

REAL ESTATE BROKERAGE CLAIMS EVALUATION – Part One

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[Note: These are my opinions alone and are not meant to supersede or replace any company’s existing policy, which may differ for various reasons. Nor are they intended to act as a substitute for prompt consultation with the company’s own legal counsel for instruction, advice and direction. In all cases, managing principal brokers¹ are encouraged to thoroughly review potential claims with their own counsel at the earliest possible time. Lastly, this article should not be interpreted as reflecting, implying, or establishing a particular standard of practice.~ PCQ]

Introduction. Litigation and arbitration cannot be avoided forever; it is a cost of doing business. Disputes are a fact of life in today’s litigious society. This is especially true in those professions where fiduciary relationships are created between the consumer and the service provider. Realtors®, doctors, lawyers, and the clergy, are just a few of the targets for litigation because of the nature of the service they provide. Trust is an essential byproduct of these relationships, and accordingly, liability can be high. But this does not mean that the risk inherent in these professions cannot be effectively managed. The purpose of this two-part article is to locate and analyze the risks, discuss how to reduce or avoid them, and develop protocols for dealing with client dissatisfaction before it ripens into an actual claim.

Identifying Risk. Every real estate company of any size should evaluate whether to create a quality assurance committee with the sole mission of determining how best to manage professional risks and handle claims. Here are some issues to consider and questions to ask:

- Are there brokers who have had multiple claims filed against them? Are they sufficiently counseled and supervised?
- Are there some brokers whose specialty (e.g. foreclosure properties - especially the buy-side - representing flippers, etc.) invites greater risk?
- Does the broker list bank/servicer REO properties? Are they using bank-created addenda? Has the company taken a close look at these documents? Remember, this is

¹ I acknowledge that the term “managing principal broker” is not yet statutorily recognized in Oregon as of the date of this article. However, I prefer that term in order to distinguish it from non-managing principal brokers.

still a consumer transaction if the buyers are purchasing the property as a primary residence. The bank may (incorrectly) believe they do not have to disclose known material defects. However, Oregon licensing law is clear that the broker *must* disclose them; a broker's duties of "honesty" and "full disclosure" run to all principals and their brokers in the transaction.²

- Are brokers permitted to develop their own forms or clauses for certain types of transactions they engage in frequently? Have they been reviewed and vetted by the company's legal counsel?
- Does the company have meetings to address some of the ethical issues we've seen in short sale transactions (such as the representation of buyers making offers on multiple properties with no ability or intent to close on all of them)? Are sellers being made aware of this when the offer comes in?
- Are brokers fully aware of potential tax and promissory note liability to sellers in short sales – especially where the property is not a primary residence? Do they encourage clients to obtain outside professional consultation?
- Is the listing broker in a short sale subcontracting out the bank negotiation portion of the transaction? Are they working with another broker in the company, or a third party provider? Is the third party providing a service for which the Oregon Department of Business and Consumer Services ("DCBS") requires registration (e.g. debt management service providers)?
- Is the listing broker involved (directly as a principal, or indirectly as a continuing referral source) with any other companies, groups, or individuals, holding themselves out as "consultants" or other designations, suggesting a superior skill in distressed transactions?
- Does your company encourage the use of the OREF³ forms? Remember that widespread acceptance of certain forms (e.g. the OREF Sale Agreement) can morph into a standard of care.
- How many brokers is a principal broker responsible for managing and supervising? Is the ratio realistic?
- Are there some brokers with other real estate related businesses, such as home construction or multiple rentals they are self-managing? Is this addressed in the company policy? Are they allowed to list and sell their own properties, or do they list with others in the company?

² See, ORS 696.805(2)(a),(c) and 696.810(2)(a),(c).

³ Oregon Real Estate Forms, LLC.

- Do brokers have non-licensed spouses or significant others engaged in some real estate related business to whom they refer their clients? Is the relationship disclosed to the clients?
- Are all brokers encouraged to fully document their professional real estate activities for inclusion in their personal file? How long do they retain these personal files?
- Are transactional files reviewed for completeness at the conclusion of the transaction *before* the commission is disbursed to the broker? Before the file is closed?
- How many brokers have licensed personal assistants and are they actually being supervised? How is compensation paid to the assistant? This can be a real issue in order to avoid the appearance of an employer-employee relationship, which can trigger worker's comp and employment claims.
- How extensive is the company's office policy regarding client complaints? Are brokers encouraged to immediately report problems to their managing principal broker, or are they left to be handled by the individual broker until the last minute?
- Is broker advertising *really* supervised? Are brokers permitted to use inflated or misleading language regarding their experience and skill – especially in more complicated forms of transaction such as distressed sales? What about advertising condominium expertise? Does the broker truly have the experience, or are they simply trying to generate business in that area?
- How does the company deal with dual representation – are single brokers allowed to represent both sides of the transaction – and if so, are they supervised any closer than others?
- Is principal broker review *truly* a review or merely a *rubber stamp*?
- Are the rules of client confidentiality sufficiently defined in written office policy and are the policies *actually* observed and enforced?
- Does the company have written office policies that comply with applicable state law and is there principal broker training to assure that each broker is familiar with them?
- Does the company have an in-depth orientation program to familiarize new brokers with all company policy – especially in identifying risk management issues early on?
- What policies, if any, does the company have regarding allowing its brokers to testify in court or arbitration about “industry standards”? The propriety of doing so should be closely examined. It is not, in my opinion, recommended.
- What policies, if any, does the company have in permitting its brokers to file complaints

against other brokers with the Real Estate Agency or local Realtor® association?

- Are the managing principal brokers sufficiently familiar with the company's E&O coverage to know which activities are covered and which are excluded? If so, are brokers permitted to engage in excluded activities inside the company?

These are just a few of the issues that should be addressed at the quality assurance level. A realistic evaluation of them is the best place to start when developing effective risk management guidelines. The next step is to implement corrective action to reduce or eliminate known risks. This requires management from the top down.

Claims Evaluation – Before The Case Is Filed. The most critical component in managing risk is the capacity to evaluate a claim at the earliest possible time. But this first requires that all brokers be required to promptly report any potential client problems to their managing principal broker and that the principal broker be skilled in handling and properly evaluating the complaint. Some managing principal brokers are better than others when it comes to dealing with unhappy buyers and sellers. This may mean that client complaints be channeled to one or more persons who are the most skilled in dealing with the problem. Claims management by a managing principal broker with a tin ear is no management at all.

Here are some tips companies may wish to consider in evaluating and handling claims *before* they become unmanageable:

- Immediately call the unhappy customer(s) to let them know you're reviewing the matter and will get back to them promptly. Then thoroughly debrief the broker about the claim. Is the broker being truthful and complete in their explanation? Is the managing principal broker willing to ask tough questions of the broker? (E.g. "Why didn't you disclose to your seller that you had an existing personal/professional relationship with the buyer?")
- Become intimately familiar with the entire transaction. Are all transactional documents in order, fully executed and reviewed? Make sure there are no documents in the broker's personal file that should be in the transactional file – or vice versa.
- In most cases the broker being complained about should be instructed to have no further contact with the customer – unless and until the problem has been fully resolved to everyone's satisfaction. If the transaction is still in progress, select an appropriate substitute broker to continue working with the disgruntled customer.
- Are there any aspects of the transaction that create more concern than others? For example, was dual agency involved? If so, was it done in an even-handed manner? Was the broker engaged in any activity involving their personal business? Did the broker have any undisclosed relationships or financial interest in the transaction (besides recovery of a commission)?
- Is the claim one for which there may be no E&O coverage? What are the reporting

requirements to the company? If there is coverage, can the claim be resolved within the deductible limits of the policy? Does it need to be turned over *immediately* to the E&O carrier in order to avoid the risk of denial later?

- Be extremely careful about making written evaluations of claims, since they may be discoverable by the other side if litigation ensues. If the company has legal counsel, consider having all broker and principal broker writings, explanations, evaluations, etc. directed to the attorney, since it is more likely to provide some level of privilege and protection from review by the other side.
- After fully investigating the case, every effort should be made to have a face-to-face meeting with the complainant(s). This may mean driving out to see them. A face-to-face meeting at their home sends a message of good faith concern and allows the principal broker to evaluate their demeanor in familiar surroundings. If the customers are a couple, try to have both of them present in order to get both versions at the same time. Take notes or make them immediately after the meeting.
- In most cases it is not a good idea to have the broker present, since it may hamper the customers' willingness to make a full and honest disclosure. Moreover, the broker may feel compelled to defend his or her actions which could result in a confrontation.
- Be timely in meeting with the complainant(s). Delay will be interpreted as avoidance.
- Be a good listener; don't argue or make excuses. Be polite. Don't minimize the complaint, regardless of how small it may seem. Don't play "devil's advocate." Remember, the customers are probably angry and upset. It is important to let them "vent."
- Above all, don't do or say anything that could be construed as an admission by the broker or the company.
- Be careful about having your legal counsel present at such a meeting: (1) It sends a mixed message to the other side (*this claim real is "serious"; or "we need to intimidate the customer"*), and (2) It could result in making the lawyer a witness if the complainants change their story. This could disqualify the attorney from representation should a lawsuit or arbitration be filed.
- If the complainants want their attorney present, you may want to reconsider holding the meeting at all. Sometimes, they can end up with both attorneys doing the talking and posturing for their respective clients.
- If there is to be such a meeting, make sure your company attorney has set the ground

rules. For example, if it is agreed in writing that the meeting is to be in the nature of settlement discussions, it will be protected under the Oregon Evidence Code.⁴ In this manner what is said in the meeting may not be introduced into court or arbitration. Set parameters on such a meeting and observe them; don't let it become a shouting match. Either adjourn or terminate the meeting if courtesy is not observed or if threats are made. The goal should be solution oriented and forward looking – i.e. *how can we get things back on track?*

- After the matter has been thoroughly reviewed and the managing principal broker has assembled all of the facts, the matter should be re-reviewed in-house. The more experienced the managers the better - group evaluation may draw differing points of view about the severity of the claim and possible legal exposure. This may be the time for legal counsel evaluation.

Conclusion: As noted above, claims are an inherent part of the business, especially where fiduciary duties are involved. But good people skills, courtesy, and a willingness to listen, will go a long way in keeping *potential* claims from becoming *actual* claims.

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⁴ OEC 408.