



MICHIGAN ASSOCIATION OF  
**REALTORS®**

## **2010 Association Legal Issues Update**

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## A PRIMER ON SHORT SALES

When the sale price of a home is not enough to cover the mortgage(s) on the home, the sale can only close if one of two things happen: either the sellers bring money to the closing or the sellers' lender agrees to take less than the amount owed. While in both situations, the sale price is "short," it is the second situation that is commonly referred to as a "short sale."

Perhaps the most important thing to keep in mind with respect to short sales is that a lender is not required to take less than the balance owed. Moreover, when the lender receives a request to consent to a short sale, the lender is not required to respond quickly or even at all. Because the approval of a short sale is wholly discretionary, a lender can ignore the request, reject the request, or approve the request subject to a whole list of conditions. If the lender approves the sale, in order for the transaction to proceed, the sellers and the buyers must agree to any conditions imposed by the lender.

Sellers and buyers frequently ask under what circumstances a lender will approve a short sale. There is no correct answer to that question. Different lenders apply different rules. Employees within the same lending institution may look at the same rule differently. Lenders themselves often change their own rules from month-to-month or even week-to-week.

In a perfectly rational world, lenders would always approve a short sale in those instances where the proceeds that the lender will receive from the short sale exceed the amount that the lender would receive if it foreclosed the home and pursued the sellers for the shortfall. But even in this rational world, in order to make such an analysis, a lender must be comfortable that it has accurate information both as to the value of the home and the sellers' financial condition. Typically, much of the short sale process is focused on convincing a lender that it has accurate information and that based on this information, the short sale should be approved.

In some cases, a seller may accept multiple offers to purchase, making them all contingent upon approval by the seller's lender and the seller's approval of the lender's terms. While this practice is discouraged because of potential inherent risks to the seller in accepting multiple offers, it does occur. The buyer making the highest-cash offer or what that buyer may view as the best offer, may believe they are entitled by law to purchase the property. That is not the case. The lender can approve any offer based on numerous factors

other than the offering price. There is no law requiring the lender to accept the highest or best offer in the eyes of a buyer.

In the real world, a lender will never simply approve a short sale; instead, the lender will approve the short sale subject to a whole list of conditions. Often the document setting forth the lender's "conditions" is longer than the purchase agreement itself. Keep in mind that this lender approval document is not "boilerplate" and should be read carefully by both the buyer and the seller. While these "conditions" are seldom negotiable, buyers and sellers are well-advised to seek the assistance of counsel in order to clearly understand their rights and obligations should they choose to accept the lender's conditions.

Remember, there are few laws that regulate the terms of a home sale transaction; rather, the transaction is governed by the terms of the sales contract. Over the years, many terms have become so standard that many people assume that they are dictated by law, when in fact they are nothing more than typical contract terms for the purchase of a home. Often times the "conditions" that a lender imposes when it approves a short sale expressly alter some of these typical contract terms. It is therefore critical that these "conditions" be reviewed very carefully. Again, it is unlikely that a party will be able to get a lender to change any of these provisions; nonetheless, a party needs to understand these "conditions" when analyzing the transaction. For example, a buyer who has negotiated what he believes to be a great short sale price on a home should take into account the seller's expenses that he is being required to assume when comparing that transaction to a standard home purchase.

It is also likely that a short sale buyer will be purchasing a home that may need numerous repairs. A lender's conditions for approving a short sale typically provide that the buyer has no recourse in the event that there were misrepresentations made as to the condition of the home and/or material defects that the sellers did not disclose. Moreover, sellers who have been facing foreclosure for many months typically have not had the funds (or the desire) to properly maintain the property. A short sale buyer is well-advised to have the home carefully inspected.

Finally, the lender's approval of a short sale typically includes a provision which states that the lender can terminate the transaction for any number of reasons right up until the time of closing. For this reason, a short sale buyer is well-advised to keep his options open until the transaction is finally closed. A buyer with a moving truck in the driveway the day before

closing will be in a very difficult position if the transaction fails to close.

Attached to this Article are two contract addendums for use in short sale situations. The first, a Short Sale Addendum to Listing Contract, is attached as Exhibit A. The second, a Short Sale Addendum to a Buy and Sell Agreement, is attached as Exhibit B.

## EXHIBIT A

### SHORT SALE ADDENDUM TO LISTING CONTRACT

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#### PROPERTY

**THIS ADDENDUM** is to be part of and incorporated into a Listing contract between \_\_\_\_\_ as Listing REALTOR®/Broker and \_\_\_\_\_ as Seller, dated \_\_\_\_\_, 20\_\_, regarding the above-captioned Property.

It is acknowledged by the parties hereto that the sale price may not be sufficient to pay the balance(s) owed on all debt secured by the Property and, accordingly, it may be necessary to attempt to negotiate a short sale with Seller's mortgagee(s) and other lienholder(s) (hereafter "mortgagee(s)").

Seller acknowledges that while agents of REALTOR®/Broker may, at the direction of the Seller, assist Seller in such negotiations, Seller understands that neither REALTOR®/Broker nor any agent of REALTOR®/Broker can provide legal advice or financial advice. Seller acknowledges that REALTOR®/Broker has advised Seller to consult with an attorney as to any such transaction and specifically as to any continued liability on any existing mortgage that may be owed to Seller's mortgagee(s) after such transaction. Seller should not assume that the mortgagee(s) approval of the short sale, acceptance of a lesser amount and the granting of a discharge of mortgage will release the Seller from any obligation to pay the mortgagee(s) for any deficiency or difference between the amounts owed to the mortgagee(s) and the amount paid to the mortgagee(s) at closing.

Listed by: \_\_\_\_\_  
Agent Seller

Agent for: \_\_\_\_\_  
REALTOR®/Broker Seller

Date: \_\_\_\_\_ Date: \_\_\_\_\_

## EXHIBIT B

### SHORT SALE ADDENDUM TO BUY AND SELL AGREEMENT

Date: \_\_\_\_\_, covering Property located at \_\_\_\_\_  
\_\_\_\_\_ between \_\_\_\_\_  
Seller and \_\_\_\_\_ Buyer for the Property commonly  
known as \_\_\_\_\_, this  
Addendum to be deemed part of the attached Buy and Sell Agreement (the  
"Agreement").

1. The sale of the Property is subject to and contingent upon the written agreement of the Seller's mortgagee(s) and any other lienholder(s) (hereafter "mortgagee(s)") to accept less than the amount(s) owed. Moreover, this sale of the Property is contingent upon the Seller's acceptance of any conditions imposed by such mortgagee(s). The parties acknowledge that neither Seller nor Seller's agent can compel any mortgagee or lienholder to agree to accept less than the amount owed or even to respond to such a request.
2. In the event all mortgagee(s) do not consent to the short sale or Seller is unwilling to agree to the conditions imposed by any mortgagee(s), Seller reserves the right to terminate the Agreement, in which event the earnest money shall be refunded to Buyer and neither party shall have any further rights or obligations hereunder.
3. Buyer reserves the right to terminate this Agreement at any time if all mortgagee(s) have not consented to this transaction, in writing, within \_\_\_\_\_ days from the acceptance of the Agreement by Buyer and Seller, in which event the earnest money deposit shall be refunded to Buyer and neither party shall have any further rights or obligations hereunder.
4. In the event of termination of the Agreement pursuant to Paragraph 2 or 3 above, neither party will have any liability to the other party for any expenses incurred by that party in anticipation of closing.

5. All timeframes referenced in the inspection clause in the Agreement shall commence upon:  
 (select one)  receipt of all mortgagee(s)' written consent.  
 acceptance of the Agreement by Buyer and Seller.
6. The Property shall be reported with the local multiple listing service as a "pending sale" upon acceptance of the Agreement by Buyer and Seller.
7. All parties acknowledge that they have been advised to obtain legal advice concerning the terms of a short sale transaction and professional tax advice regarding the tax implications of such a transaction. Seller specifically acknowledges that no agent has made any representation with respect to any continued liability on any existing mortgage or lien and that Seller has been advised to seek legal advice on this issue. Seller should not assume that the mortgagee(s) approval of the short sale, acceptance of a lesser amount and the granting of a discharge of mortgage will release the Seller from any obligation to pay the mortgagee(s) for any deficiency or difference between the amounts owed to the mortgagee(s) and the amount paid to the mortgagee(s) at closing.

\_\_\_\_\_  
 Seller Date

\_\_\_\_\_  
 Buyer Date

\_\_\_\_\_  
 Seller Date

\_\_\_\_\_  
 Buyer Date

## **CALCULATING COMMISSIONS BASED UPON “NET SALE PRICE”**

An ever-increasing number of REALTORS® have inquired as to how they can require a cooperating broker to accept commission calculated on the “net sale price.” As we understand it, the concern has arisen as a result of the fact that more and more buyers are requesting significant concessions in the form of, for example, seller paid closing costs and/or remodeling credits. As the concession amount increases, many sellers are objecting to including the value of these concessions in the purchase price for purposes of calculating the commission.

First and foremost, it is important to understand that it is not enough for the listing brokers to simply include a provision in their listing agreement stating that the commission will be based upon “net sale proceeds.” The fact that the listing contract provides for a calculation of the total commission amount based upon the “net,” will only reduce the amount that the seller is obligated to pay. It will not automatically reduce the amount that the listing broker will be obligated to pay the cooperating broker.

Consider the following hypothetical:

Listing agreement provides that seller will pay a commission equal to 6% of the “net sale price.” In the MLS, listing broker offers cooperating agents a 3% commission. Seller receives an offer for \$200,000 that requires the seller to give the purchaser a \$10,000 remodeling credit and to pay purchaser’s closing costs up to \$4,000. Understanding that his commission obligation is limited to 6% of the “net sale price,” seller accepts this offer. Listing broker then advises the cooperating broker that the commission will be calculated based on the “net sale price.” The cooperating broker refuses to agree to this commission amount. Seller will only owe the listing broker a 6% commission based upon the “net sale price,” *i.e.*, \$11,160; but the listing broker will owe the cooperating broker a commission equal to 3% of the “gross sale price,” *i.e.*, \$6,000.

How then does the listing broker require the cooperating broker to agree that the commission will be calculated based upon the “net?” In the context of a particular transaction, this can be handled fairly easily. A seller who has received an offer that contains significant concessions may decide that such offer is acceptable ONLY if the commission will be calculated based upon the sale price less the concession amount. If so, and if that commission adjustment is acceptable to the listing broker, then the listing broker should contact the cooperating broker on behalf of the seller to see whether the cooperating broker will also agree. This discussion should take place and be reduced to writing prior to the seller’s acceptance of the buyer’s offer.

Instead of working through this issue on a transaction-by-transaction basis, can the listing broker simply indicate in the MLS listing that in all instances the amount of seller concessions will be deducted from the purchase price for purposes of calculating the commission? The answer is “yes,” but if, and only if, the MLS has a rule expressly permitting such a practice. Until recently, NAR’s MLS Model Rules provided that an offer of compensation must be either: (a) based on a percentage of the gross sales price; or (b) a stated dollar amount. In May of 2008, NAR amended its model MLS rules to say that a local MLS may also choose to allow participants to offer compensation as a percentage of the net sales price defined as the gross sale price minus buyer upgrades (in the case of new construction) and seller concessions (as defined by the MLS).

It should be noted that while to REALTOR® members, the term “net sales price” clearly means the gross sales price less seller concessions, this is not quite so obvious to people outside of the REALTOR® community. To many people outside of the industry, “net” is synonymous with “profit” and, therefore, the “net sales price” would be the gross purchase price less all payouts. This would include the payoff of the seller’s mortgage. Thus, for example, if the sales price was \$200,000 and closing costs and payoff of the seller’s mortgage totals \$190,000, then the commission would be calculated based on a “net” of \$10,000. For this reason, both MLS policy and listing contracts should indicate exactly what expenses will be deducted for purposes of calculating the “net sale price.”

An MLS who wants to permit commissions based upon the net sales price should have a policy that provides along the lines of:

The compensation specified on listings published by the MLS shall be shown in one of the following forms:

1. by showing a percentage of the gross selling price;
2. by showing a definite dollar amount;  
or
3. by showing a percentage of the net sale price. "Net sale price" shall mean the gross sale price minus: (a) buyer upgrades in the event of new construction; and (b) seller concessions. "Seller concessions" shall mean . . . [insert definition].

The MLS policy will then need to insert a definition for "seller concessions." Sample definitions of "seller concessions" that we have located include:

1. Anything of value added to the transaction by the seller for which the buyer pays nothing additional and which the seller is not customarily expected to pay or provide.
2. Any costs of the buyer that the seller pays on behalf of the buyer, such as any buyer's closing costs and remodeling credits.
3. Anything of value added to the transaction by the seller.

In summary, it would appear that a number of MLSs around the State permit a REALTOR® to offer compensation calculated on the “net sales price.” These MLSs would be well-advised to adopt a formal rule which expressly permits such practice and, in doing so, explicitly defines both “net sales price” and “seller concessions.”

Where an MLS does not permit such a practice, any agreement with the cooperating broker to calculate the commission on the net sales price must be done in writing prior to the time the seller agrees to provide seller concessions.

## **ADMINISTRATIVE FEES: A NEW RESPA RISK?**

On April 20, 2009, a federal judge in Alabama ruled that a broker's "administrative brokerage commission" fee of \$149 per transaction violated Section 8(b) of RESPA. *Busby v JRHBW Realty, Inc d/b/a Realty South*, unpublished opinion of the Northern District of Alabama, issued April 20, 2009 (No. 2:04-CV-2799-VEH). The judge concluded that this particular fee had not been charged "in exchange for" the performance of any actual services. This decision received national publicity, sending shockwaves through the brokerage community.

We have received many inquiries as to how this decision affects Michigan brokers with regard to fees charged at closing attributable to general brokerage services and/or overhead expenses. As will be discussed below, it is our opinion first that the Alabama decision was incorrect and, second, that brokers in Michigan do not need to change their practices as a result of this decision.

In order to appreciate the significance of the *Busby* decision, it may be helpful to understand the background.

Section 8(b) of RESPA provides in pertinent part:

No person shall give and no person shall accept any portion, split, or percentage of any charge made or received for the rendering of a real estate settlement service in connection with a transaction involving a federally related mortgage loan, other than for services actually performed.

Section 8(b) of RESPA was long understood to prohibit two or more persons from splitting a fee for settlement services where part or all of one provider's share of the fee is not in return for goods or facilities actually furnished or services actually performed. In other words, traditionally it was assumed that in order for there to be a Section 8(b) violation, there must be some type of fee splitting arrangement.

In October 2001, HUD issued a formal policy statement indicating that Section 8(b) would not just apply in fee splitting situations. HUD indicated that Section 8(b) could also be violated if one settlement service provider marks up the cost of goods or services obtained from a third party and keeps the difference

without providing actual goods or services to justify the additional charge. For example, a lender obtains a credit report for \$20 and on the closing statement charges the borrower \$40 for the credit report, without doing anything more. This type of charge has been referred to by courts as a “mark-up.”

In the same policy statement, HUD indicated that Section 8(b) could also be violated where one settlement service provider imposes an “overcharge” – *i.e.*, a fee for no, nominal or duplicative work – or a fee that exceeds the reasonable value of the goods or services provided. For example, a lender charges a borrower an “escrow waiver fee” of \$100 in order to be released from the lender’s customary property tax escrow requirement. This type of charge has been referred to by courts as an “overcharge.”

Again, the issue in the *Busby* case was a flat administrative fee charged by the broker in addition to the percentage commission amount. The plaintiff-buyer argued that the fee was an illegal overcharge “for no, nominal or duplicative work.” The Court agreed and said that the administrative brokerage commission fee of \$149 was an “overcharge” prohibited under Section 8(b) of RESPA.

It must be remembered that the *Busby* decision was an unreported decision of the District Court in the Northern District of Alabama. The federal court system consists of twelve circuits, each with their own Court of Appeals, which each in turn have a number of lower courts known as district courts. (See Exhibit A.) Prior to the April 2009 decision by the Alabama court, only one of twelve of the Federal Circuit Courts of Appeals had explicitly held that an “overcharge” constituted a violation of Section 8(b) of RESPA. On the other hand, four federal circuits had explicitly held that an “overcharge” does not constitute a violation of Section 8(b). (The remaining circuits have not yet directly addressed the issue.) Fortunately for Michigan REALTORS®, they are governed by the law of the Sixth Circuit, which is one of the federal circuits that has held that an “overcharge” does not constitute a violation of Section 8(b).<sup>1</sup>

Even in the unlikely event a federal court in Michigan would someday conclude that an “overcharge” is covered by Section 8(b) of RESPA, an administrative fee would still be permissible unless the court went on to conclude

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<sup>1</sup> The decision was *Molosky v Washington Mut Bank*, unpublished opinion of the Eastern District of Michigan, issued January 18, 2008 (No. 07-CV-11247). The Sixth Circuit Court of Appeals has not yet addressed the issue.

that the administrative fee charged by a broker was not provided “in exchange for” the performance of any actual services.

The broker in the *Busby* case had argued that the administrative fee was simply an increase in the price or fee that the company charged for all of its brokerage services:

*In short, while called two different names, the percentage based commission and the administrative brokerage commission are what it collectively costs a buyer (or seller) to do business with [the company].*

The broker argued further that the costs that the fee helped to pay for included: “complying with various regulatory requirements, providing consumers with both standard and increased services, including, among other things, *providing facilities, offices, equipment, a far more functional and enhanced website and other technological departments, greater availability of information along with a better ability to search for and access such information, and contracts and other business forms for its agents and customers, just to name a few.*”

The *Busby* court erroneously concluded that Section 8(b) of RESPA requires that all charges must reflect a direct benefit to the customer and cannot, for example, be justified on the basis that the charges help defray overhead expenses. It is our opinion that this analysis is illogical and unlikely to be duplicated by other federal courts.

As correctly pointed out by NAR and others, the trial judge in *Busby* seemed to be particularly troubled by the fact that the total compensation was listed in two separate places in the agency contract and on the settlement form. That is, the fact that the broker referred to the percentage-based compensation in one place and the flat administrative fee in another place, caused the court to erroneously conclude that the administrative fee was duplicative and that the plaintiff-buyer had paid for the same service twice. In order to avoid this problem in the future, NAR has recommended to REALTORS® around the country that they may want to change the way they characterize their compensation:

Placing separate labels on what is all compensation to the brokerage firm exposes the firm to the same claims asserted against the defendant [in the *Busby* case]. It

allows the conclusion that each separately labeled charge represents a fee for a separate service. Likewise, disclosing separate components of the broker's compensation in different parts of the contract with the consumer or on different lines of the settlement statements creates risk. Disclosure of the brokerage firm's compensation should clearly indicate that both the commission-based component and the flat fee component represent payment for services provided by the brokerage. These combined amounts should be disclosed in the 700 section of the HUD-1 as the broker's compensation. Finally, do not create the impression that any particular fee is for a separate service if that is not the case.<sup>2</sup>

While in the interest of caution, Michigan REALTORS® may wish to adopt this practice as it is fairly easy to implement, it is our opinion that Michigan REALTORS® should not spend too much time and energy worrying about this one unreported decision from a federal district court in Alabama.

As an aside, several months after the *Busby* decision, a district court in Louisiana faced very similar arguments with respect to various fees that had been charged by a lender in connection with a mortgage loan. *Freeman v Quicken Loans*, unpublished opinion of the Eastern District of Louisiana, issued Aug 10, 2009 (Nos. 08-1626, 08-1627, 08-4744). The Louisiana court first went through an extensive analysis of the law in all of the federal circuits and found that it agreed with the majority of courts that have concluded that Section 8(b) of RESPA was only intended to apply to unearned split fees and not to either "markups" or "overcharges." For some reason, this more recent case did not generate anywhere near the amount of discussion as the *Busby* decision.

In sum, brokers in Michigan may continue to charge administrative fees which even if they were viewed an "overcharge" by a court. These fees do not constitute a violation under Section 8(b) of RESPA as interpreted within the Sixth

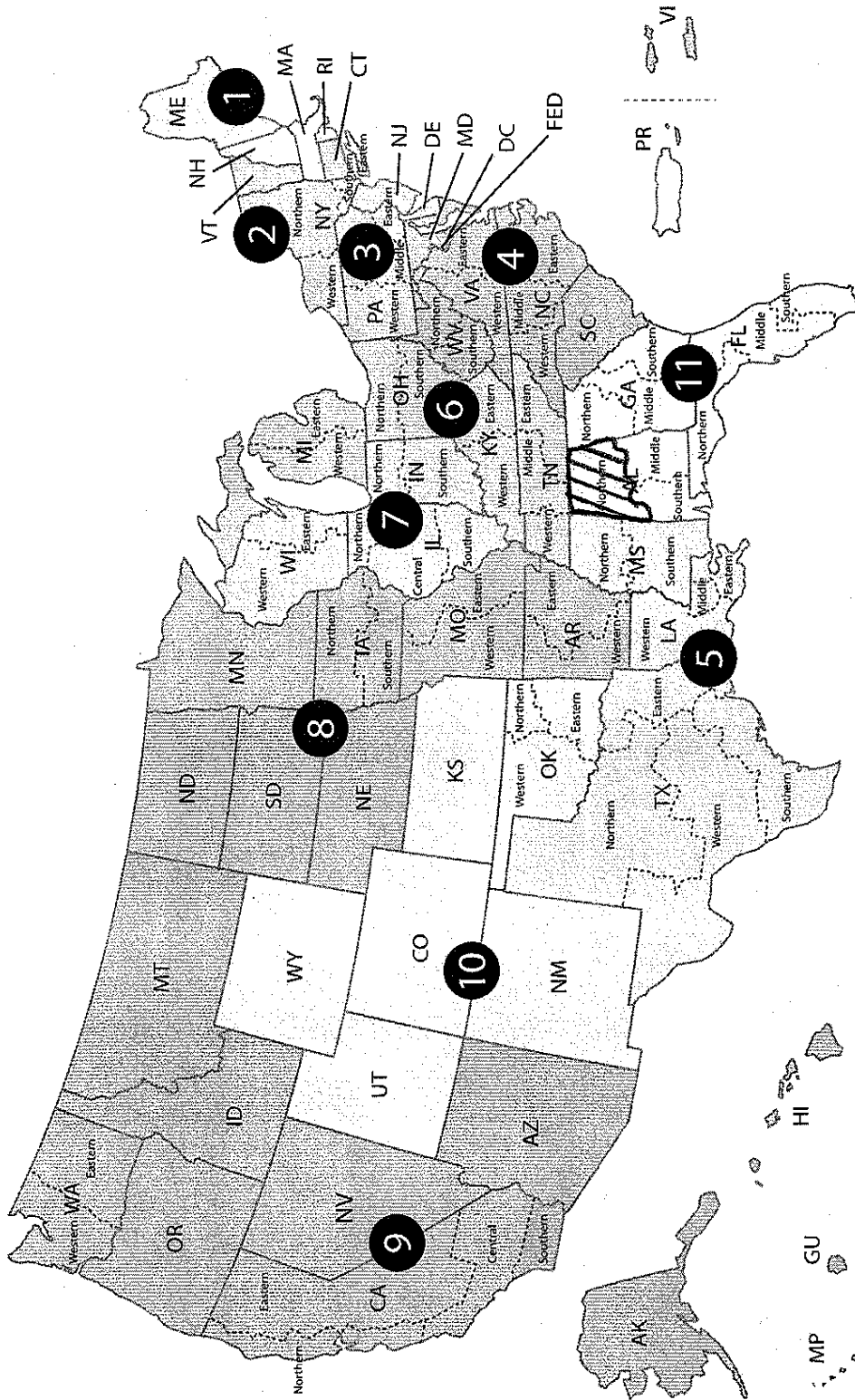
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<sup>2</sup> Janik, Laurie. *Price Increase or Unearned Fee? How to Protect Your Bottom Line* (April 29, 2009).

Circuit. No decision made by a federal court outside of the Sixth Circuit can change the law in Michigan, other than the United States Supreme Court, which has not yet addressed the issue. The charging of so-called administrative, processing or closing fees is still governed by the market in Michigan. In other words, Michigan brokers may charge these types of fees so long as the public is willing to pay them.

# Geographic Boundaries

of United States Courts of Appeals and United States District Courts



- 1. ME, NH, MA, RI
- 2. VT, NY, CT
- 3. PA, NJ, DE
- 4. MD, WV, VA, NC, SC

- 5. TX, LA, MS
- 6. MI, OH, KY, TN
- 7. WI, IL, IN
- 8. ND, SD, NE, MN, IA, MO, AR

- 9. WA, OR, CA, ID, MT, NV, AZ, AK, HI
- 10. WY, UT, CO, NM, KS, OK
- 11. AL, GA, FL

## ELECTRONIC TRANSACTIONS

In 2000, Michigan joined what is now the vast majority of states that have passed the Uniform Electronic Transactions Act, MCL 450.831, *et seq.* (“UETA”). UETA makes electronic signatures as legally valid as handwritten signatures (with a few exceptions not relevant to our discussion). UETA is a procedural statute; it does not mandate the use of electronic means to conduct transactions, nor the use of electronic signatures, but seeks only to cover those situations in which they are voluntarily used. UETA states quite clearly that the statute only applies where all parties have agreed to conduct business electronically and that consent may be determined from the conduct of the parties. MCL 450.835.

The term “electronic signature” includes any method by which an “electronic sound, symbol or process” is “logically associated” with a contract and adopted by a person “with an intent to sign.” An “electronic signature” would include, for example, a scanned copy of a handwritten signature. There is also software that can capture a person’s handwritten signature and embed it into a document. The term “electronic signature” also includes a digital signature which typically does not involve any type of replication or copying of a person’s handwritten signature. Digital signatures may be self-signed or may be purchased from third parties who provide validation of the signature each time it is used. A self-signed signature relies on the security of a person’s email account. That is, the recipient assumes that the sender has exclusive access to his/her own email account. Of course, that is the same assumption that many of us make each day when we exchange emails with our clients and customers.

For many purposes, reliance on the assumption that a person has exclusive access to his/her own email account does not provide enough security. In this instance, the parties choose to involve a third party provider who will provide validation each time the digital signature is used. With these third party providers, the digital signature is an encrypted block of text. The text block is created by the signer with a private code and used to authenticate the signature and the material it is attached to. (This is much the same as using an ATM card; when you enter your PIN in combination with your magnetic coded card, the bank knows it is you and acts upon your directions to withdraw, deposit, or transfer money.) Since the private code is known only by the person named in the certificate, it is reasoned

that the digital signature must have been created by that particular person. The certification authority also issues a separate public code which anyone else can then use to check the authenticity of the digital signature.

The advantage of using this type of digital signature is that once the process is set up and a particular person's signature is validated, the future exchange of documents signed by that person is both simple and extremely reliable. The digitally signed document is "locked" so that the recipient will know the date and time the document was signed and whether the document has been changed since the time it was signed. The major disadvantage of using digitally signed documents is that the steps needed to initially validate a person's signature are somewhat cumbersome.

Currently, the most common use of encrypted digital signatures is within an organization or between two or more organizations that regularly share information. The participants are given codes which enable them to encrypt messages before sending them to another participant and then enable the recipient to decode the information once it is received. It may also be convenient for two persons who regularly exchange information requiring signatures to set up a system by which each of them can verify that the other has signed the document and that it has not been changed since the time it was signed.

On occasion, we have been asked if a REALTOR® receives a document that has been digitally signed, may the REALTOR® rely on the certification authority? What if the signer has not used a certification authority and has simply "self-signed" the document?

Before we address these questions, let's examine how we handle documents with handwritten signatures. If a fellow REALTOR® hand delivers to you, as listing agent, an offer that has been signed by "Joseph Smith," would you take any steps to verify that "Joseph Smith" signed the document or that "Joseph Smith" even exists? It is likely that you would not. Instead, you would assume that your fellow REALTOR® had worked with a person who that member knew or reasonably believed to be "Joseph Smith" and that the REALTOR® either witnessed "Joseph Smith" sign the purchase offer or had reason to believe that "Joseph Smith" signed the document.

If you were the selling REALTOR® who had been working with "Joseph Smith" directly, even if you had not actually seen "Joseph Smith" sign the offer, you might

rely on the circumstances surrounding the signature – *i.e.*, the fact that you faxed the prepared offer to him at his office, discussed it with him over the phone and then received via email a “pdf” of the document with “Joseph Smith’s” signature on it – to conclude that the signature was valid.

Likewise, if you as selling REALTOR® had been working with “Joseph Smith” in connection with a particular home, had sent “Joseph Smith” a prepared offer and received an email from “Joseph Smith” with a digitally signed purchase offer attached, it would seem reasonable for you to conclude that “Joseph Smith” had signed the document, even if the signature was “self-signed.”

If, on the other hand, a REALTOR® arrives at her office one morning and finds a purchase offer in her fax machine from a person she has never dealt with or even heard of, it would seem logical that the REALTOR® should and would take additional steps to verify the identity of the offeror. The same would be true of a digitally signed document that showed up out of the blue.

Where the signature appears also must be considered. To be binding, an electronic signature must be used “with an intent to sign.” On a standard purchase offer form, filled in with all the terms of an offer, a signature in the signature space at the end is certainly almost always “intended to sign” the offer. Other writings may not be so clear. For example, if an email proposes an amendment to an agreement, is the block of text with the sender’s name, address, and phone numbers -- as it appears on every email -- intended as a signature? (Many attorneys now put a disclaimer at the end of their emails reciting that the name at the end of the email is not intended as a signature unless the email says so.) To avoid any misunderstanding, the wording or context should make clear what the sender intends: for example, “I accept your counteroffer. Joseph Smith.”

In summary, whether the document is hand-delivered, faxed or emailed to you, whether the signature is a handwritten signature, a scanned copy of a handwritten signature or a digital signature, the extent of the “verification” required will depend on the circumstances. If a REALTOR® is expecting a signed contract from a person she is working with, no additional verification may be necessary. If she receives a contract unexpectedly from a person she had worked with previously, she may want to place a follow up telephone call or email. If, on the other hand, she receives an offer from a person she has never met or spoken with, it is likely that she will want to investigate the situation further before presenting the offer to the listing REALTOR®.

## **ETHICS PROCEEDINGS AND LITIGATION**

Unfortunately, over the past few years, one Michigan local association of REALTORS® has been involved in four lawsuits initiated by two of its members after those members were found to have violated NAR's Code of Ethics (the "Code"). Fortunately, as a result of these lawsuits, as long as a local association substantially complies with the provisions of the Code of Ethics and Arbitration Manual, as amended to conform with Michigan law (the "Manual"), that association can proceed with confidence even when threatened with lawsuits by members who are unhappy with the results of an ethics or arbitration proceeding.

The first of the four lawsuits has been the subject of a prior article. This lawsuit involved claims by former REALTOR® Dean Borland ("Borland") against the West Michigan Lakeshore Association of REALTORS® ("WMLAR"). Borland filed his initial complaint against WMLAR on February 28, 2006 in the Circuit Court. In his complaint, Borland alleged that in addition to acting as a real estate agent, he "rents houses, townhomes, and condominiums to tourists for vacation use." It was Borland's vacation rental activities that resulted in the ethics complaint against him.

The ethics proceedings resulted in Borland receiving a written reprimand and sanctions. In his Circuit Court complaint, Borland claimed that the "rental and management of transient vacation accommodations" did not constitute transactions in real estate as defined in the Manual. Thus, Borland claimed that the agreement to abide by the Code contained in his signed membership application did not apply to the "rental and management of transient vacation accommodations" and that WMLAR did not have jurisdiction to discipline him in connection with this type of activity. Borland was, in essence, asking the Circuit Court to intervene and set aside the decision of the WMLAR ethics panel as affirmed by its Board of Directors.

The Circuit Court granted WMLAR summary disposition as against Borland, finding that the real estate activities which were the subject of the ethics complaint were covered by the Code. Borland then appealed to the Michigan Court of Appeals.

The Michigan Court of Appeals affirmed the decision of the Circuit Court and did so on a basis that is beneficial to all Michigan REALTOR® associations. WMLAR had taken the position that its conduct in carrying out the ethics proceeding was not subject to judicial review in light of a waiver contained within the Manual. This waiver provides:

Every member, for and in consideration of his right to invoke arbitration in proceedings and to initiate complaints under the Code of Ethics as a member of the NATIONAL ASSOCIATION OF REALTORS®, hereby waives any right of action against the Board, any Board Member, or any member of a Hearing Panel or tribunal arising out of any decisions, determinations, or other action taken or rendered under these procedures in the absence of willful or wanton misconduct. Further, as a condition of continued membership, every member expressly waives any cause of action for libel, slander, or defamation that might arise from the filing or consideration of any ethics complaint or arbitration request.

The Court of Appeals found in favor of WMLAR and enforced the waiver. The Court held in pertinent part:

We conclude that the court did not err in granting summary disposition to WMLAR because the disciplinary action was not subject to judicial review . . . .

The waiver provision at issue here is unambiguous and clearly reflects an intent to bar a lawsuit such as the one initiated by plaintiff [Borland]. Indeed, there was no evidence of ‘willful or wanton misconduct’ on the part of WMLAR, and plaintiff’s complaint does not even allege such conduct. Under the circumstances, plaintiff [Borland] simply cannot circumvent the Code of Ethics and the rulings of WMLAR by resorting to a lawsuit in the circuit court.

The second lawsuit was a declaratory action brought by WMLAR to obtain judicial approval of its action terminating Borland's membership in WMLAR after he failed to satisfy the sanctions rendered against him in that same ethics proceeding. Borland appeared through counsel in the Circuit Court proceeding and attempted to defend his position. On February 10, 2009, a final order was entered by the Circuit Court declaring that the sanctions against Borland were proper acts by WMLAR pursuant to the Manual and that Borland's expulsion from WMLAR would not violate any of his rights.

The next two lawsuits also arose out of one transaction. In the summer of 2006, WMLAR member, Richard Livingston ("Livingston"), represented seller Dan Miller ("Miller") in a real estate transaction that eventually fell apart. Livingston sued Miller for a commission. Miller filed an ethics complaint against Livingston with WMLAR, alleging various violations of the Code. WMLAR processed Miller's complaint and conducted proceedings pursuant to the Manual.

The ethics panel found that Livingston had not promoted or protected the interest of his client (Miller), had not followed through and had not paid proper attention to detail. Also, the panel found that Livingston did not properly address issues involved in the purchase agreement or listing agreement in a manner that demonstrated that "time is of the essence." While the Manual requires that the decision of an ethics panel be kept confidential, WMLAR obviously could not enforce that restriction against Miller. Miller, in essence, posted the decision of the ethics panel on a website, along with other disparaging comments about Livingston.

Livingston filed a lawsuit against WMLAR in which he claimed that WMLAR had defamed him by making the decision of the ethics panel public.

WMLAR immediately sought summary disposition against Livingston on his defamation claims. WMLAR took the position that Livingston's defamation claim against WMLAR failed for any of at least three reasons. First, Livingston had waived any claims for libel, slander or defamation that might arise from the filing or consideration of any ethics complaint. This is the same defense that was asserted against Borland. Second, WMLAR did not make any defamatory statements about Livingston. Circulation of the ethics panel decision by WMLAR was limited to the complainant, respondent, the association's legal counsel and

appropriate employees, and WMLAR's Board of Directors. The only publication of a defamatory statement was made by Miller. Finally, WMLAR contended that Livingston's defamation claim could not succeed because the decision by the ethics panel was a privileged publication to a third party. In other words, statements made in the context of WMLAR's processing and adjudication of the ethics complaint were protected by a qualified privilege under Michigan law.

WMLAR contended that all elements necessary to establish a qualified privilege were present in this case. Livingston could not allege any fact that would show bad faith on the part of WMLAR. WMLAR was routinely responding to an ethics complaint presented by a member of the public. The processing of the complaint and the ethics proceeding that followed were performed pursuant to an "interest to be upheld." The general public and WMLAR share a compelling interest in maintaining high ethical professional standards by investigating any alleged violations of those standards. Further, distribution of the findings and recommendations of the hearing panel were limited by the Manual to only those who needed to know, *i.e.*, the parties, WMLAR's legal counsel and appropriate employees, and WMLAR's Board of Directors. Limitations on the right to conduct such proceedings would erode that interest. Under the law, statements protected by the privilege must be "limited in scope" to upholding the protected interest. Here, the allegedly defamatory statements specifically related only to the ethics panel's findings regarding Livingston's violations of his duties as a professional under the Code and as such were narrowly tailored to respond to Miller's complaint. Finally, qualified privilege only extends to statements made during a "proper occasion" and published "to proper parties only." Again, the statements were made during WMLAR's processing and adjudication of Miller's complaint pursuant to the Manual.

No Michigan court had yet had the opportunity to address statements made in the context of a REALTOR® association's ethics panel conduct of a hearing and recommendations. However, the Circuit Court was directed to a New York appellate court case in which such statements were found to be subject to the qualified privilege. *Sobol v New York State Assn of REALTORS®*, 235 AD2d 966 (1997).

The Circuit Court found in favor of WMLAR on all three bases asserted by WMLAR for dismissal. Thus, at least one Michigan court (albeit a trial court) has

addressed the issue of whether ethics proceedings conducted pursuant to the Manual are subject to a qualified privilege and cannot form the basis of a libel, slander or defamation claim. Further, this trial court chose to follow the Court of Appeals' decision in *Borland* and enforce the waiver set forth in the Manual.

The fourth case against WMLAR was also filed by Livingston. While Livingston's claims in his complaint are too numerous to list, he basically contended that WMLAR had denied him due process during the ethics proceedings and had engaged in "willful and wanton misconduct." Livingston anticipated WMLAR's assertion of the waiver defense, which was enforced in *Borland* by the Court of Appeals and in the other Livingston litigation. The waiver in the Manual provides that the waiver does not apply if there is "willful or wanton misconduct."

Livingston tried mightily during several hearings to convince the Court that WMLAR had engaged in "willful and wanton misconduct." There are three elements which must be proven in order to prove a claim of "willful and wanton misconduct." In order to prove a claim of "willful and wanton misconduct:"

. . . the plaintiff must establish that the defendant (1) knew of a situation or requiring the exercise of ordinary care and diligence to avert injury to another, (2) had the ability to avoid the resulting harm by ordinary care and diligence in the use of the means at hand, and (3) failed to use such care and diligence to avert the threatened danger, when to the ordinary mind it must be apparent that the result is likely to prove disastrous to another.

*Lamp v Reynolds*, 249 Mich 591; 645 NW2d 311 (2002), citing *Taylor v Laban*, 241 Mich App 449, 457; 616 NW2d 229 (2000), quoting *Miller v Inglis*, 223 Mich App 159, 166; 567 NW2d 253 (1997).

WMLAR substantially complied and followed all procedures set forth in the Manual. Thus, Livingston could not beyond very general, vague and conclusory allegations, demonstrate any "willful or wanton misconduct" by WMLAR. A final order dismissing Livingston's second case against WMLAR was entered by the Circuit Court on December 11, 2009.

These four lawsuits demonstrate that Michigan courts will do the following when faced with claims from members arising from ethics proceedings:

- (1) Enforce the waiver in Section 9 of the Manual, unless the member can show “willful or wanton misconduct” on the part of the association;
- (2) Refuse to find that there has been “willful and wanton misconduct” on the part of the association if it has substantially complied with the procedures and provisions of the Manual; and
- (3) Find that communications in an ethics proceeding are subject to a qualified privilege and cannot form the basis of a defamation claim so long as the association adheres to the provisions of the Manual.