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BROKER RESPONSIBILITY FOR THE ACTIONS OF SALESPERSONS

I. INTRODUCTION

It has come to our attention that there are brokers around the State who believe that because salespersons are independent contractors, brokers are not responsible for their actions. In recent months, for example, we have been contacted by a broker asking us to talk about a potential problem with his salesperson directly, so that the broker can "stay out of the middle." Other brokers have explained that they purposefully avoid getting involved in their salespersons' activities so that there can be no claim that the salespersons were not in fact "independent." Many brokers apparently believe that "supervision" is simply a licensing requirement and do not understand that supervision is also important as a risk reduction technique. As will be discussed below, the simple fact is that notwithstanding the independent contractor status of salespersons, as a general rule, brokers are wholly responsible for the real estate activities of their salespersons. This is true whether the salespersons' actions were authorized, unknown or even forbidden.

II. DISCUSSION

In *Robertson v Carmel Builders Real* Estate, 92 P3d 653 (NM 2004), a suit was brought against an associate broker and his firm, Carmel Builders Real Estate ("CBRE") by potential purchasers in a failed transaction. The purchasers alleged that Dixie Babcock, an associate broker with CBRE ("Babcock") had made various fraudulent misrepresentations to them. Specifically, the purchasers alleged that Babcock had told them that CBRE had a valid listing when in fact it had expired. The purchasers also alleged that Babcock told them that they had a binding purchase contract with the sellers when they did not. Moreover, the

purchasers complained that Babcock had told them that utilities were at the property line, even though this was not true. The purchasers alleged further that had they known the truth, they would not have hired an appraiser, contracted for backhoe work or had blueprints done for a project that would never happen.

CBRE argued that even if it was true that Babcock had made these misrepresentations, it was not responsible for the acts of its associate broker because:

1. Babcock was an independent contractor, not an employee;

2. the broker would not have received a part of the commission had the sale gone through because Babcock only paid a monthly fee; and

3. by proceeding forward without a signed listing agreement, Babcock had violated the broker's stated policies and procedures.

The Court first noted that under New Mexico licensing law (as in Michigan), an associate broker must conduct all of his real estate business in the tradename of the broker, and may not receive any commission or fee for any real estate activities from anyone other than his or her broker.

The Court then held that when a buyer or seller employs a salesperson or associate broker, the fiduciary duty owed to that buyer or seller extends "up the chain of command" to the broker. The broker is liable for the acts of the associate broker (or salesperson) if the associate broker was acting, or appeared to be acting, within the scope of his or her authority. The Court noted that it did not matter that the associate broker was an independent contractor rather than an employee:

> . . . under a *respondeat superior*[1] theory, the liability of a principal for the tortious act of an agent is the same as liability of an employer for the tortious act of an employee.

In *Aiello v Ed Saxe Real Estate, Inc.,* 499 A2d 282 (Pa 1985), buyers in Pennsylvania brought suit against a real estate salesperson who had acted as a buyer's agent. The salesperson's brokerage firm was also named as a defendant. The buyers claimed that the salesperson had made fraudulent misrepresentations about the condition of the soil and whether the property was suitable for a sewage disposal system. The lower court had held that the broker could not be held liable unless it had known about his salesperson's misrepresentations. The Pennsylvania Supreme Court reversed the lower court's decision. Citing dozens of cases from around the country, the Court recognized:

> . . . the longstanding and widely held rule of law that a principal is liable to innocent third parties for their frauds, deceits, concealments, misrepresentations, torts, negligences and other malfeasance or misfeasance of his agent committed in the course of his employment, although the principal did not authorize, justify or participate in, or indeed know of, such misconduct, or even if he forbade the acts or disproved of them.

The Court went on to opine that there are two basic justifications for this rule of law. First, although the broker and the buyer may both be innocent parties, since one of the two innocent parties must suffer, it should be the broker who placed the agent in this position, rather than the "innocent stranger" (*i.e.*, the buyers). Second, since the broker is receiving a

[1] "Respondeat superior" is a Latin term meaning "let the master answer." The maxim means that a master is liable in certain cases for the wrongful acts of his servant, and a principal for his agent.

benefit from the transaction, it should not be permitted to deny responsibility for the transaction.

In *Johnson Realty, Inc. v Hand*, 377 SE 2d 176 (Ga App 1989), a real estate salesperson did not disclose to a seller client that the purchaser was in fact his father-in-law who was acting as a straw buyer for the salesperson himself. When the seller subsequently learned that the property had been immediately resold at a significant profit, the seller sued not only the agent, but also the agent's brokerage company and the sole shareholder of that brokerage (who was in fact the father of the agent).

The defendant broker argued that it should not be liable for the actions of the salesperson because the broker had not authorized or ratified this type of behavior. The court rejected this argument, noting:

> The prior acts of [the agent] whereby he has solicited [the seller's] property for sale and then actually sold it were acts which [the brokerage firm] had generally authorized him, in his capacity as its real estate agent, to undertake to perform. Accordingly, [the brokerage firm] would be legally bound by those acts without regard to the principle of ratification. 'The principal shall be bound for the care, diligence, and fidelity of his agent in his business, and hence he shall be bound for the neglect and fraud of his agent in the transaction of such business.' . . . If it be done in the course of his employment, the master is liable; and it makes no difference that the master did not authorize, or even know of the servant's act or neglect, or even if he disapproved or forbade it, he is equally liable, if the act be done in the course of his servant's employment.

A Hawaii appellate court was faced with a similar situation in *Silva v Bisbee*, 628 P2d 214 (Haw App 1981). In that case, Bernice Bisbee ("Bisbee") was a real estate broker employed by Midkiff Realty Inc. ("Midkiff"). Bisbee listed the Silvas' property and soon

after obtained an offer from Larsen to purchase the property on land contract. After Larsen advised Bisbee that he was not able to go through with the transaction, Bisbee put together a joint venture to purchase the property on the same terms and conditions. Bisbee did not inform the Silvas that she had an interest in the joint venture.

The joint venture put $35,000 down and made $2,000 quarterly payments through Bisbee. Whenever the joint venture couldn't come through with the necessary funds for a quarterly payment, Bisbee supplied those funds. Eventually, the Silvas sued to cancel the contract because the quarterly payments were always late. The Silvas also sued for fraud and the emotional distress caused by the continuously late quarterly payments. The Court held that because Bisbee was Midkiff's agent, Midkiff was "equally liable" with her for damages arising out of her breach of fiduciary duty as well as damages arising out of the claimed emotional distress, if any were found by the jury.

In *Ago v Begg*, 705 F Supp 613 (DC DC 1988), agent Betty Jacobsen ("Jacobsen") was employed by Noah-Cummings, Inc. ("Noah Inc."), which in turn had a license agreement with Mount Vernon Realty, Inc. ("MV Inc."), which allowed Noah Inc.'s agents to use MV Inc.'s tradename.

Jacobsen was the buyers' agent in a transaction in which the seller took back a second mortgage. When the buyers defaulted on their first mortgage, the first mortgagee foreclosed, thereby wiping out the sellers' second mortgage. The sellers sued everyone involved in the transaction for fraud, including Jacobsen, Noah Inc. and MV Inc. The trial court threw out the case against MV Inc. and the appellate court reversed that decision,

finding that Jacobsen had been the "apparent agent" of MV Inc. The Court concluded that the license situation here was different than, for example, an automobile dealership. Here:

> [t]he licensee "sells" her expertise, advice, and fiduciary capability. A customer reasonably depends on the name, goodwill, and reputation of the real estate firm whose tradename is used by the licensee . . . . It would strain credulity to consider that the purpose of the licensing agreement was other than to enable Mount Vernon Realty, one of the largest real estate firms in the Washington area, and Noah-Cummings, the employer of Ms. Jacobsen, to convince the public that the expertise, reputation, credibility, and *dependability* of Mount Vernon Realty were behind Noah-Cummings' employees, to the financial benefit of both firms. Indeed, the president of Mount Vernon Realty testified to this effect at trial. As plaintiffs have pointed out, Noah-Cummings' employees received business cards and stationery with the name of Mount Vernon Realty printed on them and Mount Vernon Realty's advertisements in the phone yellow pages listed Noah-Cummings as an affiliate.
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> . . . Ms. Jacobsen's apparent authority as an agent of Mount Vernon Realty, a large and well-known real estate firm, sensibly played a significant role in the decision of plaintiffs and their agents to enter into the transaction.

It is important to note that in each of these cases, the agent's allegedly wrongful acts involved the listing or selling of real estate – in other words, the agent was acting "within the scope of his or her agency authority." A broker is not liable for the actions of agents outside of the real estate business – for example, if the agent absconds with a girl scout troop's cookie funds. Often, of course, the question of whether the agent's activities were within the scope of his or her agency is a much closer question.

For example, in *Chamlee v Johnson-Rast and Hays*, 579 So 2d 580 (AL 1990), Diane Smith ("Smith") was a salesperson with Johnson-Rast and Hays ("Johnson-Rast"). The Chamlees had initially contacted Smith about a house she had listed in a

particular subdivision. Smith then showed the Chamlees several other houses, none of which suited their needs. Smith then persuaded the Chamlees to hire her husband's building company to build them a home in the same subdivision. Eventually, the Chamlees sued the Smiths and their building company for poor workmanship, breach of warranty, failure to pay subcontractors and breach of contract. The Chamlees also sued Johnson-Rast under the theory of *respondeat superior*.

The trial court threw out the case against the brokerage firm and the Alabama Supreme Court affirmed that decision. In reaching its decision, the Court noted that in order to recover under the doctrine of *respondeat superior*, the agent must be acting within the scope of his employment. Where, as here, the agent abandoned his principal's business for personal benefit, the employment has been suspended and the principal is not liable for the actions of the agent. The Court concluded that while generally, whether the agent is acting within the scope of his/her employment is a question for the jury, this is not the case where, as here, the departure was of a "marked and decided character." Accordingly, the trial judge's decision to throw out the case against Johnson-Rast prior to trial was upheld.

III. CONCLUSION

The only way for a business owner to avoid potential liability for the actions of others is to work alone. Obviously, that is not a realistic option for most of us. What you can do is hire wisely and provide significant training and supervision. Remember that when you allow someone to engage in business using your company name, you are allowing that person to trade on your experience and reputation. If a salesperson can't or won't follow company policies and procedures, then it is likely that you will need to let that person go.

Likewise, if a salesperson is secretive about the types of transactions he is working on, it is probably time to let him go. From time to time, a business owner needs to do a cost benefit analysis: do the benefits the salesperson provides to his company outweigh the potential risks created by the nature, quality and quantity of the work generated by that salesperson?