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ADDITIONAL COMPENSATION: IS IT ETHICAL?

If calls to the MAR Legal Hotline and this writer are any indication, there appears to be a fairly common scenario that is causing great anger and consternation between members. In this scenario, REALTOR® A has listed 123 Elm Street and is offering cooperation and compensation in the amount of 3 percent of the purchase price to any participant in the MLS who procures a buyer for 123 Elm Street. REALTOR® B procures a buyer for 123 Elm Street and submits an offer to REALTOR® A. In the offer, it is provided that as a condition of purchase, the seller must pay the buyer's agent \$3,000 in addition to the 3 percent the buyer's agent will receive through the MLS.

REALTOR® A has always understood that conditioning an offer based on additional compensation being paid to the buyer's agent is a violation of NAR's Code of Ethics. REALTOR® A reviews NAR's Code of Ethics and concludes that REALTOR® B has violated Article 16. This conclusion is based on Standard of Practice 16-16. This Standard of Practice provides:

REALTORS® acting as sub-agents or buyer/tenant representatives or brokers, shall not use the terms of an offer to purchase/lease to attempt to modify the listing broker's offer of compensation to subagents or buyer/tenant representatives or brokers nor make the submission of an executed offer to purchase/lease contingent on the listing broker's

agreement to modify the offer of compensation.

Armed with Standard of Practice 16-16, REALTOR® A files an ethics complaint against REALTOR® B alleging a violation of Article 16 of NAR's Code of Ethics. In this hypothetical, will the panel likely find that REALTOR® B violated Article 16? While the answer may appear to be a slam-dunk "Yes," in actuality the answer is not so certain.

Assume that REALTOR® B has an exclusive buyer's agency agreement with his buyer that contains a provision that the buyer shall pay REALTOR® B \$10,000 in the event REALTOR® B finds a suitable home that is purchased by the buyer. Further, REALTOR® B's exclusive buyer's agency agreement specifies that the buyer's obligation to pay REALTOR® B \$10,000 will be offset by every dollar that REALTOR® B receives as a result of the offer of compensation through the MLS. Assume further that 3 percent of the purchase price being offered by the buyer will only result in the buyer's agent receiving \$7,000. The buyer obviously does not wish to pay REALTOR® B the additional \$3,000; thus, the buyer asks REALTOR® B to write an offer to require the seller to pay the additional \$3,000 to REALTOR® B. Thus, an offer is prepared on which a condition of purchase is that the seller pay REALTOR® B an additional \$3,000 to satisfy the buyer's contractual obligations to REALTOR® B. Is this demand by the buyer through

REALTOR® B a violation of Article 16? Under the facts of this hypothetical, there would appear to be no violation of Article 16 as applied in Standard of Practice 16-16.

As those REALTORS® who have been trained in professional standards are aware, there are 136 different case interpretations set forth in NAR's Code of Ethics and Arbitration Manual to help members understand the Code. Case #16-17 is entitled "Buyer Conditions Purchase Offer on Seller's Agreement to Pay Buyer Agent's Fee." While the factual scenario in Case #16-17 is not exactly the same as the hypothetical in this article, it would appear to have direct application to the hypothetical. In Case #16-17, REALTOR® A is offering compensation only for subagency services. REALTOR® B calls REALTOR® A, identifying himself as a buyer's agent and asking if REALTOR® A would arrange a showing of the property to REALTOR® B's client and himself. The showing occurs and is followed by REALTOR® B's presentation of an offer to purchase that is contingent on the seller's agreement to pay REALTOR® B's commission as a buyer's agent. The transaction closes, and REALTOR® A then files a complaint against REALTOR® B citing Article 16, as interpreted by Standard of Practice 16-16. REALTOR® A contends that REALTOR® B has interfered with REALTOR® A's relationship with his seller client by attempting to negotiate a

separate commission agreement with the seller. REALTOR® B responds that since the request that the seller pay his commission was made by the buyer, and not by REALTOR® B, and was made directly to the seller, and not to the listing agent, there has been no violation of the Code of Ethics.

In Case #16-17 the hearing panel determines that REALTOR® B was not in violation of Article 16, since the request for payment of REALTOR® B's fees was made directly to the seller. The case interpretation also provides that if REALTOR® B, or REALTOR® B's client at REALTOR® B's urging, had demanded that a portion of REALTOR® A's commission be paid to REALTOR® B, then a valid basis would exist for REALTOR® A's claim that there had been a violation of Article 16 by REALTOR® B.

In these factual scenarios, not surprisingly, when a listing agent is presented with an offer that indicates the seller must pay the buyer's agent an additional amount to satisfy the buyer's contractual obligations to the buyer's agent, the listing agent often demands to see a copy of the buyer's agency agreement. Unfortunately for the listing agent, there is nothing in Michigan law or NAR's Code of Ethics that requires a buyer's agent to provide a listing agent with a copy of the buyer's agency agreement. Obviously, if a listing agent has a good faith belief that no such contractual obligation exists, then he may decide to file a grievance against the buyer's agent alleging a violation of Article 16 as interpreted by Standard of Practice 16-16.

In sum, Article 16 as interpreted by Standard of Practice 16-16 clearly prohibits a cooperating REALTOR® from demanding a larger portion of the listing REALTOR®'s commission as a condition of an offer. However, when faced with this situation, REALTORS® should make certain that it is not the buyer who is making this demand in an effort to offset any amounts the buyer would otherwise contractually owe to the buyer's agent. As the old adage goes, "Looks can be deceiving."

COUNTER-OFFER VS. AMENDMENT

There continues to be some confusion about inspection contingencies, the situation where a seller and buyer enter into an agreement and the buyer's obligation to close is contingent upon a satisfactory inspection. The buyer receives the results of the inspection and discovers that \$2,500 would be needed to repair the roof. The buyer has her agent prepare an addendum that provides that the seller shall provide the buyer with a \$2,500 credit against the purchase price at closing to cover the costs of repair for the roof. The addendum is presented to the seller, and the seller refuses to sign the addendum. What has happened, and where are we?

There appears to be a fairly common misunderstanding that the addendum presented by the buyer's agent is a "counter-offer." Under this misconception, when the seller rejects the counter-offer, the transaction is at an end. This analysis is not correct and can have devastating consequences.

In order to understand the legal status of the transaction at this point, it is necessary to begin at the beginning. The transaction began with the buyer making an offer. If the seller accepted the offer, then a binding purchase agreement is in place between the parties. Similarly, if the seller countered the buyer's offer, and the counter was accepted by the buyer, then a binding purchase agreement is in place. When the buyer's agent presents the addendum which calls for the \$2,500 credit, it cannot be a counter-offer, as there is no outstanding offer to counter.

Since there is a binding purchase agreement in place when the buyer's agent submits the addendum to the seller, the addendum is simply a proposal by the buyer to amend the terms of the existing, binding purchase agreement. If the seller declines to accept the proposed amendment to the binding purchase agreement, the purchase agreement remains in place unchanged.

The danger in treating the addendum as a counter-offer is that the sellers may

mistakenly believe that by rejecting the addendum, they are freed of their obligations under the existing, binding purchase agreement. Believing themselves so freed, they go out and enter into a purchase agreement with another buyer. Unfortunately, if the first buyer decides he will close without the proposed \$2,500 credit against the purchase price, the sellers could find themselves obligated to sell their home to two different buyers. In that situation, if the sellers wish to close with either buyer, then one buyer will get a check from the seller and the other one will get the home.

Some members are unhappy with this analysis, as it would appear that a seller is stuck in legal limbo when a buyer proposes to amend an existing, binding purchase agreement as a result of an inspection. There is absolutely no reason for a seller ever to be stuck in this situation. The situation could be addressed in advance, within the terms of the purchase agreement. For example, in the inspection provisions of the purchase agreement, it could be provided that in the event a purchaser seeks to amend the contract through an addendum after an inspection, the seller may either accept the proposed addendum or terminate the transaction. Alternatively, a provision could be included to indicate that the buyer's failure to waive the inspection contingency in writing on or before a particular day shall result in the automatic termination of the purchase agreement.

For REALTORS® who want a more detailed analysis of this situation, they may visit MAR's Web site and obtain a copy of an article on the subject which was prepared for the 2006 annual convention. 

