

# LICENSE LAW AND RULES COMMENTS

## Comments on Selected Provisions of the North Carolina Real Estate License Law and Real Estate Commission Rules

### INTRODUCTION

These comments on selected North Carolina Real Estate License Law and Real Estate Commission Rules provisions are intended to assist real estate licensees, prelicensing course students and others in understanding the License Law and Commission rules. The comments are organized in a topic format that often differs from the sequence in which the topics are addressed in the License Law and Commission rules. The topics selected for comment here are not only of particular importance in real estate brokerage practice but also are likely to be tested on the real estate license examination. The appropriate references to the License Law and Commission rules are provided beside each listed topic.

### REQUIREMENT FOR A LICENSE

#### General [G.S. 93A-1 and 93A-2]

Any person or business entity who directly or indirectly engages in the business of a real estate broker for compensation or the promise thereof while physically in the state of North Carolina must have a North Carolina real estate broker license. In North Carolina, a real estate licensee may only engage in brokerage as an “agent” for a party to a transaction. Thus, a real estate licensee is commonly and appropriately referred to as a real estate “agent” even though the latter term does not actually appear in the License Law. Note that a real estate “licensee” is NOT automatically a “REALTOR®.” A licensed real estate agent is a REALTOR® **only** if he/she belongs to the National Association of REALTORS®, a private trade association. Thus, the term REALTOR® should not be used to generally refer to all real estate licensees.

#### License Categories [G.S. 93A-2]

There is only one “type” of license, a **broker** license; however, there are several license status categories as described below:

**Provisional Broker** – This is the “entry level” license status category. A person who has met all the license qualification requirements (including a 75-hour prelicensing course and passing the Commission’s license examination) is initially issued a **broker license on “provisional” status** and is referred to as a “**provisional broker.**” A provisional broker generally may perform the same acts as a broker whose license is NOT on provisional status so long as he or she is supervised by a broker who is a designated **broker-in-charge**. A provisional broker may not operate independently in any way. G.S. 93A-2(a2) defines a “**provisional broker**” as “...a real estate broker who, pending acquisition and

*documentation to the Commission of the education or experience prescribed by G.S. 93A-4(a1), must be supervised by a broker-in-charge when performing any act for which a real estate license is required.”*

This license status category is comparable to a “salesperson” license in most other states except that it is a **temporary license status category**. Provisional brokers may not retain this status indefinitely – they must complete required **postlicensing education** (one 30-hour course each year for the three years following initial licensure – total of 90 hours) to remove the “provisional” status of their licenses and to remain eligible for “active” license status.

**Broker** – A “provisional broker” who satisfies all postlicensing education requirements to terminate the “provisional” status of such license becomes a “**broker**” without having to take another license examination. A broker is NOT required to be supervised by a broker-in-charge in order to hold an “active” license. An applicant who is a licensed broker in another US jurisdiction may be licensed directly as a North Carolina **broker NOT on provisional status** by passing the “State” section of the North Carolina license examination. All others must first be licensed in North Carolina as a **provisional broker** and then satisfy the postlicensing education requirement to become a non-provisional broker.

Most frequently, brokers elect to work for another broker or brokerage firm. Brokers may also elect to operate independently as a sole proprietor; however, with limited exceptions, such broker will have to qualify for and designate himself or herself as a **broker-in-charge** in order to operate independently and perform most brokerage activities (discussed further below under “broker-in-charge” and also in a subsequent section on brokers-in-charge that appears near the end of this appendix).

**Broker-In-Charge** – G.S. 93A-2(a1) defines a “**broker-in-charge**” as “...a real estate broker who has been designated as the broker having responsibility for the supervision of real estate provisional brokers engaged in real estate brokerage at a particular real estate office and for other administrative and supervisory duties as the Commission shall prescribe by rule.” Commission Rule A.0110 requires that each real estate office must have a broker who meets the qualification requirements to serve as “broker-in-charge” of the office and who has designated himself or herself as the broker-in-charge of that office. As is the case with “provisional broker,” “*broker-in-charge*” is not a separate license, but only a **separate license status category**. A broker who is to serve as the broker-in-charge (BIC) of an office (including working independently) must be designated as a BIC with the Commission.

To qualify for designation as a broker-in-charge, a broker's license must be on "active" status but NOT on "provisional" status, the broker must have **two years full-time or four years part-time brokerage experience within the previous five years** (or education/experience the Commission finds equivalent to such experience), and the broker must complete a 12-hour **Broker-In-Charge Course** no earlier than one year prior or 120 days after designation. Broker-in-charge requirements are addressed in detail in a separate subsequent section titled "Broker-In-Charge."

**Limited Nonresident Commercial Broker** – A broker or salesperson residing in a state other than North Carolina who holds an active broker or salesperson license in the state where his or her primary place of real estate business is located may apply for and obtain a North Carolina "**limited nonresident commercial broker license**" that entitles such licensee to engage in transactions for compensation involving "commercial real estate" in North Carolina. While the non-resident limited broker will remain affiliated with his/her out of state real estate company and will not have a North Carolina broker-in-charge, the non-resident licensee must enter into a "notification of broker affiliation" and a "brokerage cooperation agreement" with a resident North Carolina broker not on provisional status and the licensee must be supervised by the North Carolina broker while performing commercial real estate brokerage in North Carolina. Like a "firm" license, a limited nonresident commercial broker license is a separate license.

#### **Licensing of Business Entities** [G.S. 93A-1 and 2; Rule A.0502]

In addition to individuals (persons), "business entities" also must be licensed in order to engage in real estate brokerage. Any corporation, partnership, limited liability company, association or other business entity (other than a sole proprietorship) must obtain a separate real estate **firm** broker license.

#### **Activities Requiring a License** [G.S. 93A-2]

*Persons and business entities who for consideration or the promise thereof perform the activities listed below as an agent for others are considered to be performing brokerage activities and must have a real estate license unless specifically exempted by the statute* (see subsequent section on "Exemptions"). There is no exemption for engaging in a limited number of transactions. A person or entity who performs a brokerage service in even one transaction must be licensed. Similarly, no fee or other consideration is so small as to exempt one from the application of the licensing statute when acting for another in a real estate transaction. *Brokerage activities include:*

1. **Listing (or offering to list) real estate for sale or rent**, including any act performed by a real estate licensee in connection with obtaining and servicing a listing agreement. Examples of such acts include, but are not limited to, soliciting listings, providing information to the property owner, and preparing listing agreements or property management agreements.

2. **Selling or buying (or offering to sell or buy) real estate**, including any act performed by a real estate licensee in connection with assisting others in selling or buying real estate. Examples of such acts include, but are not limited to, advertising listed property for sale, "showing" listed property to prospective buyers, providing information about listed property to prospective buyers (other than basic property facts that might commonly appear in an advertisement in a newspaper, real estate publication or internet website), negotiating a sale or purchase of real estate, and assisting with the completion of contract offers and counteroffers using preprinted forms and communication of offers and acceptances.
3. **Leasing or renting (or offering to lease or rent) real estate**, including any act performed by real estate licensees in connection with assisting others in leasing or renting real estate. Examples of such acts include, but are not limited to, advertising listed property for rent, "showing" listed rental property to prospective tenants, providing information about listed rental property to prospective tenants (other than basic property facts that might commonly appear in an advertisement in a newspaper, real estate publication or internet website), negotiating lease terms, and assisting with the completion of lease offers and counteroffers using preprinted forms and communication of offers and acceptances.
4. **Conducting (or offering to conduct) a real estate auction**. (Mere criers of sale are excluded.) NOTE: An auctioneer's license is also required to auction real estate.
5. **Selling, buying, leasing, assigning or exchanging any interest in real estate, including a leasehold interest, in connection with the sale or purchase of a business**.
6. **Referring a party to a real estate licensee, if done for compensation**. Any arrangement or agreement between a licensee and an unlicensed person that calls for the licensee to compensate the unlicensed person in any way for finding, introducing or referring a party to the licensee has been determined by North Carolina's courts to be prohibited under the License Law. Therefore, *no licensee may pay a finder's fee, referral fee, "bird dog" fee or similar compensation to an unlicensed person*.

#### **Unlicensed Employees — Permitted Activities**

The use of unlicensed assistants and other unlicensed office personnel in the real estate industry is very widespread and the Commission is frequently asked by licensees what acts unlicensed persons may lawfully perform. As guidance to licensees, the Commission has prepared the following list of acts that an unlicensed assistant or employee may lawfully perform so long as the assistant or employee is salaried or hourly paid and is not paid on a per-transaction basis.

An unlicensed, salaried employee MAY:

1. Receive and forward phone calls and electronic messages to licensees.
2. Submit listings and changes to a multiple listing service, but only if the listing data or changes are compiled and provided by a licensee.
3. Secure copies of public records from public repositories (i.e., register of deeds office, county tax office, etc.).
4. Place “for sale” or “for rent” signs and lock boxes on property at the direction of a licensee.
5. Order and supervise routine and minor repairs to listed property at the direction of a licensee.
6. Act as a courier to deliver or pick up documents.
7. Provide to prospects basic factual information on listed property that might commonly appear in advertisements in a newspaper, real estate publication or internet website.
8. Schedule appointments for showing property listed for sale or rent.
9. Communicate with licensees, property owners, prospects, inspectors, etc. to coordinate or confirm appointments.
10. Show rental properties managed by the employee’s employing broker to prospective tenants and complete and execute preprinted form leases for the rental of such properties.
11. Type offers, contracts and leases from drafts of preprinted forms completed by a licensee.
12. Record and deposit earnest money deposits, tenant security deposits and other trust monies, and otherwise maintain records of trust account receipts and disbursements, under the close supervision of the office broker-in-charge, who is legally responsible for handling trust funds and maintaining trust accounts.
13. Assist a licensee in assembling documents for closing.
14. Compute commission checks for licensees affiliated with a broker or firm and act as bookkeeper for the firm’s bank operating accounts.

#### **Exemptions [G.S. 93A-2(c)]**

The following persons and organizations are specifically exempted from the requirement for real estate licensure:

1. A **business entity** selling or leasing real estate owned by the business entity when the acts performed are in the regular course of or are incident to the management of that real estate and the investment therein. This exemption extends to officers and employees of an exempt corporation, the general partners of an exempt partnership, and the managers of an exempt limited liability company when engaging in acts or services for which the corporation, partnership or limited liability company would be exempt.
2. A person acting as an **attorney-in-fact** under a power of attorney from the owner authorizing the final con-

summation of performance of any contract for the sale, lease or exchange of real estate. (Note: This limited exemption applies only to the final completion of a transaction already commenced. The licensing requirement may not be circumvented by obtaining a power of attorney.)

3. An **attorney-at-law** who is an active member of the North Carolina State Bar only when performing an act or service that constitutes the practice of law under Chapter 84 of the General Statutes. Thus, the attorney exemption is strictly limited and attorneys generally may NOT engage in real estate brokerage practice without a real estate license.
4. A person acting as a receiver, trustee in bankruptcy, guardian, administrator or executor or any person acting under a court order.
5. A **trustee** acting under a written trust agreement, deed of trust or will or the trustee’s regular salaried employees.
6. **Certain salaried employees of broker-property managers.** (See G.S. 93A-2(c)(6) for details.)
7. An individual owner selling or leasing the owner’s own property.
8. A **housing authority** organized under Chapter 157 of the General Statutes and any regular salaried employee with regard to the sale or lease of property owned by the housing authority or to the subletting of property which the housing authority holds as tenant.

## **THE REAL ESTATE COMMISSION**

### **Composition [G.S. 93A-3(a)]**

The Real Estate Commission consists of nine (9) members who serve three-year terms. Seven members are appointed by the Governor and two are appointed by the General Assembly upon the recommendations of the Speaker of the House of Representatives and the President Pro Tempore of the Senate. At least three (3) members must be licensed brokers. At least two (2) members must be “public members” who are NOT involved directly or indirectly in the real estate brokerage or appraisal businesses.

**Purpose and Powers [G.S. 93A-3(a), (c) and (f); G.S. 93A-6(a) and (b); G.S. 93A-4(d) and 93A-4.1 & 4.2]**

The principal purpose of the Real Estate Commission is to protect the interests of members of the general public in their dealings with real estate brokers. This is accomplished through the exercise of the following statutory powers granted to the Commission:

1. Licensing real estate brokers and brokerage firms, and registering time share projects.
2. Establishing and administering preclicensing education programs for prospective licensees and postlicensing and continuing education programs for licensees.
3. Providing education and information relating to the

real estate brokerage business for licensees and the general public.

4. Regulating the business activities of brokers and brokerage firms, including disciplining licensees who violate the License Law or Commission rules.

It should be noted that the Commission is specifically prohibited, however, from regulating commissions, salaries or fees charged by real estate licensees and from arbitrating disputes between parties regarding matters of contract such as the rate and/or division of commissions or similar matters. [See G.S. 93A-3(c) and Rule A.0109.]

#### **Disciplinary Authority [G.S. 93A-6(a)-(c)]**

The Real Estate Commission is authorized to take a variety of disciplinary actions against licensees who the Commission finds guilty of violating the License Law or Commission rules while acting as real estate licensees. These are: **reprimand, censure, license suspension and license revocation**. The License Law also permits a licensee under certain circumstances to surrender his/her license with the consent of the Commission. Disciplinary actions taken against licensees are regularly reported in the Commission's periodic newsletter which is distributed to all licensees and also may be reported in local and regional newspapers.

It should be noted that licensees may be subject to the same disciplinary action for committing acts prohibited by the License Law when selling, leasing, or buying real estate for themselves, as well as for committing such acts in transactions handled as agents for others. [G.S. 93A-6(b)(3)]

The Commission also has the power to seek in its own name **injunctive relief** in superior court to prevent any person (licensees and others) from violating the License Law or Commission rules. A typical example of when the Commission might pursue injunctive relief in the courts is where a person engages in real estate activity without a license or during a period when the person's license is suspended, revoked or expired. [G.S. 93A-6(c)]

*Any violation of the License Law or Commission rules is a criminal offense (misdemeanor) and may be prosecuted in a court of law.* However, a finding by the Commission that a licensee has violated the License Law or Commission rules does not constitute a criminal conviction. [G.S. 93A-8]

## **PROHIBITED ACTS BY LICENSEES**

G.S. 93A-6 provides a list of prohibited acts which may result in disciplinary action against licensees. Discussed below are various prohibited acts, except for those related to handling and accounting for trust funds, broker's responsibility for closing statements, and the failure to deliver certain instruments to parties in a transaction, which are discussed in the subsequent sections on "General Brokerage Provisions" and "Handling Trust Funds."

### **Important Note**

The provisions of the License Law relating to misrepresentation or omission of a material fact, conflict of interest, licensee competence, handling of trust funds, and im-

proper, fraudulent or dishonest dealing generally apply independently of other statutory law or case law such as the law of agency. Nevertheless, other laws may affect the application of a License Law provision. For example, the N.C. Tenant Security Deposit Act requires an accounting to a tenant for a residential security deposit within 30-60 days after termination of a tenancy. License Law provisions (and Commission rules) require licensees to account for such funds within a reasonable time. Thus, in this instance, a violation of the Tenant Security Deposit Act's provisions would also be considered a violation of the License Law.

Similarly, the law of agency and the law of contracts as derived from the common law may impact the application of License Law. Thus, a licensee's agency status and role in a transaction might affect the licensee's duties under the license law. Examples of how an agent's duties under the License Law may be affected by the application of other laws are included at various points in this section on "Prohibited Acts by Licensees."

#### **Misrepresentation or Omission [G.S. 93A-6(a)(1)]**

Misrepresentation or omission of a material fact by a licensee is prohibited, and this prohibition includes both "willful" and "negligent" acts. A "willful" act is one that is done intentionally and deliberately, while a "negligent" act is one that is done unintentionally. A "**misrepresentation**" is communicating false information, while an "**omission**" is failing to provide or disclose information where there is a duty to provide or disclose such information.

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### **Material Facts**

For purposes of applying G.S. 93A-6(a)(1), whether a fact is "material" depends on the facts and circumstances of a particular transaction and the application of statutory and/or case law. The Commission has historically interpreted "**material facts**" under the Real Estate License Law to include at least:

**Facts about the property itself** (such as a structural defect or defective mechanical systems);

**Facts relating directly to the property** (such as a pending zoning change or planned highway construction in the immediate vicinity); and

**Facts relating directly to the ability of the agent's principal to complete the transaction** (such as a pending foreclosure sale).

*Regardless of which party in a transaction a real estate agent represents, the facts described above must be disclosed to both the agent's principal and to third parties the agent deals with on the principal's behalf. In addition, an agent has a duty to disclose to his or her principal any information that may affect the principal's rights and interests or influence the principal's decision in the transaction.*

**Death or Serious Illness of Previous Property Occupant** — Note, however, that G.S. 39-50 and 42-14.2 specifically provide that the fact that a property was occupied by a person who died or had a serious illness while oc-

cupying the property is NOT a material fact. Thus, agents do not need to voluntarily disclose such a fact. If a prospective buyer or tenant specifically asks about such a matter, the agent may either decline to answer or respond honestly. If, however, a prospective buyer or tenant inquires as to whether a previous owner or occupant had AIDS, the agent is prohibited by fair housing laws from answering such an inquiry because persons with AIDS are considered to be “handicapped” under such laws and disclosure of the information may have the effect of discriminating against the property owner based on the handicapping condition.

**Convicted Sex Offender Occupying, Having Occupied or Residing Near a Property** — Note also that the same North Carolina statutes (G.S. §39-50 and §42-14.2) that state the death or serious illness of a previous occupant of a property is not a material fact in a real estate transaction contain a similar provision relating to **convicted sex offenders**. The statutes provide that when offering a property for sale, rent or lease, “...it shall not be a material fact...that a person convicted of any crime for which registration is required by Article 27A of Chapter 14 of the General Statutes [statutes establishing registration programs for sex offenders and sexually violent predators] occupies, occupied or resides near the property; provided, however, that no seller [or landlord or lessor] may knowingly make a false statement regarding such fact.” Therefore, an agent involved in a transaction is **not** required to volunteer to a prospective buyer or tenant any information about registered sex offenders as described above. If a buyer or tenant specifically asks about sex offenders in a neighborhood, an agent need only answer truthfully to the best of his/her knowledge. In the absence of a specific inquiry about this matter from the buyer, an agent representing the buyer who knows, for example, that a registered sex offender lives in the immediate area, will probably want to disclose the information in the interest of serving his/her buyer-client even though not required by law to do so. On the other hand, in the absence of a specific inquiry by the buyer, if the agent who knows such information represents the seller, the agent will probably want to check with his/her seller-client before disclosing that information since voluntary disclosure is likely not in the seller’s best interest. Any agent also has the option of advising a prospective buyer or tenant about how to check the statewide sex offender registry online at [www.sexoffender.ncdoj.gov/search.aspx](http://www.sexoffender.ncdoj.gov/search.aspx).

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This introductory information should assist in understanding G.S. 93A-6(a)(1), which establishes four separate (although closely related) categories of conduct which are prohibited. These are discussed below, and a few examples of prohibited conduct are provided for each category.

**Willful Misrepresentation** — *This occurs when a licensee who has “actual knowledge” of a material fact deliberately misinforms a buyer, seller, tenant or landlord concerning such fact.* A misrepresentation is also considered to be “willful” when a li-

icensee who does NOT have actual knowledge of a matter material to the transaction provides incorrect information concerning such matter to a buyer, seller, tenant or landlord *without regard for the actual truth of the matter* (i.e., when a licensee intentionally provides information without knowing whether it is true and the information provided is in fact not true).

**Note:** The following examples of willful misrepresentation apply regardless of the licensee’s status (seller’s agent or buyer’s agent) or role (listing agent or selling agent).

**Example:** An agent knows that a listed house has a severe problem with water intrusion in the crawl space during heavy rains. In response to a question from a prospective buyer who is being shown the house during dry weather, the agent states that there is no water drainage problem.

**Example:** An agent knows that the heat pump at a listed house does not function properly, but tells a prospective buyer that all mechanical systems and appliances are in good condition.

**Example:** An agent knows that the approximate market value of a house is \$225,000, but tells the property owner that the house is worth \$250,000 in order to obtain a listing.

**Example:** An agent is completely unfamiliar with the features or condition of a listed property; however, the agent informs a prospective buyer that the plumbing is in good working order without first checking with the owner. (The agent in such instance is acting without regard for the truth of the matter being represented. If the plumbing in fact needs significant repair, then the agent may be guilty of willful misrepresentation.)

**Example:** Without checking with the owner, an agent tells a prospective buyer of a listed house that heating and cooling costs are “very reasonable.” (Because the agent acted without regard for the truth of the matter, he may be guilty of willful misrepresentation if heating and cooling costs are in fact extraordinarily high.)

**Negligent Misrepresentation** — *This occurs when a licensee unintentionally misinforms a buyer, seller, tenant or landlord concerning a material fact either because the licensee does not have actual knowledge of the fact, because the licensee has incorrect information, or because of a mistake by the licensee.* If a reasonably prudent licensee “*should reasonably have known*” the truth of the matter that was misrepresented, then the licensee may be guilty of “negligent misrepresentation” even though the licensee was acting in good faith.

Negligent misrepresentation by real estate licensees occurs frequently in real estate transactions. A very common situation is the recording of incorrect information about a property in an MLS listing due to the negligence of the listing agent. When a prospective buyer is subsequently provided the incorrect information from the MLS by the agent working with the buyer, a negligent misrepresentation by the listing agent occurs.

*A listing agent is generally held to a higher standard with regard to negligent misrepresentation of material facts about a listed property to a buyer than is a selling agent who is acting as a seller's subagent. This is because (1) The listing agent is in the best position to ascertain facts about the property, (2) the listing agent is expected to take reasonable steps to assure that property data included with the listing is correct and (3) it is generally considered reasonable for a selling agent to rely on the accuracy of the listing data except in those situations where it should be obvious to a reasonably prudent agent that the listing information is incorrect. However, a buyer's agent may in some cases be held to a higher standard than a seller's subagent because of the buyer's agent's duties to the buyer under the law of agency and the buyer's agent's special knowledge of the buyer's particular situation and needs.*

**Example:** An agent has previously sold several lots in a subdivision under development and all those lots passed a soil suitability test for an on-site septic system. The agent then sells Lot 35 without checking as to whether this lot satisfies the soil test; however, the agent informs the buyer that Lot 35 will support an on-site septic system when in fact the contrary is true. (While the agent's conduct may not rise to the level of willful disregard for the truth of the matter, the agent was at least negligent in not checking the soil test result on Lot 35 and is therefore guilty of negligent misrepresentation. This result is not affected by the agent's agency status or role in the transaction.)

**Example:** An owner tells a listing agent with ABC Realty that his house has 1850 heated square feet. Without verifying the square footage, the agent records 1850 square feet on the listing form and in the listing information published in the local MLS. The house is subsequently sold by a sales agent with XYZ Realty who tells the buyer that according to the MLS data, the house has 1850 square feet. The buyer later discovers that the house actually has only 1750 square feet. (In this situation, the listing agent did not make a direct misrepresentation to the buyer; however, he/she initiated the chain of communication which led to the buyer being misinformed, and thus indirectly misrepresented a material fact. Further, the listing agent's failure to verify the square footage constituted negligence. Therefore, the listing agent is guilty of a negligent misrepresentation. Although the selling agent directly communicated the incorrect information to the buyer, he/she probably acted reasonably in relying on the data in MLS. In this case, if the selling agent had no reason to doubt the MLS data, the selling agent is not guilty of a negligent misrepresentation. Note, however, that if the square footage discrepancy had been sufficiently large that a reasonably prudent selling agent should have known the listed data was incorrect, then the

selling agent would also have been guilty of negligent misrepresentation. The result in this particular example is not affected by the selling agent's agency status (seller's subagent or buyer's agent), although this might be a factor in other situations.

**Willful Omission** — *This occurs when a licensee has "actual knowledge" of a material fact and a duty to disclose such fact to a buyer, seller, tenant, or landlord, but deliberately fails to disclose such fact.*

**Example:** An agent knows that a zoning change is pending that would adversely affect the value of a listed property, but fails to disclose such information to a prospective buyer. The agent has committed a willful omission regardless of the agent's agency status or role in the transaction.

[**Note:** Information about a zoning change, planned major highway or similar matter that would significantly enhance the value of a seller's property must also be disclosed to the seller, even if the licensee is a buyer's agent.]

**Example:** An agent knows that the city has just decided to extend water and sewer lines to a subdivision that has been plagued for years by serious water quality and sewage disposal problems. This will result in a substantial increase in the value of homes in the subdivision. The agent, who is working with a buyer to purchase a house in the subdivision, does not inform the seller of the city's recent decision. The agent has committed a willful omission and this result is not affected by the agent's agency status or role in the transaction.

**Example:** An agent knows that a listed house has a major defect (e.g., crumbling foundation, no insulation, malfunctioning septic tank, leaking roof, termite infestation, or some other problem) but fails to disclose such information to a prospective buyer. The agent has committed a willful omission and this result is not affected by the agent's agency status or role in the transaction.

**Example:** A selling agent working with a buyer as a subagent of the seller learns that the buyer is willing to pay more than the price in the buyer's offer, but fails to disclose this information to the seller (or listing agent) when presenting the offer. The selling agent has committed a willful omission. If, however, the selling agent were acting as a buyer's agent, then the result would be different because the agent does not represent the seller and has a duty not to disclose to the seller confidential buyer information that would be harmful to the buyer's interest.

**Example:** A buyer's agent becomes aware that the seller with whom his buyer is negotiating is under pressure to sell quickly and may accept much less than the listing price. Believing such information should always be kept confidential, the buyer's agent does not provide

the buyer with this information. The buyer's agent is guilty of a willful omission. An agent must disclose to his/her principal any information that might affect the principal's decision in the transaction.

**Example:** Suppose in the immediately preceding example that the seller's property is listed with the firm of the buyer's agent and the firm's policy is to practice traditional dual agency in in-house sales situations where it represents both the seller and the buyer. In this situation, the buyer's agent would not be considered to have committed a willful omission under the License Law by not disclosing the information about the seller's personal situation to the buyer. NOTE: This assumes, however, that the buyer's agent properly disclosed his/her status as a buyer's agent to the seller or seller's agent upon "initial contact," that dual agency was properly authorized by both the seller and buyer prior to showing the seller's property to the buyer, the authorization was timely reduced to writing in the agency agreements that also limit the disclosure of information in dual agency situations (as is the case with the agency agreement forms provided by the North Carolina Association of REALTORS® for use by its members).

**Negligent Omission** — *This occurs when a licensee does NOT have actual knowledge of a material fact and consequently does not disclose the fact, but a reasonably prudent licensee "should reasonably have known" of such fact.* In this case, the licensee may be guilty of "negligent omission" if he/she fails to disclose this fact to a buyer, seller, tenant or landlord, even though the licensee acted in good faith in the transaction.

The prohibition against negligent omission creates a "duty to discover and disclose" material facts which a reasonably prudent licensee would typically have discovered in the course of the transaction. *A listing agent is typically in a much better position than a selling agent to discover material facts relating to a listed property and thus, will be held to a higher standard than will a selling agent acting as a seller's subagent. On the other hand, a buyer's agent in some circumstances may be held to a higher standard than a seller's subagent because of the buyer's agent's duties to the buyer under the law of agency, particularly if the buyer's agent is aware of a buyer's special needs with regard to a property.* Again we see how the agency relationships between agents and principals to a transaction and the licensee's role in the transaction can affect a licensee's duties and responsibilities under the License Law.

Instances of negligent omission occur much less frequently than instances of negligent misrepresentation. This is because most facts about a listed property are recorded on a detailed property data sheet from which information is taken for inclusion in MLS listings. If incorrect information taken from an MLS listing is passed on to a prospective purchaser, then a "misrepresentation," rather than an "omission," has occurred. Nevertheless, there are examples of negligent omission which can be cited.

**Example:** A listing agent lists for sale a house located adjacent to a street that is about to be widened into a major thoroughfare. The thoroughfare project has been very controversial and highly publicized. The city recently finalized its decision to proceed with the project and the plans for the street widening are recorded in the city planner's office. A buyer, working with a selling agent, makes an offer to buy the house. The listing agent does not disclose the street widening plans to the buyer or selling agent and claims later that he/she was not aware of the plans. In this situation, both the listing and selling agents are probably guilty of negligent omission because each "should reasonably have known" of the street widening plans, clearly a material fact, and should have disclosed this fact to the buyer. This result is not affected by whether the selling agent is a buyer agent or seller's subagent.

**Example:** A seller has a 30,000 square foot commercial property for sale which cannot be expanded under local zoning laws. The buyer is looking for property in the 25,000 - 30,000 square foot range, but has told his buyer's agent that he needs a property where he can expand to 50,000 square feet or more in the future. The seller does not think to advise the buyer's agent that the property cannot be expanded, and the buyer's agent makes no inquiry about it although he is aware of the buyer's special needs. If the buyer purchases the property without knowing about the restriction on expansion, the buyer's agent is guilty of a negligent omission for failing to discover and disclose a special circumstance that the agent knew was especially important to his/her client.

**Example:** When listing a house, a listing agent is told by the seller that one area of the roof leaks badly when it rains, but the moisture so far is being contained in the attic. The listing agent forgets to note this on the MLS data sheet and forgets to disclose the leaking roof problem to prospective buyers and selling agents. The listing agent is guilty of a negligent omission. Because the agent's failure to disclose the leaking roof problem was unintentional, the listing agent is not guilty of a willful omission; however, his/her forgetfulness resulting in his/her failure to disclose the defect constitutes a negligent omission.

#### **Making False Promises [G.S. 93A-6(a)(2)]**

Real estate brokers are prohibited from "making any false promises of a character likely to influence, persuade or induce." The promise may relate to any matter which might influence, persuade or induce a person to perform some act he/she might not otherwise perform.

**Example:** An agent promises a prospective apartment tenant that the apartment will be repainted before the tenant moves in. The agent then fails to have the work done after the lease is signed.

**Example:** An agent promises a property owner that

if he/she lists his/her house for sale with the agent's firm, then the firm will steam-clean all the carpets and wash all the windows. The firm then fails to have the work done after the listing contract is signed.

#### **Other Misrepresentations** [G.S. 93A-6(a)(3)]

Real estate brokers are prohibited from pursuing a course of misrepresentation (or making of false promises) through other agents or salespersons or through advertising or other means.

**Example:** In marketing subdivision lots for a developer, a broker regularly advertises that the lots for sale are suitable for residential use when in fact the lots will not pass a soil suitability test for on-site sewage systems.

**Example:** A broker is marketing a new condominium complex which is under construction. Acting with the full knowledge and consent of the broker, the broker's agents regularly inform prospective buyers that units will be available for occupancy on June 1, when in fact the units won't be available until at least September 1.

#### **Conflict of Interest** [G.S. 93A-6(a)(4) and (6); Rule A.0104(d)] and (i)

**Undisclosed Dual Agency.** G.S. 93A-6(a)(4) prohibits a real estate agent from "*acting for more than one party in a transaction without the knowledge of all parties for whom he or she acts.*" Commission Rule A.0104(d) and (i) takes this a step further by providing that a broker or brokerage firm representing one party in a transaction shall not undertake to represent another party in the transaction without the express written authority (i.e., authorization of dual agency) of each party (subject to one exception, explained as part of the dual agency discussion in the "General Brokerage Provisions" section). A typical violation of this provision occurs when the agent has only one principal in a transaction but acts in a manner which benefits another party without the principal's knowledge. In such a situation, the agent violates the duty of loyalty and consent owed to his principal.

**Example:** A house is listed with Firm X. When showing the house to a prospective buyer not represented by Firm X, an agent of Firm X advises the buyer to offer substantially less than the listing price because the seller must move soon and is very anxious to sell the property fast. The agent and Firm X are contractually obligated to represent only the seller. By advising the prospective buyer as indicated in this example, the agent is acting to benefit the buyer without the seller's knowledge and consent. This act violates both the License Law and the Law of Agency.

**Example:** An agent with Firm Y assists her sister in purchasing a house listed with Firm X without advising Firm X or the seller of her relationship with the buyer. The agent is "officially" acting as a subagent of the seller in the transaction. In this situation, there is an inherent conflict of interest on the part of the agent. If the agent does not disclose her relationships to

both parties, then the agent violates both the License Law and Law of Agency. In fact, since her allegiance lies with her sister, the agent should instead act as a buyer's agent from the outset. The same would be true if the buyer were a close friend or business associate of the agent, or in any way enjoyed a special relationship to the agent which would clearly influence the agent to act in behalf of the buyer rather than the seller.

**Self-dealing.** G.S. 93A-6(a)(4) also prohibits any "**self-dealing**" on the part of an agent. For example, if an agent attempts to make a secret profit in a transaction where he is supposed to be representing a principal, then the agent violates this "conflict of interest" provision.

**Example:** An agent lists a parcel of undeveloped property which is zoned for single-family residential use. The agent knows that this property is about to be rezoned for multi-family residential use, which will greatly increase the property's value. Rather than informing the seller of this fact, the agent offers to buy the property at the listed price, telling the seller that he wants to acquire the property as a long-term investment. The deal closes. Several months later, after the rezoning has been accomplished, the agent sells the property at a substantial profit.

**Representing Another Broker without Consent.** G.S. 93A-6(a)(6) prohibits a licensee from "representing or attempting to represent a real estate broker other than the broker by whom he or she is engaged or associated, without the express knowledge and consent of the broker with whom he or she is associated." While brokers may work for or be associated with more than one real estate company at the same time, *so long as* they have the express consent of all brokers-in-charge, provisional brokers may never engage in brokerage activities for more than one company at a time.

#### **Improper Brokerage Commission** [G.S. 93A-6(a)(5) and (9)]

A broker may NOT pay a commission or valuable consideration to any person for acts or services performed in violation of the License Law. [G.S. 93A-6(a)(9)] *This provision flatly prohibits a broker from paying an unlicensed person for acts which require a real estate license.* Following are examples of prohibited payments:

**Example:** The payment by brokers of commissions to previously licensed sales associates who failed to properly renew their licenses for any acts performed after their licenses had expired. [Note that payment could properly be made for commissions earned while the license was on active status, even if the license is inactive or expired at time of payment. The determining factor is whether the license was on active status at the time all services were rendered which generated the commission?]

**Example:** The payment of a commission, salary or fee by brokers to unlicensed employees or independent

contractors (e.g., secretaries, “trainees” who haven’t passed the license examination, etc.) for performing acts or services requiring a real estate license.

**Example:** The payment by licensees of a “finder’s fee,” “referral fee,” “bird dog fee,” or any other valuable consideration to unlicensed persons who find, introduce, or bring together parties to a real estate transaction. This is true even if the ultimate consummation of the transaction is accomplished by a licensee and even if the act is performed without expectation of compensation. Thus, a licensee may NOT compensate a friend, relative, former client or any other unlicensed person for “referring” a prospective buyer, seller, landlord or tenant to such licensee. This prohibition extends to “owner referral” programs at condominium or time share complexes and “tenant referral” programs at apartment complexes.

In addition, a *provisional* broker may NOT accept any compensation for brokerage services from anyone other than his employing broker or brokerage firm. Consequently, *a broker may not pay a commission or fee directly to a provisional broker of another broker or firm. Any such payment must be made through the provisional broker’s employing broker or firm.* [G.S. 93A-6(a)(5)]

**Note:** See also the discussion of Rule A.0109 on “Brokerage Fees and Compensation” under the subsequent section titled “General Brokerage Provisions.”

#### **Unworthiness and Incompetence** [G.S. 93A-6(a)(8)]

This broad provision authorizes the Real Estate Commission to discipline any licensee who, based on his or her conduct and consideration of the public interest, is found to be unworthy or incompetent to work in the real estate business. A wide range of conduct may serve as the basis for a finding of unworthiness or incompetence, including conduct which violates other specific provisions of the License Law or Commission rules. Here are a few examples of improper conduct which do not specifically violate another License Law provision but which might support a finding of unworthiness or incompetence.

1. Failure to properly complete (fill in) real estate contracts or to use contract forms which are legally adequate.
2. Failure to diligently perform the services required under listing contracts or property management contracts.
3. Failure to provide accurate closing statements to sellers and buyers or accurate income/expense reports to property owners.

#### **Improper Dealing** [G.S. 93A-6(a)(10)]

This broad provision prohibits a real estate licensee from engaging in “any other conduct [not specifically prohibited elsewhere in the License Law] which constitutes **improper, fraudulent or dishonest dealing.**” The determination as to whether particular conduct constitutes “improper, fraudulent or dishonest dealing” is made by the Real Estate Com-

mission on a case-by-case basis. Therefore, a broad range of conduct might be found objectionable under this provision, depending on the facts in a case.

One category of conduct which violates this provision is any breach of the duty to exercise skill, care, and diligence in behalf of a client under the Law of Agency. (Note that other breaches of Agency Law duties constituting either a “misrepresentation or omission,” a “conflict of interest” or a “failure to properly account for trust funds” are covered by other specific statutory provisions.)

Another category of conduct which violates this provision is any violation of the State Fair Housing Act. This is mentioned separately under the “Discriminatory Practices” heading.

**Example:** An agent assists a prospective buyer in perpetrating a fraud in connection with a mortgage loan application by preparing two contracts — one with false information for submission to the lending institution, and another which represents the actual agreement between seller and buyer. (This practice is commonly referred to as “dual contracting” or “contract kiting.”)

**Example:** A broker lists a property for sale and agrees in the listing contract to place the listing in the local MLS, to advertise the property for sale, and to use his best efforts in good faith to find a buyer. The broker places a “For Sale” sign on the property, but fails to place the property in the MLS for more than 30 days and fails to otherwise advertise the property during the listing period. (The broker has failed to exercise reasonable skill, care and diligence in behalf of his client as required by the listing contract and the Law of Agency.)

**Example:** An agent is aware that the owners of a house listed with his company are out of town for the weekend, yet the agent gives a prospective buyer the house keys and allows such prospect to look at the listed house without accompanying the prospect. (The agent has failed to exercise reasonable skill, care and diligence in behalf of his client.)

#### **Discriminatory Practices** [G.S. 93A-6(a)(10); Rule A.1601]

Any conduct by a licensee that violates the provisions of the State Fair Housing Act is considered by the Commission to constitute “improper conduct” and to be a violation of the License Law.

#### **Practice of Law** [G.S. 93A-4(e); G.S. 93A-6(a)(11); Rule A.0111]

Real estate licensees may not perform for others any legal service described in G.S. 84-2.1 or any other legal service. Following are several examples of real estate-related legal services which licensees may NOT provide.

1. Drafting legal documents such as deeds, deeds of trust, leases and real estate sales contracts for others. Although licensees may “fill in” or “complete” pre-

printed real estate contract forms which have been drafted by an attorney, they may NOT under any circumstances complete or fill in deed or deed of trust forms.

2. Abstracting or rendering an opinion on legal title to real property.
3. Providing “legal advice” of any nature to clients and customers, including advice concerning the nature of any interest in real estate or the means of holding title to real estate. (Note: Although providing advice concerning the legal ramifications of a real estate sales contract is prohibited, merely “explaining” the provisions of such a contract is not only acceptable, but highly recommended.)

#### **Violating any Commission Rule [G.S. 93A-6-(a)(15)]**

The law also has a “catch-all” provision that subjects a licensee to disciplinary action for violating any rule adopted by the Commission.

**Note:** The provisions of G.S. 93A-6(a)(12)-(14) are addressed elsewhere in these “Comments” under the “General Brokerage Provisions” section.

#### **Other Prohibited Acts [G.S. 93A-6(b)]**

In addition to those prohibited acts previously discussed, G.S. 93A-6(b) prescribes several other specific grounds for disciplinary action by the Commission, including:

1. Where a licensee has obtained a license by false or fraudulent representation (e.g., falsifying documentation of prelicensing education, failing to disclose prior criminal convictions, etc.).
2. Where a licensee has been convicted of, or pled guilty or no contest to, a number of listed misdemeanors or felonies plus any other offense that shows professional unfitness or involves moral turpitude that would reasonably affect the licensee’s performance in the real estate business.
3. Where a broker’s unlicensed employee, who is exempt from licensing under G.S. 93A-2(c)(6) (property management exception), has committed an act which, if committed by the broker, would have constituted a violation of G.S. 93A-6(a) for which the broker could be disciplined.
4. Where a licensee who is also licensed as an appraiser, attorney, home inspector, mortgage broker, general contractor, or another licensed profession or occupation has been disciplined for an offense under any law involving fraud, theft, misrepresentation, breach of trust or fiduciary responsibility, or willful or negligent malpractice..

Lastly, be aware that under (b)(3), licensees may be disciplined for violating any of the 15 provisions under subsection (a) when selling, buying, or leasing their own property.

## **GENERAL BROKERAGE PROVISIONS**

**D**iscussed below are selected Commission rules related to general brokerage.

### **Agency Agreements and Disclosure [G.S. 93A-13 and Rule A.0104**

Provided below is a brief summary of the various provisions of the Commission’s rule regarding agency agreements and disclosure. For a much more in-depth discussion of this rule and its application, the reader is referred to the Commission’s *North Carolina Real Estate Manual*.

**Agency Agreements.** G.S. 93A-13 and Rule A.0104(a) requires all agency agreements for brokerage services (in both sales and lease transactions) to be in writing and signed by the parties thereto. Rule A .0104(a):

- Requires agency agreements with **property owners** (both sellers and lessors) of any type of property to be in writing prior to the broker providing any services;
- Allows an express **oral buyer/tenant agency agreement** from the outset of the relationship, *but the agreement must be reduced to writing no later than the time any party to the transaction makes an offer.* As a practical matter, this oral agreement needs to address all key aspects of the relationship, including agent compensation, authorization for dual agency, etc.

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**(Note: A buyer/tenant agency agreement must be in writing from the outset if it seeks to limit the buyer/tenant’s right to work with other agents or binds the client to the agent for any definite time period. In other words, an oral buyer/tenant agency agreement must be “non-exclusive” and must be for an indefinite period and terminable by the client at any time.)**

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Further, every **written** agency agreement of any kind must also:

- *Provide for its existence for a definite period of time and terminate without prior notice at the expiration of that period.* [Exception: an agency agreement between a broker and a landlord to procure tenants for the landlord’s property may allow for automatic renewal so long as the landlord may terminate with notice at the end of any contract or renewal period.]
- *Contain the Rule A.0104(b) non-discrimination (fair housing) provision,* namely: “The broker shall conduct all brokerage activities in regard to this agreement without respect to the race, color, religion, sex, national origin, handicap or familial status of any party or prospective party.” (This provision must be set forth in a clear and conspicuous manner which shall distinguish it from other provisions of the agency agreement.)
- *Include the license number of the individual licensee who signs the agreement.*

Allowing an agent to work with a buyer under an express *oral* buyer agency agreement is intended to address the prob-

lem of buyers being reluctant to sign a written buyer agency agreement at the outset of their relationship with a buyer agent. The idea underlying this approach is to allow an agent to work temporarily with a prospective buyer as a buyer's agent under an oral agreement while the agent establishes a rapport with the buyer that makes the buyer feel more comfortable with signing a written buyer agency agreement.

Although the rule allows oral buyer/tenant agency agreements until the point in time when any party is ready to make an offer, it nevertheless is highly advisable that agents have such agreements reduced to writing and signed by the buyer/tenant at the earliest possible time in order to avoid misunderstanding and conflict between the buyer/tenant and agent. Recall also that the agent must obtain a written buyer/tenant agency agreement from the client not later than the time either party to the transaction extends an offer to the other.

If the buyer will not sign a written buyer agency agreement prior to making or receiving an offer, then the agent may not continue to work with the buyer as a buyer's agent. Moreover, the agent may not begin at this point to work with the buyer as a seller's subagent unless the agent (1) fully advises the buyer of the consequences of the agent switching from buyer's agent to seller's agent (including the fact that the agent would have to disclose to the seller any information, including "confidential" information about the buyer, that might influence the seller's decision in the transaction), (2) obtains the buyer's consent, and (3) obtains the consent of the seller and listing firm, which is the seller's agent. The foregoing applies equally to brokers working with tenants as a tenant agent.

**Agency Disclosure Requirement.** While Rule A.0104(a) requires all agency agreements, whether for lease or sales transactions, to be in writing, the *Rule A.0104(c) agency disclosure requirement applies only to sales transactions. It requires licensees to provide prospective buyers and sellers, at "first substantial contact," with a copy of the Working with Real Estate Agents brochure, to review the brochure with them and then reach an agreement regarding their agency relationship.* The licensee providing the brochure should also include his/her name and license number on the brochure. Note that the obligation under this rule is not satisfied merely by handing the prospective seller or buyer the brochure to read. The agent is required to review the contents of the brochure with the prospective buyer or seller and then reach agreement with the prospective buyer or seller as to whether the agent will work with the buyer or seller as his/her agent or as the agent of the other party.

In the case of a prospective **seller**, the agent may either (1) act as the seller's agent, which is the typical situation and requires a written agreement from the outset of their relationship, or (2) work with the seller as a buyer's agent if the agent already represents a prospective buyer.

In the case of a prospective **buyer**, the agent may either (1) act as the buyer's agent under either an oral or written agreement as addressed in Rule A.0104(a), or (2) work with

the buyer as a seller's agent, disclosure of which must be in writing from the outset.

**Disclosure of Agency Status by Sellers' Agents and Subagents to Prospective Buyers:** Paragraph (e) of Rule A.0104, like paragraph (c), requires a seller's agent or subagent in sales transactions to disclose his/her agency status in writing to a prospective buyer at the "first substantial contact" with the buyer. It is recommended that sellers' agents make this required written disclosure using the form provided for this purpose in the *Working with Real Estate Agents* brochure that must be provided to buyers (as well as to sellers) at first substantial contact. This form has a place for the buyer to acknowledge receipt of the brochure and disclosure of agency status, thereby providing the agent with written evidence of having provided the brochure and disclosure. The disclosure may, however, be made using a different form — *the most important point is that the disclosure be made in writing in a timely manner.* The reason for this requirement is that buyers tend to assume that an agent they contact to work with them in locating a property for purchase is "their" agent and working primarily in their interest. This may or may not be the case in reality. *The purpose of the disclosure requirement is to place prospective buyers on notice that the agent they are dealing with is NOT "their" agent before the prospective buyer discloses to the agent information which the buyer would not want a seller to know because it might compromise the buyer's bargaining position.*

Most frequently, "**first substantial contact**" will occur at the first "face-to-face" meeting with a prospective buyer. However, the point in time that "first substantial contact" with a prospective buyer occurs will vary depending on the particular situation and may or may not be at the time of the first or initial contact with the prospective buyer. Many first contacts are by telephone and do not involve discussions which reach the level that would require disclosure, although some initial phone contacts, especially those with out-of-town buyers, could reach this level.

*"First substantial contact" occurs at the point in time when a discussion with a prospective buyer begins to focus on the buyer's specific property needs and desires or on the buyer's financial situation.* Typically, that point in time is reached when the agent is ready to solicit information from the prospective buyer that is needed to identify prospective properties to show the buyer. Therefore, *an agent planning to work with a prospective buyer as a seller's agent or subagent should assure that disclosure of his/her agency status is made in writing to the prospective buyer prior to obtaining from the prospective buyer any personal or confidential information that the buyer would not want a seller to know.*

A few **examples of such personal or confidential information include:** *The maximum price a buyer is willing to pay for a property; the buyer's ability to pay more than the price offered by the buyer; or the fact that a buyer has a special interest in purchasing the seller's property rather than some other similar property.* In any event, the disclosure must be made pri-

or to discussing with the prospective buyer his/her specific needs or desires regarding the purchase of a property. As a practical matter, this means the *disclosure will always need to be made prior to showing a property to a prospective buyer*. The best policy is to simply make the disclosure at the earliest possible time.

If first substantial contact occurs by telephone or by means of other electronic communication where it is not practical to provide written disclosure, the agent shall immediately disclose by similar means whom he/she represents and shall immediately, but in no event later than three days from the date of first substantial contact, mail or otherwise transmit a copy of the written disclosure to the buyer.

**Disclosure of Agency Status by Buyers' Agents to Sellers or Sellers' Agents.** Paragraph (f) of Rule A.0104 requires a buyer's agent to disclose his/her agency status to a seller or seller's agent at the **"initial contact"** with the seller or seller's agent. "Initial contact" will typically occur when a buyer's agent telephones or otherwise contacts the listing firm to schedule a showing. The initial disclosure may be oral, but a written confirmation of the previous oral disclosure must be made (except in auction sale transactions) no later than the time of delivery of an offer to purchase. The written confirmation may be (and usually is) included in the offer to purchase. In fact, Commission Rule A.0112(a) (19) requires that any preprinted offer to purchase and contract form used by an agent include a provision providing for confirmation of agency status by each real estate agent (and firm) involved in the transaction.

**Consent to Dual Agency.** Paragraph (d) of Rule A.0104 requires generally that an agent must obtain the written authority of all parties prior to undertaking to represent those parties as a dual agent. It is important to note that this requirement applies to all real estate transactions (sales and lease/rentals), not just sales transactions. [In sales transactions, this written authority to act as a dual agent is usually included in the listing and buyer agency contracts. If those contracts do not grant such authority, then the agent must have both the seller and buyer consent to the dual agency prior to beginning to act as a dual agent for both parties.]

Paragraph (d) of Rule A.0104 currently *requires written authority for dual agency from the formation of the relationship except situations where a buyer/tenant is represented by an agent working under an oral agency agreement as permitted by A.0104(a), in which case written authority for dual agency must be obtained no later than the time one of the parties represented by the agent working as a dual agent makes an offer to purchase, sell, rent, lease, or exchange real estate to the other party*. Thus, it is permissible for the agent to operate for a limited period of time under an oral dual agency agreement. It is very important to remember that G.S. 93A-6(a)(4) still requires agents to obtain the consent of all parties prior to beginning to act as a dual agent for those parties. Therefore, it is essential that agents electing to operate as a dual agent for a limited period of time without obtaining this authority

in writing still explain fully the consequences of their acting as a dual agent and obtain the parties' oral consent.

As a practical matter in sales transactions, agents will frequently have already obtained written authority to act as a dual agent for in-house sales transactions at the time the initial written listing or buyer agency agreement is executed. However, under Paragraph (a) of Rule A.0104, many buyer's agents may elect to work with their buyer clients for a period of time under an oral buyer agency agreement. Paragraph (d) permits such buyer's agents to also operate for a limited period of time as a dual agent under an oral agreement in order to deal with situations where a buyer client is interested in a property listed with the agent's firm. Note that, *although an oral dual agency agreement for a limited period of time is permitted by Commission rules, it is strongly recommended that agents have any dual agency agreement in writing from the outset of the dual agency arrangement*. This will provide the agent with some evidence that the matter of dual agency was discussed with the parties and that they consented to it. Such evidence could prove quite useful if a party later asserts that the agent did not obtain their consent for dual agency in a timely manner.

**Auction Sales Exemption.** Paragraph (g) of Rule A.0104 provides that the provisions of Paragraphs (c), (d) and (e) of the Rule shall not apply to real estate licensees representing sellers in auction sales transactions. Note that in auction sales, the real estate agents involved almost invariably work only as seller's agents and this fact is considered to be self-evident. Thus, there is no need for agents to distribute and review the *Working with Real Estate Agents* brochure, no need for disclosure of agency status by the seller's agents, and no dual agency. For the unusual situation where a buyer may be represented by an agent in an auction sale transaction, Paragraph (h) of Rule A.0104 provides that such a buyer's agent shall, no later than the time of execution of a written agreement memorializing the buyer's contract to purchase, provide the seller or seller's agent with a written confirmation that he/she represents the buyer.

**Dual Agency Status of Firm.** Paragraph (i) of Rule A.0104 codifies in the Commission's rules the common law rule that *a firm which represents more than one party in the same real estate sales transaction is a dual agent, and further states that the firm, through the brokers affiliated with the firm, shall disclose its dual agency to the parties*. In other words, dual agency is not limited to those situations where an individual agent is working with both a buyer client and seller client (or lessor and commercial tenant) in the same transaction. If one agent of a firm is working with a buyer client of the firm and another agent of the same firm is working with a seller client of the firm in a transaction involving the sale of the seller client's property to the buyer client, then the firm is a dual agent (as it holds both agency agreements). However, a firm functions through its employees, namely, its associated agents; thus, under the common law, whenever the firm is a dual agent of certain parties in a transaction, all licensees affiliated with that

firm are also dual agents of those parties in that transaction.

**Designated Agency.** Paragraphs (j) - (m) of Rule A.0104 authorize real estate firms to engage in a form of dual agency practice referred to in the rule as “**designated agency**” in certain **sales transactions involving in-house dual agency**. *“Designated agency involves appointing or “designating” an individual agent(s) in a firm to represent only the interests of the seller and another individual agent(s) to represent only the interests of the buyer when a firm has an in-house dual agency situation.*

The principal advantage of the designated agency approach over the “standard” dual agency approach is that each of a firm’s clients (seller and buyer) receive fuller representation by their designated agent. In the typical dual agency situation, client advocacy is essentially lost because the dual agent may not seek an advantage for (i.e., “advocate” for) one client to the detriment of the other client. The dual agent must remain completely neutral and impartial at all times. Designated agency returns “advocacy” to the services provided by the respective designated agents and allows them to more fully represent their respective clients.

Authority to practice designated agency must be in writing no later than the time a written dual agency agreement is required under A.0104(d). Additional required procedures for practicing designated agency are clearly spelled out in Paragraphs (j) - (m) and are not discussed further here. For more detailed coverage of dual and designated agency, the reader is once again referred to the Commission’s *North Carolina Real Estate Manual*.

**Dual Agency by Individual Agent.** Paragraph (n) of Rule A.0104 authorizes individual agents representing both the buyer and seller in the same real estate sales transaction pursuant to a written dual agency agreement to include in the agreement a provision authorizing the agent not to disclose certain “confidential” information about one party to the other party without permission from the party about whom the information pertains. This provision is intended to allow individual dual agents to treat confidential information about their clients in a manner similar to that allowed for firms practicing designated agency.

**Brokers As Parties to Transactions.** There is an inherent conflict of interest presented by a broker representing the very party against whom the broker, as an interested party, is negotiating. Paragraph (o) of Rule A.0104 prohibits a broker who is selling property in which the broker has an ownership interest from representing a buyer of the property. Except that a broker who is selling commercial real estate, as defined in Rule .1802 of this Subchapter, in which the broker has less than 25% ownership interest may represent a buyer of that property if the buyer consents to the representation after full written disclosure of the broker’s ownership interest. However, a firm listing a property owned by a broker affiliated with the firm may represent a buyer of that property so long as the individual broker representing the buyer does not have an ownership interest in the prop-

erty and the buyer consents to the representation after full disclosure. Paragraph (p) of Rule A.0104 prohibits a listing broker or firm from purchasing a property listed by that broker or firm unless they first disclose to the seller in writing that a potential conflict of interest exists and that the seller may want to seek independent counsel. Prior to the listing broker entering into a purchase contract, the individual listing broker and firm must either terminate the listing agreement or transfer the listing to another broker in the firm. Prior to the firm entering into a purchase contract, the listing broker and firm must disclose to the seller in writing that the seller has the right to terminate the listing. The broker or firm must terminate the listing upon the request of the seller.

#### **Broker Name and Address [Rule A.0103]**

A broker must notify the Commission in writing (may include online) within 10 days of each change in personal name, firm name, trade name, residence address and firm address, telephone number, and email address.

If a broker intends to advertise in any manner using a firm name or assumed name which does not set forth the surname of the broker, the broker must first register the firm name or assumed name with the county *register of deeds office in each county in which the broker intends to engage in brokerage activity* and must also notify the Commission of the use of such firm name or assumed name. For individuals and partnerships, a name is “assumed” when it does not include the surname of the licensee(s). For a firm required to be registered with the Secretary of State, a name is “assumed” when it is different from the firm’s legal name as registered with the Secretary of State. Note: most franchisees operate under assumed names. An Assumed Name certificate can be filed in the Register of Deeds office for uploading to the statewide database maintained by the Secretary of State.

A licensee operating as a sole proprietorship, partnership or business entity other than a corporation or limited liability company may NOT include in its legal or assumed name the name of an unlicensed person or a provisional broker.

A broker who proposes to use a business name that includes the name of another active, inactive or cancelled broker must have the permission of that broker or his or her authorized representative. This rule provision is intended to prohibit a broker or firm from using without proper authorization the name of some other broker or former broker who is not currently associated with the broker or firm, such as a former associate or a deceased broker.

#### **Advertising [Rule A.0105]**

A licensee must have the proper authority to advertise. A broker may not advertise or display a “for sale” or “for rent” sign on a property without the written consent of the owner or the owner’s authorized agent. A broker may not advertise any brokerage service for another without the consent of his or her broker-in-charge and without including in any advertisement the name of the firm or sole proprietorship with which the broker is associated.

The rule also prohibits any advertisement by a licensee that indicates an offer to sell, buy, exchange, rent or lease real property is being made by the licensee's principal without the involvement of a broker – i.e., a “**blind ad.**” *All advertising by a licensee must indicate that it is the advertisement of a broker or brokerage firm.*

#### **Delivery of Instruments** [G.S. 93A-6(a); Rule A.0106]

Among other things, this rule, which implements G.S. 93A-6(a)(13), *requires agents to deliver to their customer or client copies of any required written agency agreement, contract, offer, lease, rental agreement, option or other related transaction document within three days of the broker's receipt of the executed document.* Regarding offers, this does NOT mean that agents may in every case wait up to three days to present an offer to a seller. Rather, it means that an agent must, as soon as possible, present to the seller any offer received by the agent. If the agent is the “selling agent,” then the offer should be immediately presented to the “listing agent” who should, in turn, immediately present the offer to the seller. The “three-day” provision is included only to allow for situations where the seller is not immediately available (e.g., seller is out of town), and represents an outside time limit within which offers must always be presented. In all cases where the seller is available, the offer should be presented as soon as possible.

The same rule also means that a prospective buyer who signs an offer must immediately be provided a copy of such offer. (A photocopy is acceptable for this purpose.) Do NOT wait until after the offer is accepted (or rejected) by the seller.

In addition, this rule means that an offer must be immediately presented to a seller even if there is a contract pending on the property. Of course, in this instance, it is essential that the agent also advise the seller that serious legal problems could result from the seller's acceptance of such offer and that the seller should contact an attorney if he is interested in treating the offer as a “back-up” offer or in attempting to be released from the previously signed contract.

Copies of any signed sales contract or lease must also be promptly delivered to the parties within the three-day period. Clients should be provided a copy of the agency agreement upon signing, since both parties presumably are present, but certainly within three days of receipt by the broker.

Finally, G.S. 93A-6(a)(14) requires a broker to provide his/her client a detailed and accurate closing statement showing the receipt and disbursement of all monies relating to the transaction about which the broker knows or reasonably should know. A broker may rely on a closing statement prepared by an attorney but must review the statement for accuracy.

#### **Retention of Records** [Rule A.0108]

Brokers are required to retain records pertaining to their brokerage transactions for three years from the successful or unsuccessful conclusion of the transaction or the disbursement of all trust monies pertaining to that transaction, whichever occurs later. However, if the broker's agency agreement

is terminated prior to the conclusion of the transaction, the broker shall retain transaction records for three years after the agency agreement is terminated or the disbursement of all funds held by or paid to the broker in connection with the transaction, whichever occurs later. Documents that must be retained include sale contracts, leases, offers (even those not accepted), agency contracts, earnest money receipts, trust account records, disclosure documents, closing statements, broker cooperation agreements, broker price opinions and comparative market analyses (including notes and supporting documentation), advertising, sketches, and any other records relating to a transaction.

Rule A .0108(d) also requires an individual broker to provide a copy of such records including written agency disclosures, agency agreements, and contracts to the firm or sole proprietorship with which they are affiliated within three days of the broker's receipt of such documents.

#### **Brokerage Fees and Compensation** [Rule A.0109]

This rule addresses various issues associated with the disclosure of and sharing of compensation received by a real estate licensee.

**Disclosure to principal of compensation from a vendor or supplier of goods or services.** Paragraph (a) prohibits a licensee from receiving any form of valuable consideration from a vendor or supplier of goods or services in connection with an expenditure made on behalf of the licensee's principal in a real estate transaction without first obtaining the written consent of the principal.

**Example:** A broker manages several rental units for various owners and routinely employs Ajax Cleaning Service to clean the units after the tenants leave. The broker pays Ajax a \$50 per unit fee for its services out of rental proceeds received and deposited in his trust account. Ajax then “refunds” to the broker \$10 for each \$50 fee it receives, but the property owners are not aware that the broker receives this payment from Ajax in addition to his regular brokerage fee. The broker in this situation is making a secret profit without the property owners' knowledge and is violating the rule.

**Disclosure to a party of compensation for recommending, procuring or arranging services for the party.** Paragraph (b) prohibits a licensee from receiving any form of valuable consideration for recommending, procuring, or arranging services for a party to a real estate transaction without full and timely disclosure to such party. The party for whom the services are recommended, procured, or arranged does not have to be the agent's principal.

**Example:** An agent sells a listed lot to a buyer who wants to build a house on the lot. Without the buyer's knowledge, the agent arranges with ABC Homebuilders for ABC to pay the agent a 3% referral fee if the agent recommends ABC to the buyer and the buyer employs ABC to build his house. The agent then recommends ABC to the buyer, ABC builds the buyer's house for \$100,000 and ABC secretly pays

the agent \$3,000 for his referral of the buyer. The agent has violated this rule. (Note that the buyer in this situation likely paid \$3,000 more for his house than was necessary because it is very likely the builder added the agent's referral fee to the price he charged the buyer for building the house. The main point here is that the buyer had the right to know that the agent was not providing disinterested advice when recommending the builder.)

**Example:** A selling agent in a real estate transaction, while acting as a subagent of the seller, recommends to a buyer who has submitted an offer that the buyer apply to Ready Cash Mortgage Company for his mortgage loan. The agent knows that Ready Cash will pay him a "referral fee" of \$100 for sending him the buyer's business if the loan is made to the buyer, but the agent does not disclose this fact to the buyer. If the agent subsequently accepts the referral fee from the lender, he will have violated this rule. (The buyer has the right to know that the agent's recommendation is not a disinterested one.)

**Disclosure to principal of compensation for brokerage services in sales transactions.** Paragraph (c) deals with disclosure to a licensee's principal of the licensee's compensation in a **sales** transaction from various sources other than in situations addressed in paragraphs (a) and (b). A broker may not receive any compensation, incentive, bonus, rebate or other consideration of more than nominal value (1) from his or her principal unless the compensation, etc. is provided for in a written agency contract or (2) from any other party or person unless the broker provides to his or her principal a full and timely disclosure of the compensation.

**Example:** ABC Homebuilders offers to pay any broker who procures a buyer for one of ABC's inventory homes a **bonus** of \$1,000 that is in addition to any brokerage commission the broker earns under any agency contract and/or commission split agreements. Any broker working with a buyer-client who is considering the purchase of one of ABC's homes must comply with the disclosure requirement and disclose the bonus to the buyer in a timely manner. **Note:** If ABC Homebuilders also offers a bonus of \$2,000 on a second sale of one of its homes and \$3,000 on a third sale, and if a buyer's broker has already sold one of ABC's homes, then the broker must disclose to his or her buyer principal the entire bonus program and that his or her bonus will be at least \$2,000 if the buyer purchases an ABC home.

**Nominal compensation.** Compensation is considered to be "nominal" if it is of insignificant, token or merely symbolic worth. The Commission has cited gifts of a \$25 bottle of wine or a \$50 dinner gift certificate as being examples of "nominal" compensation paid to a broker that do not require the consent of the broker's principal.

**Full and timely disclosure.** Paragraph (d) of Rule A.0109

explains what is meant by "full and timely disclosure" in paragraphs (a), (b) and (c). "Full" disclosure includes a description of the compensation, incentive, etc. including its value and the identity of the person or party by whom it will or may be paid. The disclosure is "timely" when it is made in sufficient time to aid a reasonable person's decision-making. In a sales transaction, the disclosure may be made orally, but must be confirmed in writing before the principal makes or accepts an offer to buy or sell.

**Restrictions on compensation disclosure requirement.** Paragraph (e) clarifies that a broker does NOT have to disclose to a person who is not his or her principal the compensation the broker expects to receive from his or her principal, and further clarifies that a broker does NOT have to disclose to his principal the compensation the broker expects to receive from the broker's employing broker/firm (i.e., the individual broker's share of the compensation paid to the broker's employing broker/firm).

**Commission will not arbitrate commission disputes.** G.S. 93A-3(c) provides that the Commission shall not make rules or regulations regulating commission, salaries, or fees to be charged by licensees. Paragraph (f) of Rule A.0109 augments that statutory provision by providing that the Commission will not act as a board of arbitration regarding such matters as the rate of commissions, the division of commissions, pay of brokers and similar matters.

**Compensation of unlicensed persons by brokers prohibited.** G.S. 93A-6(a)(9) authorizes the Commission to take disciplinary action against a licensee for paying any person for acts performed in violation of the License Law. Paragraph (g) of Rule A.0109 simply augments this statutory provision by providing an affirmative statement that a licensee shall not in any manner compensate or share compensation with unlicensed persons or entities for acts performed in North Carolina for which a license is required. [Note that NC brokers may split commissions or pay referral fees to licensees of another state so long as the out-of-state licensee does not provide any brokerage services while physically in North Carolina.] One narrow, limited exception to this restriction is provided in Paragraph (h) – licensees may pay referral fees to travel agents who contact them to book vacation rentals only, so long as well-defined procedures are followed.

**RESPA prohibitions control.** Finally, Paragraph (i) of Rule A.0109 provides that nothing in this rule permits a licensee to accept any fee, kickback, etc. that is prohibited by the federal Real Estate Settlement Procedures Act (RESPA) or implementing rules, or to fail to make any disclosure required by that act or rules.

**Broker-In-Charge** [Rule A.0110].

**Requirement to Have a Broker-In-Charge.** Paragraph (a) of Rule A.0110 states the general rule that each real estate firm is required to have a broker designated by the Commission who meets the qualification requirements to serve as "**broker-in-charge**" of the firm's principal office and a different broker to serve in the same capacity at each

branch office. It is important to note, as discussed previously under “License Requirement,” that “**broker-in-charge**” is not a separate license, but only a separate license status category. No broker may be broker-in-charge of more than one office location at a time, and no office of a firm shall have more than one designated broker-in-charge. Rule A.0110(a) describes the lone exception in the rare circumstance when two or more firms share the same office space. Note that G .0103 defines the terms “office,” “principal office” and “branch office” – these definitions are not repeated here.

**Exception to BIC Requirement for Certain Firms.** Paragraph (c) of Rule A.0110 provides: A licensed real estate firm is not required to have a BIC if it: (1) has been organized for the sole purpose of receiving compensation for brokerage services furnished by its qualifying broker through another firm or broker; (2) is treated for tax purposes as a Subchapter S corporation by the U.S. Internal Revenue service; (3) has no principal or branch office; and (4) has no licensed or unlicensed person associated with it other than its qualifying broker.

**Sole Proprietors.** In addition to each firm having to have a broker-in-charge for each office, *most broker-sole proprietors (including sole practitioners) also must be a broker-in-charge.*

Rule A.0110 (b) provides that a broker who is a **sole proprietor** shall designate himself or herself as a broker-in-charge if the broker: (1) engages in any transaction where the broker is required to deposit and maintain monies belonging to others in a trust account; (2) engages in advertising or promoting his or her services as a broker in any manner; OR (3) has one or more other brokers affiliated with him or her in the real estate business. Note, however, that maintenance of a trust account by a broker solely for holding residential tenant security deposits received by the broker on properties owned by the broker in compliance with G.S. 42-50 shall not, standing alone, subject the broker to the requirement to be designated as a broker-in-charge.

The most misunderstood of the three broker-in-charge triggering requirements for sole proprietors cited above is # (2): “...engages in advertising or promoting his or her services as a broker **in any manner.**” Acts of a sole proprietor that trigger the BIC requirement under # (2) include, but are not limited to: Placing an advertisement for his or her services as a broker in any form or any medium; distributing business cards indicating he or she is a real estate broker; orally soliciting the real estate business of others; or listing a property for sale (which inherently involves holding oneself out as a broker and advertising).

Therefore, *a broker-sole proprietor may lawfully provide only limited brokerage services without designating himself or herself as a BIC.* A couple of examples of *permissible* brokerage activities by a broker-sole proprietor who is NOT a designated BIC include receiving a referral fee from another broker or brokerage firm for referring business to the broker or firm or representing a relative or friend as a buyer’s broker in a sales transaction provided the broker has not solicited the business, has not advertised or promoted his or her

services, and does not hold earnest money beyond the time it is required to be deposited in a trust account.

*The practical effect of these requirements is that a broker who will be operating independently in most cases must also designate himself or herself as a BIC.* The real significance of these requirements for a sole proprietor will be better understood when the qualification requirements to serve as a BIC are subsequently discussed.

**Requirements for BIC-Eligible Status.** Paragraph (e) of Rule A .0110 states that, in order for a broker to be designated as a BIC for a sole proprietorship, real estate firm, or branch office, the broker must FIRST have BIC Eligible status. A broker must request BIC Eligible status on a form provided by the Commission.

**The qualifying requirements for BIC Eligible Status, pursuant to paragraph (e) of Rule A .0110, are:**

- Broker license must be on “active” status but NOT on “provisional” status. A provisional broker is ineligible to serve as broker-in-charge, as is a broker whose license is inactive or expired.
- Broker must have at least 2 years of full-time or 4 years of part-time real estate brokerage experience within the previous 5 years or be a North Carolina licensed attorney with a practice that consisted primarily of handling real estate closings and related matters in North Carolina for 3 years immediately preceding application. The requirement is for actual brokerage experience, not just having a license on “active” status. Note that by submission of the request form to the Commission, a broker certifies that he or she possesses the required experience. The Commission may at its discretion require the broker to provide evidence of possessing the required experience.
- After obtaining BIC Eligible status, a broker must complete the Commission’s 12-hour Broker-In-Charge Course within 120 days of designation (unless the 12-hour course has been taken within the previous year). Failure to complete this course within 120 days will result in the broker losing BIC Eligible status. The broker must then take the course before he or she may again be granted BIC Eligible status.

**Requesting Designation as Broker-in-Charge (BIC).** A broker who has BIC Eligible status may request BIC Designation on a form provided by the Commission at any time so long as the broker continuously maintains his/her BIC Eligible status. The broker may also request BIC Eligible status and BIC Designation simultaneously.

**Broker-In-Charge (BIC) Duties.** The designated broker-in-charge is the primary person the Commission will hold responsible for the supervision and management of an office. See paragraph (g) of Rule A.0110 for a list of the specific responsibilities of a broker-in-charge.

**Maintaining BIC Eligible Status.** To maintain BIC Eligible status, paragraph (g) of Rule A.0110 requires that a broker must:

- Renew his or her broker license in a timely manner each license year and keep the license on active status at all times.

- Complete each license year the four-hour mandatory Broker-in-Charge Update Course (BICUP) as well as any approved four-hour CE elective.

The broker must begin taking the BICUP course during the same license year of designation, unless the broker completed the General Update (GENUP) course prior to designation.

The BICUP Course satisfies the broker's four-hour mandatory continuing education Update course requirement. If a broker with BIC Eligible status fails to take both the BICUP and one elective CE course by June 10 in any given year when required, then the broker will lose BIC Eligible status, and BIC designation if applicable, the following July 1.

**Termination of BIC Eligible Status and Broker-In-Charge Designation.** Paragraph (i) of Rule A.0110 provides that a broker's BIC Eligible status, and, if currently designated as a BIC, his or her BIC designation, shall be terminated if the broker: made any false statements or presented any false, incomplete, or incorrect information in connection with an application; fails to complete the 12-hour Broker-in-Charge Course pursuant to Paragraph (e) of the Rule; fails to timely renew his or her broker license, or the broker's license has been suspended, revoked, or surrendered; or fails to timely complete the Broker-in-Charge Update Course (BICUP) and a four credit hour elective course in any license year.

**Regaining Lost BIC Eligible Status and BIC Designation.** Pursuant to Rule A .0110(m), once a broker's BIC Eligible status has been terminated, the broker must complete the following steps in the order prescribed to regain the status:

1. The broker must first have a license on active status. If the license has expired, it must first be reinstated. If the license is inactive due to a CE deficiency, then the licensee must first complete whatever CE is necessary to reactivate the license and in either case, must then submit a reactivation form to the Commission requesting that the license be placed back on active status. A broker who has lost his or her BIC Eligible status should not take either the 12-hour BIC Course or the BICUP course prior to officially reactivating his/her license with the Commission.
2. Once back on active status, the broker must possess the experience required for initial designation and must first complete the 12-hour BIC Course prior to requesting BIC Eligible status and re-designation as a BIC regardless of when the broker may have previously taken the 12-hour course. There are no exceptions to this requirement to retake the 12-hour course prior to re-designation.

**Notice to Commission When BIC Status Ends.** A BIC must notify the Commission in writing within 10 days

upon ceasing to serve as BIC of a particular office. [See Paragraph (g).]

**Exception for certain Subchapter S corporations.** See Paragraph (c).

**Nonresidents.** Nonresident individuals and firms holding a NC broker and/or firm license and engaging in brokerage activity in NC are subject to the same requirements as NC resident brokers/firms with regard to when they must have a designated broker-in-charge. Thus, a nonresident company engaging in brokerage in NC must have a broker-in-charge of the company who holds an active NC broker license for purposes of its NC business, although the office need not be physically located in North Carolina. Similarly, a nonresident NC broker sole practitioner engaging in activity that triggers the broker-in-charge requirement for a resident NC broker sole practitioner (see previous discussion on this subject) also must be designated as a broker-in-charge for NC brokerage purposes as without a BIC, a company has no office anywhere.

**Education Exception for Certain Nonresident NC Brokers-In-Charge:** A nonresident NC broker who has attained BIC Eligible status and been designated as the broker-in-charge of an office NOT located in NC and who has no office, primary residence or mailing address in North Carolina is NOT required to complete four-hour mandatory Broker-in-Charge Update (BICUP) Course to maintain BIC Eligible status. [See Rule 58A .1711.] However, a nonresident broker who has attained BIC-Eligible status IS REQUIRED to complete the 12-hour BIC Course pursuant to paragraph (e) of Rule A .0110.

**Drafting Legal Instruments [Rule A.0111]**

This rule prohibits licensees from drafting legal instruments, e.g., contracts, deeds, deeds of trust, etc., but does allow them to fill in the blanks on preprinted sales or lease contract forms, which is not construed to be the unauthorized practice of law.

**Offers and Sales Contracts [Rule A.0112]**

This rule specifies what minimum terms must be contained in any preprinted offer or sales contract form a licensee, acting as an agent, proposes for use by a party in a real estate transaction.

**Reporting Criminal Convictions [Rule A.0113]**

Licensees are required to report to the Commission any criminal convictions for a felony or misdemeanor, any disciplinary action taken against them by any other occupational licensing board, or any restriction, suspension or revocation of a notarial commission within sixty (60) days of the final judgment or order in the case. This reporting requirement is ongoing in nature. *Note that Driving While Impaired (DWI) is a misdemeanor and must be reported!*

**Residential Property and Owners' Association Disclosure Statement [Rule A.0114]**

State law (Chapter 47E of the General Statutes) requires that most residential property owners complete a disclosure form to give to prospective purchasers. The form seeks to

elicit information about the condition of the property by asking various questions, to which owners may answer “yes,” “no,” or “no representation.” Failure to provide a buyer with this form may allow the buyer to cancel the contract by notifying the seller in writing within three calendar days of contract acceptance.

**Note:** Licensees in residential real estate transactions have a duty under G.S. 47E-8 to inform their clients of the client’s rights and obligations under the statute. The Real Estate Commission also views the Real Estate License Law as imposing on licensees working with sellers and buyers certain additional responsibilities to ensure statutory compliance and serve their clients’ interests. Licensees are expected to “assist” sellers with completion of the form but should not complete the form for a seller or advise a seller as to what representation (or No Representation) to make. That being said, licensees should be certain to advise sellers that the licensee is obligated by law to disclose all material facts about or relating to the seller’s property to prospective buyers regardless of what representation the seller makes on the disclosure form. See the Commission’s *North Carolina Real Estate Manual* for a full discussion of the disclosure law and an agent’s duties.

Sellers must also provide a Mineral and Oil and Gas Mandatory Disclosure Statement (MOGS) to buyers prior to making an offer to purchase and contract. The form has been developed by the Real Estate Commission and is available for download from the Commission’s website, [www.ncrec.gov](http://www.ncrec.gov). It is a separate form and is in addition to the Residential Property and Owner’s Association Statement. A disclosure statement is not required for some transaction. For a complete list of exemptions, see G.S. 47E-2.

#### **Broker’s Responsibility for Closing Statements [G.S. 93A-6(a)(14)]**

*The cited statute requires a broker, “...at the time a sales transaction is consummated, to deliver to the broker’s client a detailed and accurate closing statement showing the receipt and disbursement of all monies relating to the transaction about which the broker knows or reasonably should know.”* The statute goes on to provide that if a closing statement is prepared by an attorney or lawful settlement agent, a broker may rely on the delivery of that statement, but *the broker must review the statement for accuracy and notify all parties to the closing of any errors.* Since virtually every residential transaction in North Carolina is closed by an attorney (or lawful settlement agent), it is standard practice for brokers to adopt the attorney’s settlement statement to satisfy this License Law requirement.

**Commission Guidelines.** A settlement statement is a detailed report of all monies received and disbursed by the settlement agent in connection with a real estate sales transaction. It is essential that the settlement statement be accurate and that a copy be provided to each party. The settlement statement is prepared by the settlement agent – the individual conducting the closing, which in North Carolina is

almost always the closing attorney or a nonlawyer assistant working under the supervision of the closing attorney.

The TRID (Tila-RESPA Integrated Disclosures) rule became effective October 3, 2015, and applied to loan applications received on or after October 3, 2015. The TRID rule replaced the HUD-1 settlement statement (RESPA) and final Truth-in-Lending statement (TILA) with two Closing Disclosure (CD) documents, one for the borrower and a separate one for the seller. Closing disclosures are disclosures only and are not equivalent to a settlement statement. While the HUD-1 is no longer used in TRID-governed transactions, other types of settlement statements may be used, such as settlement/closing statements created and published by the American Land Title Association (ALTA). Also, the HUD-1 may be used as the settlement statement in non-TRID-governed transactions, such as cash transactions, construction loans, or purchases of investment property.

The Commission has published in its North Carolina Real Estate Manual the following guidelines regarding brokers’ responsibilities for settlement statements:

- A broker must confirm the accuracy of all entries about which s/he has direct knowledge. Such items include, but may not be limited to: the sale price; amount of the due diligence fee and earnest money deposit; amount of the brokerage commission and split; any amounts due either party under the offer to purchase and contract, e.g., closing costs paid by seller, as well as any sums paid by or due to third parties related to the transaction, if the broker knows or should know about the expense.
- As to amounts paid by or due to third parties, brokers generally may assume that the amounts for charges and fees as stated on the settlement statement are correct unless there is something that would lead a reasonable broker to suspect that an amount is incorrect. As to all debits and credits related to the transaction, whether paid before or at closing, the broker must:
  - 1) review and confirm that all charges and credits have been properly debited or credited to the seller or buyer and are entered in the correct column; and
  - 2) review and confirm the accuracy of the calculations for all prorated items, escrow reserves, interim interest, excise tax and the “bottom line figures,” i.e., total settlement charges to each party, cash from borrower-buyer, and cash to seller.
- If a broker is aware of any expense related to the transaction paid to or by either party or any third party that is not included on the settlement statement, the broker must notify both the settlement agent and the lender of the omission, as the settlement statement should reflect all expenses and payments related to the transaction, not just monies the settlement agent

disburses.

- A broker should notify the settlement agent if the broker believes there are any errors or omissions on the statement.

## HANDLING TRUST FUNDS

This section addresses those aspects of handling trust funds that are taught in the Real Estate Broker Pre-licensing Course and tested on the real estate license examination for entry-level brokers. All brokers are encouraged to take the Basic Trust Account course for a fuller treatment of this subject. The Basic Trust Account course schedule is available on the Commission's website at [www.ncrec.gov](http://www.ncrec.gov).

### Definition of Trust Money

In the context of real estate transactions, "**trust money**" is most easily defined as *money belonging to others received by a real estate broker who is acting as an agent in a real estate transaction. It is also any money held by a licensee who acts as the temporary custodian of funds belonging to others.* Such money must be held in trust even if the circumstances are only collateral to the licensee's role as an agent in a real estate related matter, e.g., a listing agent receives monies from his out of town seller for yard maintenance while the property is being marketed. The most common examples of trust money are:

- Earnest money deposits
- Down payments
- Tenant security deposits
- Rents
- Homeowner association dues and assessments, and
- Money received from final settlements

In the case of resort and other short-term rentals, trust money also includes:

- Advance reservation deposits
- State (and local, if applicable) sales taxes on the gross receipts from such rentals

**Trust or Escrow Account** [G.S. 93A-6(a)(12) & (g); 93A-45(c); Rule A.0116, .0117]

One of the most basic tenets of broker accountability when handling trust money is that it must be deposited into a trust or escrow account as described below. A "trust account" or "escrow account" (the terms are synonymous for Commission purposes) is simply a bank account into which trust money (and *only* trust money) is deposited. The three primary features of a trust or escrow account are that it is:

- 1) **separate**, containing only monies belonging to others,
- 2) **custodial**, meaning *only the broker or the broker's designated employee has disbursement control over the account*, but no one who has funds in the account has that ability, *and*
- 3) **available on demand**, that is, the funds may be withdrawn at any time without prior notice.

**Type and Location of Trust Account.** A broker's trust account or escrow account must be:

- 1) a demand deposit account
- 2) in a federally insured depository institution
- 3) lawfully doing business in North Carolina
- 4) that agrees to make the account records available for inspection by Commission representatives. [G.S. 93A-6(g)]

Thus, for the purpose of holding most trust money, the bank can be located outside North Carolina if the foregoing conditions are met.

**Designation of Trust Account and FDIC Insurance.** A broker-in-charge who must maintain a trust account must ensure that the bank properly designates the account and that the words "trust account" or "escrow account" appear on all signature cards, bank statements, deposit tickets and checks. Even though the escrow account typically is in the name of the company or broker, so long as the broker properly designates the account as a "trust" or "escrow" account and keeps accurate records that identify each owner of the funds and/or depositor (buyer, seller, lessor, lessee, etc.), the depositors are protected from the funds being "frozen" or attached if the broker/trustee becomes insolvent, incapacitated, dies, has tax liens, becomes involved in a lawsuit, etc. Failure to properly designate an account titled in the name of the company/broker as a trust or escrow account may result in attachment of the account by others to collect a judgment or denial of FDIC insurance coverage as to each individual's interest in the account.

So long as the account is properly designated as a trust/escrow account, *all deposits are insured by the Federal Deposit Insurance Corporation (FDIC) up to \$250,000 per each individual for whom funds are held.* Thus, a broker's trust account may contain \$500,000 total, but *all funds are fully insured so long as no one individual's interest in the account exceeds \$250,000.* (**Note**, however, that an individual still may be underinsured if the individual maintains accounts in his/her individual name at the same financial institution as the broker's trust/escrow account.)

**When a Trust Account Is Required.** A broker must open and maintain a trust account when the broker or any affiliated licensee takes possession of trust money. A broker who is inactive or otherwise not using his/her real estate license is not required to open or maintain a trust account because s/he should not be engaged in brokerage nor receiving monies belonging to others. Similarly, if an *active* practicing broker does not collect or otherwise handle the funds of others, no trust account is required. Note: A broker who leases residential property he or she owns to tenants may be required to maintain a trust account under 42-50 NC Residential Landlord Tenant law.

**Number of Trust Accounts.** Except for brokers who are managing homeowner or property owner association funds, a broker holding trust money is only required to have one trust account. All earnest money deposits, tenant security deposits, rents, and other trust monies may be deposited into this one common trust account. However, brokers

who are active in both sales and property management often find it helpful to use more than one trust account. For example, they may wish to keep a “general sales trust account” for earnest money deposits, settlement proceeds, etc., and a “rental trust account” for tenant security deposits, rents, and related receipts. Although it is not required, many brokers involved in property management and leasing elect to maintain an additional “security deposit trust account” to keep tenant security deposits separate from rents and other related receipts. However, **Rule A.0118(a)** requires brokers who handle homeowner or property owner association funds to maintain a *separate trust account for each property owner association or homeowner association they manage*. The funds of one homeowner association are not to be commingled with funds from any other association nor with any general trust monies. The broker also must provide the association with periodic written statements not less than once each quarter reporting all monies received, disbursed, and due, but not paid (i.e., delinquent), as well as the balance of funds in the account.

**“Commingling” Prohibited.** [G.S. 93A-6(a)(12)] The basic statutory provision relating to a licensee’s handling of the money or property of others states that a broker may not “commingle” his or her own money or property with the money or property of others. This means that a broker may not maintain funds belonging to others in the same bank account that contains his or her personal or business funds. Funds belonging to others must be held in a trust account and, except as described below regarding “bank service charges on trust accounts,” a broker may not deposit his or her own funds in that trust account. The prohibition against commingling also means, for example, that a broker who has an ownership interest in property is precluded from depositing monies (e.g., earnest money, rent, security deposits, etc.) related to that property in his brokerage trust account.

**Bank Service Charges on Trust Accounts.** Trust accounts usually are subject to the same service charges as regular checking accounts. Whenever possible, brokers should arrange for the depository/bank either to bill the broker for these expenses or charge these expenses to the broker’s personal or general operating account. However, if such arrangements cannot be made, the Commission will permit a broker to deposit and maintain in his trust account a maximum of \$100.00 of his personal funds (or such other amount as may be required) to cover (not avoid) such charges. So, if a broker’s monthly service charges and other fees typically are \$100, then the broker may deposit up to \$200 of his/her own money to cover these charges. A broker who deposits any of his/her own money in the trust account to cover bank charges must be careful to properly enter and identify these personal funds in his/her trust account records by use of a personal funds ledger. While this technically constitutes “commingling,” it is permissible commingling to avoid the greater evil of using other people’s money

to pay these bank charges.

**Interest-Bearing Trust Account.** Both G. S. 93A-6(a)(12) and Rule A.0116(c) permit a broker to deposit trust money into an interest-bearing trust account so long as the broker first obtains written authorization for deposit in an interest-bearing account from all parties having an interest in the monies being held. Such authorization must specify how and to whom the interest will be paid. If the authorization is contained in an offer, contract, lease or other transaction instrument, it must be set forth in a conspicuous manner that distinguishes it from other provisions of the instrument. Remember, however, that all trust accounts must be a *demand account*, so investment of trust monies in any type of security, such as a government bond or a fixed term certificate of deposit, is prohibited.

**Broker-In-Charge Responsible for Trust Accounts.** [Rule A.0117; Rule A.0110(g)(4)] Rule A.0117(a) requires a broker to maintain complete records showing the deposit, maintenance and withdrawal of money belonging to the broker’s principals or *held in escrow or in trust for the broker’s principals*. Paragraph (h) of that rule also provides that the Commission may inspect trust account records periodically without prior notice and whenever the records are pertinent to investigation of a complaint against a licensee. Rule A.0110(g)(4) refines this requirement by specifying that a **broker-in-charge (BIC)** *is responsible for the proper maintenance of real estate trust accounts and records pertaining thereto*.

**Custodian of Trust Account Records Other Than the Broker-In-Charge.** While a broker-in-charge may transfer possession of trust money to a bookkeeper, secretary, or some other clerical employee to record and deposit the funds in a trust account and to maintain trust account records, the broker-in-charge nonetheless remains responsible for the care and custody of such funds. Brokers-in-charge should closely and diligently supervise the acts of all persons having access to the trust account, since final accountability for the accuracy and integrity of the account rests with the broker-in-charge. *Access to trust money should be limited and carefully controlled*.

**Disbursement of Earnest Money** [Rule A.0116(e)] This rule permits a broker-in-charge to transfer an earnest money deposit from his/her trust account to the closing attorney or other settlement agent not more than ten (10) days prior to the anticipated settlement date. Earnest money may **not** be disbursed prior to settlement for any other purpose without the written consent of the parties. Thus, earnest money may not be used by the broker to pay for inspection reports or other services on behalf of the buyer prior to settlement without the written consent of the seller, and vice-versa.

**Disputed Trust Funds.** Rule A.0116(d) addresses disputed trust funds as follows: “In the event of a dispute between buyer and seller or landlord and tenant over the return or forfeiture of any deposit other than a residential tenant security deposit held by a broker, the broker shall retain said deposit in a trust or escrow account until the broker has

obtained a written release from the parties consenting to its disposition or until disbursement is ordered by a court of competent jurisdiction.” The rule also references the G.S. 93A-12 procedures for depositing disputed funds with the Clerk of Court as well as when one party abandons his or her claim to the disputed funds. However, these procedures are beyond the scope of these materials and are more important for brokers-in-charge to know.

#### **Handling of Trust Money [Rule A.0116(a), (b) & (g)]**

The **general rule** is that all trust monies received by a licensee must be deposited in a trust account **within three banking days of receipt**. **Exception: Earnest money** received with offers to purchase and **tenant security deposits** in connection with leases must be deposited in a trust account *not later than three banking days following acceptance of the offer to purchase or lease agreement unless the deposit is tendered in cash* in which event it must be deposited within **three banking days following receipt, even if the contract or lease has not been accepted**. In part, this is because cash is immediately available and may be refunded within a day of deposit, unlike checks which may require a few days to clear.

Understand that a broker *may* choose to immediately deposit a check received for an earnest money deposit or tenant security deposit and is *not required* to wait until contract acceptance unless so instructed by the buyer/tenant. Of course, early deposit may cause problems if the offer to purchase or lease is not accepted and the prospective buyer or tenant understandably wants their deposit to be immediately returned. The date of acceptance should be shown in the purchase or lease agreement to determine when the three banking days begins.

**Receipt of Trust Money by Provisional Broker.** [Rule A.0116(b)(1)&(2), Rule A.1808.] *All trust money received by a provisional broker must be delivered immediately to the provisional broker's broker-in-charge.* In other words, provisional brokers may not retain or hold trust money any longer than absolutely necessary to deliver the trust money to his/her broker-in-charge. Similarly, trust monies received by a **nonresident limited commercial broker** are to be delivered immediately to and held by the resident North Carolina broker with whom the nonresident is affiliated. Brokers-in-charge should have written policies that clearly state the procedures to be followed when *any agent* affiliated with the company, whether a provisional or non-provisional broker, receives trust monies.

**Handling Option Money and Due Diligence Fee.** Rule A.0116(b)(4) states in part: “A broker may accept custody of a **check or other negotiable instrument made payable to the seller** of real property as payment for an **option or due diligence fee**, but only for the purpose of delivering the instrument to the seller. While the instrument is in the custody of the broker, the broker shall, according to the instructions of the buyer, either deliver it to the seller or return it to the buyer. The broker shall safeguard the instrument and shall be responsible to the parties on the instrument for its safe delivery as required by this Rule. A broker shall not retain such an instrument for more than three business days

after the acceptance of the option or other sales contract.”

The rule is basically self-explanatory. In the rule, “custody” means possession. Recall that option money or a due diligence fee is paid directly to the seller, to whom the check is written as payee, and so it is not appropriate for a broker to deposit these checks into his/her trust account because the check is not payable to the broker or real estate company as is the case with earnest money checks. Either the listing agent or buyer’s agent may hold the check or negotiable instrument until negotiations are completed and a contract is formed, at which point the check should be delivered to the seller as soon as possible.

If, however, a buyer for some reason gives a broker *cash for the option money or due diligence fee*, then the broker must *immediately deposit the cash in his/her trust account* pending contract formation as *cash must always be deposited into a trust account within three banking days of receipt — no exceptions*. If the parties enter into a contract, then the broker would write a check from the trust account payable to the seller, noting in the memo section and trust account records that it is for the option fee or due diligence fee from the buyer.

**Safeguarding Trust Money; Improper Use of Trust Money.** [Rule A.0116(g)] This rule places on *every licensee* the responsibility to safeguard the money or property of others coming into his or her possession according to the requirements of the License Law and Commission rules. In addition, it states that: “A broker shall not convert the money or property of others to his or her own use, apply such money or property to a purpose other than that for which it was intended or permit or assist any other person in the conversion or misapplication of such money or property.”

## **BROKER PRICE OPINION AND COMPARATIVE MARKET ANALYSIS**

[G.S. 93A, Article 6; Commission Rules Chapter 58A, Section .2200]

**Definitions.** General Statute §93A-82 of the North Carolina Real Estate License Law and General Statute §93E-1-4(7c) of the North Carolina Appraisers Act both define a **“broker price opinion” (“BPO”)** and a **“comparative market analysis” (“CMA”)** as “...an estimate prepared by a licensed real estate broker that details the probable selling price or leasing price of a particular parcel of or interest in property and provides a varying level of detail about the property’s condition, market, and neighborhood, and information on comparable properties, but does not include an automated valuation model.” Thus, *the terms “BPO” and “CMA” have exactly the same legal meaning* even though an estimate provided for a seller or buyer client or prospective client is most commonly referred to as a CMA and an estimate performed for a third party for a purpose other than mortgage loan origination (for example, a foreclosure or short sale decision) is typically referred to as a BPO.

- A “non-provisional” broker with a current license on “active” status may prepare a broker price opinion

(BPO) or comparative market analysis (CMA) for a fee for a variety of persons and entities for a variety of reasons, not just for actual or prospective brokerage clients. Note, however, that a provisional broker may NOT perform a BPO or CMA for a fee for anyone. [G.S. §93A-83(a) and (b)]

- A broker may **NOT** prepare a BPO (or CMA) for an existing or potential lienholder or other third party where the BPO is to serve as the basis to determine the **value** of a property *for the purpose of originating a mortgage loan*, including first and second mortgages, refinances or equity lines of credit. [G.S. §93A-83(b)(6)]
- A BPO or CMA may only estimate the “*probable selling price*” or “*probable leasing price*” of a property, not the “value” of a property. Moreover, if a BPO or CMA does propose to estimate the “value” or “worth” of a property, it shall be legally considered a “real estate appraisal” that may only be prepared by a licensed or certified real estate appraiser, not by a real estate broker. [G.S. §93A-83(f)]
- A BPO or CMA provided *for a fee* must be performed in accordance with the requirements of Article 6 of the Real Estate License Law and standards set forth in rules adopted by the North Carolina Real Estate Commission. [Rules, Ch. 58, Section A.2200]
- A BPO or CMA must be *in writing* and must address those matters specifically required by the statute or Commission rule. [G.S. §93A-83(c)]

**Standards for BPOs and CMAs Performed for Compensation.** Article 6 of the Real Estate License Law provides a number of standards that must be followed when a broker is performing a BPO/CMA for a fee. Additionally, the Commission has adopted rules (Section A.2200) setting forth specific standards for brokers when performing such standards. A broker performing a BPO/CMA utilizes the same valuation concepts and methodology as an appraiser performing an appraisal; however, the analysis associated with a BPO/CMA is less comprehensive and detailed than with an appraisal, and the regulatory standards for brokers performing BPOs/CMAs are less stringent than those required for real estate appraisers performing appraisals. [See G.S. 93A-83 and especially Commission Rule 58A.2202.]

**Reporting Probable Selling/Leasing Price as a “Range.”** In recognition of the fact that brokers performing BPOs/CMAs are not expected to be as precise in their analysis and adjustments to comparable properties as an appraiser when performing an appraisal, the Commission’s rules permit reporting in a BPO/CMA of probable selling price or leasing price (lease rate) as either a single figure or as a **price range**. The applicable rules also states: “When the estimate states a price range and the higher figure exceeds the lower figure by more than ten (10%), the broker shall include an explanation as to why the variance is more than 10 percent. [Rule A.2202(h)]

**Use of Income Analysis Methodology Now Required Where Appropriate.** The revised statutes eliminated the old Appraisers Act restriction that a broker’s CMA for actual or prospective clients *and for compensation* was permitted only if the sales comparison approach was the only method used to derive an indication of the probable sales price. A broker performing a BPO or CMA to determine an estimated “*probable selling price or leasing price*” is now *required* to utilize methods involving the analysis of income where appropriate (i.e., income capitalization or gross rent multiplier methodology for income-producing properties) as well as the sales comparison method. [G.S. §93A-83(c)(3) and Commission Rule A.2202(e)]

**Competence to Perform BPO/CMA.** Although Article 6 of the License Law and Section A.2200 of the Commission’s rules do not specifically require a broker to perform a BPO/CMA in **competent** manner, the reader should remember that the License Law has always made incompetence a basis for disciplinary action and those provisions also apply to the performance of BPOs and CMAs. If a broker is not qualified by way of education and experience to properly utilize the appropriate methodology required for a particular property (for example, income capitalization for a commercial property), then the broker is expected to decline the assignment.

**CMAs/BPOs Performed for NO FEE.** Any broker (*non-provisional or provisional*) has always been permitted to perform a BPO/CMA for any party when NO FEE is charged, and this continues to be the case under the revised law and rules. Note that *the Commission does not consider compensation of a broker for general brokerage services under a brokerage agreement to constitute a “fee” under Article 6 of N.C.G.S. §93A.* “General brokerage services” means services provided under a brokerage agreement to property owners in connection with listing/selling/leasing property and to prospective buyers or tenants in connection with purchasing or leasing a property. Such services include the provision by a licensee of a CMA or BPO. Similarly, the possibility of entering into a brokerage agreement (and earning a brokerage fee) does not constitute a “fee” when a licensee performs a CMA/BPO for a *prospective* client without charging a fee for the CMA/BPO. *It is important for licensees to remember, however, that the Commission expects every CMA/BPO performed by a licensee to be performed in a competent manner and without any undisclosed conflict of interest, even if no fee is received for the CMA/BPO. Thus, as a practical matter, a licensee performing a CMA/BPO for no fee should still look to the standards described in Commission Rule 58A .2202 for guidance regarding the proper performance of a CMA/BPO.*

**For a full explanation of the law and rules governing BPOs and CMAs, and a Sales Comparison Analysis Illustration, the reader is referred to the Commission’s North Carolina Real Estate Manual, which may be ordered through the Commission’s website at [www.ncrec.gov](http://www.ncrec.gov).**