terminate the PMA and sent a letter to the tenant that the broker was no longer the manager while again demanding the rent payment before filing eviction proceedings. The broker then warned the owner that if he saw the property advertised on the MLS for rent with another broker, he would forward a copy of the foreclosure notice as a professional courtesy. The broker also claimed the owner terminated the PMA before the broker was able to regain possession of the property and keys, and the broker acted in the best interests of the tenant and the owner.

The broker never forwarded the second month's rent or the security deposit to the owner. Instead, he returned them to the tenant over the owner's objection. Without receipt of the rent monies and because the tenant moved out, the owner was unable to complete the loan modification process and the property was foreclosed two months later.

Result: The broker entered into an agreed order with TREC admitting that he

- leased the property on terms other than those authorized by the owner;
- engaged in conduct that demonstrates dishonesty, bad faith or untrustworthiness by not following the owner's instructions;

- took action against the interests of the owner;
- disbursed money deposited in a trust account in violation of the owner's escrow instructions; and
- published an unwarranted threat of taking action to prevent the owner from entering into another PMA or listing.

In the agreed order, the broker agreed that he understands that he did not have authority to lease the property on terms not agreed to by the owner and was not

entitled to take action against the owner's interests in returning monies being held in escrow for the owner. The broker further agreed that he understands that he must always look out for the best interest of his client and keep the client fully informed of matters affecting possible decisions to be made by the client in a real estate transaction. The broker agreed to surrender his real estate license and to not reapply for a real estate license for a term of two years.

# Appendix

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## Chapter 1 – The Canons of Professional Ethics

The duties of fidelity, integrity, and competency are aspirational goals expressed in the preamble to the Code of Ethics of the National Association of REALTORS® and the Code of Ethics of the CCIM Institute (Certified Commercial Investment Member).

The Code of Ethics of the National Association of Real Estate Brokers (Realtists) imposes a duty on Realtists to protect the public against misrepresentation, unethical practices or Fraud in their Practices (Part I, §3).

- NAR’s Code of Ethics and the CCIM Code of Ethics prohibit their members from the following:
- Denying equal professional services to any person on the basis of protected class,
- Being a party to any agreement or plan to discriminate on the basis of protected classes,
- Discriminating in their employment practices on the basis of protected classes,
- Volunteering information regarding racial, religious, or ethnic composition of any neighborhood,
- Engaging in any activity that may result in panic selling, and
- Printing or distributing material that indicates any preference or limitation or discrimination based on a protect class (Art. 10).
- CCIM members may provide demographic information when involved in the sale or lease in commercial property if the information is needed to complete the transaction and is obtained from a recognized, reliable, independent, and impartial source (SP10-3).
- Part I, §2 of the Realtist Code of Ethics provides that a Realtist should never be instrumental in establishing, reinforcing or extending restrictions that limit the use or occupancy of property to any racial, religious or national origin groups.

The duty to treat other parties to a transaction honestly is also found in Article 1 of the NAR Code of Ethics and the CCIM Code of Ethics, and is expressed as a theme in the Realtist Code of Ethics.

## Chapter 2 – Agency Relationships

- The duty to disclose who the agent represents at the first contact with the other party in the transaction or the other party’s agent is also expressed in NAR’s and CCIM’s Codes of Ethics (SP 16-10, 11 & 12).

- The NAR and CCIM Codes of Ethics require the members to advise their clients of any potential for the member to represent more than one party in the transaction. This communication is required at the time a listing or buyer representation agreement is signed (SP 1-12 & 13).
- NAR’s and CCIM’s Codes of Ethics prohibit members from selling or acquiring an interest in real estate for themselves, their immediate families, members of their firms, or entities in which they have an ownership interest without making their true position known (Art 4.). Such disclosures must be in writing before signing a contract (SP 4-1). Part I §9 of the Realtist Code of Ethics requires the Realtist to disclose if he or she has a personal interest in the property being purchased.
- NAR’s and CCIM’s Codes of Ethics prohibit the member from receiving any commission, rebate or profit on expenditures without the client’s knowledge and consent (Art 6). Any referral fees received for referring a person to a service provider must be disclosed to the client or customer to whom the recommendation is made.
- The prohibition against receiving compensation from more than one party without the knowledge and consent of all parties is also found in Article 7 of NAR’s and CCIM’s Codes of Ethics and in Part I, §6 of the Realtist Code of Ethics.
- The prohibition against interfering with the agency relationship of another broker is also found in Article 16 of NAR’s and CCIM’s Code of Ethics and Part II, §7 of the Realtist Code of Ethics.

## Chapter 5 – Advertising

- Article 12 of NAR’s and CCIM’s Codes of Ethics require members to: (1) present a true picture in their advertisements; and (2) disclose their professional status (broker, REALTOR®, etc.). The advertising of inducements is permitted if the advertisements clearly state any conditions required to obtain the inducement (SP 12-3). Advertisements of listed property must disclose the firm’s name (SP 12-5).