

FROM HORSES

TO HOUSES

A Brief History of Agency

And What Real Estate Agency

Means for You Today

A Guide, for Sellers and Buyers of Real Estate, to the
Professional Standards Governing Real Estate Agents

Sellers and buyers, be aware: what you need to know about real estate salespeople.

When you want to buy or sell your house or apartment, it's natural to feel a little overwhelmed by all the words you may hear or read. What does the term *real estate agent* really mean? Is *agent* the same as a *salesperson*? Is *Realtor* the same as *agent*?

Who are *exclusive agents*? *Escrow agents*? *Inspectors*? Does an *appraiser* mean the same thing as an *assessor*?

Understandably, you're only concerned about what you need to know right now, for what is probably the most important financial transaction of your lifetime. But it will be helpful for you to look at the history of how the real estate agency developed, in order to understand its meaning for you today.

The Beginning of Sales Relationships: The Finder

Historians think the rules for salesmen probably started, not with houses, but with *horses*. Centuries ago, in England (where most American law comes from), in the days before both automobiles and agents, a man had a horse to sell. He approached someone else who regularly sold a lot of horses, asking, "Will you find me a buyer for *my* horse? I'll pay you a portion of what I get, if you'll sell mine along with yours."

An arrangement was struck between the two of them. As that selling practice became established, the fee became called a *commission*, and such a salesman was called a *finder*.

The word *finder* continues today in our *common law*, which is the body of law created by decisions of judge, starting in England, and continuing in most American states today. Now we often use more contemporary words for that type of sales relationship. We call such a salesperson a *transaction broker*, a *mediator*, or a *facilitator*. But the concept remains the old one of *finder*: "Find me a buyer, and I'll pay you a commission."

The Beginning of Agency

But, back in old England, some horse sellers quickly found that hiring a finder wasn't nearly enough. The finder was, after all, selling his own horses in competition with theirs! He wasn't trustworthy. How could sellers know he wasn't advancing his own inventory over theirs?

Some sellers decided they needed a more personal and responsible relationship, where the seller would not sell any of his own horses to compete with their own. Instead, a sales *agent* would pledge himself to become dedicated to getting the highest price for his *client*, the seller. This became known as a *fiduciary* relationship. (Our English language descended from Latin; and the Latin word *fiducia* means *trust*.) Such a special salesperson became known as an *agent*, from the Latin *agentis* meaning *acting (for another)*.

The Duties of Agents

Various fiduciary duties, of agent to client, became established under common law. There's an acronym today to help you remember the fiduciary duties which, over many years, have become required of an agent: 'O-L-D C-A-R'.

O is for *Obedience*. The agent was responsible for following the instructions of the horse seller: "Make sure my horse is well fed when you're boarding him." Later, this became, for real estate: "Don't show our house this Saturday afternoon – we're having company." (Obviously, the duty of Obedience only applies to *lawful* instructions. "Don't show the house to any minorities", for example, is not a valid agency duty.)

L is for *Loyalty*. The agent and all his associates were required to be loyal to just one side of the transaction. In representing a seller, the agents had to get the seller the highest price for the horse (or, later, the house). The agent could not promote one of his own horses instead. An agent always has to favor the client's interest ahead of his own. That strong allegiance may seem, at first, very difficult, or even unnatural; but it's vital to understanding what's required of agency.

D is for *Disclosure*. In the course of his business, the horse-selling agent came to learn quite a bit about what horse buyers liked, how much they wanted any particular animal, and how much they might pay for it. The agent was required to disclose all of this to the horse seller: "He's in love with your animal, and may pay a lot for it." Consistent with the duty of loyalty to only one side, the agent must always disclose what he knows about the other side's motivations and financial resources. "They love your house, and they have a lot of money."

C is for *Confidentiality*. Perhaps the English horse owner wanted to ask ten pounds for his horse, but told his agent he'd settle for just eight, if he had to, because he had a debt due next Saturday. As an agent (no longer just a finder), the agent was responsible for keeping that motivation of his client very confidential from the other side.

A is for *Advocacy*. The horse agent had to argue on behalf of his client, telling buyers why the horse might indeed be worth ten pounds. The agent was given duties similar to that of a barrister, a British lawyer defending one side of a law case. Just as lawyers in the same law firm did not represent both the plaintiff and the defendant in a lawsuit, a horse agency could not represent both seller and buyer. Traditional real estate agencies in this country follow the same rule. They advocate a higher price for home sellers, not a lower price for buyers. An agency's advocacy is for one side only. 'A' also stands for *Accountability*. An agency has to account properly for all funds received.

R is for *Responsibility* (sometimes termed Reasonable Care.) The agent had to know what he was doing. He was professionally responsible for knowing the current prices for all the various types and ages of horses, for giving his clients good advice about how much to ask, and how much to take, for each horse, and for describing accurately to the public all the horses he offered for sale. In a word, an agency is responsible for representing a client in a knowledgeable, professional, *responsible* manner.

All of these ancient agency duties have been continually applied, by courts and legislatures, to modern real estate agents. Today, real estate agencies still owe all these same 'OLD CAR' fiduciary duties to their clients.

Your Choice Today: Facilitator or Agent?

Now, if you want to sell your house, you face the same fundamental choice for selling which the horse seller faced centuries ago. Do you want to deal with a facilitator, or an advocate? Do you want a finder, or an agency? There is nothing wrong with either choice. It depends upon what you want. But you must always be aware the fundamental difference. An agency has many more duties to you does than a non-agency facilitator.

Buyer Agency

But what about the buyers? Who represented them? For buying horses in old England, as far as historians can tell, the answer was “nobody”. The agents were all paid by and represented horse sellers, and the buyers had to look out for themselves. But, for real estate, in America, a new breed of agency arose, starting in the 1980’s: *buyers’ agencies*.

Buyer agencies represent buyers, and seek *lower* prices for buyers. They owe all the ‘OLD CAR’ fiduciary duties to their clients, potential buyers. For example, under the duty of Disclosure, a buyer agent will tell the buyer anything he can learn about the sellers’ motivations for selling: “They may want to sell quickly, because this is a divorce situation.” (A seller agency would never reveal that fact, without permission of the sellers.) Under Confidentiality duties, a buyer agency would never normally reveal that its client has fallen in love with a particular house and is quite willing to overpay for it.

Because of the new presence of buyer agencies, homebuyers now have a choice. If you are a buyer, you can work with a sellers’ agency as a customer, or with a buyers’ agency as a client. If you work with a sellers’ agency, that agency must describe properties to you honestly and fairly, but it will not owe you any fiduciary duties. If you work with a buyers’ agency, that agency will owe you all the ‘OLD CAR’ fiduciary duties. There is nothing wrong with either choice – it depends upon what you want. But you must always be aware of the fundamental difference.

Strategies for Successful Agency

When an agency represents your interests, that advocacy does *not* equal being impolite or unreasonable, let alone being obnoxious, to the other side of the negotiations. Just as good law firms represent clients forcefully but politely, good agencies are usually diplomatic, as appropriate, when negotiating with your opposing party. Even this phrase ‘opposing party’ needs to be kept in context. Sellers and buyers do have opposing interests about price; but both do want a transaction to occur. Of course, a good seller’s and buyer’s agency may often lead their separate clients to agree upon a fair market price, benefiting both sides....just as opposing law firms will often urge their clients to settle a lawsuit. Effective advocacy may sometimes lead to a mutually-satisfactory compromise. Giving your agency a certain amount of discretion to act for you may be in your interests.

A Modern Possibility: *Dual Agency*

Quite recently, real estate agency has become immensely more complicated than it has been in the past, because of the newest variant upon the scene: *dual agency*. In dual agency, the agency, usually a large real estate company will attempt to represent *both* the seller and the buyer of the same property. This is a much diluted form of agency, radically different from anything ever seen in the past.

Since a dual-agency brokerage firm represents both seller and buyer, it must be neutral with regard to all conflicting interests of the seller and buyer. Consequently a dual agent *cannot* satisfy fully all the fiduciary duties, including loyalty, disclosure of information learned from the other side, and obedience to lawful instructions, which are required of sellers' agencies and buyer agencies.

Law firms almost never represent both the plaintiff and the defendant in the same lawsuit, because of the inherent conflicts of interest involved. The law firm would have to get the informed consent of both sides, and explain each of the conflicts and practical difficulties involved in detail, and perhaps refer both clients to other law firms to help them decide whether or not consenting to such an unusual dual representation was in their individual interests.

Similarly, dual real estate agencies seeking to represent both seller and buyer must take sufficient time to explain the inherent conflicts and difficulties to their clients, in a way the clients actually understand, and obtain truly informed consent of both sides before such a relationship may proceed.

If you are considering dealing with a dual agency, the following may be a helpful brief checklist of some issues you need to consider before you consent to such a relationship. Any agent, before asking you to consent to any dual agency, must discuss all these issues with you and make sure you understand all their ramifications, before you consent.

Checklist of ten *dual* agency issues, for discussion by dual agencies with clients:

There are many important conflicts inherent in dual agency. This brief checklist is for convenience, but is by no means all inclusive.

1. As a seller or buyer, you are entitled to consult an *attorney* before agreeing to dual agency. You can incur significant risks from the conflicts of interest inherent in dual agency, so you may wish to consult with independent professional legal advice before you agree to it.

In asking for dual agency, the brokerage company is seeking to end any prior full fiduciary relationship it may have had with you and begin a new, limited dual agency relationship with both sides. Dual agency can happen only with (a) your informed consent and (b) the informed consent to the party on the other side. You are *never required* to consent to dual agency.

2. A dual-agency company represents *both* sellers and buyers of the same property. Since sellers prefer higher prices, and buyers prefer lower prices, this company seeks to represent both you and a client with interests directly conflicting with yours. Is that really acceptable to you?

3. Since both seller and buyer will be giving the agency their confidences, there are issues about leakage (even if unintentional and inadvertent) of your confidences to the other side. For example, are there separate files for sellers and for buyers? You are entitled to know, and should ask about, what efforts will the dual agency company be taking to protect your confidentiality. How will the company handle your confidences at its staff meetings? When negotiating, what will it, and what will it not, reveal to the other side?

Any dual agency has directly conflicting duties of (a) confidentiality to you and (b) disclosure of your motivations to its client on the opposing side. The brokerage firm must explain to you what types of information from you it will hold confidential, and what types of information it will disclose to its client on the other side.

In general, the brokerage firm should not disclose to the other side, without your permission, any information you give it that would weaken your negotiating position. It should hold confidences and try very hard to be impartial, discreet and neutral.

However, the brokerage firm will nonetheless be required to disclose information you give it in confidence if failure to disclose the information would be material misrepresentation about either the property or your abilities to fulfill your legal obligations, or as otherwise required by law.

4. If you are a buyer, you need to know whether or not the dual-agency company pays *higher* commissions or other bonuses to its brokers or salespersons for selling properties directly listed with itself. Such intra-company incentives would conflict with impartial representation of you as a buyer, since your needs might be better met by other real estate companies' listings.

Some brokerage firms, when representing buyers, do pay *the same* compensation to their agents for selling in-house inventory as they do for selling the listings of other companies. You need to know whether or not that is the case.

5. Does the dual-agency company refer consumers to mortgage, moving, insurance, title, relocation and/or home improvement firm(s) in which it has an ownership interest? Those interests may conflict with impartial representation of your interests as a consumer. This firm *cannot* represent you impartially in the purchase of these products and services. You should be aware that you might find lower rates and/or better service elsewhere.

6. You must be informed about conflicts not only generally, when you are first considering a dual agency relationship, but once again specifically, every time a *specific* conflict of interest begins to occur. You should learn, and the firm must disclose to you, the nature and extent of all current and prior relationships your company has and has had with party opposing you. For example: if you are a buyer, you should be informed how many listings the seller has given to this dual-agency company. If this particular seller/developer has given the brokerage company a *dozen* listings, and is expecting to give it many more, can that company really be as impartial about your interests as a buyer, as if it had received only listing?

In every specific conflict of interest situation, you have the right to refuse to consent, even though you have consented before generally, or to previous other specific conflicts. Each opposing party always retains a continuing right to choose to be fully represented by another brokerage firm which does not have any conflicts of interest.

7. Whenever you choose to proceed with dual agency, you need to understand fully that you are giving up your rights to undivided loyalty, full disclosure of negotiating advantages, and exclusive representation from this real estate company, and to other traditional fiduciary benefits of an agency/client relationship. The brokerage firm must now act impartially and can no longer be an advocate for you. Since you are incurring some risks, you are always entitled to consult your own attorney, at any time, before proceeding or before proceeding further.

8. Only after all such limitations and risks of dual agency have been fully explained to you, in a way you understand, may you be asked to decide whether you wish to consent to dual agency by giving your informed consent. If you agree, you will be ending any prior full fiduciary representation you may have had with the agency and agreeing that your brokerage firm may now act in a new capacity for you, as a limited-service dual agency, representing both sides of your sale/purchase. (If your brokerage firm does not obtain your informed written consent, the brokerage firm cannot represent any other parties with interests conflicting to yours, and, if you wish, you can always then choose another firm to represent your interests with advocacy and undivided loyalty.)

9. Note that all offers written by any brokerage firm acting as a dual agency should be on unbiased neutral forms, favoring neither the seller nor the buyer, specifying terms subject to a later mutually-satisfactory purchase and sale agreement and containing a written recommendation that each side consult its own legal counsel for that agreement.

10. Only after all of these issues have been discussed with both clients may an agency reasonably proceed with asking for informed consent to dual agency. If the client understands and agrees, an agent meeting with a client should memorialize in writing, in an appropriate format, that, to the best of his or her knowledge and belief, the client has actually understood the conflicts of interest inherent in dual agency and has nonetheless given his or her informed consent. In addition, dual-agency firms will then present their own consent forms, seeking the client's written agreement to dual agency.

The newest variant: *designated* dual agency.

In some states, a seller or buyer can engage the services of a particular type of dual real estate agency, whose practice is to *designate* one or more of its agent(s) to represent the seller, and other agents within the same company to represent various potential buyers of the same property. Once so designated, a real estate agent may then be the *only* agent in the company acting for the seller or the buyer. You as a consumer then become the traditional client of *only* that individual licensee. The real estate brokerage firm, its supervising broker, and the appointing broker remain dual agents representing both the seller and the buyer.

Though this type of agency is sometimes called just 'designated agency', it is not a distinct form of agency, but is just a variant of dual agency. A designated dual agency must be neutral with regard to any conflicting interests of the seller and buyer. Consequently a designated dual agency cannot satisfy fully the fiduciary duties, including loyalty, disclosure of information learned from the other side, and obedience to lawful instructions, which are required of seller and buyer agencies.

You should be aware that all other agents in such a dual agency firm may potentially represent the other side of your sale or purchase. Only the individual designated agents owe the buyer or the seller all of the 'OLD CAR' fiduciary duties. However, the individual designated agents must put their client's interest first and negotiate for the best price and terms for that client. Designated dual agency without full presentation of its limitations and risks, in a way each side understands, and obtaining mutual informed consent, is illegal. In seeking your informed consent, dual agencies must provide you with additional information to make sure you understand fully the conflicts of interest involved. See the dual agency checklist above, as well as the one below. You are *never* required to consent to designated dual agency.

**Checklist of three special issues of *designated dual agency*,
for discussion by designated dual agencies with their clients:**

In addition to the ten dual agency issues listed above, your designated agent must discuss some special issues inherent in designated dual agency with you, in order to obtain your informed consent.

First, what efforts, if any, will a designated dual agency company be taking to protect your confidentiality from the opposing designee within the same company? For example, can the buyer's agent walk behind the seller's agent's computer screen? Can phone conversations from one desk be overheard at another? Does the company have *separate* staff meetings, conference rooms, telephone lines, fax machines and computers/internet for the seller's agent and the buyer's agent it is assigning to service you as well as the other side?

Second, are the designated agents assigned to each side equal in ability, training and experience? You need to make sure that your opposing party is not represented by a successful twenty-year veteran, while you are represented by an inexperienced new agent.

Third, the designating broker is required to remain 'neutral' between seller and buyer. Yet this may be the same person who, under your state's licensing law, is responsible for supervising both agents. As a practical matter, how does he or she plan to achieve such neutrality? What if both designated agents need his advice? Is it simple or easy to give 'neutral' advice to both sides? Is having an office manager neutral to your interests really acceptable to you?

Standards of Professional Practice for Dual and Designated Agencies

A dual agent or designated agent is not in compliance with the real estate industry's professional standards unless the agent:

1. fully discloses to the prospective client/principal the conflicts of interest inherent whenever a firm represents both the seller and the buyer;
2. fully discloses the actual conflicts of interest inherent in the *specific* relationship as soon as contemplated, and thereafter as appropriate; and,
3. before entering into the relationship and thereafter, is satisfied by clear and convincing evidence that the consumer actually understands the conflicts of interest inherent in the specific relationship. (If the agent is not so convinced, the agent does not enter into or continue the relationship until the consumer is represented by independent legal counsel.)

Note that it doesn't matter if you, as an unsophisticated client, don't care about conflicts of interest and are ready to sign a seemingly simple disclosure or consent form your trusted agent places in front of you. You must nevertheless be led to *understand* all the implications of all the conflicts of interest before you consent to them. As the *Restatement of Agency* puts it: "The agent's duty of fair dealing is satisfied only if he reasonably believes that the principal understands the implications of the transaction". The burden of achieving your understanding rests not upon you, the consumer, but upon your trusted fiduciary, who benefits from the conflict of interest affecting you.

Advantages and Disadvantages of Each Type of Relationship

Which type of real estate brokerage relationship is best? That all depends upon you, and what you are looking for. It is not at all the purpose of this publication to influence your decision towards one type of real estate relationship over another, or to suggest which may be best for you. Rather, this pamphlet seeks to give you some essential factual information on the different types, so you may make your own choice.

If you are a *seller*, and you only want a company to bring you potential buyers, without expecting anyone to represent or advocate your interests, and you are prepared to do your own negotiating: hiring a facilitator may make good sense for you.

If are a *buyer* and you only want someone to show you properties, without expecting anyone to represent or advocate your interests, and you are prepared to do your own negotiating: working with a facilitator, or with a seller's agency as its customer (understanding that you are *not* its client) may make good sense to you.

If you want more than that: a company to advocate your interests as a seller or buyer, contracting with an undivided seller's or buyer's agency to become its client would be a logical choice.

If you want to deal with a firm which represents both sellers and buyers (often a large firm) and do not require that the company have undivided loyalty to your interests, and you actually understand the conflicts of interest inherent in agency representation of both sides of a transaction, a dual agency may be attractive to you. If the dual agency practices designated dual agency, you will be assigned an individual agent to represent you, including advocating your interests against other agents within the firm who may be representing the other side.

The choice of what you want in a real estate relationship is yours alone.

Choose carefully.

Choose thoughtfully from the different types of agency and non-agency options briefly described here. You may want to consult your attorney about your choices. After you have thought about your needs or had the issues explained to you, it is your own responsibility to choose what you want.

Whether you are a buyer or seller you can always choose to have the advice, advocacy and representation of your own real estate company to serve you, if you wish. But never assume that a real estate firm works solely for you, unless you have a written agreement for that kind of undivided agency relationship.

All real estate licensees must, by law, present properties honestly and accurately. They must also disclose any material defects in real estate which they or their brokerage firm know about. The duties of a real estate licensee do not relieve you of your own responsibility to protect your own interests.

You should *not* tell any real estate agent representing the other side of the transaction anything you would not tell your adverse party directly, especially anything that might weaken your bargaining position.

If you need advice for legal, tax, insurance or land survey matters, it is your responsibility to consult a professional in those areas. Real estate licensees do not have a duty to perform home, lead paint or insect inspections, nor do they perform septic system, wetlands or environmental evaluations.

You are legally responsible for any wrongful actions of your real estate agency, including all its agents and subagents. So it is obviously very important to choose an experienced, responsible and professional firm, with high ethical and business standards.

After you make your decision upon a real estate relationship, you can remember that there is, in most states, a long history of common law tradition standing behind you, providing real substance and clear meaning to the choice you have made.

Think about your costs.

You should expect to pay less for less service, and more for more service. For example, if you are a seller, and you plan to do your own price analyses, showing and negotiating, but you want your property entered into a local multiple listing service, you might ask a facilitation firm to do that for you,

for a nominal fee. If you want the firm to do more, to find you the buyer, the fee might logically be higher.

If you want still more and want an agent who will advise you and owe you fiduciary duties and act on your behalf, the fee might logically be still higher. And if you want not just one individual agent, but an undivided agency working on your behalf, the fee might logically be higher still. A dual or designated dual agency should be able to charge less, since it may be compensated twice, by both sides.

If you are a buyer, who is paying the salesperson or company you are working with? Will the seller always be paying the commission? Under what circumstances will you be obligated to pay a fee?

Read all brokerage contracts carefully. Make sure you understand not only the fees you are responsible for, but its cancellation provisions. If you turn out to be unhappy with the salesperson or company you are working with, how quickly can you get out of that contract you are signing? Commissions must never be standardized, but differ from firm to firm, determined only by what you can negotiate in the competitive conditions of your local real estate brokerage marketplace.

A final word.

We hope this explanatory pamphlet on real estate brokerage and agency has been helpful to you, as you pursue your real estate adventures. But be sure to consult your attorney with your questions. Selling or buying a home is probably the most important financial transaction of your lifetime. Make sure you choose which professionals to work with thoughtfully and carefully.

Other terms used in real estate transactions.

A **client** is the person to whom an agent owes his or her fiduciary duties (the seller for a seller's agent, or the buyer for a buyer's agent). The client may also be referred to as the agent's **principal**.

By contrast, the word **customer** is used for the party to whom the agent does **not** owe any fiduciary duties. So, a buyer is the customer of a seller's agent. And a seller is a customer of a buyer's agent.

An **undivided agency** is an agency which represents only sellers, or only buyers. A **designated agency** is the opposite: a dual agency, which assigns one agent to represent a seller and another to represent a buyer for the same property.

An **exclusive agent** is an agent who has a written contract with a client providing that the client will work only with his agency. If the client is a seller, the contract is called an **exclusive listing**. If the client is a buyer, the contract is called an **exclusive buyer representation** agreement.

The agents and finder/facilitators we have discussed previously in this pamphlet should not be confused with these other players on the real estate scene today:

Appraisers do not act as salespeople or agents, but provide an independent estimate, based upon marketplace data, of the market value (sometimes called most probable selling price) of a property.

Assessors are special types of appraisers, who work for cities and towns. They perform mass appraisals of *all* the properties in a whole community, in order to provide rough estimates of value for taxing very many properties fairly.

Escrow agents are limited special agents whose services are limited to holding and accounting for funds, before and at a property's closing. A regular seller's or buyer's agent may also serve as an escrow agent, if both parties agree. In some states, deposits are held by independent escrow companies. In some areas, lawyers usually serve as the escrow agents. In other areas, real estate agents commonly act as the escrow agents.

A home **inspector** is a professional who inspects, but does not sell properties and issues reports on their condition. An inspector is usually neither a salesperson nor an appraiser; so an inspector will not try to sell you a property nor express an opinion of its value, but will report to you only about the physical condition of the property.

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