

CAARE Attorney Survey About Residential Real Estate Practices – Executive Summary

Who or what caused the mortgage melt-down? While a lot of attention is being focused on multi-billion dollar Wall Street firms that gambled and lost on risky debt, we believe a **huge underlying cause** that has yet to receive as much rightful blame for this catastrophe is **the real estate industry**. We believe conflicts of interest and self dealing have eroded the foundations of the residential real estate industry to the lasting detriment of consumers, many of whom now find themselves dispossessed of their most important investment, their homes.

In summary, **while real estate brokers were not the single cause of the real estate crisis, widespread practices (or malpractices) within the real estate industry have been a leading contributor.**

We set out to validate this belief with a population that has an uncommonly high level of knowledge about the industry, namely attorneys. On November 14, 2008, we surveyed attorneys attending the Minnesota's Continuing Legal Education Real Estate Institute. They overwhelmingly agreed with our hypothesis (stated above), which this Executive Summary will help you understand more clearly. This survey was informal¹, however, its results are compelling and deserving of much wider national attention.

Although residential real estate agents are required by law to give undivided loyalty to their clients, consumers rarely receive it. Due to powerful and well-funded lobbying, incredibly lax standards are applied to the real estate industry. Brokers routinely engage in practices that constitute outright conflicts of interest that are forbidden in most professions, while consumers unwittingly consent to these practices through the use of disclosure forms which they are "asked" to sign early in the transaction. Here are just a few of the more egregious activities that cause us grave concern.

One-stop Shopping?

Home inspection, home appraisal, mortgage lending, title company and law firms are all vital services that are designed to protect the consumer within the real estate transaction. However in the current structure, "affiliated business arrangements" (AfBAs) are established wherein a real estate brokerage creates cozy alliances with many of these important safeguard services. In fact, many of these AfBA arrangements include so-called separate companies that are **owned** by parent real estate firms, eliminating their ability to provide objective advice and unencumbered service.

We maintain, and our survey results clearly confirm agreement, that rather than protecting consumers, these alliances are designed to do nothing more than smooth out the transaction and protect the interests of the real estate agencies. The real estate industry claims this creates "cost savings" for the consumers but it is our belief that it is nothing more than a way to sell more property, more easily, with the principal benefit going to the realtor and his so-called "partners." We maintain that these AfBAs, by their nature, eliminate competition, increase prices and reduce the quality of service.

What's more, any supposedly independent service provider can be penalized by a realtor who feels he has not done his part to make the deal go through, even going so far as to "look the other way" to avoid disclosing information that might kill the deal. That's right. If an one of these service providers discovers something that might negatively impact the sale, sale price, or mortgage origination, he can be cut off from future business by a spiteful real estate agency. Of course, nowhere is this found in writing, or in explicit company policy. However it is implicit, and it is thoroughly understood by everyone who works at these firms. What kind of motivation is that to do a good and thorough job? And whose interests are being protected?

97% of attorneys agreed that agents **will avoid service providers who are the best at finding problems** – those who earn the label "deal killer." **86%** agreed that service providers are **motivated to protect the agent's commission rather than the integrity of the transaction**. And **93%** agreed that this process **diminishes important safeguards** for the consumer.

In the agent/broker licensing scheme, brokers have a statutory obligation to supervise their agents to the benefit of the client. However in many places, and for many years, that supervision is nothing more than self-serving, protecting the firm's profits, rather than the consumer.

84% of attorneys say that **brokers abuse their responsibility by encouraging agents to use their AfBAs**.

88% of attorneys surveyed felt **agents are likely to feel pressure to steer clients to the brokers' AfBAs**.

92% of the attorneys surveyed felt that disallowing current affiliated business and service provider selection practices would result in a **more competitive marketplace that benefits consumers**.

¹ See "Methodology," on the following page.

Dual Agency

This is the ultimate “bait and switch” in real estate. Imagine hiring an agent who promises to represent your interests but who in reality is only looking after his own. Dual agency allows real estate agents to represent **both the buyer and the seller**, creating an inherent conflict of interest. Because of this, buyers and sellers are placed in a situation where **neither** has an effective representative who will advocate for their individual interests. It's like having no agency at all. In virtually any other type of complex legal transaction this conflict of interest would be unthinkable. Why is real estate exempt? Because the industry has done an outstanding job of painting this situation as somehow being in consumers' best interest, and has effectively lobbied for legislation to make it a legal practice.

What's the alternative? Real estate firms that represent buyers, **or** sellers, **not both**. **72%** of the attorneys we surveyed feel this **would benefit consumers**. This entrepreneurial market innovation was snuffed out by the Realtor Association, who gave us the now entirely legal, and totally anti-consumer, practice called “Dual Agency.”

A majority of the attorneys (**57%**) feel that **dual agency should be completely banned** from real estate.

Many more (**79%**) feel that the minimal real estate licensing education requirements are **insufficient to manage dual agency**.

Still more (**85%**) feel that the forms used to disclose dual agency are **inadequate**.

Unauthorized Practice of Law

Practicing law without a license is a misdemeanor in many states, yet it's quite common in real estate in the form of legal opinions and the preparation documents that go far beyond “filling in the blanks.” Should real estate agents (who aren't even required to have a high school diploma to get a real estate license in many states) be providing legal advice?

84% of the attorneys we surveyed felt that real estate agents **routinely engaged in the unauthorized practice of law**.

87% of attorneys felt that realtor-drafted “**free-hand**” **clauses were often voidable or seriously defective**.

Conclusion

Would the mortgage meltdown have occurred if safeguard industries were independent, separate, and unaffiliated from commissioned real estate brokerage firms? While we will never know for sure, it seems much less probable. We believe that inappropriate business activities on the part of realtors were key facilitators of the crisis. And **84%** of the attorneys surveyed agreed with us.

If you agree that these conflicts of interest are harmful, and have contributed mightily to the underlying cause of our nation's financial woes (in combination with a host of other insane and unscrupulous activities), then please join us in attempting to bring this shameful situation to light.

The real estate industry is powerful and extremely well-funded, but these anti-consumer business practices must be halted.

Survey Methodology

On November 14, 2008, approximately 1200 attorneys attended Minnesota's Continuing Legal Education Real Estate Institute. Of this larger group, approximately 400 participants were given the survey. From this subset, 98 responses were gathered, representing a response rate of 24.5%, which we believe is statistically valid. Respondents were not coached in any way, and the survey was not a primary, or required, activity. The survey was wholly optional and done at the discretion of the respondents, who received no incentive, cash or otherwise, for completing it.

While these findings have not been validated or audited by any third party research firm, they are accurate to the best of our knowledge.

In the following table, the numbers listed in *italics* are the actual number of responses in each category, while numbers in **bold** indicate the percentiles.

Survey Results from November 14th, 2008 Minnesota CLE Real Estate Institute

Please give us your opinions on the following statements:		Strongly Agree	Agree	Disagree	Strongly Disagree	TOTAL	Majority Agree/Disagree
1.	Current education and training for real estate licensing is adequate to understand and manage dual agency.	0	20 21%	54 57%	21 22%	95	75DA 79%
2.	Dual agency disclosure forms do an adequate job of disclosing conflicts of interest.	1 1%	14 14%	61 63%	21 22%	97	82 DA 85%
3.	Dual agency, disclosed or otherwise, should be prohibited in residential real estate.	21 22%	33 35%	38 40%	3 3%	95	54 A 57%
4.	Consumers would be better represented if the sellers were represented by buyer only or seller only brokerage firms.	22 23%	46 48%	25 26%	2 2%	95	68A 72%
5.	Real estate agents routinely engage in the unauthorized practice of law.	40 42%	40 42%	13 14%	2 2%	95	80A 84%
6.	Contract clauses that are "free hand" drafted by real estate agents are often voidable or seriously defective.	33 34%	50 52%	12 13%	1 1%	96	83A 87%
7.	When real estate agents (who only get paid if a transaction closes) select the service providers who are supposed to provide safeguards to the transaction:						
	a. Agents are more likely to select service providers who are not "deal killers."	45 46%	49 51%	3 3%	0	97	94 A 97%
	b. Service providers have a motivation to safeguard the referrer's commission rather than the transaction.	33 34%	50 52%	13 14%	0	96	83A 86%
	c. Important safeguards are likely to be diminished.	37 39%	51 54%	7 7%	0	95	88 A 93%
8.	It is appropriate and in the consumers' best interest for real estate agents to select service providers such as:						
	a. Home inspectors.	3 3%	24 26%	45 49%	20 22%	92	65DA 71%
	b. Loan officers.	2 2%	20 22%	46 52%	21 24%	89	67A 70%
	c. Title companies.	3 3%	25 27%	39 42%	25 27%	92	64DA 70%
	d. Real estate attorneys.	4 4%	20 22%	46 50%	22 24%	92	68 74%
9.	It is appropriate for real estate brokerage firms to engage in affiliated (aka controlled) business practices with service providers such as:						
	a. Loan officers.	2 2%	16 16%	38 39%	42 43%	98	80DA 82%
	b. Title companies.	3 3%	16 16%	37 38%	42 43%	98	79DA 81%
10.	A broker abuses their statutory supervisory responsibility when they encourage their agents to use the broker's affiliated business arrangements.	30 32%	49 52%	15 16%	0	94	79 84%
11.	Since the broker controls the real estate agent's compensation, that relationship creates inappropriate pressures to steer clients to the broker's affiliated business arrangements.	32 33%	53 55%	11 11%	1 1%	97	85A 88%
12.	Disallowing affiliated (aka controlled) business practices would result in a real estate marketplace that is more competitive, and more in favor of consumers.	30 32%	57 60%	6 6%	2 2%	95	87A 92%
13.	Affiliated businesses and service provider selection practices eroded the checks and balances in real estate and contributed to the current "mortgage meltdown."	34 37%	43 47%	11 12%	4 4%	92	77 84%