

4th Edition

Ethics

for the Real Estate Professional

By Deborah H. Long





**Ethics for the Real Estate Professional,
Fourth Edition**

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INTRODUCTION

Justified or not, the perception of real estate practitioners as unethical is commonplace—so much so that the term *real estate ethics* is sometimes considered an oxymoron by members of the public and even by members of the profession itself! Negative characterizations of real estate practitioners appear everywhere in the popular media; witness, for example, the portrayal of real estate agents in such films as *The Big Short*, *Glengarry Glen Ross*, *Lethal Weapon*, and *The Money Pit*, and in TV programs such as *The Andy Griffith Show*, *The Sopranos*, and *Modern Family*.

Ethical dilemmas are not the private property of real estate practitioners. However, real estate practitioners do face challenging ethical dilemmas that are unique to the profession. In addition, today's real estate practitioners are more likely to encounter difficult ethical issues than ever before because technological, social, and demographic changes are transforming our values, our culture, and our profession.

Real estate practitioners, even those with high standards and the best intentions, often have a difficult time doing the right thing for a number of reasons: first, the laws, rules, and codes of conduct are confusing, complex, and sometimes contradictory; second, practitioners lack decision-making experience when confronting ethical dilemmas. Unfortunately, little guidance is available through the usual educational channels, particularly for adults, to learn how to resolve moral issues. As Peter Drucker, author of numerous management texts, once wrote, even business textbooks tend to keep a discussion of ethics in the preface.

Part 1 of this text examines both psychological and business ethics models to help practitioners understand and resolve complex ethical dilemmas. Part 2 looks at the role of codes of ethics in helping us determine appropriate conduct and specifically reviews the National Association of REALTORS® (NAR) Code of Ethics as an illustration of professional standards. This material has been added to this text so that real estate professionals and their instructors can meet the obligations of the required Code of Ethics training for REALTORS® if they wish. Part 3 gives readers a chance to apply these models to five critical areas in the industry: agency, fair housing, property defects, relationships with competitors, and relationships with colleagues.

While it may be difficult to find stable ethical footing amidst the chaos of change, real estate professionals can choose to engage in responsible and morally desirable behavior; they can help people in need; and they can choose to do the right thing. This text points us in that direction.

NEW TO THIS EDITION

The fourth edition of *Ethics for the Real Estate Professional* has been revised and updated significantly. Since the last edition was published in 2008, the economy was rocked by a major recession largely fueled by a mortgage industry meltdown and banking crisis. The housing market has since recovered, but the real estate industry and its participants are under more scrutiny than ever by federal and state regulators. Moreover, the daily practice of real estate sales and management continues to be influenced and shaped by the role of technology and the internet as well as by the consolidation of large real estate firms.

As a consequence of these changes, real estate professionals face more challenges and ethical dilemmas than ever. The National Association of REALTORS® (NAR) has acknowledged this challenge by requiring that its members now take an NAR Code of Ethics course every two years instead of just every four years.

This edition recognizes these industry changes by emphasizing the role of the NAR Code of Ethics in shaping the real estate practitioner's conduct and thinking, particularly about contemporary professional dilemmas.

Specifically, Chapter 1, Models for Ethical Decision Making, (formerly Chapter 2 in the previous edition) has been refreshed with current information about psychological and business models for resolving ethical dilemmas. Chapter 2 offers a complete revision of content focusing on how codes of ethics in general shape our professional and personal behavior, and it focuses on the role of the NAR Code of Ethics specifically, from its inception in 1913 to its enforcement today. Chapter 3 on Applied Ethics has also been refreshed with more contemporary examples, case studies, and responses.

I hope that readers and ethics instructors will enjoy these changes and continue the tradition of enlightened classroom discussion and the pursuit of leading an ethical life.

ACKNOWLEDGMENTS

The fourth edition of this book could not have been accomplished without the help of my students, who so generously share their experiences with me and their classmates. I would also like to acknowledge my colleagues who teach real estate courses and ethics: they generously offer their ideas and often send articles of interest to me. My thanks also goes to the state regulators who have supported my work and who have invited me to their states to share my ideas with their licensees. I would be remiss not to mention my family members, who inspire me with their positive view of people in spite of many challenges in our personal history. I am delighted by the refreshing work ethic displayed by my daughter and my son-in-law and their desire to make the world a better place. My students, colleagues, and family members serve as constant reminders of the goodness in the world.

ABOUT THE AUTHOR

Deborah H. Long has been a real estate professional for more than 35 years. She is also a licensed real estate instructor in North Carolina. She has held the Graduate REALTOR® Institute designation, the Certified Residential Specialist Designation, and the honor of Distinguished Real Estate Instructor. She is also a Certified Distance Education Instructor.

A Chicago native, Long earned her doctorate in educational leadership. Her study on the effect of ethics instruction on Florida salespeople and brokers provoked a lightning storm of controversy in the real estate industry. As a result, her work was featured in *The Wall Street Journal* and *The Chicago Tribune*, as well as in many trade periodicals and monographs.

Her research led her to write *Doing the Right Thing: A Real Estate Practitioner's Guide to Ethical Decision Making*. Long is also an award-winning author of numerous books, articles, and educational programs.

The prestigious Josephson Institute of Ethics has certified Long as an ethics trainer. Her audiences have included corporate executives, accountants, engineers, surveyors, state regulators, nurses, appraisers, and interior designers, but as yet no politicians or attorneys have invited her to speak to their professions.

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Models for Ethical Decision Making

10 REASONS WHY WE NEED TO STUDY ETHICAL DECISION MAKING

Even though ethical dilemmas and temptations abound, it is difficult for adults to find meaningful training on the subject of ethics. In many training programs, discussions of ethical dilemmas are marginalized at best—at worst, they are sacrificed to the demands of limited class time. Nevertheless, ethical decision-making skills are critical to the long-term success of real estate professionals for a variety of reasons.

Reason # 1. The public demands higher ethical conduct from business professionals. Leading television stories indicate that the public is outraged by personal, government, and business scandals and by inappropriate and notorious conduct of individuals who are in positions of leadership.

Reason # 2. Legislatures continue to coerce practitioners to virtue by enacting statutes, rules, and regulations. When a profession does not guard its own reputation and acts in such a way to harm the public, lawmakers often respond by creating new laws. Typically, these laws deal with disclosure issues and consumers' rights. For example, in the United States, the Consumer Financial Protection Bureau (CFPB) was created in 2010 as a legislative response to the financial crisis of 2007–2008 and the ensuing recession. The CFPB is an agency of the United States government responsible for consumer protection in the financial sector. Its jurisdiction includes banks, credit unions, securities firms, payday lenders, mortgage-servicing operations, foreclosure relief services, debt collectors, and other financial companies operating in the United States.

Reason # 3. Courses on ethics are becoming a mandatory part of training, professional preparation, and university curricula. Many college students take ethics courses as part of their required undergraduate curriculum experience. Approximately 75% of all graduate business students in the United States

Objectives

By the end of this part, the reader will be able to:

1. list several reasons why ethical decision making should be studied
2. define the difference between ethics and the law
3. describe the six stages of moral reasoning
4. provide examples of the reasoning employed at each stage of moral reasoning
5. contrast ethical temptations with ethical dilemmas
6. compare various business models of ethical decision making
7. apply appropriate models of ethical decision making

KEY TERMS

ethical dilemma
moral development theory
social contract
universal ethical principles

are required to take a course on business ethics. While students may not be required to take a stand-alone course on ethics, many undergraduate and graduate programs tout an emphasis on the development of “social, ethical, and environmental stewardship” in their curricula. The National Association of Realtors® (NAR), the largest trade association in the United States, recently changed its membership renewal requirement so that its members must take a Code of Ethics training course every two years instead of every four.

Although students or professionals who participate in courses on ethics or ethical decision making do not necessarily become more ethical, mandatory participation in ethics courses sends a powerful message that ethics is important to the profession. Moreover, research studies indicate that participation in those courses may, depending on their format, enhance ethical decision-making skills, and, at the very least, orient students and professionals to the best practices of the profession.

Reason # 4. Complaints and lawsuits against professionals continue to consume the limited resources of professional associations and state regulatory agencies. In the United States alone, more than 25,000 complaints are filed with real estate licensing authorities each year.

Reason # 5. There is a clear and urgent need. A survey by the Josephson Institute of Ethics, an organization that studies ethics, revealed that cheating and lying among U.S. high school and college students is a significant issue, though in its most recent study, it appears that some of these behaviors are on the decline. Some of these young people will enter the real estate professional or the financial industry as ethical illiterates. They will look to their professional organizations, teachers, colleagues, and supervisors for guidance in making ethically sound business decisions. See Figure 1.1.

CHEATING: In 2010, 59% of students admitted they had cheated on an exam in the past year; in 2012 that rate dropped to 51%. Students who copied an internet document for a classroom assignment dropped 2%, from 34% in 2010 to 32% this year.

LYING: Students who said they lied to a teacher in the past year about something significant dropped from 61% in 2010 to 55% in 2012. Those who lied to their parents about something significant also dropped, from 80% to 76%. In 2012, 38% of the students said they sometimes lie to save money; that is a drop of 3% from 2010.

STEALING: In 2010, 27% of the students said they had stolen something from a store in the past year. In 2012 that number dropped to 20%. In 2010, 17% said they had stolen something from a friend in the past year, compared to 14% in 2012. The percentage who said they had stolen something from a parent or other relative in the past year also decreased (from 21 to 18%).¹

Figure 1.1 Cheating, lying, and stealing among high school students.

¹Since 1992, the Josephson Institute of Ethics has issued a biennial report on the ethics of American high school students. It is the largest study of its kind to look at student attitudes and behavior; an important predictor of how they will act as adults. More than 23,000 students across the United States participated in the 2012 survey (<https://charactercounts.org/national-report-card/2012-report-card>).

Reason # 6. The role of ethics training for adults becomes more important as other centers of moral influence change or diminish. For example, prior to the 1960s, it was common for schools, places of worship, and media to inculcate values. Schools promoted citizenship and patriotism. Television programs provided moral instruction. Today, in addition to facing enormous financial constraints, many schools cannot meet all of the needs of an increasingly diverse student body. Teachers often do not have the time to discuss ethics or values, and in some cases, the instructional challenge is “*Whose values shall we teach?*”

In some countries, government, business, and religious leaders are revered as icons of ethical behavior and traditional sources of ethical guidance. But many of those leaders have been a disappointment in recent years, particularly as social media has made its users more aware of human failings.

Reason # 7. Some would argue that ethics cannot be taught because of the diverse opinion regarding what is ethical. Others would argue that it is for precisely this reason that ethics should be taught: to reach consensus about approaching ethical decision making. In spite of the diversity of opinion over topics, it is possible to share basic values such as honesty, justice, caring, and a respect for others. Even in a global society or a culturally diverse country, we can find common ground in determining ethical behavior and steps to moral judgments.

A *Harvard Business Journal* contributor writes that it is possible to seek common ground based on these guiding principles:

- respect for core human values, which determine the absolute moral threshold for all business activities
- respect for local traditions
- the belief that context matters when deciding what is right and what is wrong²

Reason # 8. Unethical practitioners cost their firms in reputation and fines. Unless organizations and companies provide effective, comprehensive ethics programs for their employees, stiff penalties and heavy fines will be imposed when employees violate laws and regulations.

The good news is that *ethical behavior pays*. The *Wall Street Journal* reported that consumers are willing to pay more for ethical products; for example, the article reports that consumers will pay 65% more for coffee that is ethically produced than for coffee that is unethically produced.⁴

Forbes magazine wrote in 2010 that Japanese automaker Toyota “expected its global recall related to faulty accelerator pedals—and the sales and production suspension that resulted—to cost about \$2 billion or 180 billion yen. Analysts indicate the cost at about \$1.1 billion but pointed to *future brand damage* [emphasis added] as an additional price. Toyota estimates that lost sales from the accelerator recall will reduce earnings by 70 billion to 80 billion yen and an additional 100 billion yen to fix the faulty gas pedals and floor mats.”³

²<https://hbr.org/1996/09/values-in-tension-ethics-away-from-home>

³<http://www.forbes.com/2010/02/04/toyota-earnings-recall-markets-equities-prius.html>

⁴<http://www.wsj.com/articles/SB121018735490274425>

A Morgan Stanley Dean Witter study indicated that S&P 500 companies with sound environmental practices outperformed the S&P 5000 by nearly 2%. Assets involved in social investing, through screening of retail and institutional funds, shareholder advocacy, and community investing, grew 40% faster than all professionally managed investment assets in the United States. Investment portfolios involved in socially responsible investments grew by more than 240% over an eight-year period, compared with the 174% growth of the overall universe of assets under professional management over the same time period. Another study indicated that 75% of consumers avoid or refuse to buy from certain businesses. The first reason was poor service, but the second reason was the company's business practices.⁵

Reason # 9. New technologies and other developments will create a more competitive—and perhaps cutthroat—marketplace. If professionals do not have coping strategies to deal with unethical conduct or are unable to demonstrate ethical behavior, a great deal of time and money will be spent dealing with misconduct and litigation rather than helping clients and consumers.

Reason # 10. While it is important that students know what is required to earn a living, it is equally important that they address problems that they will face in the practice of their profession. Today's adults need help in answering questions such as “How shall I conduct my business?”

While learning ethical decision-making skills is intellectually rigorous, it is certainly worth the effort. Financial services practitioners need to acquire mature decision-making skills and habits so that they are prepared to deal with the problems they encounter. Even experienced professionals need an opportunity to discuss the ethical temptations and dilemmas they face.

THE DIFFERENCE BETWEEN ETHICS AND THE LAW

Businessman Michael Josephson wrote: “Ethical people and companies often do more than they are required to do and less than they are allowed to do. The law tells us what we can't do (i.e., prohibitions) and, sometimes, what we must do (i.e., mandates); it does not answer the bigger question: what *should* we do.”⁶ In other words, laws will typically tell us what the minimum acceptable behavior is in any given situation, whereas ethics requires us to do more. As an illustration, a law may tell us that littering is prohibited and subject to a \$200 fine. The law emphasizes punishment if one does not comply. Ethics requires us not only to avoid littering, but to keep our environment clean because it is the right thing to do. When people fail to do the ethical thing, they are not always punished, fined, or penalized (although there can be serious professional consequences to being unethical).

⁵Social Investment Forum, *2003 Report on Socially Responsible Investing Trends in the United States*. Washington, DC: Social Investment Forum, 2003), http://www.socialinvest.org/areas/research/trends/SRI_Trends_Report_2003.pdf

⁶<http://josephsononbusinessethics.com/2013/09/difference-between-what-legal-ethical>

Is it possible to do what is legal but at the same time to be unethical? Certainly. It may be legal for an employer to discuss an employee with other employees. But it is unethical. It may be legal to market credit cards to teenagers who may not have the ability to repay debt or even understand the repayment obligations they have. But it is unethical to do so.

Is it possible to be ethical and do the right thing but for that right thing be illegal? Again, yes. It may be the right thing to give a gift to a client as a thank you for business. But in some circumstances, that gift may be perceived as unlawful. In some cultures and countries, it is ethical for medical professionals to provide assistance to individuals who wish to end their lives, but in many jurisdictions, such assistance would be viewed as illegal.

It is also possible to do what is right and legal. Any organization or individual concerned with its reputation must consider laws, rules, and regulations. But they must also concern themselves with building trust. This can be challenging to do when an industry has a poor reputation.

For 30 years, Gallup pollsters have surveyed the American public's perception of honesty and integrity among professions. Historically, real estate practitioners rank in the bottom half of the poll, slightly ahead of labor union leaders and behind attorneys.⁷ (See Figure 1.2.) A minority of poll respondents indicate that real estate agents have high or very ethics.⁸ (See Figure 1.3.) Perhaps more discouraging, REALTORS® sometimes view their colleagues as unethical.⁹ Are these perceptions accurate? Are real estate practitioners less ethical than other professionals?

A study of Florida real estate salespeople and brokers revealed that relative to other professional groups, real estate professionals did not use the same level of principled reasoning and could be described as ethically immature in terms of their reasoning skills. The researcher also determined that practitioners with more sales experience and who earned more income scored lower in ethical maturity than less experienced or productive practitioners.¹⁰

Independent studies have confirmed the results of the Florida study. For example, a University of Northern Iowa (UNI) study indicates that the higher the practitioner's income level, the more likely the agent will bend the rules to close a transaction.¹¹ In another UNI study, the researcher determined that the more experienced an agent is and the higher his or her income, the less inclined he or she is to disclose property defects.¹² In a review of sanctions against Florida licensees, a researcher determined that most infractions were committed by brokers rather than by salespeople. Furthermore, committing infractions was

⁷The most recent appearance of real estate agents on the Gallup Poll was in 2015: <http://www.gallup.com/poll/1654/honesty-ethics-professions.aspx>.

⁸<http://www.gallup.com/poll/1654/honesty-ethics-professions.aspx>.

⁹"How Ethical is the Next Guy?" *REALTOR® Today*, March 1996, 11.

¹⁰Deborah H. Long, "Are Real Estate Agents Really Unethical?" *REAction*, September/October 1994, 4-5.

¹¹A. Ason Okoruwa and A. Frank Thompson, "An Empirical Analysis of Real Estate Brokerage Ethics," *Ethics in Real Estate* 5, 1999, 257-72, https://doi.org/10.1007/978-1-4757-2995-5_13.

¹²A. Ason Okoruwa. "Real Estate Agent Disclosure of Property Defects" (presented at the 1994 Annual Meeting of the American Real Estate Society, Santa Barbara, California, April 1994).

Gallup's 2015 Honesty and Ethics of Professions Ratings

Please tell me how you would rate the honesty and ethical standards of people in these different fields—very high, high, average, low or very low?

Sorted by very high/high

	VERY HIGH/ HIGH	AVERAGE	LOW/VERY LOW
	%	%	%
Nurses	85	12	1
Pharmacists	68	27	5
Medical doctors	67	27	5
High school teachers	60	29	9
Police officers	56	29	14
Clergy	45	39	11
Funeral directors	44	41	9
Accountants	39	51	7
Journalists	27	42	30
Bankers	25	49	24
Building contractors	25	55	17
Lawyers	21	44	34
Real estate agents	20	53	25
Labor union leaders	18	41	36
Business executives	17	47	32
Stockbrokers	13	42	39
Advertising practitioners	10	46	39
Car salespeople	8	41	49
Members of Congress	8	27	64
Telemarketers	8	34	56
Lobbyists	7	27	60

Dec. 2–6, 2015, GALLUP

Figure 1.2 Gallup poll on honesty and ethics of professions.

	VERY HIGH	HIGH	AVERAGE	LOW	VERY LOW	NO OPINION	VERY HIGH/HIGH
	%	%	%	%	%	%	%
2015 Dec. 2–6	2	18	53	20	5	2	20
2011 Nov. 28–Dec. 1	3	17	57	18	4	1	20
2008 Nov. 7–9	3	14	57	21	4	2	17
2005 Nov. 17–20	2	18	58	16	4	2	20
2002 Nov. 22–24	2	17	57	19	3	2	19
2000 Nov. 13–15	2	15	58	19	4	2	17
1999 Nov. 4–7	1	13	58	23	3	2	14
1998 Oct. 23–25	3	13	60	17	5	2	16
1997 Nov. 6–9	3	13	56	20	3	4	16
1996 Dec. 9–11	2	14	56	20	5	4	16
1995 Oct. 19–22	2	13	56	21	5	3	15
1994 Sept. 23–25	1	13	57	23	4	2	14
1993 July 19–21	1	14	57	21	4	3	15
1992 June 26–July 1	2	12	55	22	4	5	14
1991 May 16–19	2	15	54	18	4	7	17
1990 Feb. 8–11	2	14	54	21	4	5	16
1988 Sept. 23–26	3	10	47	27	7	6	13
1985 July 12–15	3	12	49	25	6	6	15
1983 May 20–23	2	11	52	21	7	7	13
1981 July 24–27	3	11	48	22	8	8	14
1977 July 22–25	2	13	51	24	7	3	15

Figure 1.3 1977–2015 summary of Gallup polls indication of the perception of honesty and ethical standards of real estate agents.

not a function of inexperience: the more experienced licensees committed a disproportionately high percentage of infractions.¹³ In addition to this distressing research evidence, there is also a significant number of complaints and lawsuits

¹³T. Stacy Sirmans. “Summary of Licensing Requirements, Enforcement Effort and Complaints Against (Florida) Real Estate Licensees.” Education and Research Foundation of the Florida Real Estate Commission, June, 1994.

filed against real estate practitioners, mainly on the issue of disclosure practices. (See Part 2).

There are a number of possible explanations for the misconduct and immaturity of real estate practitioners. Researchers advise that ethical maturity rises in relationship to formal education. However, the majority of real estate commissions do not require more than a high school education of candidates who wish to enter the real estate business. Some real estate agents lack commitment to the profession—few licensees dreamed of becoming real estate salespeople when they were little boys or girls. Rather, they may have entered the business during a period of life transition, such as divorce or job displacement. Some of these agents work part-time or remain in the business for only a few years. The real estate business may also attract individuals with a “get rich quick” mentality, lured to real estate by its relatively easy entrance requirements and promises of quick wealth. To add to the problem, real estate agents work in competitive, often adversarial environments where emphasis is often placed on financial success rather than on integrity and expertise.

While it is important not to generalize too broadly about the results of a few research studies or the acts of a small percentage of real estate licensees, it is equally important to note that many acts of misconduct are never reported or caught. However, the majority of real estate practitioners would not do the wrong thing deliberately. The majority of practitioners are good people trying to help others. They find the poor image of real estate agents embarrassing. They also realize that all real estate professionals face moral temptations and ethical challenges. They often have a difficult time doing the right thing because state and federal laws are confusing, complex, and sometimes contradictory. Moreover, real estate practitioners are not trained in decision-making skills to help them resolve ethical dilemmas. To add to the burden, there seem to be more ethical dilemmas every day: agency, civil rights, stigmatized properties, environmental hazards, and relationships with colleagues, employers, and the community are just a few areas where real estate professionals come across troubling issues.

These dilemmas can be an important impetus for practitioners to see what can be done to improve not only the image of the profession but also to improve its collective ethical thinking skills.

It is possible to change the way we think about ethical dilemmas, and it has never been more important to adopt strategies that will help us explore options and to make more mature judgments about the dilemmas we face. In light of the technological, social, and demographic changes sweeping so many of our institutions and countries, it is increasingly important that we learn to navigate new and uncertain ethical terrain. Learning to make sound ethical judgments is a lifetime task, usually begun in childhood by our parents, elaborated upon by teachers and peers, and never finished.

Fortunately, real estate professionals can develop the skills necessary to make more mature decisions and to become more sensitive to ethical problems in the profession. Numerous guidelines and models for ethical decision making exist, including the National Association of Realtor® (NAR) Codes of Ethics. (See Part 2.)

A PSYCHOLOGICAL MODEL OF ETHICAL DECISION MAKING

While our values may change over time, our principles become habit—rather, once we are aware of our principles, we should make them habits. This habit of thinking or behaving in a principled way could be called our code of conduct or ethics. Ethics can be defined as a system of moral behavior based on our principles.

During adulthood, we establish patterns of ethical behavior that are fairly consistent. We may agonize over social problems such as abortion and euthanasia, and we may change our minds as we mature, but the way we think about these problems and the way we respond to these issues is remarkably systematized.

Harvard University Professor Lawrence Kohlberg devoted his life to a study of the evolution of moral reasoning. His research not only transformed the landscape of **moral development theory** but also had a profound influence on ethics education. Kohlberg believed that people learn to reason morally and ethically in a sequence of stages.¹⁴ Cultural factors may speed the stages up, slow them down, or even arrest them. Nevertheless, cultural factors do not change their sequence.

Kohlberg created a map by which he charted the stages of moral development. He determined that there are six stages of moral reasoning. According to Kohlberg, most children under the age of nine, some teenagers, and many adolescent and adult criminal offenders are in Stages 1 or 2. Individuals in these stages view rules and social expectations as something external to them. Individuals in Stages 3 or 4, on the other hand, have internalized these rules and the expectations of others, especially expectations of authorities. These stages are marked by an acceptance and understanding of society's rules and by an acceptance based on the general moral principles that underlie these rules.

Sometimes these principles come into conflict with society's rules, in which event an individual in Stage 5 or 6 decides based on principle rather than convention. Only a minority of adults reach this last stage, and usually only after the age of 20.

Kohlberg and later researchers validated this theory of moral reasoning by developing ethical reasoning tests and examining the ways that participants thought about moral dilemmas. One of Kohlberg's most famous test questions asked participants to respond to Heinz's Dilemma (on page 10).

Psychologists can determine from responses to Heinz's Dilemma what kind of reasoning skills individuals have. For example, an individual reasoning at Stage 1 might respond to Heinz's Dilemma by stating, "Heinz should not steal the drug because it is bad to steal. Heinz would be a thief, and he would be punished for the theft." A Stage-1 thinker might also be concerned about punishment if Heinz doesn't steal the drug (e.g., perhaps his wife's family would shun him).

The highest reward for a person's toil is not what they get for it, but what they become by it.

—JOHN RUSKIN

¹⁴William C. Crain, *Theories of Development: Concepts and Applications* (Englewood Cliffs, NJ: Prentice-Hall, 1985), 118–36.

HOW WOULD YOU RESPOND?

Heinz's Dilemma

In Europe, a woman was near death from a rare form of cancer. There was one drug that doctors thought might save her. It was a form of radium that a druggist in the same town had recently discovered. The drug was expensive to make, but the druggist was charging 10 times what the drug cost. The sick woman's husband, Heinz, went to everyone he knew to borrow the money, but he could get only together about half of what it cost. He told the druggist that his wife was dying, and asked him to sell it cheaper or let him pay later. But the druggist said no.

Consider the following questions about Heinz's dilemma:

1. If Heinz has no other alternatives, should he steal the drug? Why or why not?
2. What if Heinz does not love his wife? Should he steal the drug? Why or why not?
3. Should he steal the drug for his best friend? Why or why not? What about his favorite pet?
4. Stealing is illegal. But is it always unethical?
5. Should people do everything they can to uphold the law? Why or why not?

THE STAGES OF MORAL REASONING

Stage 6 Universal ethical principles.

General universal principles determine right and wrong. These values are established by individual reflection and may contradict the egocentric or legal principles of earlier reasoning.

What's right: I have to show the greatest respect for the rights and dignity of all people and support a system that protects human rights.

Why: Because that is what my conscience tells me to do.

Stage 5 Social contract.

The rules of society exist for the benefit of all and are established by mutual agreement. However, if the rules become destructive or if one party doesn't live up to the agreement, the contract is no longer binding.

What's right: I have to be responsive to the needs of others within my society.

Why: To keep my society from falling apart.

Stage 4 Law and order.

Being good means being a dutiful citizen and obeying the laws set down by those in power.

What's right: I should be a responsible citizen and follow the rules and regulations of society.

Why: To keep the system from falling apart.

Stage 3 Good girl, nice guy.

Being good pleases other people and wins their praise. Approval is more important than a specific reward.

What's right: I should live up to others' expectations of me.

Why: So people will like me, and so I will like myself.

Stage 2 Look out for number one.

Each person takes care of him- or herself. The only reason to be nice to others is so they will be nice to you.

What's right: I should look out for myself and only be nice to those who are nice to me.

Why: For my own self-interest.

Stage 1 Might makes right.

Obedience to authority in order to avoid punishment is the most important value.

What's right: I should do what I am told.

Why: To stay out of trouble.

Adapted from Thomas Lickona, *Raising Good Children* (New York: Bantam, 1983); Thomas Lickona, *Moral Development and Behavior: Theory Research and Sound Issues* (New York: Holt, Rinehart and Winston, 1976).

The overriding concern about punishment rather than for the value of life over property is a response typical of Stage-1 thinkers.

A Stage-2 thinker would consider stealing for his ill wife if she were of value. If it were just an acquaintance who were ill, then the husband might not steal. A Stage-2 thinker might also reason that if Heinz could get something in return by stealing, that is, a wife who would be around a little longer to cook or clean for

him, then stealing the drug might be justifiable. Stage-2 thinkers are primarily concerned with their own needs.

Stage-3 thinkers are concerned about what others think. Some Stage-3 thinkers think, “If Heinz doesn’t steal the drug, what will people think of him?” Others may reason that people will think ill of Heinz if he is a thief.

A Stage-4 thinker considers the value of life and deems it important, even sacred. However, at this level of moral reasoning, a Stage-4 thinker may feel that no matter how valuable life is, a particular relationship with another person does not obligate one to steal. A Stage-4 thinker might also consider whether the druggist’s right to his invention should be respected. A Stage-4 thinker may consider the “contract” between a husband and wife as binding as any civil laws and may, as a consequence, think that stealing the drug for a loved one is appropriate.

A Stage-5 thinker might believe that there is some obligation to steal for anyone dying. Moreover, if the law were to punish Heinz for stealing the drug, the law would not be a just law and therefore should be broken. A Stage-5 thinker might say, “Heinz’s wife’s right to life comes before the druggist’s right to property.” However, Stage-5 thinkers may also reason that stealing is wrong because society would fall apart if everyone stole what they needed.

Where Stage-5 individuals might ask, “What does it mean to be a good member of my social system? What are my responsibilities to other members of my system?,” a Stage-6 thinker would consider, “What does it mean to be a human being? What are my responsibilities to any other human being, even people who do not belong to my system?” Where a Stage-5 person might ask, “Does this action promote my social system?,” a Stage-6 person would ask, “Does this action respect the right of the individual people affected?”

A Stage-6 thinker would take an action that would demonstrate the greatest possible respect for the human right of every individual and support a social system that protects those rights. Standing outside of their own social system, Stage-6 thinkers can evaluate the morality of the system and use the principle of respect for others to guide their actions.

Kohlberg described the higher levels of reasoning, but he was not judgmental. Heinz’s Dilemma has no absolute right or wrong answer. What Kohlberg demonstrated was that individuals can come to different conclusions about a situation and share the same level of reasoning skill. For example, Stage-4 thinkers, those with a “law and order” orientation, may say that it is wrong to steal the drug because it is illegal. However, Stage-4 thinkers could also defend stealing the drug because of one’s contractual obligations to a spouse.

Research indicates that the average adult reasons primarily at Stage 4, the law-and-order orientation. According to Kohlberg, Stage-4 thinkers will occasionally use Stage-5 reasoning, but they use Stage-3 reasoning, too. He reported that adults can comprehend moral reasoning at one and even two stages higher than their own. They may not be able to produce this higher-stage thinking themselves, but they understand it when they hear it, and they recognize it as superior to their own. Kohlberg asserted that this finding was fundamental to moral leadership.

Kohlberg’s theory gives us one strategy for evaluating our reasoning skills. An immature adult will be more concerned with punishment, self-interest, and peer pressure than with higher moral issues. A mature adult will use the criteria of law,

social contracts, and universal values as appropriate standards for debating an ethical issue. Kohlberg also made the following observations:

1. Development in moral judgment continues well into adulthood. People show dramatic changes in their 20s as in their earlier years.
2. Individuals must progress through the stages of moral judgment in sequence.
3. Once a level of moral judgment has become established, that method will not deteriorate because levels are not reversible. Individuals cannot fall from a higher to a lower stage, nor can they jump from the first stage to the third.
4. Movement through the stages is affected when a person's cognitive outlook is inadequate to cope with a given moral dilemma.

In other words, becoming an ethical person is a lifelong task, one that begins at childhood and never stops. It is a laboriously slow process that accelerates when life transitions or life crises prompt us to reexamine our perspectives. These life challenges often are opportunities for new ethical growth.

DILEMMA OR TEMPTATION?

What is an **ethical dilemma**? Contemporary philosophers suggest that most difficult situations are really moral temptations, not ethical dilemmas. Choosing between right and wrong, they argue, is not really a dilemma. Most of us recognize the difference between right and wrong, but may not be willing to do what is right when it costs more than we want to pay. A true ethical dilemma forces us to choose between two positive values: for example, between mercy and justice or between long-term goals and short-term goals.

In his book *How Good People Make Tough Choices*,¹⁵ author Rushworth Kidder discusses right-versus-wrong decisions and right-versus-right. Right-versus-wrong conflicts could be simply characterized as ethical *temptations*. For example, cheating on one's income tax, choosing high-sugar, high-fat foods while dieting, and lying about your child's age to get lower-priced movie tickets are all illustrations of ethical temptations where we know that we are doing the wrong thing. Most adults do not live in a moral vacuum where they cannot tell right from wrong. They know the right thing to do, but sometimes succumb to temptation and do the wrong thing. Generally, it is reasonably easy to distinguish between ethical temptation and an ethical dilemma. Ethical temptations are also easier to resolve because the right response is often obvious.

Kidder suggests that the real ethical problems we will face in this century will be the right-versus-right decisions (i.e., real ethical *dilemmas*) where we will have to face a choice between two or more positive values. He identifies four such dilemmas: *truth versus loyalty*; *the individual versus the community*; *short-term versus long-term needs*; and *justice versus mercy*. (See Figure 1.4, Rushworth Kidder's Model.¹⁶) Kidder suggests that determining which of these four paradigms fits a dilemma can help

¹⁵Harper Perennial, 2009.

¹⁶Ibid, 112–13.

justice versus mercy	fairness, equity, application of the law versus empathy, compassion, and love
short-term versus long-term	immediate needs or desires versus future goals and prospects
individual versus community	us versus them; self versus others
truth versus loyalty	honesty versus promise-keeping

Figure 1.4 Rushworth Kidder’s model of ethical decision making.

us “cut through mystery, complexity, and confusion—assuring us that, however elaborate and multifaceted, dilemmas can be reduced to common patterns.”¹⁷ He further proposes that if the dilemma does not fit one of these paradigms, it is because it is a right-versus-wrong issue, at which point the answer becomes more clear-cut: we should do what is right, not what is wrong.

As Kidder works through a variety of dilemmas, he shares where he would “come down . . . all things being equal”¹⁸:

- Between truth and loyalty, he would choose truth, citing that those who choose loyalty (to dictators like Hitler, Stalin, or Hussein) are capable of doing terrible damage to the world. It is less likely, he argues, to do that kind of damage from choosing truth.
- Between the individual and the community, he would choose community. Community, he proposes, includes self, but self does not always embrace community.
- Compelled to choose between short-term and long-term, he would favor the long-term because long-term thinking can include the short-term, whereas the reverse is not true.
- Finally, he would choose mercy over justice because mercy suggests love and compassion. A world with love and compassion could exist without justice, but a world of justice would still need love.

¹⁷Ibid, 22.

¹⁸Ibid, 220.

There are often signals that an ethical dilemma is on the horizon. The decision maker thinks about the problem in these ways:

- I use words such as “right,” “wrong,” “bottom line,” “values,” “conflict of interest,” or “ethics.”
- I want to call the state regulatory agency or professional association or attorney to determine my response’s legality.
- I question whether my actions or inactions will harm anyone. I list the advantages and disadvantages of my decision.
- I question whether I am being fair to everyone. I wonder if I would do the same thing if others were involved. The Golden Rule comes to mind: “Do unto others as you would have them do unto you.”
- I feel that something is wrong.
- I feel torn between two or more values, goals, or parties.
- I hesitate to share this problem with others. I worry that others may object to or oppose my decision.
- I worry what others will think about it.

HOW WOULD YOU RESPOND?

In the following case studies, are the individuals facing **temptations or dilemmas**?

Case Study #1

You make the final decisions in choosing which real estate investment opportunities are recommended by your firm to its clients. Two real estate fund managers are competing to be the one recommended. The funds are very similar. Deciding between the two is difficult. One of the fund managers offers an attractive internship opportunity to your college-age teenager. The fund manager says it’s a coincidence. It seems like a “win-win,” because no one is hurt by the offer and your teenager would benefit.

Case Study #2

A customer wishes to make a full-price offer on your listing. You discover that the customer is a known sex offender who was recently released with no conditions as to where the sex offender may now live. The listed property is near several places where children congregate.

Business Models for Ethical Decision Making

Several models of ethical decision making are effective in resolving business dilemmas. Some of these models were originally proposed by earlier philosophers. For example, the eighteenth-century philosopher Jeremy Bentham suggested that ethical dilemmas can be resolved by testing for results and consequences. If an action leads to the greatest possible balance of good consequences or to the least possible balance of bad consequences, then the action is ethical. A contemporary of Bentham's, Immanuel Kant believed that ethical dilemmas can be resolved by examining rules, policies, and laws. Kant assumed that laws are divinely inspired, and thus, legal actions are ethical. Jean Jacques Rousseau, another eighteenth-century philosopher, proposed that ethical dilemmas can be tested by filtering them through social norms or societal values. In contrast, the twentieth-century thinker Martin Buber believed that an individual's personal convictions serve as the ultimate standard for making decisions of ethical dimensions.

Rather than rely on one strategy, it is advisable for the real estate practitioner to consider them all. Each ethical system has strengths and limitations. Each ethical system sheds light on possible solutions to any given problem. Each provides us with part of the answer. The next challenge is to integrate the advantages of each philosophical orientation into a working model for ethical conduct.

Integrated Model of Ethical Decision Making

Consider the model below as a means of making an ethical decision for coping with the previously described case study:

HOW WOULD YOU RESPOND?

The Question of the Murder–Suicide

A real estate agent is called to meet an owner of a home in a middle-class suburb. The property looks somewhat run-down: the lawn has not been tended, some litter is strewn about, and the inside is vacant.

The owner of the home shows the property to the agent. When asked why he wants to sell, the owner looks embarrassed and says, “This property belonged to my cousin. About six months ago, he murdered his family in this home and then committed suicide. I inherited this property through the probate court's decision, and I just want to get rid of it as quickly as possible. Tell me what to ask for it so I can be done with this mess.”

While other similar properties in the area have been selling for \$240,000 or so, the agent knows that when buyers find out that this property was the scene of a murder–suicide, the seller will be lucky to get \$200,000.

What should the agent do when buyers ask why the seller is offering the property? Should the agent disclose the problem?

This model of ethical decision making is based on the assumption that no single ethical philosophy can provide a complete response to an ethical dilemma. On the other hand, if the best from all of the philosophies is integrated, and the decision maker considers the dilemma from all perspectives, then it is more likely that we can get closer to the “most correct” response.

Using the Integrated Model for Ethical Decision Making, let’s resolve the murder–suicide dilemma posed above. We must first consider what we know about the problem—the *facts*:

- The seller is motivated to sell the property.
- The property appears distressed.
- Comparable property value is approximately \$240,000.

Our *assumptions* are:

- The property will sell under market value because of its condition and the seller’s motivation.
- The neighbors are aware of the murder–suicide on the property, but others might not know of the tragedy, particularly prospects from out of town. One of the neighbors is likely to tell any prospect or buyer about the tragedy.
- The seller told the agent about the murder–suicide in confidence.
- Some buyers might want to know about the murder–suicide, either because they are superstitious or because they could get better terms or a better price because the property might be considered stigmatized.

We know that a number of people are *stakeholders* in the agent’s decision:

- The agent: A listing and possible commission may be at risk; the agent might be sued by the seller for revealing the information to the buyer; the buyer might sue if this information is withheld.
- The seller: The best possible price and terms for the seller may be at risk if the agent reveals that the property has been the scene of a murder–suicide; however, if the agent keeps this information confidential, the seller might be sued later.
- Prospective buyers: Buyers may overpay for the property if they are not fully aware of the stigma attached to the property; buyers may regret purchasing the property if they find out about the stigma after the fact and may have to hire an attorney to sue responsible parties.
- Superiors: The broker-manager may wish to reject the listing or accept the listing with or without reservations regarding disclosure.

- Peers: Colleagues may find this listing undesirable and may not want to show it.
- Subordinates: Office staff may regard this listing as undesirable and may not feel comfortable dealing with questions from co-brokers and prospective buyers.
- Family: Family members may regard this property as unsavory and may be unsupportive.
- Community: Neighbors may be worried about the effect the sale of this property will have on their own market values; they may also be more than willing to tell what they know about the murder–suicide to all prospective buyers.
- What resources and which advisors can be of help?

In addition to considering the feelings and possible concerns of any and all stakeholders, we may also consider the following:

- What will be the consequences of my action if I take the listing and keep the murder–suicide confidential?
- What will be the consequences of my action if I take the listing and disclose information about the murder–suicide to all prospective buyers?
- Rules, policies, and laws: What are the state laws or rules and regulations of my state regarding disclosure of such matters?
- Social contract: What does the policy and procedures manual of my office require me to do? What does my professional code of conduct advise me to do? What would my brokers and peers expect me to do? What does society (friends, family, and neighbors) expect me to do?
- Personal convictions: What does my conscience tell me to do?

Now let us consider possible answers to these concerns.

What will be the consequences of my action if I take the listing and keep the murder–suicide confidential?

I will keep the seller happy for the short term, but in the long term the risk is great. The seller may be sued by the buyers for withholding material information. As an agent, I could be held responsible.

What will be the consequences of my action if I take the listing and disclose information about the murder–suicide to all prospective buyers?

The buyers may appreciate knowing this information but may also be reluctant to make an offer on this stigmatized property. Buyers may make low

offers. The seller may be harmed by disclosure of this information, and if done without the seller's permission, it may be considered a breach of fiduciary duty.

What are the state laws or rules and regulations of my state regarding disclosure of such matters?

Some state laws, such as California's, require that a crime such as a murder-suicide has to be disclosed if committed within three years of marketing the home. Some courts have rules that disclosure of death is not material. My state does not yet have a law or court case that would help me decide what to do.

What does the policy and procedures manual of my office require me to do?

My policy and procedures manual reminds me to keep my principal's interests (the seller) interests above those of others.

What does my professional code of conduct advise me to do?

My professional code of ethics also advises me to keep my client's interests above those of others but reminds me to be honest with all parties.

What would my brokers and peers expect me to do?

The broker/owners of my firm would want me to take the listing, but would want to know all the circumstances so they could decide how to market it appropriately. My peers might feel uncomfortable with the listing.

What does society (friends, family, and neighbors) expect me to do?

My major concern would be the neighbors. They want the property sold because right now the property is poorly maintained. But they also are worried that the home has a "reputation" that could damage property value in the area.

What does my conscience tell me to do?

I think buyers have a right to know not only the material/physical defects of the property, as well as anything within reason that might adversely affect the future value of the home. I would like to be able to give this information to prospective buyers. On the other hand, I respect my seller's right to confidentiality.

By speculating about possible decisions and their outcomes, the agent is practicing investigative decision making; that is, the agent is experimenting with hypothetical results of any particular decision, a process that can help the decision maker reach the terminal, or final, decision.

What might the terminal decision be? If the agent integrates the responses to all of the questions that were raised, a possible decision would be: I will explain to the seller that I would like the listing on this property. I will explain the seller's right to keep information confidential, such as the unfortunate tragedy that took place on this property. I will also explain to the seller that sometimes a seller's right to confidentiality conflicts with the buyer's right to know. This is one of those cases.

If the courts and the legislature in this state have not yet spoken to the issue of disclosure about murder or other crimes on marketed property, I would certainly

not want my seller to be the test case, nor would I want my brokerage firm or anyone in it named in a lawsuit by an angry buyer. While I might not disclose this information to the buyer, a neighbor is likely to.

I will ask the seller to give me the listing but also to give me permission to reveal this information to buyers at an appropriate point. I would request this permission in writing. Needless to say, I will discuss this with my broker, and if the listing is acceptable on these terms, we will have a special marketing session with the other agents with our firm to discuss how to respond appropriately to questions about the murder–suicide. We will do our best to get the seller the highest price possible under the circumstances for the seller’s sake, as well as for the sake of other property owners in the neighborhood.

While other responses to this problem are possible, consider the response above (and other possible solutions) by this set of criteria:

- Have you defined the problem accurately?
- How would you define the problem if you were the buyer? The seller? Your broker? Your peers? The neighbors?
- To whom did you give your loyalty first and foremost? Was that the appropriate choice?
- Whom, if anyone, would your decision harm?
- Did (or can or should) you discuss this decision with anyone else?
- Would your response to this dilemma be the same tomorrow? One year from now? Ten years from now?

The Kew Gardens Principle

Sometimes real estate agents face an ethical dilemma where “doing no harm” is not enough. Avoiding doing harm *may* be an appropriate response to the conflict between a buyer’s right to know about a murder–suicide on the property before making an offer to purchase. But what if, by avoiding injury to one party, we have not exhausted the full range of possible moral actions?

Consider the case of the sex offender described earlier. How is the real estate agent’s dilemma in that case different from the dilemma in the murder–suicide? What are some of the ethical concerns that the seller agent faces in dealing with the sex offender? What should the agent do if the sellers decide to sell to this buyer with full knowledge of the offender’s criminal past? What if the sex offender has hired the agent as a buyer’s broker?

You may find that your best response leaves you less than satisfied in this particular instance. For example, you may have concerns having to do with the conflict between the buyer’s right to live anywhere he wishes and your personal concerns about the nature of his rehabilitation if he is choosing to live where children congregate. (In some states, such as Ohio, state laws do not permit sex offenders to live within a certain distance of schools. In those jurisdictions, the

real estate licensees would suggest to the buyer that the offender should obtain legal advice about whether he can occupy the home he is attempting to buy.)

Your desire to do what is right for the seller is also in conflict with the potential harm to the community if the buyer completes this transaction and then commits another sex offense.

Your response may also be contingent upon whether the legal system can do any more than it already has by incarceration. While you know that legally you *must* present the offer, you even debate whether you should *submit* it, knowing that the owners might accept.

Once the offer is accepted by the sellers, you might wonder if you should take a course of action to obstruct the contract from going through, such as picketing the property. To do so may be a breach of fiduciary duty to the seller and could leave you open to a lawsuit by the buyer.

The buyer's criminal record may have negatively affected his credit so that a loan contingency clause in the contract cannot be met. Thus, the sales contract itself may provide a resolution to this dilemma.

Most jurisdictions require that sex offenders must register their whereabouts within a short time of release from prison or be incarcerated yet again. One course of action available to the real estate licensee is to make certain that the sex offender does in fact register in a timely manner.

In the earlier dilemma concerning a murder–suicide on the property, it may have been sufficient to do no harm; that is, the agent had a responsibility to see that neither the seller, the buyer, nor any other parties were injured by the agent's action. In this case, it may be important and of a higher priority to help others.

Under these circumstances, it is sometimes helpful to consider a model of ethical decision making called the “Kew Gardens Principle.” The Kew Gardens Principle takes its name from a shocking New York City homicide case in the 1960s where it was at first thought that a young woman, Kitty Genovese, had been brutally murdered in front of numerous witnesses, none of whom called police or even called for help, even though they were all safe inside their homes.¹⁹

Review the case of the child molester again, this time considering the four elements of the Kew Gardens Principle:

- Is there a clear *need* for aid?
- How close is the agent to the situation? (*proximity*)
- How *capable* is the agent?
- Is anyone else likely to help? (*last resort*)

¹⁹Recent investigations suggest that Ms. Genovese's assault was not witnessed by nearby apartment dwellers because the attack was not in a clear line of sight of those apartments. Ms. Genovese may have also received some aid by neighbors. See https://www.washingtonpost.com/lifestyle/style/her-shocking-murder-became-the-stuff-of-legend-but-everyone-got-the-story-wrong/2016/06/29/544916d8-3952-11e6-9ccd-d6005beac8b3_story.html?utm_term=.91b1566b3f92.

APPLYING THE KEW GARDENS PRINCIPLE

An agent has an increased moral obligation to aid another person based on four factors:

- Need* Is there a clear need for aid (for example, harm has been or is about to be done)?
- Proximity* Are you “close” to the situation (not necessarily in space, but in terms of notice)? Do you know of the need, or could you reasonably be held responsible for knowing?
- Capability* Do you have the means to provide help without taking undue risk?
- Last Resort* Is anyone else likely to help?

*Source: D. G. Jones, *Doing Ethics in Business: New Ventures in Management Development* (Cambridge: Oelgeschlager, Gunn & Hain, 1982).*

After reviewing these four elements, is your response to the case of the child molester any different than before? Why or why not? How should this case be handled if the agent is representing the buyer? Which model of ethical decision making—the Integrated Model or the Kew Gardens Model—do you think is more appropriate in resolving this dilemma?

THE WHITE LIE TEST

While many business issues deal with potentially catastrophic matters, such as bridge design and automotive safety, fortunately most ethical problems that real estate practitioners face do not involve life and death issues. More frequently, they

HOW WOULD YOU RESPOND?

The Fire

Buyers work with a relocation agent and purchase a home after obtaining appropriate inspections. The inspections reveal little of concern. Shortly after the buyers take occupancy, a teenager in the neighborhood comes for a visit, looks around the home, and remarks, “The Fried family (the sellers) sure did a good job of fixing the house after the big fire here last year.” The buyers call the relocation agent immediately and ask if the agent knew about the fire, and the agent responds “Yes.” When asked why the agent did not tell the buyers about the fire, the agent said that she did not want to unduly alarm the buyers, particularly because all of the damage from the fire had been “taken care of.”

deal with ethical issues that require them to choose between loyalty to their firms/colleagues and obligations to clients or the possibility of earning commissions. Some practitioners choose the “If I’m not asked, I won’t tell” philosophy about problems. Real estate professionals may also minimize problems or re-characterize them in a better light. But when serious defects or risks in properties come to light, courts have made it clear that risk is not considered a confidential issue and must be disclosed to clients and, in some cases, to the public.

Here are the questions to ponder regarding disclosure concerns:

- Why am I considering concealing this information?
- Is it because I want to spare the client or firm unnecessary concern?
- Am I concerned the client will not accept the firm’s proposal or go through with a contract if the truth is known?
- Do I not know how to tell the truth in a tactful way?
- How will failure to disclose appear to the prospective client?
- Will it appear as a white lie?
- Will the client say “Thanks for sparing our feelings?” or will they say “Now that we know you lied to us about this issue, what else have you lied to us about?” In other words, will my relationship with the client or firm be damaged?

Michael Josephson, founder of the Josephson Institute of Ethics, notes that in relationships of trust, any act of concealment, any undelivered promise, any exaggeration will be perceived as a lie. It is also likely that the lie will be found out, and when it is, the public is rarely forgiving of the professional who failed to provide information that was perceived as critical and necessary to their decisions. Most professionals don’t want to lie, but they often don’t know how to tell the truth.

Real estate licensing boards usually state that problems that have been *properly corrected* do not have to be discussed with prospective buyers. However, because it is often difficult for brokers to determine whether repairs have been properly dealt with, it is best to disclose the issue and let the buyers take the appropriate steps. In the case of a fire, it would be important to determine whether the fire was caused, for example, by faulty wiring or by a grease fire in the kitchen. The former would be of more concern than the latter, but brokers should disclose the occurrence so that the buyers can govern themselves accordingly.

THE PARENT TEST

Michael Josephson, a former attorney, became an ethicist when he first became a father. He realized that he did not want his children to decide ethical outcomes based on legal parsings and interpretations, which was the way he used to teach ethics to his law students. He suggests that a viable way of choosing the best ethical outcome is to take the perspective of a parent: “Would I do it if my children were looking over my shoulder?”

Even professionals who do not have children can benefit from this outlook. All of us are being observed—by our spouses, our families, our friends, and our work colleagues. They watch how we handle ourselves in tough situations. They learn from what we do, not from what we say. In this way, we are all role models for ethics (or lack of them), even if we did not ask for the nomination.

Considering what our children and peers would think and feel if they “caught us in the act” can be a powerful deterrent to unethical behavior. In Arthur Miller’s play, *All My Sons*, a father must defend his illegal conduct to his teenage son. He says, “Son, I’m no worse than anyone else.” His son responds, “No, Dad, you’re right. But I thought you were better.” None of us want to disappoint those who look up to us.

SUMMARY

No matter which model we use to help us resolve an ethical dilemma, our final course of action may be open to public and professional scrutiny. How will our peers judge us? How would your decision look on the front page of your local newspaper? While real estate professionals may think their decisions have only minor repercussions, we are often unable to foresee all of the consequences of our actions. Everything we say and everything we do sends a message.

REVIEW QUESTIONS

Choose the letter of the answer choice that best answers the question, and check your responses with the Answer Key at the back of the book.

- 1. The average adult uses Stage-4 thinking, a reasoning level that emphasizes ____.**
 - A. obedience and punishment
 - B. law and order
 - C. self-interest
 - D. peer pressure
- 2. Providing a good example by thinking and acting ethically is consistent with Kohlberg’s findings that ____.**
 - A. adults are attracted to higher moral reasoning
 - B. hypocrisy is an ineffective teacher of moral reasoning
 - C. politicians are dishonest
 - D. values should be taught in elementary school
- 3. The Integrated Model for Ethical Decision making requires the decision maker to consider ____.**
 - A. consequences of one’s actions
 - B. societal values
 - C. laws and policies
 - D. one’s conscience
 - E. all of these

4. **The Kew Gardens Principle imposes a special burden on the decision maker if that individual is _____.**
- A. the last resort
 - B. acting on conscience
 - C. capable of harming another
 - D. aware of the dilemma
5. **The Parent Test suggests that ethical problems may be resolved by which question?**
- A. Is it a temptation or a dilemma?
 - B. What would my attorney say?
 - C. How would a child resolve this problem?
 - D. Would I do it if my children were looking over my shoulder?

THE PURPOSE OF A CODE OF ETHICS

Sometimes called a credo or mission statement or code of conduct, a code of ethics is a vital document for any business, as breaches of ethics can land companies in serious trouble with consumers, other organizations, or government authorities. Creating a code of ethics makes decision making easier at all levels of an organization by reducing ambiguity and considerations of individual perspectives in ethical standards. A code of ethics can:

- inspire individuals and to exhort them to high principles of conduct
- regulate individuals by spelling out prohibited conduct
- provide guidelines for decision making in areas of discretion
- define and protect the company or industry's culture

Having a code of ethics doesn't prevent misconduct. Codes do, however, help clarify the baseline for behavior and set the minimum level of conduct we will tolerate from one another. Most industries and professional associations have a code of conduct. As mentioned in an earlier module, a code of ethics is both a vehicle for occupational identity and a mark of occupational maturity.

Codes of ethics vary in content, format, and length. For example, the Kraft/Heinz code of ethics contains just 10 short rules of ethical behavior that all employees must follow: make food that is safe to eat; market responsibly; treat people fairly; respect the free market; compete fairly; respect the environment; deal honestly with the government; keep honest books and records; never trade on inside information; and give Kraft Foods your complete business loyalty.

Objectives

By the end of this part, the reader will be able to:

1. describe the possible purposes of a code of ethics
2. discuss the key differences between the 1913 National Association of REALTORS® (NAR) Code of Ethics and the current version
3. contrast the reasonable person standard and the professional practice standard
4. identify aspirational elements in the Preamble to the NAR Code of Ethics
5. analyze the significance of Article 1 and Article 2 of the NAR Code to real estate practitioners
6. briefly describe the professional standards enforcement process of a local association of REALTORS®

KEY TERMS

code of ethics
mediation
NAR Code of Ethics
Preamble
professional person standard
reasonable person standard

The Colgate-Palmolive code of ethics is a lengthy document, but it is broken down into 10 individual areas of conduct: Our Relationship with Each Other; Our Relationship with the Company; Our Relationship with Our Board of Directors; Our Relationship with Other Business Entities; Our Relationship with Consumers; Our Relationship with Government and the Law; Our Relationship with Society; Our Relationship with the Environment; Our Relationship with Shareholders; and Our Responsibility for Compliance.

Can a code of conduct help a company or industry navigate treacherous ethical terrain? The 1982 Tylenol tampering case serves as the gold standard in terms of crisis management. The tragedy took place when seven people in the Chicago area collapsed suddenly and died after taking Extra-Strength Tylenol capsules, manufactured by McNeil Consumer Healthcare, a subsidiary of Johnson & Johnson. The pills had been laced with cyanide. This was the first known case of product tampering. Johnson & Johnson faced an immediate crisis with little guidance to go by except the company's credo. According to the company, it was this aspirational document that helped them to manage the crisis in an ethical manner.

Following disclosure of the tainted product, the firm removed the product from the shelves of supermarkets, provided free replacements of Tylenol capsules with the tablet form of the product, and made public statements of assurance that the company would not sell an unsafe product. The company became a model for how to handle an ethical crisis.

Here is the critical passage in the company's credo that compelled the firm's action: "We believe our first responsibility is to the doctors, nurses, and patients, to mothers and fathers and all others who use our products and services. In meeting their needs, everything we do must be of high quality."

The National Association of REALTORS® (NAR) Code of Ethics was first adopted in 1913 and was one of the first codifications of ethical duties adopted by any business group. Modeled on ethical codes of physicians, engineers, and lawyers, the Code was created before California enacted the first real estate license law in the country in 1919.

The current NAR Code consists of 17 Articles, 71 supporting Standards of Practice, and 131 explanatory case interpretations. However, the 1913 version was considerably shorter than today's version and uses some language and references that seem quaint by comparison.

THE 1913 CODE OF ETHICS

The Duty of Real Estate Men toward Their Clients

The real estate agent should be absolutely honest, truthful, faithful, and efficient. He should ever bear in mind that he is an employee, that his client is his employer and is entitled to the best service the real estate

man can give, his information, talent, time, services, loyalty, confidence, and fidelity.

A real estate agent should be conservative in giving advice, and where he is not reasonably well posted should refrain from giving his opinion of value.

A real estate agent should inspect his client's property, if possible, before offering it for sale, and he should always inform the buyer if he has not done so.

An agent should not depreciate the price of property unless the price is too high; he should ask that the price be reasonable and tell the owner that it must be so if he expects his agent to make an attempt to sell it.

An agent should have the sole agency, in writing, if it is property he is willing to make a special effort to sell.

An agent should advocate either the real consideration to be shown in a deed to property, or one dollar and other valuable considerations.

An agent should not give special information to inquirers over the telephone or otherwise, unless they are willing to give their names and addresses. Let them understand he deals in the open and expects them to do likewise.

An agent should not ask for a net price on property, unless he intends to buy it himself and so notifies his client.

An agent should request his client not to discuss price with the prospective buyer, but persuade his client to refer the matter to the agent, thus strengthening the agent's position with the buyer, and thus helping the agent to make a better deal for his client.

An agent should always exact the regular real estate commission prescribed by the board or exchange of which he is a member, and should always give his client to understand at the beginning that he is entitled to such, and expects it.

The Duty of a Real Estate Man to Other Real Estate Men

An agent should respect the listings of his brother agent and cooperate with him to sell, provided the other agent has the most suitable place.

An agent should advise an owner to renew a selling contract with some other agent rather than solicit the agency himself, provided the other agent has made a reasonable attempt to sell the property during the life of his contract.

An agent should always be loyal, square, frank, and earnest in the matters that require the cooperation of brokers, and should always speak

kindly of his competitors, refusing to pass judgment on others from hearsay evidence.

An agent should not advertise anything but facts, and should be careful not to criticize by any method a competitor's proposition.

An agent should give an honest opinion concerning a competitor's proposition when asked to do so by a prospective purchaser, even though such opinion will result in a sale by the competitor.

An agent should refuse to put a "For Sale" or "For Rent" sign on property on which his competitor already has his sign, providing the placing of such sign was through the authorization of the owner.

If an agent cannot efficiently handle a proposition, he should refer the matter to some competitor who can.

An agent should solicit cooperation of the members of the board in selling sole agency listings unless he has a deal on or has some particular buyer in sight to whom he expects to make a sale, and he should always be ready and willing to divide the regular commission equally with any member of the board who can produce a buyer for any of his clients.

An agent should invoke friendly arbitrations by the real estate board, rather than action through the courts of law, in settling differences between himself and other agents.

He should not disregard the rights of other agents. He should never take the position with an owner that he will not work through his regular agent, or that he will not try to sell his property to a live buyer he may have unless he handles the entire deal and gets all the commission.

He should not put his name in the newspapers in connection with a deal unless really representing at least one of the parties and receiving a part of the commission, for such publicity is a sham, and the result is to the disadvantage of all.

When a sale or exchange is handled by two agents, each agent shall be given due credit in the report of such sale or exchange.

He should not relay property, which means he should not submit to one agent that which he obtains from another agent, unless in exceptional cases, and then he should let the third agent know that he does not have the property directly. For in case he relays, he represents neither side, and is not entitled to the same consideration as either of the other agents.

STANDARDS FOR BUSINESS CONDUCT

Codes of ethics have their shortcomings. One problem is the complexity of issues that cannot easily be reduced to a simple statement. The problem of dealing with complex issues is that codes written too broadly can be difficult to apply. The other concern is the potential gap between the ethical requirements of a society and the standards of a particular group. Additionally, a code may also experience significant time lags in reflecting changes in community standards or needs.

For example, building codes often do not change until damage is done or a tragedy results. The tragedy in 1942, when the Cocoanut Grove nightclub in Boston, Massachusetts, burned down, compelled architects, interior design professionals, and government officials to establish much higher safety standards. On the night of the fire, more than one thousand revelers occupied the club. A lit match used while changing a light bulb ignited flammable decorations, and the fire spread rapidly. Authorities estimated that perhaps as many as 300 of the 491 people who died could have been saved had the nightclub doors swung outward. The Cocoanut Grove fire prompted major efforts in the field of fire prevention and control for nightclubs and other related places of assembly. Immediate steps were taken to provide for emergency lighting and occupant capacity placards in places of assembly. Exit lights were also required as a result of the concern generated by this fire.

Building and occupancy codes at the time of this tragic fire simply did not anticipate the consequences of poor design. Likewise, codes today cannot keep pace with new technologies that permit us to create new ideas, products, and materials.

The economic meltdown experienced by many countries in the 2000s provides another example of the potential gap between an industry or profession and consumers' needs for ethical conduct by those groups. For example, unregulated or poorly regulated lenders and other financial services providers were largely to blame for many banking failures, and, as a consequence, countries responded by establishing new oversight agencies, laws, regulations, and other supervisory measures. It wasn't until after these failures that statutory codes and laws were enacted and/or enforced.

For example, in the United States, the 2010 Dodd-Frank Wall Street Reform and Consumer Protection Act created the Consumer Financial Protection Bureau (CFPB). A legislative response to the financial crisis of 2007–2008 and the subsequent fallout, the CFPB demonstrates that when an industry fails to police itself, it is not unusual for jurisdictions to take action.

In the wake of the Enron and Worldcom corporate scandals, codes of ethics have taken on yet another dimension. Legislation passed in 2002, the Sarbanes-Oxley Act (“SOX”), requires that corporations whose stock is traded under the provisions of the Securities Exchange Act of 1934 must publish their codes of ethics, if these exist, and also publish any changes to these codes as they are made. This requirement has given corporations strong incentives to formulate codes of ethics in order to win investor confidence.

Sometimes, victims of financial malpractice don't wait for legislation to change the way business is done. Sometimes, they take their cases to court. How are professionals judged when they are brought in front of a jury?

In some cases, when professionals are brought to court, the court chooses to use another test of reasonableness in business conduct, referred to as the reasonable person standard. In some cases, the test is the professional person standard.

THE REASONABLE PERSON STANDARD

The reasonable person standard assumes a hypothetical person in society who exercises average care, skill, and judgment in conduct and who serves as a comparative standard for determining liability. Beauchamp and Bowie describe the elements of the reasonable person standard as follows:

- Customers or public representatives judge whether professional determinations are adequate in terms of standards of reasonableness.
- A professional's conduct may be found negligent or otherwise deficient even if his or her behavior conforms perfectly to recognized and routine professional practice.
- The reasonable person standard is objective in that it is designed to incorporate the common body of assumptions that the members of a society make about their fellow citizens to cooperate efficiently.

Consider an employee going to a supervisor with a complaint about sexual harassment from a co-worker or leaving extension cords strewn in a hallway. Turning a blind eye to harassment between co-workers or forgetting to wind up the extension cord in the hallway are the sorts of omissions that the hypothetical "reasonable person" would respond to with some urgency because the danger of ignoring these problems is obvious and imminent. Moreover, a reasonable person would take positive actions to prevent harm, such as sexual harassment training and changing the location of outlets, if necessary. These are the responses of a reasonable person.

Similarly, if an employee indicates that a co-worker could possibly be embezzling from client accounts, a supervisor would take immediate action to determine if the allegation is true. A reasonable person would also have internal controls, such as adequate supervision and training of staff and a protocol for the careful review of work, to ensure that embezzlement does not occur.

THE PROFESSIONAL PRACTICE STANDARD

The professional practice standard is another test often used in court to examine appropriate business conduct. In civil court cases, professional organizations' codes are often cited as the norm for conduct. The professional practice standard holds that duties are properly determined by the customary practices of a professional community.

Here are the key elements of a professional practice standard:

- Duties and other standards of moral conduct are determined by the customary practices of a professional community.
- A business person is charged professionally with various responsibilities (for example, avoiding harm, honoring warranties, removing conflicts of information, and obeying legal requirements) and must use proper professional criteria for determining appropriate actions.
- Custom in the profession establishes the standards of obligatory conduct, such as “due care.”
- Because a person without expert knowledge is unqualified to establish what should be done, the professional community is the appropriate source of standards.

REALTORS® are different from non-member licensees in that they voluntarily subscribe to the NAR Code of Ethics.¹ The Code of Ethics is an illustration of the professional practice standard and is routinely used by judges and jurists to determine the verdict in cases against real estate licensees, regardless of whether those licensees are members of the the NAR.

Because of the NAR Code’s importance to its numerous members and because it is used as a standard by which to judge all brokers, the Code is worthy of a more elaborate review; the entire can be found here: www.nar.realtor/about-nar/governing-documents/code-of-ethics/the-code-of-ethics. A brief summary of the Code of Ethics appears later in this chapter.

The NAR Code of Ethics

The NAR Code is a living document that undergoes regular revision to keep it updated and relevant as the real estate industry evolves, so today’s Code of Ethics looks much different from the one that was adopted in 1913. Social customs, industry practices, and federal laws have had a significant impact on the Code. No longer do we see references to “real estate men” or “brothers.” References to clients can include not only sellers and buyers but also landlords and tenants. References to technology, such as telephones, in the first version of the Code are gone, and terms like “metatags” have replaced them to keep up with changing times. Fair housing and agency legislation and other laws have also influenced revisions, deletions, and additions to the Code.

¹“REALTOR” is a trademarked term that refers to a real estate agent who is an active member of the National Association of REALTORS® (NAR), the largest trade association in the United States. Headquartered in Chicago, NAR has more than one million members across the country. Members may also be property managers, appraisers, real estate counselors, and other professionals involved in the real estate industry.

THE PREAMBLE

The Code of Ethics was over a decade old before the preamble was introduced. In 1924, the Association's committee assigned with revising and modernizing the Code decided that the rules should have an introduction, and they prepared two versions of a preamble for consideration. The first one was written as a personal pledge, but the second one, which was the one accepted by the board of directors, was considered more poetic. Written by a minister, the Preamble "... [set] forth the social responsibility of the association and of the local real estate boards who make up its membership."²

In 1955, the Preamble was revised, but in 1961 the NAR went back to its original wording. The Preamble as it appears today changed one more time in 1994, when the first six Articles of the Code were incorporated into the Preamble, adding the paragraphs regarding REALTOR® obligations to share their professional knowledge and stressing the importance of maintaining a spirit of cooperation with other real estate professionals.

It should be noted that a member of the National Association of REALTORS® cannot be expelled from the organization because of a violation of the Preamble. The Preamble is meant to be aspirational rather than enforceable. The Preamble cannot be used as a basis for disciplinary action against a REALTOR®. Only the Articles of the Code are used as the basis for discipline.

Of the numerous lofty ideals expressed in the Preamble, two deserve special mention: sharing knowledge and experience, and the Golden Rule. REALTORS® are exhorted to "willingly share the fruit of their experience and study with others." This concept encourages a high standard rarely established by business and professional groups. As a general rule, business competitors do not share the lessons of their experience with each other for the benefit of the public. Rather, such experience is zealously guarded, lest it fall into the hands of competitors. But REALTORS®, although intensely competitive with each other, at the same time cooperate with each other in the best interest of clients and customers. In cooperative transactions, it is desirable that the combined professional abilities and talents, as well as the shared commitment to high standards of conduct, prevail.

The collegial spirit also benefits competitors. Veteran brokers know that they will do business with their colleagues many times during their careers. Not only does it reward long-term relationships if co-brokers help each other, but this spirit also makes transactions go more smoothly for the benefit of all participants. Moreover, cooperation and mentorship helps the public realize the challenges of the profession and brings more respect to everyone in the industry.

The Preamble also refers to the Golden Rule: Treat others as you would want to be treated. The Golden Rule is a pillar of most of the world's religions, and it lies at the heart of secular ethics. It is an expression of the basic human instinct to bond with others, to feel their pain, and to act accordingly. The Golden Rule is a unilateral moral commitment to others without the expectation of anything in return.

²<http://infoservices.blogs.realtor.org/2013/02/05/uncovering-the-origins-of-%E2%80%9CUnder-all-is-the-land%E2%80%A6%E2%80%9D/>.

Here are some examples of the Golden Rule from various ethical systems and religious texts:

Confucius: What you do not want done to yourself, do not do to others.

Aristotle: We should behave to others as we wish others to behave to us.

Judaism: What you hate, do not do to anyone. All else is commentary.

Hinduism: Do nothing to thy neighbor which thou wouldst not have him do to thee thereafter.

Islam: No one of you is a believer unless he loves for his brother what he loves for himself.

Buddhism: Hurt not others with that which pains thyself.

Christianity: Do unto others as you would have them do unto you.

There is scientific evidence that the Golden Rule has its origins in the way that human brains operate. One neurobiologist suggests that human beings have neural mechanisms that make us care about others. These systems generate empathy by making us literally feel another's pain in our own brains. This mirroring of emotion often motivates us to alleviate the other's distress. The key molecule inducing empathy is called oxytocin, a simple chemical ancient in origin that motivates us to care about others, even complete strangers. Oxytocin released in the brain modestly moves the balance between distrust and trust of others toward the latter. It is trust that causes us to play fair.³

Is the Golden Rule a practical business strategy? According to one analysis, when a company treats you right or sells you a terrific product, you feel happy. You feel loyal. You're likely to buy more from that company. You're likely to recommend that company's products and services to friends, family, and colleagues. And here's some math: *In most industries, companies that are the loyalty leaders have a compound annual growth rate that is more than twice that of their competitors.* [Emphasis added.]

The reverse is true as well. When customers feel mistreated or misled, they give what they get. They leave—if they can—and they complain if they can't. They demoralize your employees, and they badmouth your company, alienating your prospects. They're costly.⁴

³Donald W. Pfaff, *The Neuroscience of Fair Play: Why We (Usually) Follow the Golden Rule*. (New York: Dana Press, 2007).

⁴<https://www.linkedin.com/pulse/20121106215128-7928939-why-the-golden-rule-is-good-business>

As discussed earlier, the current NAR Code of Ethics has three sections: Duties to Clients and Customers (Articles 1–9); Duties to the Public (Articles 10–14) and Duties to REALTORS® (Articles 15–17). They are summarized here:

A BRIEF SUMMARY OF THE CODE OF ETHICS⁵

<p>Article 1 Protect and promote your client’s interests, but be honest with all parties.</p>	<p>Article 10 Provide equal service to all clients and customers. Reveal all pertinent facts, but do not reveal facts that are confidential under the scope.</p>
<p>Article 2 Avoid exaggeration, misrepresentation, and concealment of facts that are confidential under the scope of your agency relationship.</p>	<p>Article 11 Be knowledgeable and competent in the fields of practice in which you ordinarily engage. Obtain assistance or disclose lack of experience if necessary.</p>
<p>Article 3 Cooperate with other real estate professionals to advance client’s best interests.</p>	<p>Article 12 Present a true picture in your advertising and other public representations.</p>
<p>Article 4 When buying or selling, make your position in the transaction or interest known.</p>	<p>Article 13 Do not engage in the unauthorized practice of law.</p>
<p>Article 5 Disclose present or contemplated interest in any property to all parties.</p>	<p>Article 14 Be a willing participant in code enforcement procedures.</p>
<p>Article 6 Avoid side deals without the client’s informed consent.</p>	<p>Article 15 Ensure that your comments about other real estate professionals are truthful, not misleading.</p>
<p>Article 7 Accept compensation from only one party, except with full disclosure and informed consent.</p>	<p>Article 16 Respect the agency relationships of other exclusive relationships, recognized by law, that other REALTORS® have with their clients.</p>
<p>Article 8 Keep the funds of clients and customers in escrow.</p>	<p>Article 17 Arbitrate contractual and specific non-contractual disputes with other REALTORS® and with your clients.</p>
<p>Article 9 Assure, whenever possible, that transactional details are in writing.</p>	

⁵Greater Rochester Association of REALTORS®, https://www.grar.org/file/sites%07C*%07C662%07C*%07CResources%07C*%07Cgr4briefsummaryofethicscode.pdf.

While all of the Articles merit discussion and analysis, Articles 1 and 2 are most frequently cited in complaints filed against REALTORS®. In general, issues regarding representation and disclosure, the subjects of Articles 1 and 2, are the most common causes of litigation against real estate brokers. According to a NAR report, breach of fiduciary duty lawsuits accounts for the largest single number of residential real estate–related court cases. Notably, in the cases where a determination was made, licensees were found liable only 40% of the time. Nevertheless, brokers who are sued must still bear the financial and professional trauma of the lawsuit. The NAR report indicated that property condition disclosure and “as is” clauses are an ongoing source of disputes and the second-most common legal issues faced by members.⁶

ARTICLE 1

The nature of real estate brokerage services, particularly those provided in residential sales transactions, has changed significantly in the last 70 years. Through the 1950s, real estate brokerage firms were primarily one-office, family-run operations. The broker listed the owner’s property for sale and found a buyer without assistance from other companies. Then the sale was negotiated and closed. It was relatively clear that the broker represented the seller’s interests. But things started to change in the 1960s when brokers started to share information about properties they had listed by participating in a multiple-listing service (MLS). This sharing resulted in two brokers or firms cooperating with one another to sell a property.

The result was confusion over which party the brokers represented in co-brokered transactions. Consumers thought that the broker who had the property listed for sale represented the seller, and the broker who found the buyer represented the buyer. However, this was not the case. Up until the mid-1990s, it was commonplace in these shared transactions that both brokerage firms and their brokers or salespersons represented the seller as agents and owed all loyalty to the seller and owed no duties other than honesty and fairness to the buyer.

Brokers were as confused as the public. Often brokers who worked with buyers felt a closer kinship with their buyers but had to act in their legal capacities as representatives of the seller. These brokers were subagents of the seller and the seller’s listing firm. Sometimes this subagency relationship was established by a local MLS, which provided for a unilateral subagency, a relationship created when a seller listed property with a listing broker or firm.

This confusion ultimately led to a lawsuit that gained national prominence and forced the industry to acknowledge that often buyers were harmed by their lack of information about agency relationships. (See Part 3, Applied Ethics, and the Edina Realty lawsuit.) Starting in the mid-1990s, U.S. states passed legislation coercing real estate firms and their affiliated brokers to more candidly disclose the possibilities of representation.

⁶<https://www.nar.realtor/articles/top-legal-risks-members-face-today>.

Today's consumers are much more likely to receive information about agency relationships early in their dealings with brokers. They are also likely to have much more choice in whether they are going to be represented or not.

The Edina case also motivated brokers to re-evaluate their services. They choose whether they will represent the seller, the buyer, or both (if permitted by state law) in the sale or rental of property. They also must decide how they will cooperate with other brokers in a transaction. Since the Edina case, the brokerage business has undergone many changes as brokers focus on ways to enhance their services to buyers and sellers.

As a consequence of these industry changes, the NAR Code now anticipates the possibility of a variety of agency and even non-agency relationships where the seller, buyer, landlord, or tenant could be clients or customers. Article 1 also emphasizes that, regardless of a legal relationship between a REALTOR® and a principal, the duty of honesty remains an ethical obligation. (See Part 3 for a more extensive discussion of the application of Article 1.)

ARTICLE 2

Article 2 of the NAR Code of Ethics cautions that REALTORS® should not exaggerate, misrepresent, or conceal relevant facts relating to the property or the transaction. Further, REALTORS® are not obligated to discover latent defects in the property or to disclose those matters that are confidential as described by various state laws.

This mandate is challenging to follow because of the patchwork quilt of legislation and rules under which brokers operate. The general standard is that brokers must disclose to any and all consumers, regardless of agency relationship, any property defect, such as a defective heating system. However, some states also require that brokers disclose that a seller is facing imminent foreclosure or a short sale, or that prospective buyers have poor credit. These disclosures may be required despite rules regarding client confidentiality.

In some states, it is unlawful to disclose issues related to stigmatized properties; for example, it may be unlawful to disclose that a murder or a suicide took place on the property. Yet in some U.S. jurisdictions, it is required to disclose certain crimes, such as murders, that took place on the property within a certain period of time prior to the listing. In some states, such as Georgia, there is a geographical limitation to disclosure: the broker must also inform the buyer of any material information known to the broker about the neighborhood within one mile of the home.

Even the definition of “material facts” varies from state to state, and independent of those definitions, buyers often believe that information about a property that is important to them is therefore “material.” In other words, buyers may want to know about the ethnicity of the neighbors, but real estate brokers are not permitted under federal and state fair housing laws to discuss these matters.

Some states require that sellers complete and provide to buyers comprehensive property disclosure forms and separate forms about issues such as Megan's Law, radon, or mold. Federal laws may also require property owners to make disclosures. Some of these forms, once completed, may create

liability for the owners; some do not, permitted the owners to answer “no representation.”

It is no wonder that consumers sometimes think that they have not been the recipient of important information and allege that their brokers have omitted or misrepresented critical information. (See Chapter 3 for a discussion of cases regarding disclosure issues.)

ENFORCEMENT OF THE NAR CODE

The enforcement of the NAR Code is handled mainly by local REALTOR® associations. The Code describes the enforcement process that is available to anyone who believes a REALTOR® has committed a violation of the Code. Associations of REALTORS® only determine whether the Code of Ethics or association membership duties have been violated, *not* whether the law or real estate regulations have been broken. When broken laws or regulations are suspected, or when the real estate professional is not a REALTOR®, consumers should contact the real estate licensing authority in that jurisdiction or take their concerns to the courts. If litigation is being pursued by the complainant, the local association typically will not proceed with the ethics or arbitration complaint until the litigation has concluded.

There two basic types of complaints that are handled by local associations: ethics complaints and requests for arbitration.

An ethics complaint is a complaint about the conduct of a REALTOR® who has allegedly violated one of the Articles of the Code of Ethics. Under Article 17 of the Code, REALTORS® are required to arbitrate certain types of monetary disputes they have with other REALTORS®. So, a second type of matter handled most frequently by local associations is a request for arbitration falling under Article 17 of the Code.

Generally, a request for mandatory arbitration is based on a monetary dispute. The dispute must be of a contractual or specific non-contractual nature, and it must be between REALTORS® (principals) in different firms arising out of their relationship as REALTORS®. Article 17 specifies the types of disputes that are required to be arbitrated. A request for arbitration is most commonly based on a dispute about a cooperative (selling) commission, sometimes also known as a co-brokerage commission. In the residential field, the offer of compensation is most commonly made by a listing broker in the context of filing listings with the MLS. In the commercial field, offers of compensation are often made directly among brokers in a market.

There are three committees or groups that are involved in the Code enforcement process: the Grievance Committee, the Professional Standards Committee, and the Board of Directors

The Grievance Committee is a screening committee that initially reviews ethics complaints and requests for arbitration. The Grievance Committee does not hold hearings but simply determines, on the basis of the written information presented in the complaint/request, whether a possible violation of the Code may exist or whether the request for arbitration presents a matter that can be arbitrated within Article 17.

If the Grievance Committee believes that a possible violation may exist or that a matter can be arbitrated, it forwards the complaint/request to the Professional Standards Committee. The Professional Standards Committee appoints a hearing panel (usually three or five members of the Committee) to conduct a hearing. The hearing is a due process hearing similar to a court proceeding. The hearing panel decides whether a violation of the Code occurred and makes a recommendation for discipline, if any. In an arbitration request, the hearing panel decides which party is entitled to a monetary award. In either case, a right of appeal or review exists to the Board of Directors. See Figure 2.1.

As part of the due process that is afforded to those involved in complaints, there may be hearings where the parties can bring legal counsel, and there may be penalties (the most extreme being expulsion from the association). A common remedy for disputes, and a method that has become more popular for resolving conflicts, is mediation. **Mediation** is an entirely voluntary alternative dispute-resolution method that is available to parties to an arbitration dispute. Mediation provides an opportunity for the parties to come together in an informal setting to resolve their differences amicably without the time and expense of a formal arbitration proceeding. It is not required and is not intended as a substitute for arbitration.

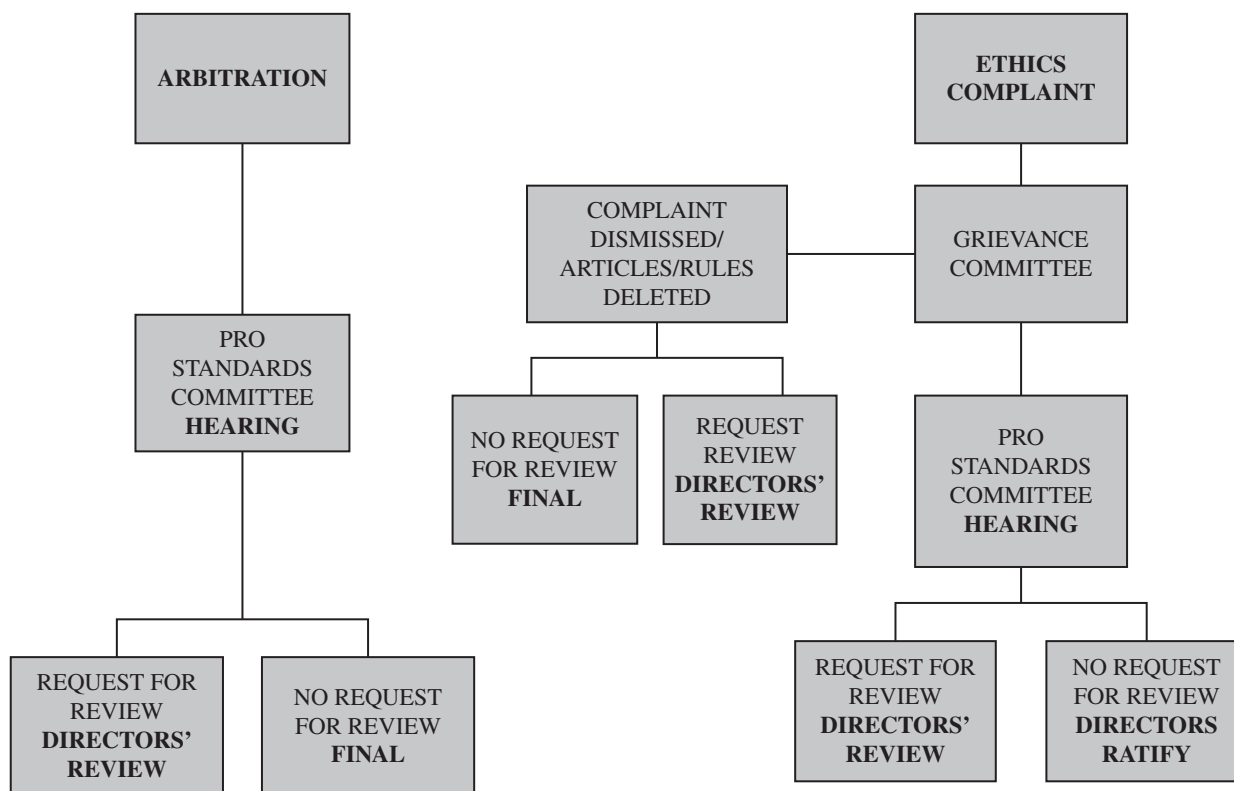


Figure 2.1 Code enforcement process.⁷

⁷<https://www.ivaor.com/association/professional-standards-and-ethics/>.

SUMMARY

As discussed earlier, the NAR Code of Ethics provides a framework for acceptable conduct for real estate professionals and serves as an example of the professional practice standard. In many cases, the professional practice standard and the reasonable person standard will bring us to the same conclusion: the practitioner was (or was not) negligent. In other circumstances, the reasonable person standard would hold us to a tougher standard; that is, it would have us consider what an average practitioner would need to know about risks, alternatives, and consequences to make an informed decision rather than consider routine practices in the real estate industry.

Of course, not all ethical dilemmas can be resolved using professional codes of ethics. Some of our dilemmas are going to be the result of new technologies that no one anticipated when codes and policies were written. This will be particularly true of medical research, where genome research will make it possible to alter the DNA of humans. The ethical implications are difficult to imagine. A code of ethics developed today may be inadequate to cope with the challenges of tomorrow.

Some ethical dilemmas will not be from the workplace. They will be personal, perhaps rooted in family relationships and friendships. Again, a professional code of conduct may not be of much use.

In many cases, ethical dilemmas are resolved privately. No one may be aware of our thoughts or actions in the unfolding events. In fact, in many situations, our thoughts and actions are not often held up to the scrutiny of our peers and colleagues. We may think to ourselves, “Who will know? Who will ‘catch’ me?”

It is at these times, when laws, regulations, and codes of conduct may provide little guidance or relief, that we must rely on our personal codes of ethics. Once we are aware of our deepest values and the fundamental principles that guide our choices, that give use our identities and self-esteem, we are empowered. Our personal environments may change daily, but with these principles we have an unchanging personal constitution that allows us to act ethically.

Of course, knowing what the right thing is can be different than acting ethically. The only way to make the right choice is having the will to do so. We must see ourselves capable of doing the right thing, having the moral courage to do so, and believing that we can make a difference in the lives of people who depend on us.

Recall the story of the starfish:

A young man is walking along the ocean and sees a beach on which thousands and thousands of starfish have washed ashore. Further along he sees an old man, walking slowly and stooping often, picking up one starfish after another and tossing each one gently into the ocean. “Why are you throwing starfish into the ocean?” he asks. “Because the sun is up and the tide is going out, and if I don’t throw them further in they will die.” “But, old man, don’t you realize there are miles and miles of beach and starfish all along it! You can’t possibly save them all. You can’t even save one-tenth of them. In fact, even if you work all day, your efforts won’t make any difference at all.” The old man nodded calmly and then bent down to pick up another starfish and threw it into the sea. “It made a difference to that one.”

If we root our personal code of ethics in moral principles, we can offer guidance and inspire others. Ethics is vital to our success as professionals, as wives and husbands, as parents, as friends, and, ultimately, as human beings.

REVIEW QUESTIONS

Choose the letter of the answer choice that best answers the question, and check your responses with the Answer Key at the back of the book.

1. **Which statement is FALSE regarding the NAR Code of Ethics?**
 - A. It was created before any state enacted licensing laws.
 - B. It has been revised numerous times since it was first enacted.
 - C. It is an example of the reasonable person standard.
 - D. It has three sections: duties to clients and customers; duties to the public; and duties to REALTORS®.

2. **The reasonable person standard _____.**
 - A. considers what an average practitioner would need to know about risks, alternatives, and consequences to make an informed decision
 - B. holds that duties are properly determined by the customary practices of a professional community
 - C. is illustrated by the NAR Code of Ethics
 - D. is never used by judges and juries

3. **The Golden Rule _____.**
 - A. refers to the common business precept that “He who has the gold, rules”
 - B. originated in the United States
 - C. is not mentioned in the NAR Code of Ethics
 - D. considers the impact of behavior on others

4. **The issues that cause REALTORS® and brokers the most problems in terms of complaints and litigation are _____.**
 - A. zoning and plumbing problems
 - B. title issues and property defects
 - C. foreclosures and short sales
 - D. representation and disclosure

5. **Under Article 17 of the Code, REALTORS® are required to _____ certain types of monetary disputes they have with other REALTORS®.**
 - A. litigate
 - B. settle
 - C. arbitrate
 - D. mediate

ETHICS AND AGENCY RELATIONSHIPS

Many issues in the real estate business have ethical dimensions. Relationships with colleagues and competitors, political involvement in zoning and development matters, and environmental hazards are just three areas that generate ethical dilemmas. Of the many controversial issues that test the soul of today's real estate practitioner, none is more rankling than that of agency. Even state regulators have not been able to create rules or regulations that simply, fully, and satisfactorily deal with this complex issue. (See discussion in Part 2.)

Very broadly, an agent is someone who represents the interests of one person or party in dealing with another. An agent offers specialized expertise and a **fiduciary relationship** to clients. A fiduciary relationship usually includes legal responsibilities, such as loyalty, confidentiality, full disclosures of all known facts, obedience, reasonable skill and care, and accountability.

Many professionals act as agents: physicians, attorneys, accountants, as well as real estate professionals. But few professionals work so closely with adversarial parties as real estate agents do. Agents who work for sellers frequently work with buyers, and almost as often, agents who work for buyers also work with sellers in the same transaction. The majority of states and the District of Columbia require that whomever the agent represents—whether it is the buyer, the seller, neither, or both—the parties who are unrepresented must be made aware of this agency relationship. Some states' requirements allow agency relationships to be disclosed as late as the signing of a contractual offer. Other states require that disclosure be made very early in the relationship between the agent and the parties to the transaction.

In addition to dealing with these various disclosure requirements, practitioners must also grapple with the complex relationship with buyers and sellers. In the past,

Objectives

By the end of this part, the reader will be able to:

1. describe the possible agency and non-agency relationships between real estate professionals and buyers and sellers
2. describe and evaluate options in dealing with ethical dilemmas in agency relationships
3. identify and describe illegal discriminatory conduct
4. describe and evaluate options in dealing with ethical dilemmas in fair housing
5. describe and evaluate options in dealing with ethical dilemmas and property defects
6. define circumstances that create a stigmatized property
7. describe and evaluate options in dealing with ethical dilemmas in relationships with competitors
8. describe and evaluate options in dealing with ethical dilemmas in relationships with colleagues
9. identify the NAR Code of Ethics articles that pertain to the various case studies in this section and apply them appropriately

KEY TERMS

buyer's broker caveat emptor
disparate impact
dual agency broker facilitator
fiduciary
gender identity
latent defects
limited agent
procuring cause
seller's broker
sexual orientation
single-agency broker
stigmatized properties

When self-interest, rather than honor, duty, and ethical obligation, determines choice, one cannot expect people to live up to their moral potential. And those who use others as mere instruments of personal goals, teach others to do likewise.
—MICHAEL JOSEPHSON

real estate practitioners were usually employed by the seller. In that role, the practitioner's objective is to obtain the best possible price and terms for the seller from a buyer. Buyers traditionally have been in the role of customers, not clients. However, with the public's rising awareness about the various roles a real estate agent can play, many buyers now insist on representation.

As a result, brokers today must consider not only offering buyers representation but also a number of alternative relationships with sellers and buyers.

Seller's broker: This is the most traditional form of operation in the real estate business. In this type of brokerage, the firm represents sellers, never buyers. Seller brokerage firms encourage their agents to get listings. While seller brokerage firms work *with* buyers, they never work *for* buyers. Buyers are always customers, never clients. Thus, they can expect honesty and information but they can never expect advice or confidentiality. Seller's brokers must disclose their relationship to buyers. Buyers should then be offered options: they can choose to remain unrepresented or they can choose representation by another broker or by an attorney.

Buyer's broker: In this form of brokerage, the firm represents only buyers. This firm never takes employment (listings) from sellers. Sellers are treated as customers and buyers are treated as clients. Buyer brokers negotiate the best possible price and terms for their buyers.

AN AGENT'S DUTIES/RESPONSIBILITIES TO THE CLIENT AND THE CUSTOMER

Agent	
Client	Customer
Client-Level (Fiduciary) Services	Customer-Level Services
1. Salesperson works <i>for</i> client	1. Salesperson works <i>with</i> customer
2. Loyalty (good faith)	2. Good faith
3. Confidentiality	3. Honesty
4. Full disclosure	4. Disclosure of facts/property condition
5. Obedience	5. Good service
6. Accounting for all aspects of transaction	6. Accounting for escrow funds
7. Care, skill, and diligence	7. Reasonable care, skill, and diligence
8. Advice	8. Information
9. Advocacy	9. No advocacy
10. Relationship based on highest degree of trust and confidence	10. Relationship based on ordinary degree of trust and confidence

Single-agency broker: The single-agency firm represents only one side of the transaction: *either* the seller *or* the buyer. This type of brokerage will accept employment from sellers (e.g., take listings) or from buyers (e.g., act as buyer brokers). The single-agency broker will never get involved in representing both in the same transaction (dual agency).

The advantage of this approach for brokers and consumers is that the consumer is always treated as a client or principal. If consumers want to sell their properties, the single-agency brokerage can represent them. When the same consumers now want to buy property, the same brokerage firm can represent them. Single-agency brokerage is the only way a firm can represent clients as they move through various transactions and maintain a fiduciary relationship.

Dual-agency broker: The dual-agency broker represents *both* the buyer *and* the seller in the same transaction. Dual agency requires informed consent to be legal. Often dual agency happens accidentally due to lack of proper disclosure. For example, seller's brokers allow the buyer to share confidential information (such as negotiating strategy) without clearly warning the buyer of the broker's role. Accidental dual agency is unlawful.

Designated (dual) agency: This form of lawful dual agency is recognized in some states and permits the brokerage firm to assign one licensee from the firm to represent the seller and another licensee to represent the buyer. Even though the firm still acts as a dual agent, the buyer and seller should be able to receive a high level of advocacy and other elements of a fiduciary relationship from their individual agents.

Facilitator: This is a form of brokerage in which the real estate practitioner represents *neither* the buyer *nor* the seller. The real estate practitioner brings the parties together and acts as a conduit through which offers and information are passed between both parties. Facilitators do not have a fiduciary relationship with buyers or sellers. Facilitators are also called *mediators* or *transaction brokers*. A growing number of U.S. states now require facilitation as the default relationship.

Limited agent: This form of dual agency permits the real estate firm to represent both the buyer and the seller without owing the full range of fiduciary duties to both. In the states that permit limited agency, practitioners are permitted to keep confidential information regarding the clients' motivation to buy or sell, the terms they are willing to offer or accept, and other similar matters. Limited agents must provide accounting and disclose material matters to both parties.

The Edina Realty lawsuits demonstrate that it is best to establish a policy regarding the type of agency representation a brokerage firm will practice and to disclose that representation to all parties as soon as is possible. The majority of states require that licensees must disclose their agency status at first substantive contact.

Even if state law permits brokers and salespeople to disclose representation late in the relationship with consumers, it's not a good idea to delay: waiting increases the possibility of dual agency. The reason dual agency is likely to occur under these circumstances is that buyers and sellers begin to place a degree of trust in the real estate agent early in the relationship. We never really know when that trust is placed in us, but that trust is the beginning of an agency relationship. An agency relationship can actually be formed unintentionally. The relationship

CASE STUDY: EDINA REALTY

Real estate practitioners received a clarion call to improve their agency disclosure practice in the landmark 1993 Edina Realty lawsuit. The Minneapolis, Minnesota, brokerage, one of the largest independent realty firms in the nation, was sued by a home buyer who worked with an Edina agent. The buyer alleged that dual-agency relationships were not explained to her as she went through the process of buying a home listed by another Edina agent. The class-action lawsuit charged Edina Realty with fraud, breach of fiduciary duty, breach of contract, and violation of racketeering statutes. The federal lawsuit could have jeopardized as much as \$200 million in commissions from more than six thousand transactions.

A second lawsuit for \$75 million was filed in a class action by sellers who contended they were not fully apprised of the various agency relationships involved in the transaction. In the summer of 1993, a state district court judge issued a declaratory judgment in favor of the sellers in the second lawsuit, ruling their case was so clear that there was reason to bring it to trial. The parties to the lawsuits settled in early 1994. The plaintiffs agreed to accept a settlement where they could receive future services from Edina Realty at a discount. In addition, Edina Realty was ordered to make a donation to an undisclosed charity and to pay for all court costs.

does not necessarily begin with the signing of an employment contract but can be construed from our actions. For that reason, we must provide buyers and sellers with all the information necessary for them to make a decision regarding the degree of trust they wish to place in us.

CASE STUDY: COLUMBUS V. MEHNER

In a 2002 case, *Columbus v. Mehner*, the Alaska Court held that real estate licensee Bonnie Mehner had engaged in undisclosed dual agency and had violated her fiduciary duties to her client. The prospective buyer, Joseph Columbus, wanted to see one of Mehner's listings, but the buyer's agent with whom he was working was out of town at the time.

Columbus then called Mehner, who met him at the property. He gave her his agent's card. After noting that she usually does not show properties to other people's clients, Mehner agreed to show Columbus this listing and then offered to show him some of her other listings.

The next day, Mehner showed Columbus the same property again as well as several other properties. Because his own buyer's agent was still out of town, Columbus asked another agent in the buyer's agent's company to draft up an offer and present it to Mehner. Mehner indicated that the offer "would not fly," as well as anger that the buyer was still working with this other agent's firm instead of through her. She indicated that Columbus became her client when he called her the second time.

Mehner contacted Columbus, berated him, and told him that she expected to receive both sides of the commission on this sale. She told Columbus the offer price would have to be close to full price for Columbus to secure the property. She also told Columbus that the seller did not have to negotiate on the price because his employer would make up any difference between the sales price and the listing price. This statement was false.

Believing that he had to work through Mehner to purchase this property, Columbus had Mehner draft up a full-price offer. For the first time, Mehner brought up the issue of dual agency. She presented Columbus with an agency disclosure form, which he signed. Columbus then made a full-price offer on the property, which was accepted.

Columbus and his buyer's agent eventually filed suit against Mehner, alleging that she had breached her fiduciary duties to Columbus and had intentionally interfered with the contractual relationship between Columbus and his agent. The court ruled in favor of Columbus and the buyer's agent and awarded damages to both parties. The buyer received the difference between the price he actually paid for the property and the price he would have paid had Mehner acted in accordance with the law. The buyer's agent received half of the commission.

The court held that Mehner had violated Alaska's dual-agency disclosure laws by waiting until Columbus had already seen several of her listings and made an offer on one to even broach the subject of dual agency. In addition, the court found that Mehner had violated her fiduciary duty to the buyer by failing to disclose her dual-agency status, because, as a dual agent, her role was limited.

The buyer was also eligible to receive punitive damages because the court found that Mehner's actions were so egregious as to merit such additional damages. A hearing was set to determine the amount of punitive damages, but the parties settled the matter for \$200,000 prior to the court's ruling on the issue (Harris, L.B. 2003. Undisclosed Dual Agency in Alaska Could Affect Kentucky Licensees. *Kentucky Real Estate News*, 194).

For more information, go to <https://www.nar.realtor/legal-case-summaries/columbus-v-mehner-salesperson-who-acted-as-undisclosed-dual-agent-settles-lawsuit-for-200000>.

Because newer forms of agency representation are still evolving, real estate practitioners must cope with increasingly complex questions from real estate consumers. Many of these questions pose ethical concerns.

HOW WOULD YOU RESPOND?

Working with Buyers and Sellers

- A. What should I say if I work for the seller and the buyer asks me, “What price will the seller take on this property?”
- B. What should I say if I work for the seller and the buyer asks me, “Have the sellers had any offers? What were they?” or “What did the sellers pay for their house?”
- C. The seller’s property has a design flaw: the family room faces due west. In the afternoon, that part of the house is like an oven. If I work for the seller, should I disclose this defect to buyers?
- D. I work for the buyers. They want to make offers on property where the seller is willing to hold paper. They have told me in confidence that their credit history had some blemishes on it, but the problems were resolved several years ago. Do I have an obligation to tell prospective sellers about those past problems?
- E. A potential listing client confides that she is in grave financial circumstances and must sell quickly. She lists with a competitor. A short time later, a buyer-client expresses interest in that seller’s property. Should I tell my buyer about the seller’s reasons for selling?

Possible Responses

- A. An appropriate response for the listing agent might be: “I know that the seller has offered the property at the listed price. I cannot quote you any other price. However, I must submit any offer you would like to make and the seller will make the final decision on the price.” The NAR Code of Ethics, Article 1, states that “When representing a buyer, seller, landlord, tenant, or other client as an agent, REALTORS® pledge themselves to protect and promote the interests of their client.” This statement means that if a broker represents a seller or landlord, it is the goal of the broker to get the *highest price* and best terms for the client. If the broker were to represent the buyer or the tenant, the broker should work to get the *lowest price* and best terms for that client.

Practitioners should not reveal any other price or suggest a suitable initial offering price *unless* the seller has given those instructions. When you state, “I must submit all offers,” you have indicated that the price and terms may be negotiable. You should not indicate anything more.

B. This information is strictly confidential unless the seller-clients give you permission to reveal it. You might respond, “Since I represent the sellers and I am trying to get them the best price and terms, I cannot disclose that information. However, I will be happy to submit any offer you would like to extend to the sellers.” Note that Article 3 of the NAR Code advises that REALTORS® only must disclose the “existence of accepted offers,” but not the existence of offers in play or the terms of accepted offers.

The price that the sellers paid for the property is a matter of public record, in most cases. Direct the buyer to the place where they can obtain the information, but do not be the source of that information.

C. You may choose to show the property when it can be seen in its best light (no pun intended). However, you should also point out to the buyers that the rooms facing west may be very warm in the afternoon. If the buyers want to see the home in the afternoon, you should show it to them. If in fact the warmth of the room is a design defect, one that cannot be overcome by adequate air conditioning, window shades, or tinted glass, the wisest course would be to disclose this design flaw. Note that Article 2 of the NAR Code of Ethics states that “REALTORS® shall avoid exaggeration, misrepresentation, or concealment of pertinent facts relating to the property or the transaction.”

D. The appropriate answer here is that even though the agent has a fiduciary responsibility to the buyer, the agent cannot be dishonest with the sellers. (Note that Article 1 of the NAR Code of Ethics states that “REALTORS® remain obligated to treat all parties honestly.”) In particular, if the buyers are asking the seller to provide financing, it would be critical for the buyer broker to reveal the buyer’s credit problem. In some states, it is required that brokers reveal information about the buyers’ financial problems if it would likely lead to an extended closing period or other problems for the seller.

The agent may wish to advise the buyers that concealing information about their credit could risk a lawsuit later. The agent should also consider working with them to present their case fairly, e.g., help the buyers obtain information (audited tax returns, credit reports) to help the sellers decide about providing financing. As an additional note, brokers who are working with buyers should always have consumers determine their financial qualification for purchasing real estate before getting too invested in working with these consumers.

E. Sellers should be told that information won’t be held confidential until a listing agreement is signed. If the seller hasn’t been warned, then real estate practitioners should keep the information confidential.

(Many states require that consumers are provided with a Miranda-like disclosure about agency relationships and confidentiality at first substantial contact.) If the seller has been warned and discloses personal information anyway, then the agent can give the buyer-client the information.

*I am only one but still, I am one.
I cannot do everything but I can do
something. And, because I cannot do
everything, I will not refuse to do what
I can.*

—EDWARD HALE

ETHICS AND FAIR HOUSING

The civil rights of home buyers are legally protected by the federal 1968 Fair Housing Act and a host of state and local legislation. In spite of these laws, minorities seeking to buy or rent a home still experience discrimination. According to the National Fair Housing Alliance 2017 report, there were 28,181 reported complaints of housing discrimination in 2016: 55% of these complaints involved discrimination on the basis of disability, followed by 19.6% based on racial discrimination and 8.5% based on discrimination against families with kids; 91.5% of all acts of housing discrimination reported in 2016 occurred during

rental transactions.¹

Real estate agents have a special mandate to ensure that all buyers and renters are treated fairly. The Civil Rights Act of 1866 prohibited racial discrimination in the purchase, sale, or rental of real and personal property. The Fair Housing Act of 1968 prohibits discrimination in residential sales or leasing on the basis of race, color, religion, national origin, gender, handicap, or familial status. The U.S. Department of Housing and Urban Development enforces federal housing laws and defines these protected classes broadly. For example, the term *handicap* describes individuals who may have mental as well as physical disabilities. *Familial status* not only describes families with children but also pregnant women. Some state and local ordinances have added more protected classes, such as marital status and sexual orientation. Real estate firms that violate federal, state, or local civil rights statutes could lose their license to operate and be heavily fined as well.

Most buyers and sellers are aware of civil rights legislation. Some are personally opposed to integration or have other political sentiments that contradict fair housing laws. Brokers and their agents may also have personal feelings in conflict with civil rights legislation. Sometimes those concerns create ethical dilemmas for real estate agents.

Many real estate agents and members of the public misunderstand the agent's responsibility with regard to fair housing. The purpose of the Fair Housing Act is to give everyone a chance to buy a home that is affordable,

¹2017 Fair Housing Trends Report, <http://nationalfairhousing.org/2017-fair-housing-trends-report/>.

WHAT CONSTITUTES DISCRIMINATION IN THE SALE OR RENTAL OF HOUSING?

1. to refuse to sell or rent after the making of a bona fide offer, or to refuse to negotiate for the sale or rental of, or otherwise make unavailable or deny, a dwelling to any person because of race, color, religion, national origin, sex, handicap, or family status
2. to discriminate against any person in the terms, conditions, or privileges of sale or rental of a dwelling, or in the provision of services or facilities in connection therewith, because of race, color, religion, national origin, sex, handicap, or family status
3. to make, print, or publish, or cause to be made, printed, or published any notice, statement, or advertisement with respect to the sale or rental of a dwelling that indicates any preference, limitation, or discrimination based on race, color, national origin, sex, handicap, or family status, or an intention to make any such preference, limitation, or discrimination
4. to represent to any person because of race, color, religion, national origin, sex, handicap, or family status that any dwelling is not available for inspection, sale, or rental when such dwelling is in fact so available
5. for profit, to induce or attempt to induce any person to sell or rent any dwelling by representation regarding the entry or prospective entry into the neighborhood of a person or persons of a particular race, color, religion, national origin, sex, handicap, or family status

regardless of ethnic, racial, religious background or sex, national origin, handicap, or family status. Other than discriminating against an individual's ability to afford a home, a real estate agent can use no other form of legal discrimination.

Even though the public may be cognizant of fair housing laws, buyers and sellers nevertheless ask questions of real estate professionals that are at best awkward and, at worst, ethically problematic.

ETHICS AND PROPERTY DEFECTS

Real estate industry experts report that nondisclosure of property defects is the most likely event to trigger litigation against real estate practitioners. Most states require that real estate salespeople disclose property defects, such as leaky roofs and environmental hazards, to prospective buyers, regardless of agency relationships. In many states, residential sellers must sign a property disclosure regarding any information they have about the physical defects of a property. This disclosure helps deflect liability from the real

When it comes to mortgage lending, redlining is more widespread than most people realize. The court entered a consent (settlement) order in *United States v. JPMorgan Chase Bank* for monetary relief of \$53 million, including a civil penalty of \$55,000. The complaint had alleged that the defendant charged black and Hispanic borrowers higher rates and fees for wholesale mortgages than similarly situated white borrowers.

Source: Bernice Ross, "Why Redlining and Discrimination Are Still Real Estate's Problem," Inman, April 3, 2017, <https://www.inman.com/2017/04/03/why-redlining-and-discrimination-are-still-real-estates-problem/>.

CASE STUDY: FAIR HOUSING AND THE BROKER

An Atlanta real estate broker has achieved notoriety by creating the first civil rights case in the nation taken before an administrative law judge as authorized by the 1988 amendments to the Fair Housing Act.

In Stone Mountain, Georgia, broker Gordon Blackwell listed a home he owned through a Coldwell Banker agent in April 1989. In May and June, a black couple being assisted by a Re/Max agent entered into negotiation for the property and reached an agreement. After the contract was signed, but before closing, Blackwell learned that the couple was black and advised his agent that he would not close. At the time, he argued that he was not aware of contract clauses that required him to pay points and closing costs.

A few days before closing, Blackwell called the agent and stated that he had rented the house to a white couple.

The Re/Max agent and the buyers filed a complaint with the Atlanta office of HUD, which brought charges against Blackwell. The judge found Blackwell guilty and ordered him to pay about \$75,000 in fines and penalties and to close on the house.

Blackwell filed for bankruptcy and the home was foreclosed upon by the mortgagee before the black couple could take ownership. The federal government filed an injunction against the mortgagee to prevent the sale of the home.

The Georgia Real Estate Commission revoked Blackwell's real estate license.

Does a real estate licensee have a duty to a buyer-client to respond to questions about the racial demographics of a community? In *Hannah v. Sibcy Cline Realtors*, (Ohio Ct. App. 2001), the court said no.

The client had requested that her agent provide properties to choose from in ethnically diverse neighborhoods so that her children would not be the only black children in the school. This court held that a broker who provides such information may be liable for unlawful racial steering, while other courts have held that a broker has not engaged in steering when the racial information is provided in response to a buyer's question.

HOW WOULD YOU RESPOND?

Fair Housing Issues

- A. My sellers refuse to sell to certain minority groups. What should I tell them?
- B. After I showed an apartment to my customer, the manager called me to say that she would not rent the unit to my customer because he was disabled. The reason the manager gave was that she didn't want to depress the other tenants. What should I do?
- C. My landlord charges male tenants a higher security deposit than he charges female tenants because he thinks males are messier than females. He wants me to handle the rental listing on all his properties and to enforce his security deposit policies. What should I do?
- D. What if my buyers say to me, "I know you can't tell me this, but what kind of people live in the neighborhood?"
- E. What if my buyers persist by asking: "But will I be comfortable living here?"
- F. What if my buyers say, "I belong to a particular religious group (or ethnic group), and I want to be with people of my own kind?" Can I assist these buyers?
- G. My buyers want to know, "How are the schools in this area?" "What kind of children attend the schools?" How should I respond?
- H. My buyer-clients have asked me to direct them to a neighborhood that is exclusively of one race. Are my obligations to buyer-clients who ask me to steer them to a neighborhood based on race different than the obligations I have to seller-clients who ask me to show their property to people of a certain race?
- I. I've noticed that real estate agents in my firm are relatively inconsistent in the way they treat different customers. Although buyers are all treated courteously, I notice that well-dressed customers are not asked as many questions about finances before they are taken to see property as less well-dressed customers. And younger people are always asked about whether commuting distance to work is a factor and older people aren't. Is this a problem?
- J. My sellers have made unkind and negative comments about people who are gay. Should I be concerned?
- K. I provide property management services for my clients. My policy is to consistently refuse to rent to anyone that has any criminal conviction. Doesn't that remove the possibility of being accused of discrimination since the criterion is the same for everyone?

Buyers may ask questions about the quality of neighborhood schools or about crime in the area. Sometimes, these questions are just thinly veiled attempts to determine the ethnic composition of a neighborhood. Generally, the best response to these questions is to suggest that buyers obtain this information directly from the appropriate sources; for example, the school board or the local police department. Here are some more specific ways to respond to each of the above situations.

Possible Responses

- A. First, address the legal issue: "Mr. and Mrs. Seller, the Fair Housing Act of 1968 prohibits me from marketing your home based on a buyer's race (or religion, etc.). As a matter of fact, no real estate broker can market your home on that basis."
Next, address the marketing issue: "If I were to follow your instructions, I would be limiting the number of people who could afford your home, and in today's market, any kind of buying restriction would increase the time to sell your home."

If the sellers persist: “I cannot take this listing under these circumstances. Please understand that any buyers who feel discriminated against on the basis of their race (color, religion, national origin, sex, handicap, or family status) could file charges against you and my company with HUD. It is not worth it to me to lose my real estate license or to see you in court facing a \$100,000 fine just to take your listing.”

- B.** Under the 1988 amendments to the Fair Housing Act, people with disabilities were declared a protected class. Under the law, the manager or owner is not obligated to rent to someone who would be a threat to the health and safety of others. The reaction of others to a disability is not the disabled person’s responsibility. It is not your responsibility, either. You should consider advising the manager that she is violating the Civil Rights law and what the possible consequences are.

Under the Fair Housing Act, it is also illegal for a property manager to make inquiries as to the nature of a person’s handicap. In other words, a manager could deny a home or apartment to someone who is dangerous, but that manager is not allowed to ask questions that would determine if that individual is dangerous. A standard rental application form that provides references is one way managers can obtain this kind of information.

- C.** Under the 1974 amendment to the Fair Housing Act, gender (or sex) was declared a protected class. Treating tenants differently because of their gender is illegal.

You should consider advising the manager that he is violating the Civil Rights law and the possible consequences. If he persists, you should discuss with your broker the possibility of a release from the listing arrangement.

- D.** The buyers are right: You cannot advise buyers what kind of people live in the neighborhood if they are asking you to characterize the neighborhood regarding the resident’s race, color, religion, national origin, sex, handicap, or family status/age.

However, you can respond: “The residents here are middle-class professionals.” Or “The neighborhood is working class.” Or “The people here are upper-income.” You can describe the neighborhood in shades of green—in other words, in terms of its economics, but you cannot describe the neighborhood by the predominance of one ethnic, racial, or religious group, or by the color, sex, handicap, or family status of the residents.

Never use the expression, “This neighborhood is in transition.” Never say, “The neighborhood is mixed,” or “It’s a salt-and-pepper area.” Those euphemisms, as subtle as you think they are, are nevertheless interpreted by the courts as overtly discriminatory.

- E.** You can always respond, “I will be happy to show you any homes in this neighborhood in your budget, but if you want to know if you will like living here, the best thing to do is to talk to the neighbors yourself.” If you feel it is appropriate, drive around the neighborhood and even introduce the buyers to the residents of the area.

You can also advise the buyers to drive through neighborhoods by themselves and have them choose the neighborhood they like. Then you can show them houses they can afford in that neighborhood. You may even want to give them specific house addresses to drive by, but get permission from your broker first. Your broker may have a policy against giving out client addresses.

- F.** Absolutely not. They are asking you to describe the neighborhood in terms of the residents’ religious or ethnic qualities. Again, you can only describe the neighborhood in terms of affordability and economics. Let the buyers decide for themselves what neighborhoods have the “right” kind of people.

You may tell the buyers, “I cannot describe the neighborhood in that fashion. However, if you want to ask your friends, relatives, or members of your congregation/church/parish where they live, I will be happy to show you homes in their neighborhoods that you can afford.” Remember to always disavow any suggestion that you would help discriminate illegally and always get back to the issue of economics and affordability.

- G.** There are a number of problems in dealing with questions about neighborhood schools. For one, you may very well sell the buyers on a home because it is in a particular school district. What happens if next year, the school boundary lines change and that home now is served by another school? Ultimately, you may be liable.

Second, if you say the schools are “wonderful” or “excellent,” by what standards are you measuring those schools? Parents and educators have individual standards by which a school’s excellence is measured. For example, would a parent of a teenage boy or girl say that the school program is wonderful because the soccer team won first place in state last year? Would another parent state that sports are a minor issue in rating the school and that academic achievement by students is more important? The age of the buyers’ children and what the parents expect of the school program are additional factors in any such assessment.

Rather than make yourself an expert on the schools, defer to the experts—in this case, the buyers themselves. Give them a school boundary map and have them speak with the appropriate officials of the school board regarding the various programs offered in the area. Then let the buyers research which schools offer the programs they want. At that point, they will have identified the neighborhood they wish to live in, and you can better satisfy your customer’s requirements.

Remember, you should never characterize a school by saying, “The schools here are bad.” The courts may interpret that remark as saying, “The schools are integrated.” Thus, your remark would be discriminatory and unacceptable. Again, refer the buyers to the experts on the school system: other parents, the school board, principals, teachers, and guidance counselors.

School boards usually have available at little or no cost for agents and parents an “Attendance Boundary Map Book.” In addition, school boards also have information regarding a school’s accreditation, enrollment, procedures, transportation, and telephone contact numbers.

- H.** HUD suggests that it is “legally prudent and ethically responsible to refuse to accommodate a buyer’s request to conduct a housing search based on race” (Agency Law Quarterly, Volume 8, Number 1, Winter 1997, 3.). It is advisable to treat buyer-clients as you would buyer-customers when it comes to requests to steer based on race: advise them you will help them select homes based on affordability.
- I.** It could become one. Every buyer in your office should be treated consistently. Your office may wish to create a list of information that must be gathered from every buyer within a reasonable time of working with the prospect. Important information might include property specifications (e.g., number of bedrooms and bathrooms), financial considerations, and mortgage prequalification, among many other details. If buyers already have been prequalified, then that information should be added to their file. It is not important that every customer go through the buying process in the same sequence, but it might prevent a discrimination charge if you can demonstrate that every buyer provided the same information to complete the buying process. A report suggests that, at least for some agents, discriminatory practices are routine. A two-year study was conducted

between 2003 and mid-2005 in 12 metropolitan areas using teams of “paired testers”—individuals or couples posing as home seekers to compare how randomly selected agents treat African-Americans, Latinos, and whites. Examples of the discriminatory practice: almost 20% of the time, African-American and Latino testers were refused appointments or offered very limited service. This first category of discrimination was further delineated into several distinct patterns. In 17 instances, the African-American or Latino tester either (1) left several messages for an agent and never received a return call; or (2) had an appointment scheduled with an agent, but the agent never showed up for the appointment. This conduct translates to a rate of outright denial of service of nearly 6%. (The full report can be found at <http://www.nationalfairhousing.org/>.)

- J.** While there may be no need to directly confront the seller about unkind or negative remarks about sexual orientation (a person’s sexual identity in relation to the gender to which they are attracted; the fact of being heterosexual, homosexual, or bisexual) or gender identity (a person’s perception of having a particular gender, which may or may not correspond with their birth sex), REALTORS® should note that in the early 2010s, the NAR amended Article 10 of the Code of Ethics to read: “REALTORS® shall not deny equal professional services to any person for reasons of race, color, religion, sex, handicap, familial status, national origin, sexual orientation, or gender identity. REALTORS® shall not be parties to any plan or agreement to discriminate against a person or persons on the basis of race, color, religion, sex, handicap, familial status, national origin, sexual orientation, or gender identity.”

Thus, the NAR Code has defined “protected classes” differently than federal fair housing laws. While sellers may discriminate based on an individual’s sexual orientation or gender identity under the 1968 Fair Housing Act, REALTORS® may not. If the seller’s personal positions on these matters become an issue in a transaction, the broker should suggest that the seller discuss any legal liability for discriminating against individuals with an attorney. It should also be noted that while federal fair housing laws do not protect sexual orientation or gender identity, it is still possible that state or local laws do.

- K.** While it is true that having a criminal record is *not* a protected characteristic under the Fair Housing Act, criminal history-based restrictions on housing opportunities violate the Fair Housing Act if, without justification, their burden falls more often on housing market participants of one race or national origin over another. A practice or standard that creates an adverse effect or is neutral and non-discriminatory in its intention but, nonetheless, disproportionately affects individuals is called **disparate impact**. Across the United States, African Americans and Hispanics are arrested, convicted, and incarcerated at rates disproportionate to their share of the general population. Consequently, criminal records-based barriers to housing are likely to have a disproportionate impact on minority home seekers.

HUD specifically acknowledges that housing providers have a significant interest in protecting the safety and property of others and a prospective tenant’s previous criminal convictions may be one factor in that evaluation, but *it shouldn’t be the lone factor*. In other words, you should take into account the current age of applicants, their age at the time of the offense, the nature of the offense, their conduct since their convictions, etc.

HOW WOULD YOU RESPOND?

Facing a Bigot

Imagine that you are showing homes to buyers in a protected class in various neighborhoods. While they are looking at one particular property, a next-door neighbor emerges and threatens that if the prospects buy that property, he will harm them. He insinuates that other neighbors feel the same way he does.

Possible Responses

The Civil Rights Acts of 1866 and the Fair Housing Act of 1968 tell us that buyers and tenants cannot be discriminated against if they are members of a protected class. Clearly, if you steer this couple away from this property because of their protected class status, you would be violating the law. (If you are working for the seller of the property, you may also be breaching fiduciary—another legal obligation—by suggesting this property is not suitable based on their protected class status.) However, if you did not warn them about the neighbor's threat and the couple is later harmed in some way, you would feel personally responsible. Your conscience tells you to advise the buyers about the threats, and let them draw their own conclusions about purchasing the home.

This conflict between the law and ethics presents enormous personal challenges for most of us. Some agents would take the risk of following their conscience—that is, advising the prospects of the potential danger of buying a home next-door to a bigot—and suffer the possible consequences. Others might follow the letter of the law and obey federal and/or state statutes regardless of the potential harm that could be done.

While either approach is justifiable in its own way, it is sometimes possible to find a solution to an ethical problem without compromising the law or one's conscience. Often there are other choices available in solving an ethical dilemma—if only we can see them.

For example, in the illustration involving the prejudiced neighbor, these options may exist:

- The neighbor could be advised about discrimination laws and the potential consequences of his behavior (he could be sued by his neighbor, the seller, as well as by the broker and all potential buyers).
- Hate laws or local ordinances may be in effect for this community, in which case the neighbor could be reported and dealt with by the legal system.
- The neighbor and the buyers can be introduced to one another to let them determine for themselves what kind of neighbors they would be.
- The property seller could be advised that the neighbor is making it difficult to market the property, which would allow the seller to address the problem.
- All prospects could be told what the neighbor's threats were to let them decide if they are still interested in the property.
- Civil rights and housing organizations could be contacted for help and advice on this matter.

The purpose of fair housing legislation is to make sure that everyone is given a chance to buy an affordable home, regardless of race, color, religion, gender, national origin, handicap, or family status. A prospect's sexual orientation and gender identity, as well as other factors, may be protected as well. Real estate practitioners can't legally use any form of discrimination other than inability to afford a home. It is their legal and ethical responsibility to be advocates of fair housing and to give everyone an equal opportunity to enjoy the American dream of home ownership.

Whenever you are to do a thing, though it can never be known but to yourself, ask yourself how you would act were all the world looking at you, and act accordingly.

—THOMAS JEFFERSON

estate salesperson; however, real estate professionals cannot merely pass along information given by their principals without verifying it. Salespeople must be knowledgeable about the property they are marketing.

An "As is" contract clause, the standard defense used by sellers in the past to hide property defects, is no longer a viable response. Neither is **caveat emptor** (buyer beware). Owners, lending institutions, and real estate agents are held by the courts to be financially responsible to a buyer for any damages caused to a property by an environmental contaminant.

Real estate professionals are expected to be experts on a property's condition. Because real estate practitioners are rarely educated about construction standards or inspection issues, this expectation may not be fair or appropriate. Nevertheless, the public expects (and court decisions suggest) that real estate practitioners should be responsible for discovering defects on the property by asking sellers the appropriate questions and performing some inspection. Should the seller and/or the evidence indicate that some property defects exist, the practitioner has the obligation to investigate further—perhaps by insisting on an expert inspection.

Fortunately, most property defects are not likely to result in serious injury or fatalities. Nevertheless, many states have enacted legislation requiring that sellers at the very least acknowledge in writing that they are aware that they have a duty to disclose property defects as well as issues surrounding the property, such as zoning and nuisances. In other states, sellers must do more: they must provide a list of any defects of which they are aware.

Television programs, movies, and news stories have been written about properties stigmatized by death and violent crimes. *The Amityville Horror* and *Poltergeist* started a run of films that popularized the notion of **stigmatized property**. While some real estate practitioners might just shrug off these stories and headlines, sellers want a property's negative features to be kept confidential by their agent, while buyers assert a right to know how such problems affect present and future value.

CASE STUDY: FATAL CARBON MONOXIDE LEAK

The state of Vermont charged REALTOR[®]/home-seller Stephen C. Brooks with involuntary manslaughter in the deaths of three members of a family that purchased his home.

According to court records, Brooks had been warned at least twice that the gas-fired boiler in his basement had a lethal defect. Prosecutors maintained that Brooks never informed John and Linda Cifarelli that the boiler leaked carbon monoxide. A year before Brooks sold his home, his own wife and daughter had been overcome by fumes and had to be hospitalized. Three days later, a plumbing company repairman found a wire mesh screen blocking the exhaust vent, forcing fumes to back up into the house. The repairman warned Brooks to leave the boiler off and then notified Vermont Gas Systems of the faulty boiler. Vermont Gas repairmen advised Brooks it was unsafe to operate the boiler and rendered the unit inoperable.

The Cifarelli family purchased the home in September 1988. Three months later, John Cifarelli started the boiler for the first time. While his family slept, carbon monoxide from the boiler filled the home. A house guest, awakened during the night, opened a window and survived. The Cifarelli's 5-month-old daughter also survived. Killed, however, were Cifarelli, 34, his pregnant wife, Linda, 26, and another daughter, Nina, 2.

According to prosecutor William Sorrell, it is the first time the state's real estate disclosure law has been used in a manslaughter case. "To my knowledge, the involuntary manslaughter statute has not been used for a death resulting from a hidden defect in a piece of real property," Sorrell told the *Boston Globe*.

The case was the first in which a home-seller has been held criminally liable for selling a house with a fatal defect. Brooks was sentenced to a four-year prison sentence. The court found that failure to disclose the information constituted voluntary manslaughter.

Though Brooks was a licensee and a REALTOR[®], he was not acting as a broker in this sale, but only as the seller.

Under the settlement, Vermont Gas Systems, the company that installed the home's boiler system in 1972, was ordered to pay \$2.8 million to the estates of John, Linda, and Nina Cifarelli. In addition, C & L Plumbing, whom Mr. Brooks said he had called to repair the system, will pay \$400,000.²

Real estate professionals spend an average of 1 hour and 5 minutes of each residential transaction explaining environmental issues to buyers and sellers. Commercial specialists average 2 hours and 3 minutes on environmental matters. (From: “Study Pinpoints Broker Costs for Environmental Compliance,” *Today’s REALTOR*, February 1997, 21.)

Among the many factors that can stigmatize a property are crimes that have occurred on the property; a seller’s illness, particularly AIDS; and real and suspected environmental hazards. About half of the states have adopted laws dealing with questions about stigmatized property. Most say real estate agents do not have to disclose such stigmas to buyers. What must be disclosed, however, are matters that are “material” to the purchase.

The issue then becomes what is “material.” The courts have ruled that “material” information relates to the physical structure of a property. Thus, buyers have a right to information about physical defects, such as leaky roofs, faulty equipment, and the like. However, buyers argue that anything that could affect future resale value is material to the purchase, and therefore the buyer has a right to information that may involve something other than a structural flaw.

In many states, sellers must sign a property disclosure statement regarding any information they have about the physical defects of a property. Many are forthcoming about past or present problems, with or without mandatory disclosure laws. However, sellers may not wish to reveal information about nonphysical elements of the property. Consider, for example: Is the history of a property a material fact? And how could its potential effects be determined?

In a Florida case, buyers sued their real estate agent for failure to reveal that a murder–suicide had taken place on the premises some months before closing. When the buyers found out about the tragedy, they stopped making their mortgage payments, were foreclosed upon, and sued the agent for failure to disclose a material fact. This case raises the issue of the time frame of the event that “psychologically impacts” the property. Does an agent have a responsibility to disclose “ancient history” as well as more recent events?

State laws are inconsistent in their response to this type of disclosure dilemma. Florida, where the above case took place, presently has no statute to govern the agent’s decision not to disclose the murder–suicide. On the other coast, California prescribes that if such an incident occurs within three years before an offer to buy, lease, or rent the property, the information must be disclosed.

Many buyers want to know about any psychological stigma attached to the property. Their reasons may range from “We’re superstitious, and we don’t want to own such a property” to “This information will allow us to get a lower price on the property.” Real estate practitioners also work with buyers who may have cultural concerns about the “spiritual orientation” of the property.

Perhaps the issue of AIDS as a potential psychological stigma is the most troubling legally and ethically for real estate practitioners. Confusion and hysteria

²<http://www.nytimes.com/1993/01/29/news/orphaned-girl-to-get-millions-over-faulty-heater.html>.

about whether a buyer could contract the disease merely by living in a house once occupied by someone with AIDS has caused some purchasers to refuse to buy such homes. An argument could be made that a property owner's AIDS condition is material to the buyer's purchase, given the fear that some people have about transmission of the illness through casual contact. Even though scientific evidence indicates that this fear is irrational, a social stigma is also attached to the property

CASE STUDY: THE HAUNTED HOUSE

A New York court refused to order the return of a \$32,500 down payment to Mr. and Mrs. Jeffrey Stambovsky, who wanted to leave their newly purchased \$650,000 Rockland County home because it was inhabited by ghosts. The seller not only knew about the apparitions, but also wrote about them in publications such as *Reader's Digest*. The New York Supreme Court ruled that the seller did not have a duty to reveal her beliefs about supernatural inhabitants or to discuss her published stories.³ Upon appeal, however, the court ruled that the sale was dishonest because not only did the seller fail to tell the Stambovkys that the house was haunted, the seller had publicized the house's haunting in numerous magazines which would certainly affect the resale value of the home.

because of the circumstances associated with AIDS transmission: intravenous drug use and homosexuality.

HUD's advice to real estate brokers is that federal fair housing laws supersede any state statute or common law that might require a real estate practitioner to disclose AIDS. HUD states that real estate brokers have no duty to investigate whether an occupant has AIDS and should not attempt to obtain such information. Furthermore, HUD's general counsel advises that agents who are asked whether an occupant has AIDS should decline to respond.

Many states have deemed that whether occupants have AIDS or the HIV virus is not a material fact, and, furthermore, that there can be no cause of action against the owner or the real estate agent for failing to disclose such information.

Regardless of state and federal statutes that govern the real estate practitioner's behavior and response regarding stigmatized property, buyers still made demands for such information. While they have a right to seek the answers on their own, buyers may not be able to expect real estate practitioners to help them.

³Janie Rosman, "The Famous Ghosts and Hollywood Homes of the Nyacks," *Rockland County Times*, last modified January 28, 2016, <http://www.rocklandtimes.com/2016/01/28/the-famous-ghosts-and-hollywood-homes-of-the-nyacks>.

CASE STUDY: A MURDER HOME

Two Australian real estate agents were fined \$20,900 for failing to reveal to buyer Ellin Lin that the previous owner had killed three family members in the house that Lin was in contract to purchase. Lin refused to complete the transaction. Public pressure forced the agents to refund Lin's \$80,000 deposit. The Australian regulatory agency, the Commission for Fair Trading, fined the agents \$20,900 for failing to act honestly, fairly, and professionally in not revealing the house's history. One of the agents claimed that the house's history was not relevant to the purchase and had described the home as a "deceased estate."⁴

CASE STUDY: THE BRIDGE

Andrea Meaney purchased a waterfront island cottage at the end of a dirt road near an abandoned bridge. What she didn't know was that the bridge was the site of Senator Edward Kennedy's car accident in 1969—and a tourist attraction. The Dike Bridge in Chappaquiddick often brings more than 50 cars and bicycles down Meaney's remote road. Meaney found it necessary to put a sign in her front yard asking drivers to slow down and respect her private property. Meaney advises that her real estate agent didn't tell her that the bridge was the scene of a notorious event.⁵

HOW WOULD YOU RESPOND?

Property Defect Issues

- A.** The sellers have just advised me that they have a roof leak. They told me this in confidence. What do I say when the buyer asks me about the condition of the roof?
- B.** My sellers want to offer their home "as is." They don't want to be responsible for any repairs that may be necessary on their home. What should I advise them?
- C.** My buyers don't want to order any inspections. They think the house looks great and don't want to spend hundreds of dollars.

⁴"Agents Fined \$20,000 Over Horror House Sale," *The Sydney Morning Herald*, last modified December 19, 2004, <http://www.smh.com.au/news/National/Agents-fined-20000-over-Gonzales-house-sale/2004/12/19/1103391621560.html>.

⁵Anne Thompson, "Chappaquiddick: A Fatal Attraction as Tourists Flock to Accident Site," *Los Angeles Times*, last modified July 24, 1994, http://articles.latimes.com/1994-07-24/news/mn-19156_1_mary-jo-kopeczne.

- D. What if my buyers don't ask me anything about the condition of the property, and I know of several defects? Do I have to tell them about the problems if they don't ask?
- E. What if my sellers tell me that the reason they are selling the home they just inherited is because their uncle murdered his entire family in the home and then committed suicide?
- F. What if I work for the buyer and have no fiduciary responsibility to keep the information about AIDS confidential? Don't I have a duty to disclose this information to the buyer under these circumstances?
- G. A sex offender lives across the street. He is in compliance with sex offender registration laws. Do I have to disclose this information to prospective buyers?

Possible Responses

- A. First, you must advise the sellers that you cannot keep this information confidential. If you did, both you and the sellers could be sued for failure to disclose a defect. Tell the sellers that the roof problem must be disclosed, but that they do not have to pay for the repair if they don't want to. Who pays for the repair is a matter of negotiation.

It is advisable to ask the sellers many questions about the operating condition and structure of the property. For example, the sellers could be provided a checklist with questions regarding interior walls, ceilings, floors, roof, windows, doors, foundation slab, fences, electrical system, plumbing, sewers, septic system, and other mechanical components of the home.

Some real estate offices use a "Seller's Property Disclosure Statement," which is a checklist of items that the seller completes as part of the listing process. The form asks such questions as:

- Does the property have any filled ground? Do you know of any past or present settling or soil movement problems on the property or on adjacent properties?
- Do you know of any structural additions or alterations, or the installation, alteration, repair, or replacement of significant components of the structure upon the property completed without an appropriate permit during the term of your ownership or that of a prior owner?
- What is the source of your water? Public? Private well? If well, when was the last time the water was checked for safety? Are the water supply pipes copper or galvanized?
- Is the electrical wiring up to code? Are you aware of any damaged or malfunctioning receptacles or switches? Is the house insulated? What type of insulation?
- What type of heating system is used in the house? When was it last inspected? Do you have solar heating?

Special checklists should be created for condominiums, which have unique concerns, and for newly constructed residences.

Many states require that property owners complete a property disclosure statement and have its receipt acknowledged by purchasers. While having your sellers complete and sign these forms does not prevent a lawsuit from taking place, this precautionary measure is evidence that you attempted to determine whether the property had any material defects.

REALTORS® should note that Article 2 of the NAR Code of Ethics states: “REALTORS® shall avoid exaggeration, misrepresentation, or concealment of pertinent facts relating to the property or the transaction.” While REALTORS® are not obligated to discover latent defects in the property, since the sellers in this case have already disclosed the leaky roof to the broker, then the REALTOR® must disclose this information to prospective purchasers. A broker in this situation should also suggest that the purchasers obtain an expert opinion on the nature of the roof leak.

- B.** Many states require that sellers reveal any defects in a dwelling. Describing the sale as “as is” will not remove this legal obligation. “As is” simply means that the seller will not perform any requested repairs. In other words, sellers may refuse to pay for any repairs, but they still may be required to reveal any condition in the home that would be material to the buyer’s purchase.

A real estate agent should be concerned when sellers want to sell a property “as is.” It may be a red flag that something is wrong. The agent should ask the appropriate questions or be ready to face charges of negligence. Courts expect agents who see a “red flag” to take the time to discover any potential problems. Needless to say, buyers may stay away from a property that is perceived to have a lot of defects. Suggest to seller-clients to avoid marketing the property “as is,” and instead wait for offers to determine if purchasers make repair requests. The seller can always limit the amount of repairs that the buyers require to a certain amount, such as 2% of the purchase price.

If the buyers are borrowing the money to purchase this home, their lender will likely require inspections. You should encourage the buyers (even if you work for the seller) to have the entire property inspected. The inspector can give them professional advice about the dwelling’s systems, which is information brokers do not provide because they have no expertise in this area. Having the buyer bear this responsibility lessens the possibility of a lawsuit against you and the seller for failing to disclose material information.

REALTORS® should note that Article 2 of the NAR Code states: “REALTORS® shall only be obligated to discover and disclose adverse factors reasonably apparent to someone with expertise in those areas required by their real estate licensing authority. Article 2 does not impose upon the REALTORS® the obligation of expertise in other professional or technical disciplines.” Thus, REALTORS® should encourage purchasers to hire home inspection experts, whether they represent the buyers or the sellers.

- D.** Yes, even if your buyers don’t ask you questions, if you have material information about the property, you must disclose it. In many states, this is a legal obligation, not just an ethical one.
- E.** Courts in many states have rules that information about crimes taking place on the property is not material to the buyer and therefore need not be disclosed. About half of the states have laws stating that real estate agents need not tell buyers about psychological stigmas attached to properties, such as suicides and accidental deaths that occurred on the properties. However, some states, such as California, require that real estate agents tell buyers about crimes that took place within three years of marketing the home.

You should check with your broker's attorney regarding the legality of disclosing information such as crimes associated with the property. If you live in a state that has no law regarding the mandatory disclosure of information regarding a psychological stigma, consider discussing the matter with the seller:

"Mr. and Mrs. Seller, you have shared information about the death of your family on the property in confidence. I am bound by my fiduciary relationship with you to keep this matter confidential. However, we know that, sooner or later, the buyer of this property will find out about this unfortunate event. Probably the neighbors across the street will tell the buyers on moving day. This information may upset them very much. While state law requires that I disclose latent defects and/or material information to the buyer, the information about the death on this property falls into a gray area of the law.

"I would prefer to tell interested buyers about the unfortunate tragedy that happened here. That way, the buyers can determine up front whether they consider this disclosure to be an obstacle to the purchase. If we disclose, they cannot sue us for keeping information from them. If we do not disclose, they may sue us and ask the courts to resolve the issue. If your buyer is upset by the news about this property, you may very well be the test case for this state. Is that something you wish to risk?"

"Please release me from confidentiality (in writing) on this one matter and allow me to tell buyers about the stigma attached to this property. Let them decide now whether this affects their decision to purchase. This way, we can avoid potential litigation."

You may also advise your sellers to check with their attorney regarding their rights in this matter. If your sellers do not wish to release the information to the buyers regarding the stigma, you always have the choice of refusing the listing. Consult your broker first, however, before refusing a listing.

- F.** This question is more difficult to answer because the agent cannot rely on the issue of confidentiality to the seller. Federal fair housing laws are not clear on this matter either. Federal law does not stop a home seeker from making buying choices using criteria that a seller is forbidden from using when making selling decisions. Home buyers can exercise their freedom of choice and not violate the Fair Housing Act by doing so.

The question here is whether you should provide the information about the criteria the buyer is using: in other words, should you be the one advising the buyer that the occupants have AIDS? HUD has indicated that it is unlawful for real estate licensees to make unsolicited comments about the occupants having AIDS. You may wish to suggest that purchasers who feel that this information is relevant can investigate on their own.

- G.** Most brokers are not required to disclose the presence of sex offenders in nearby areas. However, it is understandable that buyers would be concerned about this issue. There are numerous problems with disclosing this information. First, it is challenging to determine the nature of the sex offender's violation and to make a determination as to potential threats. Second, disclosing this information could really harm the chances of the seller obtaining offers and thus violate your fiduciary duties to your client. Finally, to whom do you make the disclosure? Just buyers with children, or all buyers?

Such a disclosure is not legally required except in a few states with somewhat ambiguous laws, such as California, where sellers are expected to disclose when “equity, justice, and fair dealing demand disclosure.” In an Arizona case, homebuyers with small children sued sellers and their agent for nondisclosure, breach of fiduciary duty, and fraud for not mentioning a neighboring pedophile. However, the purchasers had signed a seller’s disclosure statement saying “buyer acknowledges that, by law, sellers, lessors, and brokers are not obligated to disclose that the property (is or has been) located in the vicinity of a sex offender,” and lost the case.

Remember that brokers cannot lie if asked a direct question, but purchasers can simply be given various websites where they can check on such matters themselves. All purchasers, regardless of family status, should be given the same information.

*We start out wanting to do good and
wind up wanting to do well.*

—MICHAEL JOSEPHSON

ETHICS AND RELATIONSHIPS WITH COMPETITORS

Achieving and maintaining harmony among real estate practitioners can be a challenge for the best of brokers. The real estate business is one that thrives on competition and individual performance. Moreover, state and federal laws encourage practitioners to obey the spirit and letter of independent contractorship. Thus, it can be difficult to instill a spirit of cooperation among real estate professionals. The thousands of grievances and complaints filed yearly by licensees against competing practitioners at the state and professional level attest to the sad fact that cooperation among brokers and agents often does not happen. Yet agents from different offices often work together to consummate real estate transactions, so their competitive tendencies must be subordinated to more cooperative ones.

While state statutes often determine the duties real estate agents owe to their clients and customers, few state or federal statutes prescribe the ethical obligations they have to one another. NAR attempts to regulate conduct between competitors with its Code of Ethics. Local associations of REALTORS® seek voluntary compliance with the Code and will, on occasion, determine violations of the Code during grievance hearings. (See Part II for additional discussion.)

Of the many disputes that agents have with one another, the most common is procuring cause. **Procuring cause** issues typically arise when customers (usually buyers) are working with a number of agents who share the same inventory (typically the local MLS). Battles over procuring cause and the resulting wars over commissions can be eliminated by a number of methods:

- Encourage customers to commit to exclusive relationships, preferably in writing. Where possible and advisable, encourage buyers to become clients in an exclusive relationship with a buyer broker.

- Educate customers about the shared inventory, about local real estate agents, about agency relationships, and about commission splitting.
- Give business cards to buyers and encourage them to hand them to other agents when they are seeking property on their own; encourage them to say that they are already working with a broker, and discourage them from seeking property without assistance.
- Avoid the appearance of abandoning buyers or sellers. Follow up with consumers by returning phone calls and by making clients and customers aware of your work on their behalf.
- When salespeople work with real estate consumers, they should ask, “Are you working with another real estate agent?” If the answer is yes, the agent should elicit a list of the properties already viewed by the prospect to avoid showing the buyers a property already shown to them by another salesperson.

The determination of which broker is procuring cause rests on a number of factors, including:

- nature of the transaction (listing and buyer representation agreements)
- offer of cooperative compensation
- conduct of the seller, the buyer, and the brokers and their affiliate licensees
- roles and relationships of the parties
- initial contact with the purchaser
- continuity of contact (abandonment and estrangement)⁶

The NAR Code of Ethics replaced its use of the word *competitors* in 2011 and replaced it with the expression *real estate professionals*. The Code also began to emphasize the concept of mediation over arbitration for the resolution of disputes between REALTORS®. This change in language suggests that NAR is attempting to reframe the relationship between competing firms and brokers as one of collegial and cooperative nature rather than an adversarial one.

Real estate practitioners create another common problem when they fail to respect exclusivity. Generally speaking, when clients have identified an agent as their exclusive representative, all other practitioners should contact that representative directly. Only under the most extreme circumstances should an agent contact another office’s buyer or seller directly. Both the Preamble and Article 3 of the NAR Code stress the importance of obtaining exclusive contracts

⁶<http://realtomag.realtor.org/law-and-ethics/law/article/2005/11/procuring-cause-who-gets-paid>.

***EXERCISE: TEN COMMANDMENTS FOR WORKING WITH
BROKERS OF COMPETING FIRMS***

If you were to write a “Ten Commandments” prescribing behavior for relationships with agents from competing firms, what would you include? (You may use “Thou shalt” or “Thou shall not” language if you wish.)

- 1.
- 2.
- 3.
- 4.
- 5.
- 6.
- 7.
- 8.
- 9.
- 10.

to avoid disputes over procuring cause as well as to emphasize the need to respect other agents’ relationships with their clients.

The submission of offers, particularly multiple offers, can also be a problem. Again, if sellers have identified an exclusive agent, all offers must be submitted through that agent. Real estate agents also have an ethical obligation to present all offers—regardless of price, terms, or format—as quickly as possible. Even the possibility of offers must be communicated to the principal. Sellers and buyers should be educated about the possibility of multiple offers on desirable properties and the way they will be handled according to state law and the ethics of fair play.

To obtain the most favorable terms for the client, real estate practitioners should cooperate with all agents, unless cooperating would somehow harm the client. It should be noted that REALTORS® are encouraged to cooperate with other brokers, according to their Code, but cooperation does *not* necessarily imply compensation. Compensation agreements between co-brokers should be clearly articulated and put in writing before co-brokers work together.

HOW WOULD YOU RESPOND?

The Question of the Undisclosed Offer

Broker A is working with a buyer and called a competing broker, Broker B, to advise that the buyer was going to make an offer on Broker B’s listing within 48 hours. Broker B called back the next day and advised the

agent that one of her buyers just submitted an offer on the property, and the offer was accepted.

When the Broker A angrily inquired why Broker B did not advise the sellers about the possible offer that would have been delivered the next day, Broker B replied that he had no obligation to tell the sellers about an offer that had not been formally expressed. Broker A accused Broker B of withholding information about the coming offer so that Broker B could earn the full commission and not split it with Broker A.

How should this situation be handled?

Possible Response

Brokers are obligated to disclose information to their clients that is relevant to their selling/buying decisions. Broker B should have advised his sellers about the possibility of an offer, even if it had not been submitted or written. The possibility of an offer may influence sellers to revise their negotiating strategy. Broker B deprived his clients of this opportunity by withholding information that another offer could be coming in.

CASE STUDY: THE SLEAZY BROKER: PUTTING YOURSELF BEFORE THE CLIENT

Broker Eric's friend had listed a home with a competitor, but the friend determined in a short time that she did not like her listing agent and characterized her agent as "sleazy." Eric's friend said she wanted Broker Eric to be her buyer-agent when her listing sells, and she shared this information with her listing agent.

The listing agent said that he had a buyer interested in her home and would bring the buyer only if she agreed to choose him as her buyer-agent for her next purchase. As an additional incentive, he would lower the listing commission. If she did not agree to those terms, the listing broker said he would show the buyer other homes.

The seller was highly motivated to sell. With profuse apologies to Eric, the friend accepted the listing broker's offer of a reduced commission. The property sold with the listing agent acting as a dual agent and then becoming a buyer-agent.

While making the seller an offer to reduce professional fees is not unlawful, it is illegal and unethical for the listing agent to advise the seller that buyers would not be shown the property unless the seller agreed to engage the listing agent as a buyer-broker on the next transaction. This behavior is a clear violation

of the listing agent's fiduciary duties to his client, as well as of Article 1 of the NAR Code: "When representing a buyer, seller, landlord, tenant, or other client as an agent, REALTORS® pledge themselves to protect and promote the interests of their client." The listing agent should also discuss some of the ethical compromises that brokers make when they act as dual agents and commit the understanding between the agent and the clients to writing per state law. (Recall from Part 2 that dual agency may not be lawful in certain U.S. states.)

HOW WOULD YOU RESPOND?

Limited Services Brokers

A potential listing client is interviewing you as well as two other competing firms in your community. Your firm is a full-service traditional brokerage firm that charges a 5.5% listing fee. After you present your firm's services to the seller, the seller asks, "Why should I pay your firm such a high commission on the sale price of my home? One broker in town can list my home for a flat fee of \$595. The other one is offering to list my home at 1.79%. Why should I pay you more?" You know that the flat-fee company will place the seller's listing in the MLS and not provide any other advertising, marketing, or negotiation service. The listing office charging 1.79% has not explained to the seller that co-brokers will charge an additional percentage if they are responsible for bringing a buyer to the transaction. What should you say about your competitors' practices and fee structures?

Possible Responses

Real estate professionals must refrain from discussing and/or disparaging their competitors' business practices and fees. For one, brokers who discuss their colleagues' compensation may inadvertently violate federal price-fixing laws. Since there is no standard commission rate (brokerage firms establish their own pricing policies), brokerage firms may charge whatever fee they wish for their services based on their cost of business and what the market will bear. Price-fixing laws also prohibit suggesting that brokers in one community will boycott another broker because of his pricing structure. Violations of price-fixing laws can result in prison sentences and hefty fines.

Another reason to avoid criticizing a competitor's business is because doing so is inconsistent with the Preamble to NAR Code of Ethics, which prohibits REALTORS® from disparaging competitors. The competition's business and/or business practices should not be criticized unless it can be done in an objective, professional manner. If asked about a competitor, instead of saying, "Sailaway Realty is a terrible company—their sales staff is inexperienced," a more appropriate comment might be, "Sailaway Realty is a good company. But let me tell you why my firm could do a great job marketing your property."

It is completely appropriate to compare and contrast your services to those of your competition in an objective manner. Today's brokers must be able to defend and justify their fees because consumers have more choices of firms from which to choose. You may wish to discuss the services your firm may provide compared to your competitor, including:

- analyzing current sales and comparative markets
- setting price
- providing marketing materials (e.g., yard sign, flyers, etc.)
- listing your house with MLS services
- tapping into the real estate network of buyers
- screening prospective buyers
- showing your home to prospective buyers
- negotiating contract terms with buying agents
- managing all contract offers/counteroffers
- assisting with closing and settlement
- cooperating with and paying cobrokerage firms

HOW WOULD YOU RESPOND?

Submitting Offers

- A.** I had a good offer on a property listed by a competitor. When I called the broker to make an appointment to present the offer, the broker advised me the property was already under contract and was due to close in a month. The broker refused to present my offer. Was that broker right?
- B.** I told a listing broker that my sellers were going to submit an offer in two days on a property that broker had listed. The broker called me back in the interim and advised me that he had found a buyer whose offer was accepted. Shouldn't the broker have advised his sellers that another offer was pending?

Possible Responses

- A.** No. All offers must be submitted as long as the property sale has not closed. It is up to the seller whether any other offers are to be

considered during a pending transaction. If the seller doesn't want any other offers submitted, the broker should request those instructions in writing so that problems like this are addressed.

The broker should submit all offers for a very practical reason as well: the seller can accept the second offer as a back-up contract; if the initial contract falls apart, the broker can still have a viable sale.

Note that the NAR Code of Ethics clearly states in Article 1-6 that "REALTORS® shall submit offers and counter-offers objectively and as quickly as possible."

- B.** Yes. In all fairness to the seller, not only should the listing broker's offer have been submitted, but the possibility of other incoming offers also should have been revealed. It is possible that the listing broker was concerned that if a cooperating agent were involved, the listing broker would have to split the commission, so he concealed the possibility of your offer.

Although handling multiple offers can be nerve-wracking, a seller should be advised to wait, if possible, for all offers, evaluate the merit of each, and counter all viable offers by requesting that the buyers bring their best offer within a specified time period. That way, the seller can choose the best among them. (In some areas, only one offer is presented at a time, although the seller is informed of all possible offers.)

Considerations about the size of the broker's commission should always be secondary to the best interests of the client. To do otherwise is an ethical breach and, in some states, a violation of statutes.

Real estate professionals also have an ethical responsibility to keep up-to-date on practices, principles, and laws as part of their professional obligations. In fact, most states have made continuing education a legal requirement to maintain licensure. However, these requirements establish a legal minimum in terms of professional education, and often can be satisfied with a correspondence course. A wise real estate agent would seek regular and extensive training beyond the state-required minimum.

ETHICS AND RELATIONSHIPS WITH COLLEAGUES

Whether a real estate office has many practitioners or only a few, brokers and managers may find it challenging to establish harmonious relationships among their salespeople. They often use a policy manual to create a framework in which practitioners can see what constitutes acceptable office performance and behavior and what does not. The best policy manual will not prevent problems from arising, but it does provide a structure so that brokers can act consistently and fairly with all salespeople. Unfortunately, authors of such policy manuals cannot always anticipate the problems that can arise among office colleagues and their broker.

***EXERCISE: TEN COMMANDMENTS FOR WORKING
WITH COLLEAGUES***

If you were to write a “Ten Commandments” to guide agents regarding their relationships with colleagues in your real estate office, what would you include? (You may use “Thou shalt” shall not” language if you wish.)

- 1.
- 2.
- 3.
- 4.
- 5.
- 6.
- 7.
- 8.
- 9.
- 10.

The relationship between brokers and their sales staff is also fraught with potential ethical concerns. In most states, brokers are liable for the actions of their agents. Thus it behooves brokers to supervise their associated licensees as closely as possible. On the other hand, affiliated brokers have an obligation to follow office policies and the managing broker’s directives and to keep office matters confidential.

HOW WOULD YOU RESPOND?

The Question of Mishandled Escrow Funds

One of the associate brokers in a real estate firm knew that the broker/manager was experiencing some personal and financial difficulties. In a confidential discussion with the broker/manager, the associate broker learned that the manger was going through an expensive divorce and was occasionally using the escrow (trust) funds to take care of attorney’s fees. The broker/manager assured the salesperson that every time he used the escrow funds, he returned the funds within a few days.

What should the associate broker do?

Possible Response

The associate broker should contact his personal attorney and, depending on the attorney’s advice, notify the state regulatory agency. (Many

regulatory agencies allow you to report such problems anonymously.) The associate broker should also consider terminating his relationship with the broker/manager.

In most states, any business generated by an associated broker “belongs” to the broker. That is, any listings or sales or leads are the property of the broker, and if the relationship between the broker and an associated broker is terminated, those current and pending and future transactions that originated in that office must stay with the firm. To take business away from an employing broker is a breach of trust and, in some cases, larceny.

HOW WOULD YOU RESPOND?

The Question of the Commission Dispute

Real estate agents who handled a multimillion dollar sale of oceanfront property battled over the \$1,400,000 commission from the transaction. The broker claimed that her managing broker terminated her before the sale closed and denied her the appropriate share of the commission, approximately \$300,000. The managing broker claimed that the associate broker was dismissed from the firm because of differences in business philosophy.

How should this situation be handled?

Possible Response

Real estate brokers have the difficult task of supervising licensees who, for the most part, are highly independent individuals. Ultimately, managing brokers are legally responsible for the acts of their associates and so must accept responsibility for their ethics as well. While terminating an agent may be difficult, keeping one who is unproductive, incompetent, or unethical may ultimately threaten the livelihood of all of the individuals affiliated with the office. If in fact the associate broker in the case study was incompetent or unworthy, the managing broker should terminate that individual before he or she causes damage to clients and the firm. If the associate broker were fired simply to avoid paying a large commission that was earned, then the manager’s behavior is unethical and could perhaps lead to litigation by the associate broker.

Terminations should be in compliance with employment laws as well as in as positive an environment as possible. Associates who terminate their relationship with their firms should return all proprietary materials to their broker firms and remember to keep confidential any information learned

about their firm. Customers and clients should not be contacted unless the broker has given permission to do so.

The role of ethical leadership is perhaps the most challenging of all the supervisory tasks of brokers, requiring them to be a model of professionalism and ethical conduct at all times.

HOW WOULD YOU RESPOND?

The Case of Seniority

While Jennifer Fried was serving on floor duty, a customer, Rebecca Greene called in requesting information about a storefront property listed for rent with the firm. Jennifer gave the appropriate information to the customer and wrote down Rebecca's name and phone number, promising to get back to her within a few days with some other storefront rental possibilities.

Two days later, Rebecca called back but could not remember Jennifer's name. Jori Miller was on floor duty that morning and tried to find out who had assisted Rebecca earlier in the week. She was unsuccessful because there was no telephone logbook or office policy manual. After checking with the office manager regarding assisting Rebecca, Jori made an appointment to show her several properties and was successful in negotiating a lucrative long-term lease.

When Jennifer called Rebecca back, she learned that her colleague, Jori, had already helped Rebecca rent one of the properties that Jennifer had intended to show her.

Jennifer was very angry that Jori had "stolen her customer" and threatened the broker that if she did not receive the commission on this transaction, she would quit the firm. Jennifer was the top producer and had worked for the firm for more than five years.

Jori, on the other hand, was relatively new to the business and to the firm. As a matter of fact, this was only her second transaction.

How would you handle this dilemma if you were the broker?

What would you do if Rebecca had asked for Jennifer by name and Jori had lied about Jennifer being unavailable?

Possible Response

A telephone log or office policy would have prevented the negative results of this encounter. However, Jennifer's poor attitude would still cause a problem. To give Jori's commission to Jennifer would send a

message to Jori that her actions were inappropriate when, in fact, Jori's conduct was exemplary. The broker may wish to pay Jennifer a referral fee from company funds. However, the broker must also develop a new policy regarding employee seniority. If Jori had been deceitful about Jennifer's availability, Jori's behavior should be at the least reprimanded and Rebecca's account turned over to Jennifer.

HOW WOULD YOU RESPOND?

Working with Colleagues

- A.** I am thinking about leaving my broker. I think another brokerage firm will give me greater financial and/or business opportunity. What do I need to do?
- B.** One of my firm's listing clients, a seller, has expressed dissatisfaction with the handling of his property by one of my colleagues. The agent handling the listing is lazy and incompetent. The listing will expire soon. What should I advise the seller?
- C.** The top producer in the office makes sexist jokes and remarks. What should I do?

Possible Responses

- A.** There are a number of legal, ethical, and procedural matters that you must consider as you terminate your relationship with your broker.

Before giving notice to your broker, review the policy manual regarding termination procedures or policies. Usually addressed in the manual are such issues as the disbursement of commissions on pending sales, returning proprietary items (e.g., office keys and signs), and notifying clients regarding the management of their accounts.

While many brokers will pay a commission on pending transactions as long as the salesperson continues to follow up on the details leading to a closing, state laws usually do not require a broker to do so. It's advisable, then, if your broker does not have a written policy regarding commissions on pending transactions, to discuss this matter with your broker when you give notice.

You may wish to give your broker a list of your current and pending transactions, detailing what you have taken care of so far and what remains to be done. You may wish to recommend which office salesperson would be best suited to take over the customers and clients with whom you are doing business.

It would be unethical to contact your customers and clients after you leave your broker. You could be diverting your broker's business. You may do so only with the permission of your broker and with utmost tact and discretion. You might say, perhaps, "Mr. Brown, I'm calling to let you know that I am no longer affiliated with Super Realty as of this coming week. However, the company will still be handling your property and has assigned Broker Smith to assist you. Would it be all right if Mr. Smith meets with you this week to review the marketing of your property and to get to know you?"

Most customers and clients will want to "follow" you to your next position. After all, they have established a relationship with you and haven't even met your broker. That is why your broker will probably prefer to handle the transfer of your business. Any questions your clients have about your new business relationship should be deferred to your present broker.

It's advisable to give the firm at least one week's notice so that the broker can make adjustments to floor duty and advertising schedules. If you are an independent contractor, you can, of course, terminate your relationship on a moment's notice, but that will not make you look professional.

You may want to give a written notice to the broker in person. Be prepared for the broker to give you an exit interview. If the broker is concerned about the staff and company, the broker will want to know why you are leaving. Your broker may even wish to negotiate with you, offering you terms that are competitive with those your new firm is offering you.

When you do leave, you are not permitted to discuss proprietary information with your new broker. You enjoyed a fiduciary relationship with your past broker—a relationship of trust and confidence. Any confidential information you received must remain confidential forever. It would also be unethical for you to make disparaging remarks about your previous broker to anyone. Return all of the broker's property before leaving: client files, office and property keys, books, and manuals. And don't forget to notify your local board and state real estate commission of your change of broker and new business address.

- B.** Before you speak to the seller, you should tactfully approach your colleague and hear your colleague's side. If you feel the handling of the account has been inept, you may wish to help your colleague or consult your broker. This matter should be handled by your broker, not by you. Your comments to the seller should demonstrate concern for the seller's property but also respect for your colleague's feelings. Remember that the NAR Code of Ethics also encourages you to refrain on commenting on a colleague's business.

- C. Whether it is your top producer or your best customer, you cannot tolerate sexual harassment. Tolerance sends the message that more aggressive conduct (e.g., seductive behavior, sexual bribery, sexual coercion, assault) is acceptable. Develop a clearly communicated, substantive sexual harassment policy and give a copy to all employees and agents in the firm. Make sure the policy has a reporting mechanism with suggested dispute techniques. If you are the manager, you must discuss this matter immediately with the agent and express your concerns about the inappropriate comments. If the behavior persists, you should consider terminating this agent's relationship with the office because the conduct puts the office at legal risk.

A FINAL NOTE

Ethical dilemmas are not the private property of real estate practitioners, but in fact are inherent in many situations. This is obvious every time we turn on or read the news. Public personalities from the fields of medicine, politics, sports, and entertainment confront ethical dilemmas before the nation and the world. Perhaps some of these dilemmas appear more dramatic and threatening than those confronting real estate professionals; nevertheless, moral issues are increasing in frequency and complexity.

As real estate practitioners, we are the gatekeepers of the American dream of home ownership; we are guardians for appropriate land use and a clean environment; we provide invaluable service to businesses, citizens, and government; and the results of our work fuel the economy. Although wrestling with ethical dilemmas is not an everyday experience, ethical dilemmas are becoming more commonplace. We read more and more often about moral failures, individual and institutional. As technological, demographic, and social changes push us into the future, our talents and skills will stretch to their limits. The ultimate challenge to confront us—as real estate professionals and as human beings—will be to do the right thing.

REVIEW QUESTIONS

Choose the letter of the answer choice that best answers the question, and check your responses with the Answer Key at the back.

- 1. A form of relationship in which the broker represents neither buyer nor seller is termed ____.**
 - A. facilitation
 - B. single-agency brokerage
 - C. dual-agency brokerage
 - D. subagency

2. **When a client or customer asks a broker to engage in discriminatory conduct, the broker should first _____.**
 - A. attempt to educate the consumer about fair housing laws
 - B. withdraw from employment
 - C. report the consumer to HUD
 - D. file a complaint with the licensing authority

3. **The best practice for listing agents regarding properties that have been stigmatized may be to _____.**
 - A. disclose this information to all prospective buyers after obtaining permission from the seller-client
 - B. not disclose this information unless asked
 - C. refuse listings of this type
 - D. notify the state regulatory agency about the listing

4. **The competition's business practices _____.**
 - A. must be described in a listing presentation
 - B. should be described in negative terms to generate business
 - C. should not be criticized
 - D. should not be criticized unless it can be done in an objective, professional manner

5. **Achieving harmonious relationships with other brokers is difficult primarily because _____.**
 - A. policy manuals are often ineffective
 - B. the real estate business thrives on competition
 - C. agents cannot be required to be cooperative
 - D. state laws and federal laws do not control commission rates

6. **Procuring cause disputes could be eliminated by _____.**
 - A. exclusive representation agreements.
 - B. open listing agreements
 - C. encouraging buyers to see properties without assistance
 - D. eliminating the MLS

7. **Sunshine Properties' top producer, Judy, decided to leave her firm for another agency. Judy _____.**
 - A. can call her clients and advise them to move their listing to her new firm
 - B. can take copies of any listing or representation agreements procured by her
 - C. can take originals of listing or representation agreements procured by her
 - D. should provide appropriate notice to her broker/manager so that her clients and customers' needs can be addressed.

8. **When brokers have multiple offers on a listed property, they should consider all of the following EXCEPT _____.**
- A. how much commission would be earned if a particular offer is accepted
 - B. that all offers must be submitted to the listing client
 - C. that offers must be presented objectively to the listing client
 - D. that listing clients should be advised on the merits as well as the disadvantages of waiting until all offers are in front of them

Additional Resources

RESOURCES FOR ADDITIONAL INFORMATION

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WEBSITES

Center for Business Ethics (CBE). <http://www.bentley.edu/cbe/>

CBE is a non-profit education, research, and thought-leadership organization, focused on business ethics and corporate responsibility. CBE hosts conferences and global business ethics symposia, and offers executive development course in partnership with the Ethics and Compliance Officer Association.

Ethics Resource Center (ERC). <http://www.ethics.org>

Founded in 1922, the ERC is a non-profit educational organization devoted to independent research and the advancement of high ethical standards and practices in public and private institutions. ERC works with the private sector to address corruption internationally, and also works with organizations to create ethics programs or to improve existing programs.

Institute for Global Ethics. <http://www.globalethics.org>.

The Institute for Global Ethics was founded by Rushworth Kidder in Camden, Maine, in 1990. The Institute is dedicated to exploring the idea of shared moral values as well as committed to helping organizations and individuals put those values into practice, finding frameworks that tackle tough issues.

International Business Ethics Institute (IBEI). <http://www.businessethics.org>

The IBEI is a private, non-profit, nonpartisan, educational organization that was founded in response to the growing need for transnationalism in the field of business ethics. The Institute is dedicated to disseminating business ethics information to demonstrate the positive, tangible changes that responsible business can generate.

Josephson Institute of Ethics. <http://www.josephsoninstitute.org> and <http://www.charactercounts.org>

The mission of the Josephson Institute is to improve the ethical quality of society by changing personal and organizational decision making and behavior. Ethics faculty provide expert insights and resources to promote professional development and leadership effectiveness of executives and managers and to create an ethical business culture that enhances morale, growth, and profitability while reducing risks of costly and reputation damaging lawsuits and scandals.

National Association of REALTORS®. <http://www.nar.realtor>

The National Association of REALTORS® is a trade association representing more than 1 million real estate professionals. Its members subscribe to a professional code of ethics.

Society for Business Ethics. <http://www.societyforbusinessethics.org>

The Society for Business Ethics is an international association whose objectives are to promote the study of business ethics and to provide a forum in which moral, legal, empirical, and philosophical issues of business ethics may be openly discussed and analyzed.

Answer Key for Review Questions

Part 1

1. B
2. A
3. E
4. A
5. D

Part 2

1. C
2. A
3. D
4. D
5. C

Part 3

1. A
2. A
3. A
4. D
5. B
6. A
7. D
8. A

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