LEGAL PULSE NEWSLETTER

First Quarter 2016

Welcome to the Legal Pulse Newsletter. The Legal Pulse examines legal liability trends in the real estate market so you can understand the risks and implement appropriate risk management practices. In this edition of Legal Pulse, we review recent case decisions and legislative activity in the areas of Agency, Property Condition Disclosure, and RESPA. We also review Employment decisions and legislative activity from the past twelve months.

So far this year, there are no major trends to report in the Agency cases. The most common issues addressed this quarter were general agency issues, vicarious liability, and breach of fiduciary duty. One recurring issue in several cases this quarter was whether an individual served as a seller's representative, or merely as an intermediary transaction broker. In addition, there were a few statutory and regulatory developments relating to the timing of a written agreement between a licensee and a prospective buyer, the real estate transaction-related actions that may be performed by licensees, and the acceptable methods of storage for real estate transaction records.

The Property Condition Disclosure cases this quarter examined three issues we encounter regularly: structural defects, sewer/septic, and mold and water intrusion. The licensees fared well in the cases, with none held liable in the property condition disclosure cases for this quarter. With respect to legislative activity, Virginia amended its disclosure form regarding adjacent parcels and covenants and restrictions on the property.

The courts continue to see a significant number of alleged kickback schemes in cases asserting RESPA violations. In many of these cases this quarter, the claim was barred by the statute of limitations. An issue that came up in several of the anti-kickback cases was whether fees were split between two or more entities.

This quarter, we also review decisions in the Employment context. There were relatively few Employment cases this past year, and the majority of these cases involved independent

contractor issues. With respect to legislative activity, Arkansas and Wisconsin clarified the activities that an unlicensed employee of a brokerage firm or licensee may perform, and Wisconsin also amended its licensing laws regarding independent contractor status of licensees.

For the details, read the summaries below, and check out the tables showing cases and liability figures to learn more about recent trends in real estate law.

I. AGENCY

In several of the cases discussed below, the court found that the licensees were acting as transaction brokers who merely passed information between the parties. In that situation, the brokers were required to satisfy statutory duties, but did not owe a fiduciary duty to the client. A broker might be liable, however, if it was responsible for late delivery of documents, as demonstrated below.

A. Cases

1. **Humphries v. Becker**, No. 41897, 2016 WL 275310 (Idaho Jan. 22, 2016)

Seller's son and daughter-in-law did not serve as seller's representative in the sale transaction and were not liable for any misrepresentations in the disclosure form, even though they provided information for the form.

Several months after purchasing a property, the purchasers learned that they did not have water rights to the well to which the sprinkler system on their property was connected. Purchasers sued the seller and the seller's son and daughter-in-law ("Children") for fraud and misrepresentation with respect to statements made about sources of water to the property. Purchasers alleged that the Children acted as the seller's representative in the transaction, and made misrepresentations regarding water sources. The Children had lived on the property for many years and had knowledge of the property, while the seller had only recently traded properties with the Children to obtain ownership of the property prior to the sale. The Children provided information about the property to the seller and her representative to assist in drafting the disclosure form and MLS listing.

The court found there was no agency relationship between the Children and the seller, and that the Children did not make any affirmative statements of fact regarding water sources on the property. Despite the Childrens recent residence and knowledge of the property, they had no duty to disclose any information regarding statements in the property disclosure form or MLS listing because they were not parties to the contract.

Summary judgment for the Children was affirmed, but the court reversed summary judgment in favor of the seller, who could be held liable for possible misrepresentations regarding water sources to the property in the disclosure form.

2. **Spies v. Deloach Brokerage, Inc.**, CV 214-053, 2016 WL 901300 (S.D. Ga. Mar. 3, 2016)

Licensee did not owe a fiduciary duty to a purchaser while serving as a transaction broker.

After closing on a property, the purchaser discovered that she could not install a spa due to erosion issues on the land. The purchaser brought claims for fraud, breach of contract, and statutory violations against the licensee who assisted her with the transaction. According to the purchaser, the licensee should have known about the erosion because he had knowledge about the island and lived near the property.

Because there was no written representation agreement between the parties, the listing broker served as a transaction broker and only owed limited statutory duties to the client. The court held that there was no fiduciary or confidential relationship between the purchaser and the licensee because they did not sign an agreement or other writing that would establish such a relationship between them. The court also did not imply a fiduciary relationship based on the parties' behavior. The purchaser was a sophisticated party and there was no evidence that the licensee tried to take advantage of or defraud her, so the licensee did not implicitly undertake a fiduciary obligation to the purchaser. Furthermore, the licensee did not conceal the erosion, and did not know of the issue because it was not possible to detect the erosion from mere observation of the land. The court granted summary judgment in favor of the brokerage firm.

3. **Rogers v. Wright**, No. S-15-0127, 2016 WL 280942 (Wyo. Jan. 22, 2016)

Licensee was not liable for statements made while the licensee was acting as an intermediary between the parties.

After discovering cracks in the walls and the foundation, leaks in the foundation, and improper grading on a recently purchased property, the purchaser sued the seller for breach of contract, negligence, intentional misrepresentation, and breach of warranty for failing to disclose those issues. In the claim for intentional misrepresentation, the purchaser argued that the seller could be liable for statements made by the licensee.

The court determined, however, that the licensee was in a nonagency relationship with the client and was serving as an intermediary. The licensee was not acting as seller's agent or buyer's agent, and this non-agency status was noted in the sales contract. There was no evidence that the licensee breached any statutory duties. The court affirmed summary judgment for the seller on the intentional misrepresentation claim.

3. **RZI Properties, LLC v. Southern REO Assocs., LLC**, No. A15A2090, 2016 WL 718441 (Ga. Ct. App. Feb. 24, 2016)

Brokerage firm could be held liable if its broker was responsible for late delivery of documents and information to the seller.

A prospective purchaser sued its brokerage firm after the seller rejected the purchaser's offer. The purchaser claims the licensee, acting as transaction broker with limited statutory duties to the parties, caused late delivery of documents and failed to notify him of deadlines set by the seller. The trial court granted summary judgment for the firm. On appeal, the court reversed the summary judgment because there were questions of fact regarding whether the broker was at fault for untimely delivery of the information.

B. Statutes and Regulations[1]

Georgia

Georgia added a statute clarifying the permissible actions of a licensee that do not constitute the practice of law. A licensee may perform the following actions: provide information and advice regarding a listing, management, sale, purchase, exchange, renting, lease, option, or conveyance of real property; prepare special stipulations to forms prepared by an attorney; provide legal forms prepared by an attorney; and complete legal instruments prepared by an attorney for clients and customers.[2] The

[1] This first quarter update reviews legislative activity from the following jurisdictions: Arizona, Arkansas, Georgia, Idaho, Indiana, Iowa, Kansas, Kentucky, Maryland, Massachusetts, Montana, New Mexico, North Dakota, South Dakota, Utah, Virginia, Washington, West Virginia, and Wyoming.
[2] Ga. Code Ann. § 15-19-59 (2015).

licensee may not close a real estate transaction or express or render a legal opinion regarding the status of title to property.

Georgia also amended its statute regarding escrow accounts to change the term "banks" to "financial institutions." As amended, the statute also allows accounts other than bank checking accounts to be used for escrow accounts.[3]

Virginia

Virginia amended its statute regarding the establishment of an agency relationship. A written agreement between the licensee and a prospective buyer does not need to be executed before the licensee shows properties to the prospective buyer.[4]

Washington

An amended regulation in Washington modifies the storage options available to licensees for the storage of real estate records. Real estate records, including initial listing agreements, trust account records, negotiations, price reductions or changes in status, initial offers, counteroffers, electronic communications, and final disposition of the transaction, may be stored electronically or on remote devices if retrieval of the documents is immediate.[5]

C. Volume of Materials Retrieved

Agency issues were identified 18 times in 14 cases (*see* Table 1). Agency: Other was the most commonly raised issue, while Vicarious Liability and Breach of Fiduciary Duty issues were considered in many cases as well. Four Agency statutes and one regulation were retrieved this quarter.

II. PROPERTY CONDITION DISCLOSURE

Two of the following cases address a familiar question in property condition disclosure cases: did the licensee know about the property condition? Where the answer is no, the licensee is not liable. In one of the cases discussed below, however, the facts showed that the licensee *did* know about the condition. At that point, the inquiry turned to when the licensee knew of the condition. The licensee could be held liable if she knew of the condition prior to closing on the property transaction.

[3] Ga. Code Ann. § 43-40-20 (2015).
[4] Va. Code Ann. § 54.1-2132 (2016).
[5] Wash. Admin. Code § 308-124C-110 (2016).

A. Cases

1. **The Finest Place, Inc. v. Skidmore**, 477 S.W.3d 745 (Mo. Ct. App. Jan. 25, 2016)

Licensee could be held liable for failure to disclose water system problems if she was aware of the problems prior to closing.

The purchasers of a mobile home park brought claims against the sellers and the seller's representative for failure to disclose problems with the park's water system. The trial court entered judgment against the sellers and awarded damages, but denied purchaser's claim against the licensee and the broker.

On appeal, the court reversed the decision with respect to the licensee and the broker. If the licensee knew about the water system problems prior to closing, she could be held liable for fraud and misrepresentation. During the trial court proceedings, the court concluded that the licensee learned about the water system problem either "prior to closing or just after the closing." The appellate court remanded the case back to the trial court for a factual determination as to whether the licensee knew about the problems before closing on the property.

2. **Raffield v. Hursh**, No. A15-0828, 2016 WL 456949 (Minn. Ct. App. Feb. 8, 2016)

Licensee was not liable for alleged misrepresentations regarding a section of the property because he was not aware that any statements were false.

The purchasers sued the seller and seller's representative for allegedly misrepresenting that there were no drainage problems on a section of the property and that the property was buildable. There was no evidence that seller's representative knew his statements about the property were false.

The court stated that a licensee cannot be held liable for relying on the seller's representations if he did not know they were false, and there was no evidence to suggest the licensee should have known of a problem with the property. Further, the purchasers'

negligent misrepresentation claim failed because the licensee did not owe a duty to the purchasers. Summary judgment for the licensee was affirmed.

3. **Long Rockwood VII, LLC v. Rockwood Lodge, LLC**, No. 2:14-CV-00318, 2016 WL 335853 (D. Idaho Jan. 26, 2016)

Letter sent to the purchasers' broker might not be sufficient to prove that the sellers adequately disclosed a problem with rotting wood at the property.

The purchasers of Rockwood Lodge brought claims against the sellers for allegedly failing to disclose rotting wooden substructures in deck balconies at the lodge. Prior to closing, the sellers sent a letter to the purchasers' real estate broker, asking him to forward the letter to the purchasers. The parties disputed the extent of the disclosure in the letter. The letter disclosed an issue regarding sealing of the decks, but according to the purchasers, the letter was misleading because it suggested the issue was one of routine maintenance rather than a major repair project.

The court granted summary judgment for the sellers on most of their claims, but allowed the fraud and fraudulent concealment claims to proceed. The court held that a jury might conclude that the letter was misleading. The court also noted that the adequacy of the broker's disclosure of the letter to the purchasers could be an issue to be decided in the case, but the court did not reach that issue in this decision.

B. Statutes and Regulations

Virginia

Virginia recently amended the statute setting forth the disclosures to be provided by the seller of property. The revised disclosure form indicates that the owner of property makes no representations regarding adjacent parcels of property "including zoning classification or permitted uses of adjacent parcels."[6] The seller also makes no representations regarding "covenants or restrictions as may be recorded among the land records affecting the real property or any improvements thereon."[7]

[6] Va. Code Ann. § 55-519 (2016).
[7] Va. Code Ann. § 55-519 (2016).

C. Volume of Materials Retrieved

Property Condition Disclosure issues were identified 12 times in nine cases (*see* Table 1). The cases addressed issues of Structural Defects, Sewer/Septic, Mold and Water Intrusion, Pollution or other Environmental Issues, and Boundaries. One statute regarding Property Condition Disclosure was retrieved this quarter.

III. RESPA

A common theme in this quarter's cases was whether the lender in an alleged kickback scheme divided fees with another entity. Also, in one case discussed below, the court considered an alleged kickback scheme we have seen in other cases – the lender's receipt of fees from reinsurance agreements for private mortgage insurance.

A. Cases

1. **Cunningham v. M & T Bank Corp.**, No. 15-1412, 2016 WL 683372 (3d Cir. Feb. 26, 2016)

Claim based on alleged kickback scheme involving reinsurance fees paid on private mortgage insurance was barred by the statute of limitations.

Borrowers brought a class action lawsuit against the lender for alleged violations of RESPA's anti-kickback and anti-fee-splitting provisions. The borrowers paid for private mortgage insurance ("PMI") as a condition of their mortgages. The lender referred the borrowers to PMI insurers who reinsured the insurance policy with the lender's captive reinsurer. The borrowers alleged that the Bank colluded with the PMI insurers and received funds from reinsurance agreements that required the entity to take on little or no actual risk. The trial court granted summary judgment for the lender, finding that the claims were barred by the statute of limitations. The judgment was affirmed on appeal.

2. **Schonebaum v. Shellpoint Mortgage Servicing**, No. 14-CV-03093, 2016 WL 1104875 (D. Colo. Feb. 29, 2016)

RESPA claim should be dismissed because the complaint did not allege that the lender divided any fee with another entity.

The borrower alleged that the lender violated RESPA by accepting charges for something other than services actually performed. However, the borrower's complaint did not include an allegation that any fee was divided between the lender and another entity. Because a RESPA violation requires the dividing of a charge with another entity, the magistrate judge recommended that the court grant the lender's motion to dismiss.

3. **Arace v. Quicken Loans, Inc.**, No. 15-CV-382, 2016 WL 390088 (S.D.N.Y. Feb. 1, 2016)

Because borrower could not show a single fee that was split between two separate entities, her RESPA claim failed.

Borrower brought a class action suit against the lender for improperly charging and splitting an unnecessary "tax service fee" in connection with her mortgage. The borrower alleged that because she lives in a building that is a cooperative and the cooperative association is responsible for paying the taxes, the lender had no reason to charge the fee. The borrower also claimed the lender split the fee with other entities, none of whom performed services in exchange for the charge. The documentation showed that the borrower was charged two separate fees that went to two separate entities; there was not a single charge that was split between two parties. Because a RESPA violation requires a fee divided by two or more parties, the court granted the lender's motion to dismiss the claim.

4. **Collins v. First Financial Services, Inc.**, No. 7:14-CV-288-FL, 2016 WL 589688 (E.D.N.C. Feb. 10, 2016)

Borrower's anti-kickback claim failed because the lender performed services in connection with the loan and did not split fees with another entity.

Borrower obtained a mortgage loan with the lender FFSI. Through the course of several transactions, the loan was transferred to several different entities. The borrower alleged that the lender violated RESPA by giving or receiving fees or kickbacks while acting as the lender in the origination of the loan. However, the allegations in the complaint stated that FFSI kept all of the fees it charged. Therefore, there were no facts showing that FFSI split the fees with another entity. Furthermore, because FFSI engaged in substantial conduct regarding the loan, the fees it received were in exchange for services performed. Lender's motion to dismiss was granted.

B. Statutes and Regulations

No RESPA statutes or regulations were retrieved this quarter.

C. Volume of Materials Retrieved

RESPA issues were identified 18 times in 15 cases (*see* Table 1).

IV. EMPLOYMENT HIGHLIGHTS: YEARLY UPDATE

A. Cases

Three decisions regarding employee or independent contractor status and vicarious liability, all arising out of the same case, were decided this past quarter. As discussed below, the court considered whether the lender, brokerage firm, and a contractor hired to perform trash-out services could be held liable for conversion of a borrower's personal property. In a decision from last year, the court concluded that Massachusetts' independent contractor statute does not apply to real estate licensees.

1. **Mwangi v. Federal National Mortgage Assoc.**, No. 4:14-CV-0079, 2016 WL 770820 (N.D. Ga. Feb. 16, 2016), 2016 WL 759909 (N.D. Ga. Feb. 16, 2016), and 2016 WL 770818 (N.D. Ga. Feb. 16, 2016)

Individuals and entities involved in removal of borrower's personal property from her foreclosed home might be held liable for conversion of property, depending on the employment status of the parties.

The borrower defaulted on her mortgage and moved out of the property while attempting a short sale of the home. After foreclosure, the lender hired a brokerage firm to perform preservation services on the property. The brokerage firm's licensee determined that the property had been abandoned, and hired a contractor to "trash out" the property. The borrower claimed that she did not abandon personal property at the home and that the brokerage firm and its licensee, the contractor who performed the trash out, and the lender were all liable for conversion of her personal property.

The court issued separate decisions with respect to each of the three defendants, but denied the defendants' motion for summary judgment in each of the three decisions. With respect to the brokerage firm and its licensee, the court noted that real estate licensees are generally considered independent contractors. In this case, however, the court found that factual questions existed as to whether the brokerage firm could be held responsible for the licensee's actions. The broker had considerable control over the time, manner, and method of the licensee's work, so the licensee might technically be considered an employee rather than an independent contractor. The court also found a factual dispute as to whether the individual who performed the trash-out services was actually an independent contractor or employee of the company who hired him. With respect to the lender, summary judgment was denied because it was unclear whether the borrower had abandoned the property and whether the brokerage firm and its licensee were employees or independent contractors of the lender.

2. **Monell v. Boston Pads, LLC**, 471 Mass. 566 (June 3, 2015)

Massachusetts independent contractor statute did not apply to real estate licensees.

Licensees sued their former brokerage firm for allegedly violating the Massachusetts independent contractor statute by misclassifying them as independent contractors instead of employees. The licensees claimed there was a conflict between the real estate licensing statute and the independent contractor statute, because a licensee cannot satisfy the requirements of both statutes at the same time. The licensees argued that the independent contractor statute, which presumptively classifies workers as employees, should apply.

Both the trial court and appellate court rejected this argument, holding that the independent contractor statute did not apply to real estate licensees because the real estate licensing statute makes clear that licensees can be classified as independent contractors or employees. Summary judgment for the brokerage firm was affirmed.

B. Statutes and Regulations

Arkansas

Arkansas amended its statute regarding the licensing exemption for real estate brokerage firm employees. An unlicensed employee of a brokerage firm may deliver lease applications, receive security deposits, show units, and convey information prepared by a principal broker.[8] An unlicensed employee may not engage in acts performed by principal brokers.

Wisconsin

Wisconsin recently amended its licensing laws to recognize that a licensee may be classified as an independent contractor. A licensee is not considered an employee of a firm if: (1) there is a written agreement between the firm and licensee indicating that the licensee shall not be treated as an employee for federal and state tax purposes; and (2) 75% or more of the compensation "related to sales or other output" paid to the licensee is directly related to brokerage services performed by the licensee on behalf of the firm.[9] Correspondingly, a number of other statutes were modified to change references to

[8] Ark. Code Ann. § 17-42-104 (2015).
[9] Wis. Stat. § 452.38 (2016).

"employees" or "employed by" to "licensees associated with a firm."[10] Likewise, the definition of out-of-state salesperson was amended to include independent contractors.[11]

Wisconsin also added a provision regarding unlicensed personal assistants. Prior to hiring an unlicensed personal assistant, a licensee must enter a written agreement with the licensee's firm indicating the duties of the assistant, how the assistant will be compensated, and the supervisory responsibilities of the licensee and the firm.[12] An unlicensed personal assistant may not perform any services at an open house which require a license, and may not assist at an open house unless a licensee is present and directly supervising the assistant.[13]

C. Volume of Materials Retrieved

Employment issues were identified four times in four cases in this quarter (*see* Table 1). For the past twelve months, Employment issues were identified 7 times in 7 cases. One statute regarding an Employment issue was retrieved this quarter; no other Employment statutes or regulations were retrieved in the past twelve months.

V. VERDICT AND LIABILITY INFORMATION

A. Agency Cases

Liability was determined in seven Agency cases, and the licensee was not held liable in any of the cases (*see* Table 3).

B. Property Condition Disclosure Cases

Liability was determined in six Property Disclosure Cases, and the licensee was not held liable in any of the cases (*see* Table 3).

C. RESPA Cases

Liability was determined in 14 RESPA cases; the defendant was not liable in any of those cases (*see* Table 3).

[10] *See*, *e.g.*, Wis. Stat. §§ 452.12(3), 452.134(4).
[11] Wis. Stat. § 452.01(5p) (2016).
[12] Wis. Stat. § 452.34 (2016).
[13] *Id*.

D. Employment Cases

Liability was determined in one employment case retrieved this quarter; the defendant was held liable in that case[14] (*see* Table 3). The court remanded the case to determine damages.

[14] *Mahoney Realty Group, Inc. v. Lamm*, No. 499-EDA-2013, 2014 WL 10987207 (Pa. Super. Ct. Jan. 28, 2014) (appellate court reversed summary judgment in favor of licensees and remanded the case; appellate court found licensees breached the independent contractor agreement).

VI. TABLES

Table 1
Volume of Items Retrieved for First Quarter 2016
by Major Topic

Major Topic	Cases	Statutes	Regulations
Agency	14	4	1
Property Condition Disclosure	9	1	0
RESPA	15	0	0
Employment	4	1	0

Table 2
Volume of Items Retrieved for First Quarter 2016 by Issue

Issue	Cases	Statutes	Regulations
Agency: Dual Agency	0	0	0
Agency: Buyer Representation	2	0	0
Agency: Designated Agency	0	0	0
Agency: Transactional/Nonagency	1	0	0
Agency: Subagency	0	0	0
Agency: Disclosure of Confid. Info.	0	0	0
Agency: Vicarious Liability	5	0	0
Agency: Breach of Fiduciary Duty	3	0	0
Agency: Disclosure of Financial Ability	0	0	0
Agency: Agency Disclosure	0	1	0
Agency: Minimum Service Agreements	0	0	0
Agency: Pre-listing Marketing of Properties	0	0	0

Issue	Cases	Statutes	Regulations
Agency: Teams	0	0	0
Agency: Coming Soon Listings	0	0	0
Agency: Other	7	3	1
PCD: Structural Defects	3	0	0
PCD: Sewer/Septic	3	0	0
PCD; Radon	0	0	0
PCD: Asbestos	0	0	0
PCD: Lead-based Paint	0	0	0
PCD: Mold and Water Intrusion	2	0	0
PCD: Roof	0	0	0
PCD: Synthetic Stucco	0	0	0
PCD: Flooring/Walls	0	0	0
PCD: Imported Drywall	0	0	0
PCD: Plumbing	0	0	0
PCD: HVAC	0	0	0
PCD: Electrical System	0	0	0
PCD: Valuation	0	0	0
PCD: Short Sales	0	0	0
PCD: REOs & Bank-owned Property	0	0	0
PCD: Insects/Vermin	0	0	0
PCD: Boundaries	1	0	0
PCD: Zoning	0	1	0

Issue	Cases	Statutes	Regulations
PCD: Off-site Adverse Conditions	0	0	0
PCD: Meth Labs	0	0	0
PCD: Stigmatized Property	0	0	0
PCD: Megan's Laws	0	0	0
PCD: Underground Storage Tanks	0	0	0
PCD: Electromagnetic Fields	0	0	0
PCD: Pollution/Env't'l Other	3	0	0
Property Condition Disclosure: Other	0	1	0
RESPA: Disclosure of Settlement Costs	3	0	0
RESPA: Kickbacks	13	0	0
RESPA: Affiliated Business Arrangements	1	0	0
RESPA: Marketing Service Agreements	0	0	0
RESPA: Other	1	0	0
Employment: Wrongful Termination (cases only)	0	N/A	N/A
Employment: Personal Assistants	0	1	0
Employment: Independent Contractors (cases only)	4	N/A	N/A
Employment: Wage and Hour Issues (cases only)	0	N/A	N/A

Table 3

Liability Data for First Quarter 2016

Topic	Liable	Not Liable	% Liable	% Not Liable
Agency	0	7	0%	100%
Property Condition Disclosure	0	6	0%	100%
RESPA	0	14	0%	100%
Employment	1	0	100%	0%