



**House
Legislative
Analysis
Section**

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**REQUIRE REAL ESTATE AGENTS
TO DISCLOSE AGENCY**

**House Bill 4269 as enrolled
Second Analysis (4-5-94)**

**Sponsor: Rep. Joseph Young, Jr.
House Committee: State Affairs
Senate Committee: Commerce**

THE APPARENT PROBLEM:

Over the past few years, a number of lawsuits and questions have arisen that have prompted the Michigan Association of Realtors to request certain changes in the part of the Occupational Code governing real estate brokers and salespeople. Reportedly, lawsuits have been brought regarding real estate agents' obligations to reveal to prospective clients who the agent actually works for, as well as questioning whether independent contractor relationships can exist between real estate brokers and real estate salespeople, and whether or not referral fees can be paid to unlicensed people.

Traditionally, all residential real estate agents work for home sellers, even when contacted by prospective buyers who wish to view a home for sale. That means that all of the real estate agent's legal and professional duties are owed to the seller, even though the agent may be working with a prospective buyer. This is possible because of a system involving multiple listing services and "subagency." A real estate company that lists (that is, puts on the market) a property is called the listing broker, and its real estate agents represent the seller. Other real estate agents or companies that show the property to prospective buyers (either through a multiple listing service or through direct inquiry from a prospective buyer) are called "subagents" because they actually work for the listing agent on behalf of the seller, even though they work with prospective buyers. Although the buyer is provided a service by the real estate (sub)agent, the buyer in this situation does not have a real estate agent formally working for him or her in the sense of putting his or her best interests ahead of those of the seller.

In fact, until very recently, the official policy of the National Association of Realtors required all subagents to be seller's agents, so that all real estate agents participating in multiple listing services were

required to act on behalf only of the sellers listed with the service and were prohibited from acting on behalf of buyers. Reportedly, NAR has modified this multiple listing policy to allow offers of subagency to be optional rather than mandatory, though participants in multiple listing services still are required to "offer cooperation" to other agents participating in the service (in the form of subagency or cooperation with buyer's agents), including offers of compensation.

This system works only if buyers are aware that real estate agents represent the seller and the buyer doesn't rely on the agent for any advice that might not be in the seller's best interests (such as an offering price that is lower than the asking price). However, many prospective home buyers -- especially first-time home buyers -- are not aware that most real estate agents work for the seller and relate to the real estate agent as though the agent worked for them, the buyer, rather than the seller. In fact, in 1991 the National Association of Realtors (NAR) estimated that two-thirds of all lawsuits against real estate brokers or agents in the United States alleged either misrepresentation on the part of the agent (that is, the prospective buyer thought the agent worked for the buyer, not the seller) or failure to disclose defects in the property offered for sale.

In order to reduce real estate agents' legal liability, the NAR advocated legislation or regulations requiring both mandatory property condition disclosure and disclosure of agency. In fact, the NAR joined with the Consumer Federation of America in January of 1993 to promote specific legislation for notifying buyers and sellers in home sales transactions of who represents whom. Specifically, the alliance calls for legislation that requires written disclosure, a state-prescribed form written in easily understood language, disclosure at the first "substantive" contact with the prospective

buyer or seller, and the signatures of both the real estate agent and the prospective buyer or seller.

At the request of the Michigan Association of Realtors, legislation has been introduced to address these issues.

THE CONTENT OF THE BILL:

The bill would amend the part of the Occupational Code that regulates real estate brokers and real estate agents to require real estate agents to tell prospective clients who the agent works for before he or she received any confidential information from the prospective client. The bill also would recognize in statute an "independent contractor" relationship, clarify the prohibition against paying unlicensed people for referrals, and prohibit discrimination on the basis of handicap or familial status.

Disclosure of agency. The bill would add a new section to the Occupational Code (Public Act 299 of 1980) to require real estate agents to tell prospective home buyers whether the agent worked for the seller (was a "seller's agent"), the buyer (was a "buyer's agent"), both (was a "dual agent"), or neither (was a "transactional coordinator"). Agents would have to explain to potential buyers or sellers the possible kinds of agency relationships and the licensed agent's duties in each relationship. Disclosure of agency would have to be made to prospective buyers or sellers before the buyer or seller had given the licensed real estate agent any confidential information specific to that buyer or seller.

Disclosure of agency would have to be in writing, and the bill would require that written disclosure "substantially conform" to a form provided in the bill. The written disclosure regarding real estate agency relationships would have to have a general statement regarding the bill's requirements, definitions of three types of agency, a "licensee disclosure" section to be signed and dated by the real estate agent, and an acknowledgment section to be signed and dated by the prospective buyer or seller.

The written disclosure of agency would have to say that before a potential buyer or seller disclosed confidential information to a licensed real estate agent regarding a real estate transaction (defined in the bill) the potential buyer or seller should

understand what kind of agency relationship he or she had with the agent. The disclosure also would have to inform the potential buyer or seller that Michigan law required licensed real estate agents, who were acting as agents for buyers or sellers, to "advise" the potential buyer or seller of the nature of the "agency relationship" between the real estate agent and the potential buyer or seller.

The written disclosure would have to include descriptions of "seller's agent," "buyer's agent," and "dual agent," and basically tell the prospective buyer or seller that the agent would reveal "known information" that could be used to the benefit of the person for whom the agent was working. Thus, the description of seller's agents would have to specify that seller's agents, under agreements with a seller, act solely on behalf of the seller and would disclose to the seller known information about the buyer which could be used to the benefit of the seller. (The description also would have to include a description of a "subagent.") Descriptions of buyers' agents would have to specify that, under a buyer's agency agreement with the buyer, the buyer's agent acted solely on behalf of the buyer and would disclose to the buyer known information about the seller which could be used to benefit the buyer. The description of dual agents would specify that, with the knowledge and written informed consent of both a buyer and a seller, licensed real estate agents could be agents of both the seller and the buyer in a transaction. The description also would have to say that in dual agency situations, licensed agents would not be able to disclose all known information to either the seller or the buyer, and that the agents' obligations would be subject to the specific provisions of the agreement between the dual agent, the seller, and the buyer.

Written disclosure would have to include a "licensee disclosure" section that provided a place for the agent to check off his or her relationship with the potential buyer or seller (seller's agent, buyer's agent, dual agent, or "none of the above," which basically would mean a "transaction coordinator"), a statement that the agent had provided the form to the prospective buyer or seller before the disclosure of any confidential information, and a place for the agent to sign and date the document.

Finally, the written disclosure would have to have a section in which the prospective buyer or seller acknowledged having received and read the form required by the bill before having disclosed any

confidential information specific to the buyers or sellers. The prospective buyer or seller would have to indicate which he or she was, sign, and date the document.

Independent contractor relationships. The bill would define the terms "employ" and "employment" so as to allow the inclusion of an independent contractor relationship between a real estate broker and an associate broker or real estate salesperson if two conditions were met:

(1) There was a written agreement between the real estate broker and the associate broker or salesperson in which the latter are not employees of the former for federal and state income tax purposes; and

(2) not less than 75 percent of the annual compensation paid by the real estate broker to the associate broker or salesperson was from commissions from the sale of real estate. (However, the bill would make clear that real estate brokers would remain responsible for the actions of real estate brokers or salespeople who had independent contractor relationships with the broker.)

Other provisions. The bill also would do the following:

- * Specify that it would not prevent a licensed real estate agent from acting as a "transaction coordinator" (defined in the bill as a licensed agent who was not acting as the agent of either the buyer or the seller), "upon proper notices to all parties to a real estate transaction";

- * Define the four possible relationships between a licensed agent and a prospective buyer or seller, namely, "buyer's agent," "dual agent," "seller's agent," and "transaction coordinator"; and

- * Include in the prohibition against paying commissions ("or valuable consideration") to "unlicensed" people the sharing or paying of a fee to anyone providing names of ("or any other information regarding") potential buyers or sellers of real estate. (The bill would specifically exempt payment for commercially prepared lists of names, and the currently allowed referral of prospective tenants.)

Effective date. The bill would take effect on January 1, 1994.

MCL 339.2501 et al.

BACKGROUND INFORMATION:

Enrolled Senate Bill 480 (Public Act 177 of 1994) is tie-barred to House Bill 4269. The Senate bill would amend the Occupational Code (Public Act 299 of 1980) to add "failure to disclose agency" to the list of offenses for which licensed real estate agents could be penalized. (The Occupational Code penalties for real estate agents who violate its provisions include license actions -- denial, suspension, revocation, limitation -- probation, censure, mandatory restitution, and maximum civil fines of \$10,000.)

The enrolled version of House Bill 4269 incorporates the provisions of House Bill 4057 of 1993 as that bill passed the House.

FISCAL IMPLICATIONS:

The Senate Fiscal Agency reports that the bill has no fiscal implications for the state. (1-26-94)

ARGUMENTS:

For:

In the traditional residential real estate transaction, the real estate agent works for the seller and represents the seller's interests. In fact, the traditional real estate transaction is weighted in favor of the seller in the sense that most of the parties involved -- the seller, the listing agent (who markets the house), and the subagent (who shows the house to prospective buyers) -- represent the seller; the buyer is the only one representing himself or herself.

But there are other kinds of relationships between prospective buyers or sellers and real estate agents, including "dual agency" and "buyer agency." In the case of dual agency, a single real estate broker represents both the seller and buyer as clients, often through using two different agents working for the company. Dual agency may arise when an agent working for a broker is approached by a close relative, friend, or former client who wishes to buy a property listed with the agent's company. Such buyers would expect the agent to give them advice that would treat their interests fairly. And in fact

when such dual agency arises, the clients (seller and buyer) and agents agree to limit the agency relationship so that the agents do not disclose any information that would create a negotiating advantage or disadvantage for either client.

Finally, and most recently in residential real estate transactions, there can be what is known as "buyer agency," where the buyer -- as well as the seller -- has enlisted the formal services of an agent. (Buyers' agents have been common for some time in commercial real estate transactions.) In real estate transactions involving buyers' agents, the listing agent and the seller represent the seller's interests, while the buyer's agent and the buyer represent the buyer's interests. The buyer can freely discuss with his or her agent the value of properties, negotiating strategies, and personal finances, because his or her agent is obligated not to disclose to the seller or the seller's agent any information that could give the seller a negotiating advantage.

The bill would provide consumers with valuable information -- and therefore, ultimately, protection -- concerning the kinds of real estate agency and, specifically, the kind of relationship he or she has with a specific real estate agent in a real estate transaction. Consumers will be protected from disclosing to inappropriate real estate agents information that might give other parties to the transaction an unfair negotiating advantage, while at the same time protecting real estate agents from legal liability so far as agency disclosure is concerned. Reportedly, since 1986, 43 states and the District of Columbia have adopted some form of mandated real estate agency disclosure, either through legislation or regulation, though apparently many do not require disclosure at the first "substantial" contact. It is time for Michigan to join this roster of states in protecting consumers from fraud and real estate agents from legal liability by adopting strong real estate agency disclosure laws.

For:

Historically, most real estate salespeople in Michigan have operated as independent contractors, and not as employees of the real estate brokers with whom they are affiliated. Both state and federal agencies have recognized the validity of real estate salespeople acting as independent contractors rather than employees. For example, the federal Internal Revenue Service allows independent contractor relationships for purposes of income tax withholding

and Social Security payments, and the validity of this relationship also has been recognized under the state workers compensation act. However, recent lawsuits have cited the real estate licensing part of the Occupational Code as the basis (and the sole basis) for holding that real estate salespeople cannot be independent contractors. The bill would clearly establish in statute that an independent contractor relationship could exist between real estate brokers and associate brokers or salespeople, and would specify the conditions under which such a relationship existed.

For:

In 1988, the director of the Bureau of Commercial Services in the Department of Licensing and Regulation issued an opinion (later reconfirmed in early 1989) that took the position that licensed real estate agents could pay unlicensed people for the simple referral of potential sellers or buyers. Before this, the real estate community had interpreted the Occupational Code (specifically, Section 2512[f]) as prohibiting such payments. The bill would clarify the issue, reinstating the real estate community's interpretation of the law.