

downpayment rather than letting the sellers assume that he has cash.

- ☐ - The broker is responsible for the actions of her/his salespersons.



III. Concealment, Dishonest Dealings and Fraud

In this section you will learn:

- ☐ - what constitutes concealment.
- ☐ - how dishonesty can occur with legal documents.
- ☐ - when advertising is dishonest.
- ☐ - how personal dishonesty affects an agent.
- ☐ - the value of a good reputation.
- ☐ - the reasons for rapidly depositing the buyer's earnest money into trust.

Overview: This chapter warns the licensee against concealment, dishonest dealings and fraud. As these true life scenarios unfold, the student will be reminded of the public harm caused by a broker or salesperson whose business is characterized by such practices.

A. Concealment

Question #9:

Can a licensee receive discipline for activities for which a real estate license is not required?

Answer:

Because of the fiduciary relationship present in real estate transactions, the agent must be of high moral character. Dealings, whether real estate or not, can reflect the licensee's character. If such dealings show bad faith and dishonesty, they may accurately predict how this person may act when in a fiduciary relationship. Such dealings may be used to deny renewal or the granting of a real estate license.

Case Study Answer #9

A broker in Florida had an agreement with another broker to split their commission on sales. The first broker persuaded the other to release him from the contract, and shortly thereafter he was involved in the sale of the piece of property covered under the prior agreement. He collected the full commission for himself and refused to give anything to the other broker. He was charged with "fraud, concealment, dishonest dealing, trick, scheme or device." This was due to the fact that he knew of the sale prior to his breaking the agreement with his colleague. The broker's license was suspended.

Upon appeal, the broker attempted to quash the complaint information filed reasoning the broker was not, at the time the release was obtained, acting as a real estate broker, and that therefore, the Real Estate Commission would not have jurisdiction over the transaction or the complained of act.

The court responded to this appeal argument by stating *Blakeley v. Miller*, 232 Iowa 980, 7 N.W.2d 11:

In the *Blakeley* case, the court commented:

One could think of many good reasons why it would be better to have the actions outside of his conduct in acting as a real estate agent apply to his right to hold a real estate license, but this is for the legislature to say and not for the court to write into the statute.

It is noticeable that our statute obliges an applicant for the license to furnish to the Commission evidence of good moral character...Compare, applicant for

insurance broker's license...It seems inconceivable that the Legislature intended to establish one standard for the issuance of a license and another for its renewal or revocation. The Commission may 'in its discretion' refuse to grant any new license 'upon sufficient cause being shown'...No license shall be issued to any person who has been convicted of certain specified criminal offenses...Those provisions display the broad legislative object and purpose to limit the licensees to reputable, honorable and conscientious persons.

It is therefore in recognition of the indubitable intent of the Legislature that a significant meaning be ascribed to the specifications of [the applicable statute] such as 'any conduct which demonstrates unworthiness, ***bad faith*** being convicted of a crime*** and 'any other conduct, whether of the same or a different character than specified in this section which constitutes fraud or dishonest dealing.

It seems from the examination of the statute that the advantageous object exhibited by its composition was to create and maintain a commission to scrutinize in general and with care the character, competency, and integrity of license applicants and license holders to the end that in the interest of the public welfare, competent, unworthy and unscrupulous persons would be excluded from the real estate brokerage business.

Conclusion:

The real estate professional must exercise honesty and integrity even in private dealings.

Question #10:

Do prospective purchasers need to know of liens on properties?

Answer:

Just as a ship may have barnacles attached to its underparts, a property may have liens attached to its title.

And the price a buyer will pay for a property is related to the number of liens attached to it. Possibly

the most important aspect of a property is its 'Title.' The most important aspect of the title is its condition of liens or encumbrances.

Many precautions are taken to assure the buyer no hidden liens may exist against the property. They include:

- 1) abstract continuations, up-date continuations.
- 2) pre-closing 'last minute' lien searches.
- 3) title insurance and title guarantees.
- 4) attorney's opinions of title.
- 5) mechanic lien waivers.
- 6) inspections of property to determine unrecorded easements, recently completed work, encroachments, and the rights of parties in possession if other than the title holder. All of these things are completed so the buyer will become aware of liens against the property.

Case Study Answer #10

A broker in Florida, during his normal course of business, made representations that certain lots were free from any encumbrances and all liens. Putting their confidence in such information, the prospective buyers agreed to purchase the property. They received from the broker a statement such that the land was free of all liens. However, the buyers soon found out that certain unpaid mortgages were in existence, and that the broker was fully aware of this. A complaint was made, and the broker was charged with misrepresentation, concealment and dishonest dealing.

Such charges were not contested, but the broker appealed to the District Court of Appeal on the basis of a point of law. This court decided that the commission had acted fully within its powers, and the decision to suspend the broker's license was justified.

Conclusion:

Intentionally hiding information about liens and encumbrances is concealment.

Question #11:

What is the broker's responsibility concerning offers on his client's property?

Answer:

The agent must present all offers promptly to the sellers. He may not delay the presentation of offers from buyers working with other brokers simply to present offers from his own buyers first. If he does, the broker is advancing his own interests ahead of his principal's. When acting in a fiduciary capacity, the agent must place the seller in the same good position as the agent to receive information regarding the transaction.

Case Study Answer #11

A broker (broker 1) in Colorado was contacted by the executors of an estate who listed two tracts of land with him.

Broker 2 submitted a written offer for the purchase of parcel 1 from his customer at a price of \$2,000 per acre

through
broker 1.

Broker 1
assured
broker 2
he would
forward
the offer
to the
co-
execu-
tors.

John
H. Gayer
owned
property
located
between

parcels 1 and 2, and had previously transacted real estate business with broker 1. Broker 1 notified Gayer that a written offer had been made on parcel 1, and

Gayer and broker 1 then met personally with the co-executors to discuss the terms for the purchase of both parcels. As a result of those discussions, Gayer submitted a written offer to purchase both parcels for approximately \$1,750 per acre, and broker 1 urged the co-executors to accept.

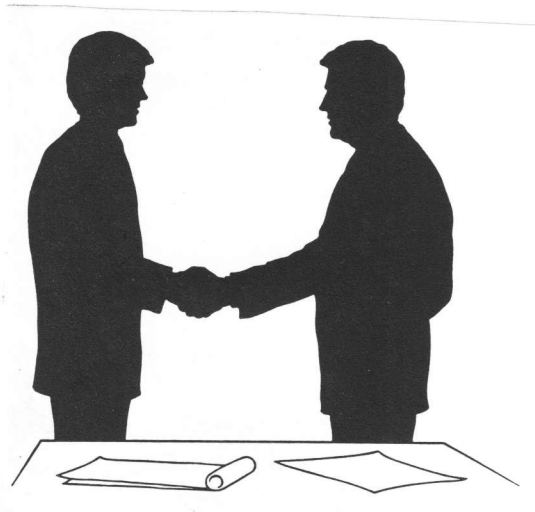
During the course of these discussions and subsequent to submission of the written offer by Gayer, broker 1 failed to disclose to the co-executors that broker 2's customer had made an offer on parcel 1 at \$2,000 per acre. The co-executors refused to accept the Gayer offer because the purchase price was too low.

Thereafter, broker 2 contacted broker 1 relative to the status of his customer's offer and broker 1 did not disclose that this offer had not been forwarded to the co-executors, nor did he advise broker 2 that the offer would not be submitted because it covered only parcel 1. The customer submitting this offer made arrangements to meet with the co-executors and thereupon the co-executors learned of this offer for the first time. As a result, the co-executors notified broker 1 that his listing was terminated, and broker 1 made no objection to the termination.

The real estate commission was informed and a hearing ensued. He was charged with willfully misrepresenting to the other broker that he would pass the news of the higher offer to the executors and of failing to respond truthfully to inquiries about the state of the transaction made by the other broker.

Broker 1 challenged the commission's findings; the Court of Appeals responded by saying "...if the broker advances the interests of the purchaser to the detriment of the interests of his principal, the seller....the finding that [broker 1] failed to disclose the Lanvail offer at a higher price for one parcel while urging the co-executors to accept [broker 1's customer's offer] for both parcels at a substantially lower price per acre is sufficient to support the Commission's conclusion on this issue."

A broker is obligated to his principal to



communicate promptly all definite offers for purchase of the principal's property, even if the broker feels that any particular offer is inadequate. This obligation is founded upon the broker's general duty to make a full, fair, and prompt disclosure to his principal of all facts within his knowledge which might affect the principal's rights or influence his actions....the broker's obligation to communicate all offers is not only imposed for the benefit of the seller but the buyer as well.

Thus the Court of Appeals endorsed the decision of the commission and ordered that the broker's license be revoked.

Conclusion:

The licensee must always immediately communicate information to the seller regarding his property.

The last statement in the above case reads: "...The broker's obligation to communicate all offers is not only imposed for the benefit of the seller but the buyer as well." What does that mean? Once a buyer has made an offer, he is keenly interested in its acceptance. He generally stops looking at other properties in the hopes his offer will be accepted. If a licensee delays unnecessarily, a buyer may miss, among other things, the opportunity to purchase a different property.

B. Dishonest Dealings

1. In Legal Documents

Question #12:

When is it wrong to accept property payments?

Answer: It is dishonest to accept and keep payments under a sales contract which has been forfeited or foreclosed.

Case Study #12

A certain seller sold a parcel of land to a licensed real estate broker on an installment contract. After making numerous payments to the seller, but before making total payment for the property, the broker sold a portion of this property to a certain buyer.

The seller sent "notice of intention to declare a forfeiture" to the broker when the broker became delinquent on his contract with the seller. Even so, the broker continued to collect payments under his own contract with his buyer. Eventually the broker lost all rights to the property being purchased from the seller. After the forfeiture was complete, the broker collected payments from his own purchaser on a property to which he now had no interest. The court put it this way:

"...[the broker] received \$420 from Lundgren which he could and should have used to avoid the forfeiture if he were acting in good faith. After forfeiture on July 6, [broker] received and retained \$560. Yet at no time did [broker] notify Lundgren of the forfeiture or even attempt to enforce any of his rights under the ...sales contract because of any default by [the buyer]. How his silence and inaction in this respect after his own default can constitute a good faith claim to receive payments for property he did not own and could never convey is beyond comprehension. ...fraud or dishonest dealing constitute grounds for suspension or revocation. The term "dishonesty" has been defined in the scope of real estate disciplinary proceedings as follows: 'Dishonesty' necessarily includes the element of bad faith. As defined in the dictionaries and in judicial decisions, it means fraud, deception, betrayal, faithlessness.... 'Dishonesty' denotes an absence of integrity; a disposition to cheat, deceive, or defraud; deceive and betray. ...As so defined dishonesty in itself demonstrates unfitness to be a broker or at least to require discipline as authorized by the statute.'"

"The record does disclose substantial evidence, without conflict, and to a reasonable certainty that [broker] was dishonest by accepting and retaining the eight payments made after July 6, when he knew he could not comply with the terms of the [broker-buyer] sales contract."

The object of an administrative proceeding aimed at revoking a license is to protect the public, that is, to determine whether a licensee has exercised his privilege in derogation of the public interest, and to keep the regulated business clean and wholesome.

The broker's license was revoked for dishonest acts.

Conclusion:

Unless prohibited by law or contract, a purchaser may sell on installment contract a property previously purchased and financed by the seller.

A sells on contract---> B sells on contract---> C

If B does not keep payments current on his loans, B as well as C will lose their interest during contract forfeiture or foreclosure. The licensee must notify the contract purchaser of his loan payment status to protect the purchaser's interest. This notification must be done in a timely fashion.

Correct (assume both sales are financed)

A sells to---> B sells to---> C

C makes payments--> B makes payments--> A

Incorrect (assume both sales are financed)

A sells to---> B sells to---> C

C makes payments--> B doesn't make payments
--> A

Both B and C will be foreclosed or forfeited upon because of B's failure to make payments to A.

The broker mentioned above deceived his buyer by not informing him that the land had been returned to the previous mortgage holder; he cheated his buyer by keeping eight payments. The definition of dishonesty includes a disposition to cheat or deceive.

Questions #13:

What liberty does a licensee possess to change a buyer's contract without the buyer's informed consent?

Answer:

None!

Case Study Answer #13

A broker found a buyer to purchase the seller's house. This contract was subject to financing.

Four days later the broker had the buyer sign a different purchase agreement with the seller which did not contain the contingency of financing but did contain a warning about the condition of the septic system. This second signing was performed because the broker did not like the first purchase agreement. This latter item was not mentioned at all in the earlier agreement. Five days later the buyer signed yet another purchase agreement which repeated the septic tank warning and again omitted any financing conditions. Never did the broker tell the buyer his financing contingency had been removed without his permission.

Unfortunately, the septic system at that time was completely out of order and was unsuitable for a subsurface sewage disposal system. Therefore it was not possible for the financing to be obtained and the prospective buyer was liable to lose his downpayment of \$4,600.

A complaint was sent to the real estate commission and as a result the broker's license was suspended for sixty days. The commission's actions were based on the Real Estate Broker's License Act, whereby the commission was empowered to investigate any complaint against a licensed broker and to suspend or revoke the license if he, the broker, was guilty of, among other things, demonstrating "incompetency, bad faith or dishonesty."

The court found the broker guilty of demonstrating "dishonesty" and affirmed the commission's order suspending his license for sixty days.

Conclusion:

The action of secretly withdrawing a financing contingency, protecting a buyer who cannot merit loan approval, should be shocking to the normal conscience. The buyer probably signed each new contract presented to him by the broker. And by signing he indicated he had read the document. But did he really know that his financing contingency had mysteriously been removed? Probably not. Real estate licensees must take affirmative steps to notify parties to the contract of any changes...before they sign.

B. Dishonest Dealings

2. In Advertising

Question #14:

When is it wrong for an agency to charge a listing fee?

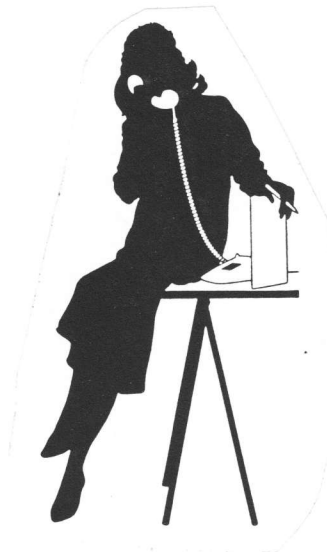
Answer:

It is wrong when the agency advertises that they will list and sell the properties but have no intention of doing so.

Case Study Answer #14

A group of brokers in Florida banded together to form a corporation advertising as agents to Florida property owners living out-of-state. Telephone and mail advertising promised, that after the payment of a fee, the properties would then be sold to persons within Florida. Such promises were false and made merely to persuade the owners to pay the listing fee to the brokers.

One salesperson, who engaged in late night telemarketing, misrepresented to the property owner that she was experienced in the field and was able to resell the property, if so desired, in six months to one year for a price several times higher than originally paid. She also claimed the sellers would receive a warranty bond to guarantee full compliance by the broker corporation with the listing contract and that great emphasis was placed on the efforts to be made to sell the property and on the refund of the listing fee to the seller when the property was sold because



the broker corporation earned a ten percent commission on the sale. This salesperson, however, received compensation for participating in the operation based upon the advance listing fee revenues and not upon sales commissions (as there were no sales).

After the corporation had failed to sell the properties, the brokers were reported to the Florida Real Estate Commission. At the hearing it was found that no efforts were made by any of the staff to sell those properties that were on the list. Indeed, the salespersons worked solely on the listing and no one was employed in sales whatsoever. It was held that those provisions made by the corporation in its listing agreement "agreed to direct the efforts of its organization to bring about the sale of the property" were flagrantly violated as no real effort to market the listed property was ever made or attempted."

The brokers were shown to be "so dishonest and untruthful that the money, property, transactions and rights of investors with whom they sustained a confidential relationship were not able to be safely entrusted to them." Each broker was, therefore, found guilty and had his or her license suspended or revoked.

Conclusion:

When a licensee lists a property for sale, the licensee must use diligence in procuring a purchaser ready, willing and able to buy on the seller's terms to sell.

To change one's mind after agreeing to act in a certain manner is a wrong. But to know that one has no intention of completing an agreement when making the agreement is fraud of the highest degree. So it was in the above case study. If an agency promises to market property, the agency must not only list that property but also make a diligent effort to sell it.

B. Dishonest Dealings

3. For Personal Gain

Question #15:

What behavior must a licensee possess when inside the property of another?

Answer:

The licensee must protect the seller's property as if it were his own. Duties include:

- 1) making sure all doors are securely latched.
- 2) notifying an absentee owner during the heating season of any critical temperature changes.
- 3) communicating break-ins, flooding, broken pipes, etc., to the owner.
- 4) not stealing the seller's possessions.

Case Study Answer #15

A licensee from Nevada accompanied another licensee on an inspection of a condominium in Las Vegas, which was for sale. Upon arriving at the condominium, they found a portable fireplace, which the first licensee claimed to be very useful having one of her own. She returned to the car leaving the other licensee in the condo, who later carried the fireplace to the car, loaded it in and drove it to his apartment, where his landlord helped him to carry it upstairs. Another lady observed what took place on that day, wrote down the license plate number and contacted the police.

A few days later the licensee from Nevada was contacted by a detective. After being questioned by him, she contacted the licensee who had accompanied her on that day and told him to return the fireplace. In the course of conversation, she denied that she knew the fireplace belonged to the owners of the condo and that the licensee had illegally taken it away. Later, she admitted that she had observed everything and had even cleared out her trunk to make room for the fireplace.

The commission filed judgment against her and

ordered that her license be revoked because her behavior was "extremely damaging to the dignity and integrity of the profession" and also she had "failed to do her utmost to protect the public against unethical practices."

The decision made by the commission to revoke her license was affirmed.

Conclusion:

Notice that the broker lost her license even though she did not benefit from the theft (the other person took the fireplace); her wrongdoing was assisting in stealing.

Is it not true that any employee on any job would be fired for stealing or aiding another employee engaged in stealing? Certainly! Now consider the standards required for a career in real estate. The standards required for real estate professionals are much higher standards than those found in the normal job. This case study only dealt with the actions of the licensee transporting the stolen fireplace. You can be assured the licensee removing the actual fireplace from the condominium also received a license revocation.

Question #16:

What is the value of a good reputation? (May one have his license suspended for an isolated act out of step with his character?)

Answer:

A good reputation, reflecting years of scrupulous business practices, may reduce the penalty levied by a regulatory agency.

Case Study Answer #16

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 days suspension of the broker's license.

The Court of Appeals said the following:

The taking away of a person's license to engage in a privilege business or profession by administrative action is one of the most drastic proceedings known to the law. At one stroke of the pen it takes away his means of livelihood, and casts an immediate blight

upon his whole life and that of his family and business associates. The real estate broker's license to engage in that business is no less important to him or her than a license to practice law or medicine is to a lawyer or doctor. Such license is not only a paper writing that permits the holder to legally engage in the activities described therein, but it is also a proclamation to the world that the person to whom the license is issued has qualified to be chosen as a recognized member of a privileged business or profession. It is a most valuable property right; one to be proud of and to be zealously guarded and protected. It singles out a person as being an honorable citizen in the society of people.

This is not to say that an administrative licensing board should hesitate to take away such license--in a proper case and upon sufficient cause. An undeserving recalcitrant or chronic offender, especially in the field of serious matters, should be severely dealt with: he has forfeited his right and privilege to stand with the honorable members of his profession. But the struggle to acquire the privileged license in the first instance necessarily entails much sacrifice, hardships, expense, and physical and mental labor and endurance; and the revocation of such right is a most solemn thing.

*We hold that the subject matter of the violation here involved, to-wit, the theft of one \$3.00 beef-steak, was not such a substantial "dishonest dealing * * * in a business transaction" as to warrant suspension of the defendant's license as a broker; assuming with tongue-in-cheek that the incident ever assumed the status of "a business transaction." It was her doctor's opinion that she could not have helped herself under the physical and mental stress she was undergoing at the time. Also, a number of her fellow brokers, as well as the Vice President of one of the leading abstract and title insurance companies in St. Petersburg, evidence her*



good character and honesty over a number of years and stated their opinion that her honesty and integrity had not been affected by knowledge of the Supermarket incident.

For the above reasons, the real estate commission's action to suspend the broker's license was quashed.

Conclusion:

A real estate licensee should jealously guard his reputation-- one never knows when such reputation may preserve his livelihood in the real estate profession.

Question #17:

How do the qualifications and standards required to engage in the practice of real estate differ from those to practice other occupations?

Answer:

The real estate licensee must possess the highest degree of honesty and integrity. The real estate licensee holds the money of others in protected care, is in the property of the owner during their absence, speaks for the owner in matters about the property being sold and holds the secrets of his principal with utmost secrecy. The licensee must help protect the most important investment made by most Americans --their home.

The licensee must possess character qualities to help his client during difficult times, including:

1) job relocation requiring rapid liquidation of the property at fair market values.

2) mortgage foreclosures; the licensee must understand the client's rights before, during and after the foreclosure sale.

3) sensitive transactions (i.e., deaths/probates, divorces, bankruptcies). The licensee must protect against purchasers who would take advantage during the seller's distress.

4) buyer transactions (e.g., zoning use verification, safe guarding the buyer's trust money, assurances

against cloudy property titles, purchases at fair market value, property defect disclosure and truth-in-lending disclosures).

As can be noticed, the real estate licensee doesn't just possess a job--he has a profession! Because of this high calling, the licensee must be accountable to very strict standards of professional conduct.

Case Study Answer #17

The broker admitted to being an occasional user of marijuana. On July 4, 1974, he landed a small airplane at the Santa Nella Airport, located near a lake, in Merced County, California. He had a certified private pilot's license. The plane contained 800 to 1,000 pounds of marijuana with an agreed street value of \$256,000. He had obtained the marijuana in Mexico. It would appear the airplane ran out of gasoline, the broker overrunning his rendezvous point. He stated he was to meet a truck for delivery three to five miles on the California side of the Mexican border but could not locate the truck so decided to fly back to Oakland where he had rented the airplane. However, he explained landing where he



did on the basis that as he flew over he observed a body of water and felt there was an excellent opportunity to develop the land. (i.e., the broker flew from Oakland to Mexico to pick up his shipment. He flew his shipment out of Mexico to California to evade border

police but missed his rendezvous point with the person who would ultimately distribute the illegal substance in the United States. Running out of gasoline, he made an emergency landing at an airport near a lake.)

When his license was revoked, his doctor indicated he should be allowed, as a form of therapy, to return to the field of real estate where he had shown an affinity for such type of work. (His doctor indicated he had suffered from a mental illness characterized by alternating moods as well as grandiose thinking and impaired judgment. It had been the broker's stated intention "to make a large sum of money by working for a very short period of time.)"

The court responded:

Honesty and truthfulness are two qualities deemed by the Legislature to bear on one's fitness and qualification to be a real estate licensee. If the broker's offense reflects unfavorably on his honesty, it may be said to be substantially related to his qualifications. Illegal possession and transportation by airplane with the attendant sophisticated planning of a quarter of a million dollars worth of marijuana, admittedly for the purpose of personal gain, is clearly an illicit act of deceit and dishonesty in a fundamental sense.

The crime here, of course, does not relate to the technical or mechanical qualifications of a real estate licensee, but there is more to being a licensed professional than mere knowledge and ability. Honesty and integrity are deeply and daily involved in various aspects of the practice. To prevent a person engaging in a lawful and innocuous business or occupation because of his moral character or reputation is in our opinion an arbitrary invasion of private rights and liberties. This may be true of some businesses and vocations. It is certainly not true of all. Where the occupation is one of which it can be fairly said that those pursuing it should have certain particular qualifications, it is within the power of the legislature to exact reasonable assurances of those pursuing the occupation that they do possess these qualifications. The most familiar illustrations of this are the qualifications of preliminary training and learning required of professionals such as lawyers, physicians, dentists, pharmacists and architects. When the occupation is one wherein those following it act as the agents and representatives of others and

in a more or less confidential and fiduciary capacity, it certainly can be fairly said that those pursuing it should have in a particular degree the qualifications of 'honesty, truthfulness and good reputation.' The occupation of a real estate agent is of just this sort. He acts for others and in a more or less confidential and fiduciary capacity.

In view of the nature of the felony conviction of the broker, the quantity of marijuana involved and the motivations of the broker, it was reasonable and proper for the commissioner to conclude that the crime of the broker demonstrated a lack of honesty and integrity in his character.

Conclusion:

Illegal activity for the purpose of personal gain shows a lack of honesty and integrity of character and rightfully results in the revocation of an agent's license.

C. Fraud

Question #18:

If a salesman does not turn over a deposit check to his broker promptly, is it wrong?

Answer:

Yes.

Earnest money is most often held within a real estate company's trust account. A trust account shields the purchaser's money from the broker's judgment creditors. Should the broker place the buyer's earnest money in a personal account, creditors may seize the buyer's money to pay the broker's bills. By holding the money in "trust," notice is given that this money is not subject to levy as the broker is a mere custodian of the money and not the true owner.

State rules and regulations govern the timely deposit of these funds and condemn the broker who commingles or converts the buyer's money to his own use.

What could result should the licensee not deposit

the trust funds in a timely fashion?

- 1) The broker may cause the seller unnecessary delays in consummating his transaction.
- 2) Creditors may levy upon such funds.
- 3) Buyer's funds may be tied up in the broker's probate/estate.
- 4) The seller may miss other opportunities to sell should the licensee finally discover the buyer's check is not covered by adequate resources in the buyer's account.

Case Study Answer #18

Buyers made an acceptable offer on the seller's property located in Nevada. The sales agent procuring the offer inadvertently took the \$1,000 earnest money check with her in her briefcase when she went on a ten day family vacation.

Problems of an unspecified nature arose and the escrow was cancelled. The sellers complained and the real estate commission charged the real estate agent with failing to deposit the money with the brokerage. ("Every real estate salesman, promptly on receipt by him of a deposit on any transaction in which he is engaged on behalf of a broker, shall pay over the deposit to the real estate broker.") The commission suspended the salesperson's license.

An appeal was made to the district court and eventually to the Supreme Court. The Supreme Court found that a license could only be suspended or revoked if the user was clearly found guilty by "sufficient competent evidence." None of the evidence dealt with by the commission was any more than hearsay and as such was seen to be inadmissible. The sellers had been shown the photocopy of the check and there was no indication that the check would not be honored.

It is unrefuted on the record, however, that the retention of the check by Mrs. Jones was inadvertent. Such human frailty, in the context of the single incident here presented, did not, therefore, rise to the level of perfidy, incompetence or negligence which would justify the imposition of either a revocation or

suspension of her license. In short, the record does not reflect evidence of the kind of conduct described by the Commission's findings of fact and conclusion of law regarding ...Jones.

It was agreed that it was not good policy for the woman to take the check with her on vacation, but it was seen only as an error and did not in any sense constitute fraud. The order of the commission was reversed.

Conclusion:

The licensee should transfer trust funds to the broker immediately!

Question #19:

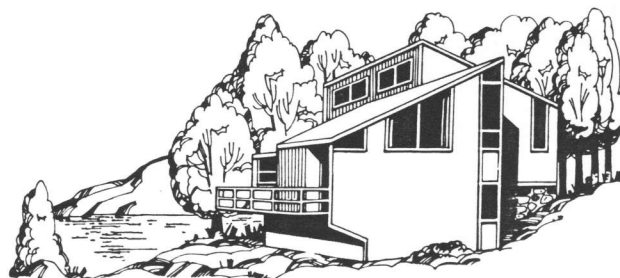
Can a licensee be charged for making false promises of a nature likely to influence, persuade or induce a sale?

Answer:

Yes--such false promises cannot be used to promote real estate sales.

Case Study Answer #19

A real estate broker practicing in the state of New York acted as an agent for a partnership developing



an area of land close to a small town. It was charged that the broker misled prospective purchasers of the lots by indicating that a new road would soon be built

in the area allowing them easy access to their homes. This piece of information persuaded the buyers, as the locality was mountainous and heavily wooded. It was alleged that the broker assured all parties involved that the local town would soon take over responsibility for the road, and so induced the people to buy. It was found that such events were not likely to occur in the near future and the buyers complained to the Secretary of State of the State of New York.

The broker's response to these charges was that he had made promises of only filling in of washed-out areas of the road or soft spots, all of which he had accomplished.

The broker's license was suspended after he was found to have "committed fraud on the purchasers and demonstrated incompetence and untrustworthiness in his dealings with the buyers of the lots." His license was ordered suspended until such time as he provided proof satisfactory to the Department of State that all requirements for dedication of roads within the subdivision had been met and that said roads had been offered for dedication.

The New York Supreme Court responded:

The conditions imposed here are unreasonable. It is uncontested [the broker] neither owns nor has control over the road in question. He is, therefore, unable to legally conform to the imposed conditions. The evidence also disclosed that to prepare a road for dedication would cost approximately \$75,000 a mile. The roadway here is some three and one-half miles long. The costs involved are so prohibitive as to be entirely out of line with the monies realized by [the broker] in commissions....We therefore find the conditions to be unreasonable and disproportionate to the offense.

The matter was remitted to the secretary of state for reconsideration of the penalty to be imposed.

Conclusion:

A licensee must be careful to represent a property in its truest light. To "over sell" a property is nothing other than misrepresentation. A licensee may not rationalize his misrepresentation in the name of

"sales talk."

Suppose you were the licensee mentioned above. What could you have done to prove you accurately represented the subject property? Several methods of verification could include:

- 1) newspaper ads publicizing the road situation and proposed work projects to improve travel conditions.
- 2) disclosure forms listing road conditions and proposed future improvements.
- 3) sales brochures describing present road hazards and future road improvements.
- 4) sales contract disclosures.

In this section you should have learned that:

- ☐ - Concealment is intentionally hiding information from others, including other agents and buyers.
- ☐ - Downpayments that are legal are not always honest. The agent has the duty to inform persons when changes to those documents have occurred and what those changes mean.
- ☐ - Advertising must properly represent the work which will be done.
- ☐ - Illegal personal activity may result in the revocation of an agent's license.
- ☐ - A good reputation is of great value.
- ☐ - Trust funds should be immediately turned over to the broker for deposit.

IV. Unworthiness and Incompetence, Bad Faith and Good Faith.

In this section you will learn:

- ☐ - the major ingredient in unworthiness and incompetence.
- ☐ - the major ingredient in worthiness and competence.
- ☐ - the elements of bad faith and good faith.

Overview: To better safeguard the interests of the public, disciplinary actions can be taken against the licensee demonstrating unworthiness, incompetence, and bad faith. In this chapter, you will have opportunity to study other licensees who have acted contrary to the laws prohibiting such activities.

A. Unworthiness and Incompetence

Question #20:

Are a broker's actions the only thing to be considered when determining unworthiness or incompetency?

Answer:

No. Omissions to act must also be considered.

Case Study Answer #20

The Illinois Department of Registration and Education filed a complaint against a real estate broker who owned apartment buildings, which allegedly were in violation of the Municipal Code of Chicago and endangered the health and safety of the inhabitants. At the hearing (which the broker did not attend), two City of Chicago code inspectors testified about the condition of several apartment buildings which the broker owned.

Building #1 63 unit building: 25 building code violations including peeling paint, broken windows, leaking faucets, vermin infestation and debris, garbage and general neglect to locks and doors.

Building #2 broken plaster, peeling paint, rats, roaches, a defective boiler and a rusted-out steel fire escape.

Building #3 21 code violations including broken plaster, peeling paint, garbage, roaches and defective plumbing.

Building #4 61-unit partially occupied building: 39 code violations including general exterior neglect, a chimney in a dangerous condition, improper doors, no boiler room door, holes in the boiler room wall, peeling paint, rusted fire escape floors, broken concrete walk, the lack of lights on the fire escape, holes in the clay tile in the basement, holes in the plaster throughout the building, evidence of mice in the building, broken windows, and rotting window sashes.

Inspections were made at various times, and numerous violations were found in each of the buildings over a period of about three years. The inspectors said that the violations were "readily correctable;" however, they were not corrected until a court ordered the broker to deposit a sum of money for a receiver to use in repairing the buildings. Ninety percent of the violations were corrected at that time, but the buildings then were allowed to revert "to a state of disrepair."

The Department scheduled a hearing and revoked the broker's license.

The broker took legal action and cited several errors in the hopes of finding some way to have the revocation reversed. The court reviewed them all and agreed with the charges. The broker appealed the decision, and the superior court affirmed the suspension.

In the process of reviewing the case, the superior court made some pertinent statements which are included below.

The broker claimed that these charges could not be

brought against him since they “did not arise out of a real estate transaction.” The court responded that the Act which he violated “applies not only to a registrant acting as a real estate broker or salesman but also where a registrant, in handling his own property, is found guilty of unworthiness and incompetence or disregards or violates any provision of the act.”

Unworthiness or incompetence on the part of a registrant as set forth in...the Act may consist of both acts and omissions to act. Omissions to act and a failure to safeguard the interests of the public in the buying or selling, the negotiation of sales or exchange of real estate, the leasing or renting of real estate wherein the premises are known by the registrant to be in violation of ordinances made for the protection of the public in regard to fire, health, sanitation and other hazards shall be deemed ‘unworthiness or incompetence.’

Here, the broker was such a registrant, handling his own property and, in any event, the rental of residential units was viewed to be real estate transactions.

Conclusion:

This broker was deemed to be unworthy and incompetent because he failed to take necessary steps to safeguard public interest. The actions he did take were good, but they were not enough and they were not followed with the required maintenance.

Question #21:

What is a major factor in demonstrating worthiness to sell real estate?

Answer:

Demonstrating worthiness in real estate means safeguarding the interest of the public.

Case Study Answer #21

A lady in Chicago bought a dwelling for \$13,500. Some improvements were needed on the property and about \$2,000 was spent on them. She paid for an

F.H.A. appraisal and listed the building with a brokerage. The broker and his salesman advised the lady that the property was only worth about \$2,200, due to its poor location. The broker also told the lady that he knew of a man who was willing to pay that price. Without seeing the F.H.A. appraisal, she sold the building to the man, who was only a nominee for the broker. Thus the broker acquired the property for only \$2,200 when it was worth, subject to a few improvements, \$19,000. The broker testified that the alterations cost \$8,000, but there was no substantial evidence to that effect.

The Department of Registration and Education brought an action against the broker and revoked his license, charging that he had acted for more than one party without the knowledge of all the parties involved, had failed to give account for documents (the FHA appraisal) coming into his possession which belonged to another person and demonstrated unworthiness to act as a real estate broker or salesman in such a manner as to safeguard the interest of the public.

Although the broker appealed this decision to two higher courts, the Department’s judgment was upheld. The broker’s appeals were based on minor points of judicial law and the substantial findings of fact were found to be indisputable. Thus the case was decided against the broker.

Conclusion:

The real estate salesperson must concentrate on the good of those he serves rather than simply his own personal gain.

Acting for more than one party to a transaction without the knowledge of all parties concerned is an undisclosed dual agency. In secretly buying the property for himself, the broker took a position in direct conflict with the seller’s best interest. This can only be done with full disclosure.

A fiduciary relationship requires the agent to place his principal in as good a position to receive certain information as the broker. The broker did not reveal the F.H.A. appraisal results. This appraisal was critical to determine the true value of the property.

The seller paid for the appraisal and was the owner of such appraisal. Such activities by licensees must never be tolerated by regulatory agencies or practicing professionals.

Question #22:

What are various ways a licensee may show incompetence and unworthiness?

Answer:

There are many ways a licensee may demonstrate incompetence and unworthiness. Such ways include:

- 1) soliciting "net" listings where a licensee usually puts his interest ahead of his principals.
- 2) converting trust funds to one's personal use.
- 3) conducting closing improperly. Performing closings on types of properties which the licensee has no experience may prove incompetency.
- 4) making false promises of a nature likely to influence, persuade or induce.

Also read below!

Case Study Answer #22

Two brokers in Oregon conducted a real estate educational school and offered courses for brokers and salesmen. They received an anonymous package in the mail which contained sample questions and answers of a type used by the school for their courses. The questions were similar in nature to those used by the Real Estate Division in their examinations. The brokers substituted these questions in one of their courses, and it later transpired that these same questions were used in the June examination of that year. (Several of the questions were specifically created for the June examinations.)

The Real Estate Commissioner charged the brokers knew or should have known that the questions were obtained illegally and their conduct was found to be "untrustworthy and incompetent" and he suspended their licenses. Their license to practice as a school was also suspended. They did not contend the sentences except that they felt that it was

unfair to have both their personal licenses suspended in addition to that of the school's. The Court of Appeals disagreed, however, and further said that their conduct was such that an application for a real estate broker's license was unlikely to be granted, and thus confirmed the decision of the commissioner.

[Licensees] were engaged in preparing applicants to take the broker's and salesman's license examinations. To prepare applicants in such a manner that the purpose of the test is violated, i.e., giving to applicants questions and answers which will appear on a license examination and therefore aiding possibly unqualified applicants to pass was highly improper, and demonstrated a lack of trustworthiness which would justify the Commissioner's refusing a license to an initial applicant.

Conclusion:

From the time one enters the real estate profession, there are many opportunities to faithfully serve one's principal. Demonstrating unworthiness or incompetency may place a licensee's professional career in jeopardy.

Question #23:

May a licensee be held accountable for his actions, even after the listing has expired?

Answer:

Yes!

Case Study Answer #23

A broker in Oregon had a listing agreement with a couple to sell their house for \$13,500. The broker tried to do this but failed to find a buyer. A discussion between the broker and the wife of the couple ensued such that the broker would buy their property, and he gave them a promissory note for \$1,600. A week before this transaction, however, another couple had indicated to the broker that they would pay \$13,000 for the property. It was not until later that the broker told the sellers that he had resold their property at no profit to himself.

A complaint was made to the real estate commission, stating that the broker had not advised the sellers of his intended sale to the final buyers as was his duty. The broker held that he was not under any such obligation as the contract between himself and the sellers had terminated after 90 days and that he was not benefitted by the sale. The Supreme Court disagreed, however, as the seller did not use his right to waive the listing agreement even after the expiration of the time limit, but instead decided to keep looking for a buyer with the aid of the broker.

The following observations were made by the court:

(Wallace v. Oregon Engineering Co.) A provision in a contract terminating it as of a given date, like the one in the present case, is for the benefit of the principal, and like all other provisions in favor of a party, may be waived if he chooses, either expressly or impliedly.

In Bell v. Scudder, (78 Cal.App2d 448) the court said that although a 60-day listing agreement period had terminated, the broker still owed the owners a fiduciary duty for he continued attempting to sell their property and the parties assumed that the agency relationship was still in force.

The Supreme Court agreed with the commission and the broker's license was suspended.

Conclusion:

A licensee may be held accountable for his actions even through the listing had previously expired.

In the above case study, whether the broker gained financially or not from the transaction was seen to be immaterial. The important fact was that the broker withheld information which he was bound by law to disclose.

Question #24:

When must a time limit be definite, and what does "definite" mean?

Answer:

A time limit must be definite for listing

agreements. "Definite" means that a specific time limit must be set.

Case Study Answer #24

Some years ago in California, two brokers were in the practice of claiming commissions on listings which had no termination date. Their agency agreement included this clause: "This agency shall continue 30 days from date hereof and thereafter until three days have elapsed after receipt of written notice from the Owner, terminating this agency, sent by registered mail, or delivered in person to said agent." The Business and Professions Code of California stated that the real estate commissioner was entitled to temporarily suspend or permanently revoke the license of a Realtor if he, the agent, was guilty of "The practice of claiming or demanding a fee, compensation or commission under any exclusive agreement...where such agreement does not contain a definite, specified date of final and complete termination."

Although the agency agreement in question did state that the contract would end after a given number of days, this clearly did not fall under the exact conditions as required by the Business and Professions Code. Obviously, the Realtors were acting legally before the Code was established, but continuing in the same way afterwards being in the "practice of demanding or receiving a fee under agreements which contained no termination date were clearly in violation of the requirements outlined above."

In summary, the Realtors' plea that the agreement contained a "method" of termination was deemed to be insufficient and their licenses were revoked. The licensees' contract contained a very definite method of a final and complete termination of the agency but the statute does not refer to a method of computation of the termination date upon the happening of some future event, but rather to the failure to set forth a definite specified date of final and complete termination. The contracts in question were printed on small cards with the figures "30" typed in. The thirty days constituted a minimum period during

which the owner could not terminate the agency, and in no event would the agency terminate except upon the owner's compliance with the conditions of notice contained in the phrase which follows: "and thereafter until three days have elapsed after receipt of written note..." The statute can only be construed to denote a definite date of termination specifically set forth in a contract at the time of its execution by the owner. An interpretation to favor the licensees would only perpetuate the very indefinite feature which the legislature has said is contrary to the general public welfare.

A similar action was taken in New Jersey where a real estate broker made an agreement with a seller that gave him exclusive sales rights for five weeks or until he gave ten days notice in writing of the termination. Without terminating the agreement, the owner sold the land seven months later and refused to pay the commission. A New Jersey real estate statute required that such listing agreements contain a definite termination date; failure to do so gave the real estate commission the right to revoke a broker's license. Noting that the commission had the right to revoke the broker's license, the Supreme Court said the broker still had rights to commission since the contract itself remained enforceable. (*Maraziti v. Corigliano*, 101 A.2d 559).

Conclusion:

Regulations are made concerning time limits on contracts in order to protect and benefit the public. When a regulatory code requires a definite end to a contract, a specific date or time period must be set.

B. Bad Faith and Good Faith

Question #25:

When a broker agrees to purchase a house which he was unable to sell, is he under any time limit?

Answer:

The broker is responsible to act in a timely manner so as not to inconvenience the sellers or injure their reputation.

Case Study Answer #25

A couple from New York gave a broker the exclusive listing on their home. The keys were given to him also and the couple moved to Texas. The broker was unable to sell the house and consequently the owners asked him if he would be willing to purchase it for himself. This he agreed to do, with his secretary. The purchase offer was signed July 2, and the owners accepted the offer the next day. The offer, as is usual, was subject to the bank agreeing to put the mortgage under a new name. The couple wished the transaction to be completed by the 15th, as that was the day upon which the mortgage payment was due. It was expressly stated in the offer that the sale had to be closed by a certain time of July 17, but the time of closing was not made of the essence. (Contingencies not made of the essence can be fulfilled within a reasonable period of time after the specified date.) Closing did not take place on July 17.

On the 26th of July, the couple informed their attorney that they no longer wished to sell their property, and returned to Rochester. Upon their arrival, the couple called the brokerage and asked that the keys be returned to them. The secretary refused, saying that the house was now under contract for sale. The couple visited their old home, forced an entry, and found that the building was being lived in at that time, and that certain "improvements" had been carried out. Built-in beds had been ripped out; some of the wallpaper had been painted. The couple complained to the Secretary of State, claiming that the bank was foreclosing its mortgage due to the broker's delay.

It transpired that the broker's secretary, unbeknown to the broker, had entered the property shortly after the purchase offer had been made. The broker reprimanded the lady, but did not require that she move. Further, it was found that the bank wished either to have the assurance that the broker would continue the mortgage payments or that he would furnish a financial statement. He agreed to do the latter, but in actuality failed so to do.

The broker held that he was acting purely as a

purchaser and not as a broker. It was found, however, that he was under an obligation greater than that normally upon a buyer. The broker was unaware of his secretary's actions and hence was not liable for them. However, the broker stood in a fiduciary relationship with the sellers. The fact that he then undertook to buy the property individually did not divest him of his responsibility to the sellers to act in a trustworthy manner. He remained obligated to make a good faith attempt to have the transaction closed promptly, as he had assured the sellers would and could be done, to avoid embarrassment to them by a default on their mortgage and thus to avoid putting them in a worse position than they would have been in had they not agreed to sell to him. Under the circumstances the broker was in control of the transaction, and he violated his duty as broker to the sellers by dragging his feet in his own interest.

The broker received a censure for his actions.

Conclusion:

Certainly if a seller makes clear a date by which he would like the sale to be closed, the broker should make every effort to meet that deadline. To delay the closing for his personal gain is to show bad faith.

Question #26:

If a licensee promotes a property as being in "A-1" condition, what responsibility may the licensee have should this be untrue?

Answer:

A licensee must promote a property in its truest light. A licensee may receive discipline from a state regulatory agency or receive a monetary penalty from a court of jurisdiction for the following reasons:

- 1) guessing wrong about an existing property condition.
- 2) intentionally "covering up" a known property defect.
- 3) lying about a known property defect.

Case Study Answer #26

A broker asked a lady if she would be interested in buying the house then owned by the broker and his wife. The lady specifically told the broker that the building must be in good condition and that the roof must be sound. The broker made assurances to the effect that the lady need have no concern about any physical aspect of the premises. He also said that the roof was in "A-1" condition. The buyer inspected the property, which had been freshly painted white throughout approximately four times, before she purchased it.

Within two months after settlement, the roof began leaking and required \$1300 worth of repairs.

The Commission found the broker guilty of demonstrating "incompetency, bad faith, or dishonesty." This charge was ratified by the Court, as the lady had been very specific about her requirements and the broker had not been very honest with her.

Conclusion:

It is obvious from the above study that the licensee was aware of certain defects within the property. Stating the roof to be in "A-1" condition is not merely sales talk but a representation upon which the buyer could rely. Water stains are difficult to cover. Even four coats of paint could not keep the roof from leaking!! Honesty is always the best policy.

Question #27:

What precautions should a licensee take when describing the quantity and exact boundaries of land being sold?

Answer:

One of the most troublesome aspects of property representations is the accurate portrayal of the exact quantity and location of land being sold by the seller.

The licensee may rely on several sources of information to determine the true quantity and location of land in the seller's plottage. Such sources may include:

- 1) The seller's own estimate of land. This estimate

is always suspect as the seller may exaggerate his property to effect a speedy sale.

2) The broker's own estimate of land. The licensee, being unfamiliar with the property, may not know the location of underground benchmarks or reference markers describing property limits. It is a common occurrence in court for a licensee to defend his inaccurate representation regarding a property's true land quantity.

3) Published plat maps. Such plat maps will not reflect recent land conveyances.

4) Auditor's books. County offices change property boundary lines on special plat books to reflect recent real estate transfers. Because of lag time between the actual transfer and the official plat book boundary line change, the licensee should not make representations based on these books.

5) ASC offices. Government ASC offices may rely on crop yield rather than legal descriptions. The licensee should make no representations based on ASC office records.

6) State licensed, bonded and registered surveyors. The licensee should always recommend the purchaser hire this trained professional to determine true boundary lines.

Case Study Answer #27

A broker in Montana acted as agent for a farmer who wished to sell his property. The farmer informed the broker that there were 100 acres of meadow land in the property. Some time previous, the broker had acted as the agent who originally sold the farm to the farmer, at which point it was advertised as having 128 acres of meadow land. The seller, after cutting the hay on the land, came to the conclusion, based on amount of hay produced, that this figure was too high, but he felt that there were 100 acres in the meadow, and he instructed the broker to advertise the place to that effect.

A prospective buyer contacted the broker and before a sale was agreed to, the buyer twice went

over the land, once on foot and once in a jeep and was well-acquainted with land and buildings. At the time the buyer inspected the property he expressed disbelief that the meadow land contained 100 acres. His stated opinion was the meadow did not contain

100 acres and that it was the smallest 100 acres he had ever seen. However, he proceeded with the deal and a contract was drawn up. After a short time, when it was apparent that he would not be able to finance the purchase, the man attempted to withdraw from the transaction. His demand was refused, and the man then complained to



the real estate commissioner, stating that the broker had been deceitful in his representation of the acreage available.

The real estate commission found that the statement made in the advertisement was incorrect, in that there were not 100 acres in the meadow land. The basis for this statement was that an aerial map of the premises had been viewed by the buyer, and from this map, according to the buyer, it would appear that there were less than 100 acres. There was no evidence that the aerial map was properly taken or that it correctly surveyed the premises. After the buyer had refused to complete the transaction, the real estate commission had a survey made of the

meadow land. The surveyor testified at a hearing that the meadow land was less than 100 acres, but there was considerable doubt as to what was included in "meadow."

The broker had been practicing for 27 years with no blemish on his record. Without any substantial evidence, however, the commissioner decided to cancel the broker's license. The broker appealed and both the district court and the supreme court decided to overrule the commissioner's decision. No evidence was given at the hearing that in fact the estimate of 100 acres was false.

The broker's license was not revoked.

Conclusion:

When asked about the quantity and exact boundaries of land being sold, the licensee should always suggest the use of a state licensed, bonded and registered surveyor.

In this section you should have learned that:

- ☐ - Safeguarding the interest of the public is the major ingredient in worthiness or competency as a real estate salesperson.
- ☐ - Actions taken without regard to the public interest prove unworthiness or incompetence.
- ☐ - Bad faith includes deceit or duplicity. Good faith involves honesty. Representing properties fairly is demonstrating good faith.

V. Earnest Money, Downpayments and Trust Accounts

In this section you will learn:

- ☐ - when the broker should not disburse trust funds.
- ☐ - how uncompleted contingencies may affect trust fund distributions.
- ☐ - the importance of good record keeping.
- ☐ - examples of the improper use of trust fund.

Overview: This chapter discusses one of the licensee's greatest opportunities to harm the public: improper care of trust funds.

A. Returning Earnest Money and Trust Funds

Question #28:

What should a broker do with the down payment money if there is a dispute concerning the sale?

Answer:

Some states require the listing broker to hold all trust funds until a written release is obtained from all parties permitting distribution of the funds. If a dispute arises concerning these funds:

1. the broker should wait until a court makes a determination as to the future dispersion of the funds, or
2. if no court action has been initiated, the broker should return this money to the purchaser if the purchaser has, in good faith, been unable to fulfill a contract contingency, or
3. the broker should rely on other remedies provided by state law.

Case Study Answer #28

After a broker in Pennsylvania obtained a listing for a house his salesman showed a prospective purchaser the premises. During the visit the salesman told the man about the existence of the boundary lines and where these lines were situated. A couple of days later, the attorney representing the buyer wrote to the broker.

“Yesterday I received a call from my client concerning the condition of the property which was to be sold under the agreement of sale negotiated through your office. According to the information supplied by the surveyor, there has been a substantial misrepresentation by your salesman concerning the location of the lines on the property. Apparently Mr. DiBello was told that the property line ran along some trees which were located behind a small storage shed. He was also told that the storage shed was included in his property. A survey has apparently been completed and results indicate that neither the shed nor the trees are within the legal description. Accordingly, it does not appear to me there is any alternative but to request that the down money deposited with you be refunded to Mr. DiBello. If for any reason you are unwilling to refund the down payment, you are requested to withhold the funds in accordance with the provision of the broker’s law requiring you to retain down payments in the case of a dispute.”

Two days later the broker wrote to the buyer stating that all was well and that settlement would be held at the end of the following month. This was soon followed by another letter from the attorney stating that the buyer wished to rescind the transaction and once again requested the return of the downpayment. No further correspondence was entered into and the “buyer” obviously failed to attend the settlement meeting.

Shortly thereafter, the broker split the downpayment between the seller and himself, explaining his actions by suggesting that the buyer had “abandoned the transaction and voluntarily forfeited the down money.”

The court found, however, that the real estate commission had been correct in deciding that the broker had violated the Real Estate Broker’s License Act, namely, he distributed down money held by him in escrow under an agreement of sale before the consummation or termination of the agreement which did involve a dispute between the parties to the transaction.

The decision to suspend the broker’s license was affirmed by the court.

Conclusion:

State laws require a licensee to conform to strict rules regarding trust funds and the return of such funds. Should a licensee not act in accord with these rules, disciplinary action may be taken against the licensee.

Question #29:

If a buyer is unable to fulfill his contingency, may the licensee keep the earnest money for his own benefit?

Answer:

No!

Case Study Answer #29

A buyer responded to an ad placed in the paper by the broker offering for sale a house in Oklahoma City. The broker took the lady to see the house and, at that time, received from the lady \$600 cash for



which a receipt was given. The broker said he was too busy to prepare a contract at that time but would do so later and get it to the lady for her signature. That was on Friday evening. The next evening the broker brought the contract to the lady but unsigned by the seller. The buyer said she wanted her lawyer to look at it, so the broker left. The following Wednesday morning, the lady told the broker she decided she did not want the property and asked him to return her money. "He hemhawed around," she said, "and asked me to name three specific reasons why he should give me my money back." She told him she had not signed the contract. To the broker that was of no concern, however, because he refused to return the money--and, for that matter, still had not done so by the time the commission hearing was held.

The broker's reason for not returning the money consisted merely of equivocal doubletalk. Said he to the commission: "Now, here is why I never did return the money...She would come to the office with her daughter and, well, I wanted to talk to find out the truth about these things [apparently the buyer's reasons for not wanting to buy the property]. Well, she refused to talk then...so, [that's] the reason I am out here today." Another reason he had not returned the money was because the lady had not returned "my contract." Yet, at another point he said the main reason was that "the things that she has told wasn't the truth. I want to talk to her about those [unspecified] things because, legally speaking, I shouldn't have taken that \$600 without her signing the contract...And, I am going to put the \$600 in the mail and mail it to her. I had objected to that, I don't object to giving her her money."

Apparently the broker did not mail the money to the lady. Instead he appealed the revocation order of the commission to the district court. The district court vacated the commission's revocation contingent upon the broker completing a 30 hour advanced real estate education program and returning the \$600. Since the broker did not fulfill either requirement above, his license was revoked.

...his refusal to comply since then provides a

foundation for finding that he is guilty of 'untrustworthy, improper, fraudulent and dishonest' dealing. This recalcitrance not only exposes him to a charge of indirect contempt of court, but it also encourages the inference that [the broker] had no intentions of ever returning the money regardless of whether [the buyer] signed a purchase contract or not--a species of fraud.

Conclusion:

A licensee may place his license in jeopardy by improper handling of a customer's earnest money deposit should his offer not get accepted or his contingency not be able to be performed in good faith.

B. Trust Account Record Keeping

Question #30:

What information must be recorded about trust/escrow funds?

Answer:

As a practical matter, the broker should keep records of the buyer's name, buyer's address, a description of the monies received, the check number of the buyer's check, the date the monies were received, for whose properties the monies were received, the general ledger page entry number, the individual ledger page entry number, whether the ledger entry was a debit or credit, a balance for the individual transaction ledger and other pertinent information regarding the final disposition of the funds as prescribed by state law.

Case Study Answer #30

A broker in Pennsylvania offered a house for sale by placing an advertisement in the local paper. This advertisement was answered by a lady who was told by the broker of a \$500 downpayment and certain monthly payments. Permanent financing could be arranged a year later. At this time, the house was jointly owned by the broker and another man, with the responsibility for the property being taken by the

broker. An agreement of sale was entered into, but, the broker was delinquent in his own mortgage payments on the house and the property was repossessed under the mortgage.

The mortgage holder then sold this same property to the lady mentioned earlier. The lady wanted to recover money she had paid to the broker. Being unable to locate the broker, she complained to the real estate commission.

The broker explained his failure to return the lady's money by asserting that his bank accounts were levied upon and taken by the Internal Revenue Service. He stated he maintained an escrow account but admitted he made no effort to prevent its being taken in partial satisfaction of his obligation to the United States Government. He testified, "I suppose it was panic, trying to cover this lien by the government." Further, the broker failed to apply any part of the total of \$800 paid him to the mortgage loan on the property which was nine months in default when he took her money. The court declared, "Incompetency is manifest and there is more than a suspicion of bad faith."

On another related point, the following questioning took place:

"Q. Did you keep escrow records, Mr. Farkas?

(instructor's comment: some states require escrow accounts be titled "trust" rather than escrow.)

A. I kept escrow records on folders; if they were sales transactions they were kept on the folder.

Q. Do you have those records with you?

A. No, I don't

Q. You were subpoenaed to bring those records were you not?

A. Yes, but all my records are now in chaos.

Q. Did you save any records as they pertained to the property at 122 St. Mary's Street?

A. None pertaining to Christine Johnson, no.

Q. Did you have any records pertaining to her?

A. With Mrs. Johnson, no."

And since "Every real estate broker shall keep records of all funds deposited therein, which records shall indicate clearly the date and from whom he received money, the date deposited, the dates of withdrawals, and other pertinent information concerning the transaction, and shall show clearly for whose account the money is deposited and to whom the money belongs....," the brokers license was revoked recognizing noncompliance with this statute.

The court upheld the revocation of the broker's license.

Conclusion:

A broker is responsible for keeping clear and accurate records of the funds entrusted to him. If such funds are being levied upon by a creditor, the broker should identify these funds to the creditor as being trust funds held for others, notify his customers of such levy and, above all, consult with his lawyer immediately.

The broker mentioned above failed to keep his payments current on a property for which he had financial obligations. Tremendous harm can be done by sellers accepting payments in bad faith by not using these payments to prevent the property from entering foreclosure, forfeiture, trustee's sale, etc. Please see an earlier study where this same disaster took place.

There is no evidence from the story whether the broker informed the purchaser that he was also the seller. License laws prescribe disclosure when a licensee is transacting business with the public on agent owned property.

C. Improper Use of Trust Funds

Question #31:

Is it acceptable for a broker to use deposit money which will eventually be his?

Answer:

NO! The broker must place all deposit money into a trust fund and leave it there until he is authorized to withdraw it.

Case Study Answer #31

A broker, his salesman and the corporate brokerage under which they worked acted for five different persons or organizations. Each client deposited a sum of money with the brokerage with the understanding that it would be returned if the transactions were never consummated. When each of the deals fell through for different reasons, the clients demanded the return of their deposits. The brokerage refused, and the real estate commission investigated the matter.

It was found that the brokerage had deposited the money directly into its operating account. Indeed, the trust/escrow account had not been used for over a year! The law clearly states that it is unlawful for a broker to deposit such monies in any other account except the one used solely for the purpose of trust. When the broker became aware that he was under investigation, he prepared affidavits that the parties had permitted him to use this trust money pending final disposition of the matter. All but one purchaser or seller signed such affidavits. During this time, the broker's office was being moved and/or renovated and money for the improvements was needed. The broker said the parties whose money he was holding authorized the firm to use the deposits before the transactions closed.

It is true that after closing the broker secured from some parties their after-the-fact-consent to the use of the deposit monies pending closing. The fact that these parties were in retrospect not unhappy with the licensee's use of the deposit money prior to closing is certainly not determinative of the issue of whether this misconduct constitutes a statutory violation. Actually, these consent forms signed by the parties after closing were totally irrelevant to the issue of whether the deposit monies had ever initially been placed in a trust or escrow account as required by the statute.

The commission's decision to revoke the licenses of the broker, the salesman and the corporate brokerage was confirmed.

Conclusion:

The licensees violated the law by failing to immediately place the earnest money deposit received from the buyers in trust. Once these deposits had been placed in trust, the broker could disburse them only when properly authorized to do so. The activities complained of were not isolated transactions whereby one deposit was not placed in escrow, but were the standard practice of the real estate company. No action of a real estate broker or salesman can result in greater danger to the money and property of investors and those with whom the licensee may sustain a confidential relation than misusing funds entrusted to the licensee by his client.

In this section you should have learned that:

- ☐ - A licensee may not be able to pay out trust funds when the transaction is in dispute.
- ☐ - An uncompleted contingency may entitle the buyer to an earnest money refund.
- ☐ - It is essential to have good record keeping pertaining to all trust account records.
- ☐ - Trust funds cannot be used for the licensee's personal gain.

The End