

# REAL ESTATE

## Ethics



### Iowa Real Estate Seminars

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# Ethics

## *I. Introduction*

**Overview:** Welcome to the study of ethics! In this introductory chapter, you will receive elementary information regarding ethics and its application. Many benefits may be derived from an ethical business practice. Some of these benefits will be highlighted in this chapter.

**Learning objectives:** *As a result of studying this chapter, the agent should learn:*

- ☐ key definitions of ethics.
- ☐ about various ethical philosophies.
- ☐ the flaws of situation ethics.

Note: This course may not be substituted for competent legal advice.

### *What is professional business ethics?*

Ethics is the study of standards of right and wrong. It is that part of science and philosophy dealing with moral conduct, duty, and judgment. It includes the formal or professional rules of right and wrong.

If you were the only person in the world, laws and ethics would not be necessary. Obviously, this is not true and we need laws and ethics to govern our relationship with others.

One aspect of law making focuses on protecting a person's possessions and body from another person. The same could be said for ethics; it is our moral conduct, duty and judgment used when dealing with another person.

### *In this program we will take a view of ethics which says:*

- ☐ a business person should fulfill the law.
- ☐ a business person should go beyond the law in the moral treatment of others.

To be known as a law abiding professional will earn you a reputation of being ethical. In this program we will spend time studying our responsibilities under the law, the law of agency and the common law. The law, however, may only be a "de minimus" of what we should do. To fulfill the law is proper but to go beyond the law may be the better action ethically.

For example: The real estate commission has requested information from your files regarding a complaint. The law specifically gives you a certain period of time to respond. The ethical agent would not only respond with the information requested but would also include any other known details to help the commission resolve the case. The ethical agent would not wait until the last moment possible under the law to submit documents but would respond at the earliest moment possible knowing that the public may suffer less harm with a speedy resolution of the complaint.



## ***Benefits***

There are many benefits derived from professional business ethics.

Such benefits may include:

- ☐ continuance in the real estate business.
- ☐ good reputation.
- ☐ a financially successful career.
- ☐ satisfaction in knowing you've done your best for others.

## ***Continuance in the real estate business.***

It's guaranteed--follow the law and you will not lose your real estate license.

## ***Good Reputation***

It is trite but true. No monetary value can be placed on a good reputation. Years of good reputation bring satisfaction. Also, should a disciplinary action ever arise in which your real estate license is placed in jeopardy, proof of a long and ethical business practice may reduce the penalty invoked by the real estate department. Here is an example:

The licensee was 49 years old, the wife of an insurance executive, and for a number of years had been engaged as a real estate broker in the Gulf Beaches area west of St. Petersburg, Florida, during which time she had enjoyed the confidence of the community as one of its more prominent brokers. She had entered a store to purchase items for a family dinner, it being the day following her son's graduation from the University of Florida and a family celebration was to follow. Another son in the family of the husband had likewise graduated on the same day. She was going through some medical problems and had experienced persistent headaches and emotional problems for some time. She was observed by the manager and assistant manager of the store who saw the broker take a steak from the meat container in the store and subsequently place the steak in her purse. They continued to observe her until she checked out and paid for some other groceries that she had purchased, but not the steak, and started out the front door of the store. After walking out of the store, the manager accosted her and asked her if she had not forgotten to pay for something. She said she did not think that she had forgotten to pay for anything and appeared not to understand what it might have been until she was told what it was, and then she took the steak out of her pocketbook. She was asked to come into the office of the store which she did, and the Madeira Beach police were called. While she was in the office she offered to pay for the steak and the manager told her it was too late. The value of the beef steak was under five (\$5.00) dollars, being valued at something between \$2.58 and \$3.08. She was then taken to the police station. Her arrest became somewhat of a 'cause celebre'. The Florida Real Estate Commission ordered a 60 day suspension of the broker's license.



The court of appeals ordered the return of her license citing a number of her fellow brokers, as well as the



vice president of one of the leading abstract and title insurance companies evidenced her good character and honesty over a number of years.

A good reputation derived from many years of impeccable business practices may minimize incurred penalties resulting from an isolated personal problem.

### ***A Financially Successful and Rewarding Career***

The ethical agent will receive a successful and rewarding career in real estate.

The unethical agent may make more money *initially* than an ethical agent but it will not last. An unethical real estate agent might create immediate windfall profits by:

- ☐ falsifying loan applications.
- ☐ secretly removing contingencies from the buyer's contract.
- ☐ refusing to make necessary repairs which jeopardize the health of tenants.
- ☐ slandering a competitor's product.

And the profits will be great!.... for a short time.

The ethical agent may not realize immediate success but, in time, the profits will build (assuming the agent has product knowledge, sales ability, good time management and the desire to be successful).

The ethical agent will rise above the crowd-- she will be the agent receiving promotions-- he will be the one obtaining the highly desirous management position.

There are exceptions to this rule; the exceptions prove the rule, however.

**Summary:** Ethics is the study of standards of right and wrong dealing with our moral conduct, duty and judgment. This program teaches that the agent should go beyond the law in his duty to be ethical. Being ethical has many benefits, such as: career longevity, reputation building, financial success and satisfaction.

### ***Types of Ethical (Ethics) Systems***

There are three types of ethical (ethics) systems. They are:

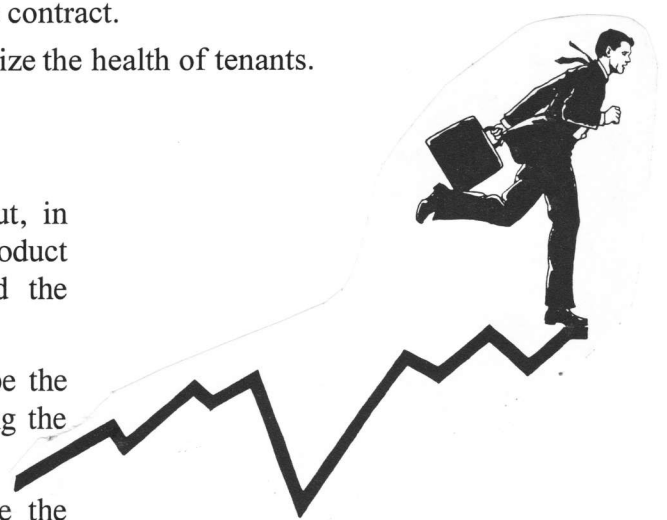
- ✓ 1. Legalism
- ✓ 2. Antinomianism
- ✓ 3. Situationism

#### ***Legalism***

This method of dealing with everyday events and circumstances prescribes certain laws which need to be adhered to. Examples of laws which are to be followed include:

**State and Federal laws**

**The Mosaic Code; the Ten Commandments**



**Company policy and procedure manuals**

**The N.A.R. Code of ethics**

**The Golden Rule**

### ***Antinomianism***

This is the opposite of legalism. It is lawlessness. The person subscribing to this philosophy does not acknowledge any authority, law or sovereign.

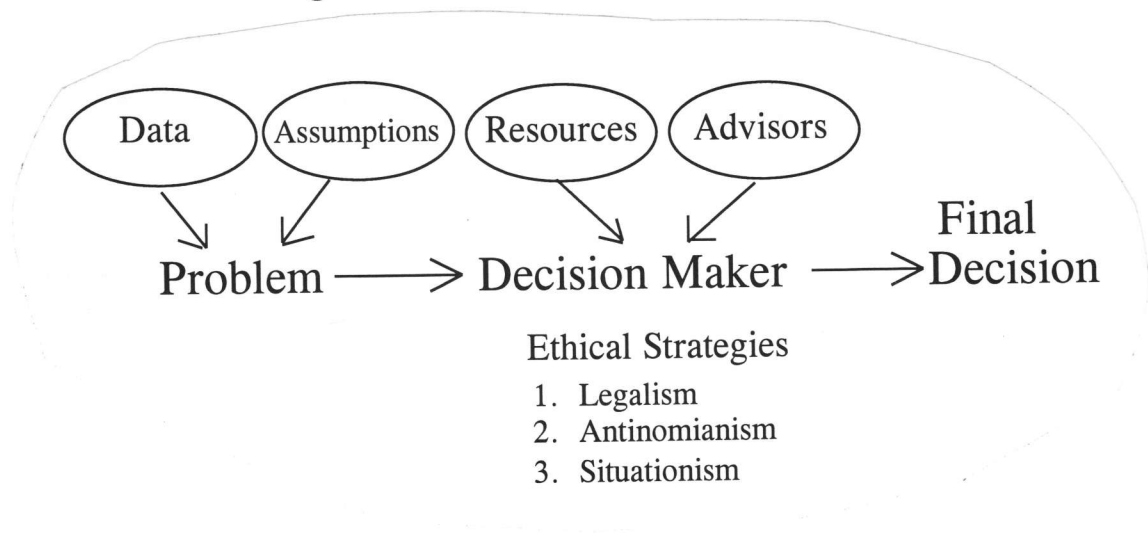
### ***Situationism***

This type of philosophy analyzes each problem or event and allows the individual to decide his response based on the nature of the situation. It differs from antinomianism because sometimes it would be proper to follow the law. It differs from legalism because sometimes it would be proper not to follow the law. It all depends on the situation!

### ***History of ethics***

For an outline showing the history of ethics, turn to the appendix. Here you will see that no small effort has been put into this subject. Observe that men such as Plato and Socrates wrote concerning ethics and its implications. The topic of ethics is ancient and very complex.

### ***Model for ethical decision making***



Once the decision maker possesses all the information regarding the problem or situation, she processes this information. The legalist will make his decision based on a completely different moral standard compared to the antinomianist. The same could be said for the situation ethicist. The final step is the end result or final decision.

## Converting the “decision” into action

But how does one now act in an ethical manner? It is not enough to merely make a decision to act in an ethical manner; one must carry out their decision. How do we implement this decision?

The following quotes restate this very problem. How would you respond?

*“the things I want to do, I don't;  
the things I don't want to do, I do.”* saint Paul

*“The practice of declaring codes of ethics and  
teaching them to managers is not enough to deter unethical conduct.”*

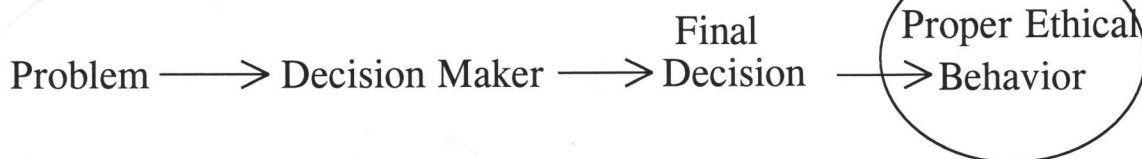
Saul W. Gellerman, University of Dallas School of Management, Harvard Business Review, July/August 1986

This is the dilemma. How do I perform my ethical decision?

To know and understand that something is wrong is the first step to take for making it right. But it is only the first step.

Look again at the decision making process.

There must be a mechanism for doing the right thing. There must be a way to get the final decision transferred from our brain to our hands and our feet.



An evolutionist might say that mankind will eventually get there through natural processes. A Christian might say that such a problem will only be solved by Divine intervention. Another might suggest “will power.” Some propose education.

**Respond:** Once the real estate agent has been able to make a decision regarding ethical behavior, how does she/he carry it out?

### ***Caveat: Situation Ethics***

Situation ethics is the belief that it is sometimes right to do wrong and that the end justifies the means. It teaches that when one chooses the lesser of two evils, the lesser evil now becomes a non-evil. It teaches that it is sometimes right to steal; that it is sometimes right to tell a lie; that it is sometimes proper to break the

law.

Incredible situations are posed by the situation ethicist to prove their philosophy. Here are several examples:

**Example:** Suppose that you work as a clerk in a drug store. Your spouse suffers from a certain ailment which can be cured by a very expensive prescriptive drug shelved in the pharmacy. Your insurance has lapsed and you have no means to purchase this drug. Would it be ethically permissible to steal the drug? The situation ethicist would say that stealing is normally wrong, but, under these circumstances it would not be wrong to steal the drug. (“If I don’t steal the drug, my spouse will die!”)

**Example:** Your wife has indicated that it is time to drive to the hospital as your third child appears anxious to be delivered. The first two children were delivered after a short period of labor; it is predicted that your third child may be born even sooner. Dilemma: should you break the speed limit when driving to the hospital? The situation ethicist would say that it is normally wrong to travel faster than the speed limit, but, under these circumstances it would not be wrong.

**Example:** If a mad and ruthless killer were to pursue a friend of his whom he had hidden in his house and demanded of him to know where his proposed victim was hiding, would he be compelled to tell him he was there? The situation ethicist would say that it is normally wrong to lie but, under these circumstances it would not be wrong to lie.

**Example:** If you torture a certain person to reveal “top secrets” many innocent lives could be saved. The situation ethicist would say it is normally wrong to torture persons, but, under these circumstances it would not be wrong to torture a fellow human being.

**Example:** To kill is wrong, but to murder a tyrant could shorten a war. The situation ethicist would say that it is normally wrong to engage in tyrannicide, but, under these circumstances it would not be wrong to murder.

According to oral tradition, at the turn of the 19th Century, a local Baptist association at Long Run in Jefferson County invited people from far and wide to a log rolling, and as part of the entertainment somebody posed a hypothetical problem of conscience. You are a settler in a frontier community and get wind of an impending Indian raid. When the Indians arrive, they succeed in invading the stockade and in the course of rooting around, they find 3 of your 4 children and destroy them. When they set about making an armistice and withdraw, they ask you the settler, if you have any more children hidden anywhere. Problem: Do you tell the truth or do you lie? They say the debate over this question split that community right down the middle and the original congregation at Long Run is still known locally as the “Non-lying Baptists” whereas the dissidents who removed themselves about 20 miles down the road to Flat Rock and started another congregation are even today known as the “lying Baptists.”

The situation ethicist would say that it is ordinarily wrong to lie but in the situation described above, lying would not be wrong.

In summary, situation ethics says that, depending on the situation, it would be proper to engage in lies, thefts, killings and breaking of promises.

### ***The Flaws of Situation Ethics.***

Situation ethics is a type of self-seeking and self-centered morality. If this belief were to become the norm in our society, the results would be devastating to all businesses, business contracts, and inter-personal relationships.

Imagine a court of law trying to discover the truth. Should a person believing in situation ethics swear under oath to tell the truth, could you believe him? If the end result is that a good friend who has been helpful to the court witness is set free and an innocent person is sent to prison, what good is this "ethic?"

Imagine the real estate industry with situation ethics being the main pillar of ethical thought. An agent would believe it proper to misrepresent the property so that a commission would be paid and he ultimately would be able to finance a better home, vacation, savings account and life style. This would all be done at the expense of the client who may suffer a loss.

Real estate contracts and disclosures might contain truthful or false statements depending on who could best benefit from placing a lie on such documents. Who could be trusted?

### ***Situation Ethics: Predicting the future.***

The situation ethicist is trying to predict the future.

The agent says to herself: "If I tell the truth, I'll certainly get fired; if I lie, I can keep my job-- I think I'll lie!" The agent believing in situation ethics would be trying to predict the future by saying, "I'll certainly get fired!"



Let's suppose this agent tells the truth. Maybe they will be fired but find a better job! Maybe their boss will be so impressed with their honesty, that instead of letting the agent go, the boss gives the agent a promotion! Suppose she decides to lie. Once the boss discovers her nature of prevaricating, job loss is certain. Finding a new job would be difficult understanding the prospective employer's hesitation of hiring a new employee who was recently fired for lying.

Suppose the agent lies, keeps her job, but is found out by other employees. What type of relationship will the other agents have with this agent/what kind of relationship can be built with fellow agents knowing of the agent's propensities to tell lies?

To tell the future is impossible. The present and past are more easily handled. The situation ethicist would spend endless minutes trying to predict the consequences and out-guess them. The situation ethicist would need to be mystic when formulating the outcome. Respond: what do you think would be the best response? Do you agree that it is sometimes correct to shade the truth? How would the situation determine your response to situation ethics?

Read page 28. The CPA was following a new code of ethics which required him to disclose shortfalls in the insurance company's mortgage-portfolio reserves. The CPA was fired. I doubt the CPA will be jobless for any length of time. Ethical professionals are needed in every business. By following his ethical code he has preserved his dignity and the dignity of his profession. To predict his firing and change his results might save his job but his quality of life would be depressing. To place "certified" on falsified documents has got to tear at the heart of any professional CPA.

**Respond:** was it correct for the CPA to be a whistle blower? Maybe no one was financially injured; how would this change your opinion of his actions?

### ***Situation Ethics: Ends and Means***

The person affirming situation ethics believes that the end will justify the means. If a certain result is desired,

a person may use any tactic, scheme or device to attain this desired result. In this “anything goes” philosophy, no person or statement could be trusted.

Contract law establishes that all contracts be acted upon with diligence and good faith. What would happen under contract obligations should situation ethics become the norm?

If the agent has the only goal of earning a lot of money in a short period of time with little or no effort, any law breaking would be moral to achieve this goal. What statute or law would not be in jeopardy? Instead of learning and obeying the law, the agent would engage in the murky process of determining what pleasure is best for him absent any well thinking on behalf of the client, customer or employer.

If the agent swears under oath to give loyalty to her boss and agrees not to abscond with company funds but does so with reservation about absconding with funds, should the agent tell the boss about such reservation?

Suppose you promise a dying friend that you will take care of his children. You make this promise in private. What if other children come along who are more intelligent and talented? The person subscribing to situation ethics might abandon his death bed oath to his friend believing more can be accomplished with the other children.

**What do you think?** “If situation ethics became the norm, every real estate law and regulation would become arbitrary and the agent would try to evade these statutes.”

**Summary:** situation ethics is a belief that it is sometimes right to do wrong and that the end justifies the means. Isolated and incredible problematic scenarios are used to demonstrate its value. The student was challenged to describe their response to some of those situations and to make up their own mind concerning the value of situation ethics.

## **II. The ethical relationship between the agent and the client**

**Overview:** The real estate business is a relationship business. The following chapter will guide you in this relationship with the client as you perform certain fiduciary duties.

**Learning Objectives:** As a result of studying this chapter, the agent will:

- ☐ learn ethical duties pertaining to the clients monetary assets.
- ☐ learn about others who went beyond their legal responsibility to act ethically.
- ☐ understand how certain unethical practices could be detrimental to the client.

### ***The duty not to commingle or convert client funds.***

The ethical real estate agent must be able to give proper accounting of monies accepted on behalf of the client and customer.

#### ***Duty not to commingle***

To commingle or mix one’s money with that of the client is improper and unethical. Such commingling may be the honest mistake of simply depositing the funds into the wrong account or maintaining more of the agent’s funds in the bank



account than necessary to pay the service fee for such account. The agent must use care not to allow commingling of funds.

#### *Duty not to convert*

To convert or embezzle funds is illegal and unethical. Conversion of funds may be *subtle* as when an agent allows the customer's monies to be used to pay bank service fees, or, *blatant* when the agent knowingly uses the customer's money to pay living expenses or business expenses. The ethical agent will be vigilant to prevent any form of conversion of the customer's/client's funds.

#### ***Importance of Fiduciary Accounts***

It is important that funds belonging to other persons be placed into an account which is exempted from judgments which may go against the custodian of that account. (In context here, the agent would be the custodian of the account). Having deposited the money into this fiduciary account (sometimes called an escrow or trust account) the judgment creditor of the custodian is alerted to the fact that this account contains funds not belonging to the custodian of the account. Should a creditor, such as the IRS, attempt to satisfy a judgment against the agent from this account, the court would quash any attempt at taking the client's money from the fiduciary account.

Here's a worst case scenario describing what could happen should a fiduciary account not be maintained.

Otto D. Strucht, real estate agent, has hired the Harvey Wallbanger remodeling team to install a new kitchen into his home. About this same time, Otto collects \$20,000 in earnest money from a buyer which accidentally is deposited into his *personal* account.

Claiming poor workmanship, Strucht refuses to pay Wallbanger for the remodelling job. Wallbanger places a mechanic's lien on the Otto D. Strucht home. Wallbanger takes court action to convert the mechanic's lien into a judgment. The judgment becomes a general lien on all assets owned by agent Strucht in that county. A debtor's exam shows that Strucht has a personal checking account with funds sufficient to satisfy the debt; the court allows a levy on this account. The customer's monies are used to pay the agent's debts! Had the agent deposited the funds into a fiduciary account, the funds would have been protected.

Knowing the advantages of the fiduciary account, the ethical agent will not use this account as a type of asset protection for his/her own money.

The agent will also be quick to correct the mistake of placing funds into an account other than a fiduciary account. In a study to follow, the agent immediately informed the insurance company that a large sum of money had accidentally been placed into his personal account. It was the agent who discovered the problem. It was the agent who made immediate notification to the insurer. It was the agent who immediately corrected

the error. When the state regulatory agency brought action to revoke his insurance license, the court exonerated the agent declaring him worthy of keeping his license: it was the agent who made notification of the mistake and took quick steps to correct the problem once it was known. This agent engaged in ethical practices. We all have propensities for making mistakes; the ethical agent will take care to correct mistakes quickly.

Example (from the insurance industry with application to real estate):

Dorfman entered the insurance field about 1948, and specialized in group coverage, particularly locals of international unions. His



business grew rapidly and by the middle of 1959 he had written over \$100,000,000.00 in premiums and was collecting in excess of \$1,000,000 in premiums per month. In May 1953 Union, through Dorfman, entered into a general agency agreement for group coverage with an insurance company, now named Northeastern Life Insurance Company of New York. The agreement contained typical general agency provisions such as making reports and collecting and transmitting premiums. Union writes approximately 90% of the insurance company's business under that agreement.

One of the group policies contained a provision stating that when any of the assureds were laid off from work they were permitted to make small monthly payments called "layoff premiums" to keep their insurance in force. These payments averaging \$4 to \$5 each, were paid to Union and remitted daily to the company. In May 1954, the company complained about the volume and expense of handling layoff premiums and instructed Union to accumulate them and remit periodically. In the following three years Union collected approximately \$51,461 in layoff funds. None of these funds were remitted to the company until March 11, 1957. At that time a check for \$39,155.33 accompanied by a check list of over 10,000 names of individuals who had paid layoff premiums aggregating that sum was mailed to the company. On June 21, 1957, a check for \$12,306.31 was drawn payable to the company to cover the remainder of the layoff collections, but it was deposited to Dorfman's personal account. Several months later this erroneous deposit was discovered and the amount transmitted to the insurance company. Both checks were drawn on the fiduciary premium account of Union, which had been established in early 1957, and the deposits making up the \$51,461 came from other accounts of Dorfman or Union. The detailed data with respect to the layoff premiums was given and remittances made to the insurance company before an investigation by the Insurance Director, the company or any agency of government.

...While the record shows that layoff premiums were not segregated and were commingled with other funds and that more than 90 days elapsed before remittance of premiums, it also disclosed some other interesting and undisputed facts. All regular premiums (as differentiated from layoff premiums) amounting to more than one million dollars a month were remitted daily. At all times the credit balance due the agency for commissions was far in excess of the layoff premiums held, the excess being over \$100,000 at the time of the hearing. The agency's bank balances always exceeded the aggregate of the layoff premiums, and at the time of the hearing amounted to between \$100,000 and \$130,000.

The handling of the balance of the layoff premiums in the sum of \$12,306.31 by Dorfman does not show an intent to misappropriate or convert the amount to his own use. When one of his employees found that the funds had been deposited to his personal account, Dorfman made immediate arrangements to have that amount sent to the insurance company. The only evidence concerning this transaction was introduced by the Department and consisted of testimony of a bank officer that a mistake had been made by the bank, and the introduction of a letter from the bank to the insurance company admitting its mistake.

....The Insurance company never raised any question about the failure to remit the layoff premiums. Its comptroller testified that it was in large measure due to the company's neglect that the layoff premiums were permitted to accumulate and that Dorfman was the first to call attention to the accumulation. Under these circumstances the elements of fraud are totally lacking and the findings of fraudulent misappropriation and conversion are contrary to the manifest weight of the evidence and cannot be sustained. Nor does the record substantiate the finding that Dorfman failed to demonstrate trustworthiness and competency to transact insurance business in such a manner as to safeguard the public....the findings and order of revocation are not supported by the record, and were clearly arbitrary and capricious and constituted an abuse of discretionary power.



Did Dorfman use good ethics in this situation? Absolutely! The books and records were subjected to the closest scrutiny by teams of investigators for a period of more than a year, yet the only irregularity shown by the record was the retention of the layoff premiums which constituted approximately 1/20 of 1% of total premiums collected for the period. Accurate and detailed records were kept of all transactions of the agency and they were furnished to the company in accordance with the agency agreement. The layoff premiums were remitted daily until the company requested that they be held and sent in only periodically. Dorfman himself called attention to the accumulated funds, took steps to segregate these funds from the other accounts of the agency, and remitted the entire accumulation with detailed data as to the source of the funds shortly thereafter.

As another example, consider agent Gurewitz. Compare the ethical behavior of Dorfman above to the actions of Gurewitz.

#### Gurewitz vs. Kinder

In 1964, Gurewitz began selling package bar and restaurant policies, which resulted in a successful new business for him. Until December 31, 1973, Gurewitz was an agent for the Mission Insurance Company. In 1973, Fireman's approached Gurewitz and agreed to provide a market for his business and to remain "on risk" for three years. Gurewitz became a representative of Fireman's on January 1, 1974. In 1974, Gurewitz began to expand his business to other states. The expansion, however, was beyond his administrative capabilities and he sustained an operating loss that year. After Gurewitz discovered that his funds were not sufficient to pay the premiums to Fireman's in 1974, he sold 85 percent of the stock of some of the corporate licenses to Holding Co., Inc. However, he retained control of the insurance business and the corporate licensees until February 1976.

Gurewitz received an annual salary of \$27,400 for 1973, and \$32,000 for 1974, 1975 and 1976, plus business expenses; all of these were paid out of premium trust fund monies. In addition, Gurewitz borrowed about \$35,000 from the corporate licensees for living expenses, and then repaid the loans in full with interest. The corporate licensees also purchased with premium trust fund monies an automobile and tennis club membership for the use of Gurewitz; these were subsequently sold by the entities for a profit.



An audit by the insurance commissioner's investigative staff determined that as of February 4, 1976, there were deficits in trust accounts of three corporations owned, controlled and directed by Gurewitz in the total amount \$335,356.25. These monies represented premium payments received by Gurewitz on behalf of Fireman's for insurance policies issued by Fireman's. The auditor's report, based on an extensive analysis of the financial records of Gurewitz' corporations, established that the shortages had existed from 1973 to February 1975, and concluded that some of these trust fund diversions were the fault of Gurewitz' use of incoming premium payments from Fireman's policies to satisfy Gurewitz' obligations to Mission. For example, on February 19, 1974, the board of directors of one of Gurewitz' corporations resolved that the corporation would pay Mission the sum of \$455,609.25 in five monthly installments commencing in February 1974 and ending in June 1974.

The capital promised by Holding Co. to Gurewitz did not materialize and Fireman's filed an action against him for unpaid premiums. (Any person who diverts or appropriates fiduciary funds to his own use is guilty of theft and punishable for theft as provided by law). Here the court found that the funds received by Gurewitz as premiums and return premiums on policies of insurance issued by Fireman's were not remitted

to Fireman's, as required by law and were diverted by Gurewitz and never paid back. Gurewitz converted almost one-third of a million dollars. Although Gurewitz has been licensed for 24 years and has had no prior disciplinary record, he has failed to pay back any of the diverted fiduciary funds.

In analyzing the actions of Gurewitz, it could be said that many circumstances contributed to his fall.

It appears his business grew rapidly. Unknown to persons lacking business acumen is the danger of rapid, over expansion. The wise agent will take care to expand at a healthy rate which will not endanger present business. He broke-even in the year he expanded his business;-- *it's easy to go broke breaking even!* The ethical agent must weigh the pro's and con's of business expansion.

At about this time it became less profitable to sell bar/restaurant insurance. It may be inferred that after *Vesely vs. Sager* 486 P 2d 151, that bars and restaurants in certain circumstances became liable to persons injured by inebriated customers and Gurewitz' business of providing insurance for bars and restaurants became less profitable. Over expansion and less profit!-- the double headed monster which ultimately can lead to the demise of any business.



In an attempt to save his insurance licenses, Gurewitz responded that no private citizen was injured by the loss of money. The ethical agent would understand that not only do we have a duty to protect the public but also to protect the insurer. Ultimately, any loss incurred by the insurer will be passed along to the consumer in the form of higher rates. The \$335,356.25 which had been converted to the personal use of Gurewitz had remained unpaid. Even if less money had been lost, it is cause for revocation of license. In *Brown vs. Gordon*, 49 Cal.Rptr.906-907, the court upheld the revocation of a real estate license for conversion of \$420. In *Bohn vs. Satson*, 278 P2d 454, the revocation of a real estate license for conversion of \$55,000 was upheld. These cases demonstrate that it is not always the amount of money which gives rise to license revocation but the action of converting any sum of money to personal uses which is the main reason for concern.

**Summary:** To protect the public, the ethical agent will take all precautions preventing loss of entrusted funds. Duties include: 1) the placement of funds into a fiduciary account. 2) immediate notification should funds be mistakenly placed into the agent's personal account 3) wise business decisions to prevent an untimely business failure and the ultimate loss of customer funds.

### ***Duty not to engage in the unauthorized practice of law.***

The ethical agent will not attempt to practice law for his client.

The practice of law is difficult to define. Perhaps it does not have an exact definition. Attempts to draw boundaries around the practice of law usually result in blurred lines. Some have tried to discourage labeling the practice of law by calling such labeling unwise or improper. Why label something which may later require a change in its definition to better serve future generations?

It would be extremely difficult to formulate an accurate definition of "the practice of law" which might endure, for the reason that under our system of jurisprudence such practice must necessarily change with the ever-changing business and social order. (*Grand Rapids Bar Asso. vs. Denkema*)

Some courts have defined the practice of law as what lawyers do in serving their clients. (*Stern v. State Board of Law Examiners*) In suppressing unauthorized practice, this is scarcely more informative than

defining burglary as what burglars do to their victims. (University of Florida Law Review XXIX p648)

*What harm may result by giving legal advice to my customers?*

There are many dangers when trying to perform a task reserved for a lawyer. An Iowa real estate broker dissuaded a buyer from obtaining an abstract continuation; because of an unknown foreclosure the buyer lost money. In Syester vs. Banta, the customer was urged NOT to use a lawyer. Advising against the use of a lawyer is the unauthorized practice of law. A Sioux City, Iowa broker declared that he was equally capable of drafting deeds and charged \$15 for doing so. It was the practice of law without a license. Even lawyers have in engaged in wrongful practice. In Committee vs. Baker, a lawyer relied on the advise of an insurance person for estate planning strategies rather than personally interviewing the family members desiring such services. In the past, some insurance agents had obtained improper executions on legal forms which caused such forms to become a nullity. One agent practicing estate planning obtained initials on important documents rather than the required signatures. Another agent did not obtain proper acknowledgments of legal forms. Another transferred real property assets into a trust not realizing the potential for loss of homestead protection and termination of title insurance rights. Another agent caused potential problems to an estate by dividing assets "per capita" rather than "per stirpes" as requested by the customers. The ethical agent will require a properly trained and licensed lawyer to practice law for the customer.

The professional real estate agent should never engage in the unauthorized practice of law. Ethics demands the best for our customer. Ethics requires the real estate agent to allow licensed attorneys to practice law for our customers.

### ***III. The ethical relationship between the agent and the agent's competitors.***

**Overview:** Our ethics study now takes on a new relationship: the agent and her relationship to the competitor. To be circumspect in all aspects of practice, the ethical agent must become cognizant of their treatment of competitors. The real estate agent is benefitted by having other professionals in the market place; but this professional turns competitor when vying for certain properties in demand.

**Learning Objectives:** As a result of studying this chapter, the agent:

- ☐ will learn detailed information about slander, libel and defamation.
- ☐ will learn how others have been reprimanded by courts in their words about others.
- ☐ will understand an ethical response to non-compete contracts.
- ☐ will have studied general principles about wrongful interference in another's contracts.

### ***Slander, Libel and Defamation***

The ethical agent will not make malicious statements about a competitor.

### ***Definitions***

**Slander:** the speaking of base and defamatory words tending to prejudice another in his reputation, office,

trade, business, or means of livelihood.

**Libel:** a method of defamation expressed by print, writing, pictures, or signs. In its most general sense any publication that is injurious to the reputation of another. Accusation in writing or printing against the character of a person which affects his reputation, in that it tends to hold him up to ridicule, contempt, shame, disgrace or to degrade him in the estimation of the community, to induce an evil opinion of him in the minds of right-thinking persons, to make him an object of reproach, to diminish his respectability or abridge his comforts, to change his position in society for the worse, to dishonor or discredit him in the estimation of the public, or his friends and acquaintances, or to deprive him of friendly intercourse in society, or cause him to be shunned or avoided...

**Defamation:** the offense of injuring a person's character, fame, or reputation by false and malicious statements; Making, publishing, disseminating, or circulating, directly or indirectly, or aiding, abetting or encouraging the making, publishing, disseminating, or circulating of any oral or written statement or any pamphlet, circular, article or literature which is false, or maliciously critical of or derogatory to the financial condition of any person, and which is calculated to injure such person.



### **He's a crook!**

One of the most common epithets used in the business environment today is the phrase, "He's a Crook!" (from 1 alr 3d, 844-860)

To characterize any person "as a crook" may be actionable slander or defamation. The epithet "he's a crook" may be understood in a double sense: merely as general words of abuse, or as charging the person with having been guilty of the crime of cheating and swindling. The professional saying such words should be warned that courts have issued monetary judgments against the offending party. Using these words against a competitor have been cause for loss or diminution of business market share. Courts may also award actual and punitive damages against the person slandering another.

Here are examples of persons accused of making slanderous statements. Notice the words spoken and the finding of the court.

Case: Texas Plastic, Inc. vs. Roto-Lith, Ltd.

Alleged slanderous statement: *a cheap chiseler and a "crook."*

Additional comments: the plaintiff had been accused of short-counting and short-weighing customers. This was actionable slander.

Case: Pandolfo vs. Bank of Benson

Alleged slanderous statement: *"crooked more people and in more ways than most any fellow we have ever had in this part of the country in a long time."*

Additional comments: such words were held to disgrace the plaintiff.

Case: Ulman vs. Farm, Stock and Home Co.

Alleged slanderous statement: *"precious bunch of crooks" and "as straight as a rail fence and as honest as Ananias."*

Additional comments: such words were held to disgrace the plaintiff.

Case: Weiner vs. Leviton

Alleged slanderous statement: *"You dirty crook, you are the biggest crook on Bedford Avenue."*

Additional comments: the court held that the word "crook" was slanderous per se, stating that the word "crook" seemed to be a colloquialism in this country, and that slang had given it, at least to most minds, a well-understood meaning, namely that a "crook" is one who violates the criminal laws, and the court itself expressed the opinion that the word was synonymous with "a criminal."

Not all words spoken are defaming. The following examples show *no* slander on the part of the speaker.

Case: Eggleston vs. Whitlock

Alleged slanderous statement: *"worst kind of a crook" and that he had swindled a certain person out of a sum of money*

Additional comments: this was not slander since they did not impute the commission of a crime

Case: Gaare vs. Melbostad

Alleged slanderous statement: *"crooked"*

Additional comments: crooked meant "not straightforward or upright in conduct; tricky; perverse; dishonest."

Case: Nelson vs. Rosenberg

Alleged slanderous statement: *"One of the biggest crooks" in the county.*

Additional comments: The word "crook" is ordinarily used to denote a person who has been guilty of some dishonest, wrongful, or deceitful conduct, such as might or might not subject him to criminal prosecution, but it certainly does not of itself express, or with any degree of certainty suggest, the nature of the wrong done, for while it is a term of reproach, it is not a word that clearly charges any particular crime.

Case: Bruno vs. Schukart

Alleged slanderous statement: the defendant stated in a loud voice, *"You're a liar and a crook," and "You're a no-good crook."*

Additional comments: these words were uttered in anger and nothing more could be inferred from them; they were not slanderous under these circumstances.

Case: Pallotta vs. Uhtenwoldt

Alleged slanderous statement: *"You're a dishonest woman; you're a crook and you're a bum."*

Additional comments: these words standing alone would doubtless be slanderous per se. However, the court held that under the circumstances and conditions, the words were not slanderous, and defendant was entitled to judgment, it appearing that sometime previous to the day the alleged slander was uttered, plaintiff had been a tenant of defendant and had moved, owing him rent, and later came to him and offered to pay the amount due, in monthly installments, which proposition the defendant declined to accept and immediately uttered the words complained of. Prior to this occurrence the relations between the parties had always been



cordial.

**Analysis:** to make derogatory statements about a competitor is easy and done on a frequent basis. Making derogatory statements about others can be like a bad habit that won't go away. The student can read for himself that sometimes the speaker of the alleged slanderous statement is held for a judgment and sometimes not held.

**Respond:**

- 1) How would you view the above material on slander, libel and defamation?
- 2) Have you encountered agents who enjoy reducing others by use of slander?
- 3) Is it possible that the public has a lower opinion of our profession compared to other professions because of our unsolicited comments which we have made about our competitors?
- 4) What might be the reaction of our clientele when they hear us slander our competition?
  - A. they will continue to do business with us
  - B. they may refuse to use the services of any real estate agent
  - C. they may become so curious about the slandered competitor that they desire the competitor's services
  - D. they will think more highly of you, the slanderous agent
  - E. they will think more highly of the real estate industry as a whole

**Summary:** To slander, libel or defame a competitor may cause the agent making such statements to sustain a penalty. Not all statements spoken are slanderous. If no damage is done, or if the statement was not made to a competitor, or if the statement was qualified or is an exception to the rules establishing slander, the speaker may be released from penalty under these technicalities. The learner was challenged to make a personal decision regarding ethics and slander, libel and defamation.



Auctioneer

**Duty to honor non-compete contracts**

It is a modern business practice to limit the activities of a former employee to prevent him from competing with his previous employer.

Many such businesses have had such a practice of including "non-compete" clauses in employment contracts. Examples of businesses and professions with restrictive covenants or non-compete clause:

Abstracting  
Accounting  
Advertising  
Architect  
Attorney

Automobile renting

Banking

Beautician

Dentist

Exterminator

Hotel

Insurance

Interior decorating

Launderer

Moving

Optometrist

Pawnbroker

Photographer



Physician; surgeon; hospital

Plumber

Realtor

Shoe repairing

Surveyor

Tailor

Teaching

Ticket office

Undertaker

Veterinarian

Warehouse; Grain sales

Well drilling

Window cleaning

### General Principles

In the absence of any agreement between employer and employee to the contrary, the general rule is that an employee, after his term of service has expired, is entitled to compete in business with his former employer. Accordingly if an employee does not bind himself by contract to refrain from entering the services of a competitor after termination of the employment, the employee violates no duty to his former employer in so doing. Thus, unless restricted by some agreement with his former employer, the employee's right to compete in business with such former employer is the same as that of a stranger to the contract of employment, subject to the qualification that a former employee is precluded from using for his own advantage, and to the

detriment of his former employer, information or trade secrets acquired by or imparted to him in the course of his employment. Aside from this limitation, the employee, after the termination of the contract of employment, may seek the patronage of his former employer's customers; and in so doing he may make use of information which he gained in the course of the employment. (43 ALR 105)

For this reason contracts of employment very frequently contain express provisions which restrict the right of the employee, after the conclusion of the term of service, or the termination of the employment for other reasons, to engage in a business similar to or competitive with that of the employer.

Provisions of this type, which are usually referred to in legal terminology as restrictive covenants not to compete are in most cases limited to a specific area, varying in extent from a small part of a governmental subdivision, such as a town, village, or city, to whole states, countries, or hemispheres. In some instances, no territorial limitation of the restriction is stated at all, while in other cases the restraint may expressly include the whole world. Not infrequently, the prohibited territory is described by circles with a named radius, such as five or ten miles from a certain city, or it may be described by geographical or even imaginary lines, such as all of the state east of the Mississippi, or all the territory west of a line drawn through the city of Detroit. (98 ALR 964)

But how have the courts interpreted such protective/restrictive clauses? Have they strictly enforced them or rendered them unenforceable in certain cases?

Martin vs. Hawley

The restrictive covenant must be limited both as to time and territory. The court said two questions must be answered to determine the validity of such a covenant:

- 1) Is the restraint placed upon the employee, after the employment has ceased, necessary for the protection of the business or good will of the employer?
- 2) Does it impose upon the employee any greater restraint than is reasonably necessary to secure protection for the business of the employer or the good will thereof?

Milwaukee Linen Supply Co. vs. Ring

Contracts in restraint of trade may be held void, being against public interest, because the public should have the benefit of the services and business ability of everybody everywhere.

Wisconsin Ice and Coal Co. vs. Lueth

A restrictive covenant in a contract of employment is illegal if the restraint is greater than is required for the protection of the person for whose benefit it is imposed, or imposes undue hardship upon the person restricted.

By this time, the student should realize that protective or non-compete clauses are not favored by the courts. The question now arises, "How should the ethical agent respond when faced with an employment situation which would violate such job restrictions?"

Here is a hypothetical conversation between an agent and his lawyer. The agent has asked advice of the lawyer and the lawyer instructs the agent concerning his former employment contract.

Lawyer: "I've studied your employment contract and I have some good news."

Agent: "What's the good news?"

Lawyer: "Well, even though your contract says that you agree not to sell real estate in this area for five



years, such contracts are generally unenforceable unless your boss has taught you trade secrets you could not have learned anywhere else PLUS your boss would have to demonstrate that you would cause severe harm to her business.”

Lawyer: “Now isn’t that good news? ....you should be excited!”

Agent: “Yes, but, even though a court of law may not enforce my contract, to demonstrate good ethics I will choose to go beyond the court’s interpretation and abide by my word-- I will not violate my conscience by doing something diametrically opposite what I agreed..... even though I might be exonerated.”



**Respond:** How would you respond to the above conversation? Would you agree with the agent above that your promise is more important than the court’s interpretation of unenforceability? Or, is it more ethical to go by the court’s determination and help *stamp-out* all contracts which may restrict trade?

**Summary:** Almost every industry and profession has used non-compete agreements to protect market share and restrict the activities of a former employee. Courts have generally failed to enforce such non-compete

agreements. The student was challenged to decide for themselves regarding the ethical response to non-compete clauses which will probably be rendered unenforceable.

### ***Duty not to interfere in another’s contracts***

The ethical agent will not interfere in another’s contracts.

When the agent knows that her competitor has listed certain properties it is against state rules and regulations to solicit said listings when the competitor possesses an unexpired, written, exclusive agency or exclusive authorization listing. (This wrongful method of generating business could be called: *Pirating Listings*. “Jump ship and list with me,” the agent says to the seller, “we could have had your property sold months ago!”)

Please notice the limitations above placed on the soliciting agent. These limitations only pertain to exclusive listings. What if the competitor has an open listing; is it unethical to solicit this listing? Yes. The agent should go beyond the law and stay distant from a principal listed under *any* type of listing, even if the listing is other than an exclusive listing.

Recent changes in the law permit the agent to take a “post-dated” listing. When called by the seller, the agent may list property currently listed with another agent, the listing having an effective date after the current listing expiration. The ethical agent will not take the liberty made available by this law; instead, the agent will wait until the present listing is expired to make conversation with the principal.

### **Example**

The Byers Brothers Real Estate Company (Broker 1) received an exclusive agency listing that was irrevocable for thirty days for the sale of a house in Clay County, Missouri. The agreed commission was five percent of the gross amount of the sale.

During Broker 1's 30 day listing, Mr. Campbell (Broker 2) brought a prospective purchaser to the home and he decided to buy it. The owner informed Mr. Campbell that an exclusive listing already existed with Broker 1. The broker admitted that at the time there was little he could do, but after consultation with his superiors returned the next day offering a new sales contract (sales contract, not listing) that would not go into effect until after the thirty day exclusive listing had expired. This, it was said, would prevent the seller from paying a double commission. He assured the seller that he would not get him in trouble and that it would not be necessary to have an attorney examine the contract.

Broker 2 testified that the sellers, upon finding that the prospective purchasers had enough money for the purchase, offered to sell even though that would mean paying a double commission.

The sellers signed a sales agreement with Broker 2 and, shortly after the expiration for the exclusive 30-day listing, gave their deed for the property to the purchaser. The sellers paid a 5 percent sales commission to Suburban Realty Company (Broker 2), but refused to pay any commission to the Byers Brothers Company (Broker 1). Evidence was presented to clearly demonstrate that Broker 1 had expended considerable time, effort, and money to secure a buyer for the property. In fact, a prospective buyer secured by Broker 1 was turned down by the seller even when certain conditions for a sale had been agreed to by the prospective buyer.

The Court of Appeals said:

...when the owner of the property bound by a listing contract conspires with a second broker, who knows that there is a contract of that nature in effect, to contract for the sale of that property within the contract agency time of the first broker and to conceal that fact from the first broker in order to deprive him of the commission to which he is entitled by withholding from him the fact that such sale has been agreed to and in pursuance thereof they carry out their conspiracy, the result is an actionable conspiracy and both the owner and the second broker are liable for the resulting damages.

Is it always safe to solicit a listing and a sale after the competitor's listing has expired?

It is permissible to solicit a listing or sale with the seller after the first broker's listing has expired. There are at least two exceptions however. First, should the first broker have "hold over" or residual rights that may still accrue to him during the protective clause, the allegation of wrongful interference may be claimed. A second exception may apply. It may be unethical for an agent to take advantage of certain situations. The following case study demonstrates this very point.

Harold Thomas was employed by John J. Kaiser Realty as a real estate salesman, and in that capacity secured on August 1, a listing agreement from Gladys Martin, owner of a home. The agreement was to continue for a period of three months ending November 1.

A portion of that agreement specified that, "It is further agreed that you shall be entitled to your commission if the property...is sold within ninety days after the period of this agency to anyone with whom you have negotiated with respect to a sale during the period of this agency and of whom I have notice or knowledge."

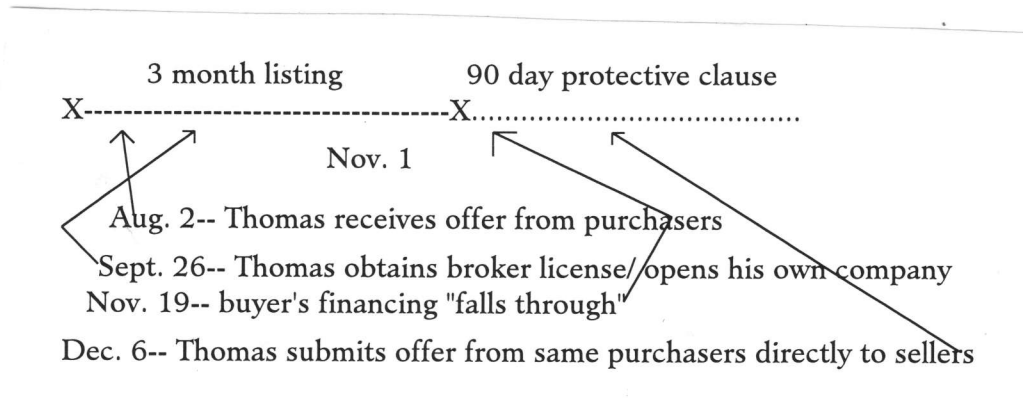
On August 2, Thomas obtained a written offer from Harold McDonald to purchase Mrs. Martin's property. The offer was contingent upon financing.

Around September 26, Harold Thomas obtained his license as a real estate broker. This license allowed him to open his own office and prospect for his own listings.

On November 19, the financing for buyer McDonald was refused.

On December 6, Thomas secured a new offer from this same buyer to purchase Mrs. Martin's property---the same property and the same seller for which his original offer was made---the only difference being that Broker Thomas was no longer employed by Kaiser Realty. The offer was accepted for Mrs. Martin through her daughter and the sale closed about a month later.

The John Kaiser Company charged Thomas of breaching the Ohio Real Estate Commission regulation by having negotiated the sale, exchange, or lease of any real property directly with an owner or lessor knowing that such owner or lessor had a written outstanding contract granting exclusive agency in connection with



such property to another real estate broker.

The Court agreed that the evidence was such that Broker Thomas had directly negotiated the buyer's offer with sellers still having contractual obligations under Broker 1's listing. For this reason, Broker Thomas' license was suspended for 90 days.

**Conclusion:** Even though the active period of the listing had expired, Broker 1 still had rights to a commission under the 90 day protection clause if the property was sold to the buyer with whom the seller had earlier negotiated. Broker 2 had wrongfully interfered with Broker 1's rights.

#### *IV. The ethical relationship between the agent and the customer*

Overview: Our study of ethics ends with this final chapter describing the relationship between the agent and the customer. The real estate profession has come a long way from the early days of caveat emptor to the present day fair treatment regulations mandated by the real estate commission. The agent is again encouraged in this chapter to go beyond the law and give ethical services to the customer.

**Learning objectives: as a result of studying this chapter, the agent will:**

- ☐ know reasons for disclosing all property defects to the customer.
- ☐ know additional items for disclosure which may not be on disclosure forms.
- ☐ know reasons for making speedy repairs as a property manager.

**Disclosure of "material" facts or disclosure of "All" facts about the property.**