Between the Lines

Insights from the

Real Estate Bulletin

A real estate elective course designed to address some of the most commonly asked questions posed by real estate brokers as published by the N.C. Real Estate Commission in their publication *Real Estate Bulletin* from 2007 to 2017

Compiled & Arranged by:

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George Bell Productions, Ltd.

Between the Lines…

Insights from the Real Estate Bulletin

A real estate elective course
designed to address some of the
most commonly asked questions by real estate licensees,
and
to provide insight into many misunderstood positions
taken by the Commission on transactional matters.

The articles in this book previously appeared in the
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Real Estate Bulletin

(from 2007 to 2017)

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As a North Carolina real estate licensee, you should be familiar with the Real Estate Commission's publication *Real Estate Bulletin*. The first issue of this newsletter was produced in March 1970. This four-hour elective course surveys the Real Estate Commission's position on various issues as appearing in articles published in the *Bulletin* from 2007-2017.

It is believed that many of the current "active" licensees have had their licenses for less than ten years. Furthermore, many licensees admit to not reading *most* of the *Bulletin* – though everyone admits to reading the section titled "Disciplinary Action." While the later admission is good, the former is disturbing, especially when one realizes that the *Bulletin* and the (CE) Update courses are the greatest vehicles the Real Estate Commission has to communicate law and rule changes to licensees. As a result, this elective course attempts to share information "from the past."

The key to understanding the reference information is as follows:

ANS: Answer

REF: References the *Bulletin* volume (Vol.), number (No.), and publication date, as well as the title of the article

As this publication can serve as a valuable resource, each licensee is encouraged to retain this book for future reference as licensees often encounter situations or transactions that involve one of the articles addressed herein. Also, one is encouraged to visit www.ncrec.gov and click on Publications for additional and updated information regarding many of the issues addressed in this book.

THIS IS A TEST!
This is only a test.
But just how smart do you feel?
And what do you think the *Real Estate Bulletin* articles say about…

SECTION ONE: Advertising

T F 1. A broker should be careful not to advertise a property as having more bedrooms than the number permitted by the septic system permit.

T F 2. A broker's advertisement must NOT overstate or exceed the allowed limits and design parameters of the property's sewage disposal system or occupancy permitted by the local municipality.

T F 3. Agents should be aware of the dangers of advertising occupancy levels for any property served by a septic system without first verifying the system's legal capacity

T F 4. A room in a house must have a "clothes closet" to be advertised as a bedroom.

T F 5. The Real Estate Commission requires listing brokers to report square footage.

T F 6. It is okay to use the square footage in tax records or an old appraisal as a source.

T F 7. It is okay for a listing broker to get an appraiser to measure a property being listed.

T F 8. When listing and selling properties in residential subdivisions, especially newly developed subdivisions, brokers should check on the status of the streets (public vs. private), as all streets essentially begin as private streets and some eventually become public streets.

T F 9. The mere presence of a radon mitigation system is not, in and of itself, a material fact.

T F 10. A broker is required by Commission rule to enter into a written brokerage agreement with a seller-client before marketing the seller-client's property, and this includes the use of any "Coming Soon" marketing.

T F 11. My client wants to list now, but she doesn't want a lot of traffic in her home. I'd like to take the listing and place a "Coming Soon" sign in the yard, but not advertise the property in the MLS and only show it to a few buyers I know are interested in her type of property. This way I can generate leads without opening her home to a lot of traffic. My BIC said this is okay.

SECTION TWO: Licensing Matters

T F 12. The number one complaint the Real Estate Commission receives deals with trust monies.

T F 13. Only cases involving sufficient, admissible evidence of a violation of the Real Estate License Law or the Commission's rules result in disciplinary action, and records of complaints filed against licensees are a matter of public record.

T F 14. Common knowledge may be defined as "knowledge that is widely or generally known to everyone or nearly everyone in a community" and, brokers are expected to possess such in the area(s) in which they work as a broker should become an expert on his/her market area.

T F 15. The Commission is a public/governmental agency, and therefore is required to make available to the public my name, email address, and other contact information.

T F 16. Prior to conducting any real estate brokerage services, a real estate licensee must obtain both an individual and/or firm license from the NC Real Estate Commission and a state privilege license from the NC Department of Revenue.

T F 17. Commission rules require the retention of all materials and statements used for the marketing and advertising of a listed property, including but not limited to, all Facebook, Twitter, Instagram and other social media posts that provide information regarding a listed property, and be prepared to reproduce legible hard copies of the posts upon request of the Commission.

T F 18. An unlicensed assistant may lawfully perform each the following acts.

a. Submit listing and changes to MLS
b. Obtain keys for listed properties
c. Record and deposit trust monies
d. Place "for sale" or "for rent" signs on property
e. Show rental properties managed by the broker to prospective tenants
f. Complete and execute preprinted form leases for rental property managed by firm

T F 19. A "full broker" that works alone, from home, and is not a BIC and has no BIC, may lawfully perform the following acts.

a. Solicit properties to list for sale or rent
b. Advertise or otherwise promote his/her real estate services
c. Regularly show properties to prospective buyers or tenants
d. Hold trust monies and/or manage trust accounts
e. List properties (owned by others) for sale or rent

T F 20. If the name of your sole proprietorship (company) does not include your last name, then you must register the name of your sole proprietorship with the Register of Deeds in the county where you intend to do business but there is no need to obtain a firm license from the Commission.

T F 21. Each NC real estate firm must remain current, active, and in good standing with the NC Secretary of State and the Department of Revenue and, if a firm does not satisfy the requirements to remain in good standing with each, yet continues to act as real estate brokers, they may face disciplinary action by the Real Estate Commission.

T F 22. A broker may simultaneously have his/her license affiliated with more than one firm and, when brokers have multiple affiliations, they need to use business cards and forms that identify the correct real estate firm(s) with which the consumer is dealing.

T F 23. When a licensee is convicted of a misdemeanor or who has disciplinary action taken against him/her by an occupational licensing board, the licensee is required to file a report with the Real Estate Commission.

SECTION THREE: Broker Duties & Obligations

T F 24. Any person that operates a "small Unmanned Aircraft System" (sUAS), a.k.a., a drone, for purposes of aerial photography in real estate must obtain a remote pilot certificate issued by the Federal Aviation Administration (FAA).

T F 25. A client may lawfully place a surveillance device in their home to monitor showings, inspections, etc., provided there is no audio turned on.

T F 26. Matters of survey, which relate to anything that could negatively affect the use of property being purchased, may be covered in a "lender's title policy", but generally do not protect the purchaser unless a survey (in the name of the purchaser) is performed prior to issuance of the policy.

T F 27. The accuracy of any survey plat, as a snapshot in time, is only assured by the licensed surveyor on the date of performance of the survey.

T F 28. Brokers who represent prospective buyers and tenants should advise and encourage their clients to order inspections, tests and surveys for properties they wish to buy or lease and should never discourage a client from ordering an inspection, test or survey, even if it is not required.

T F 29. Even if a lender does not require a particular inspection or test, buyers should consider protecting their long-term interests, as an effort to save money and forgo inspections may cost the buyer much more than the cost of the inspection in the long run.

T F 30. If a listing agent does not know for certain the correct facts about septic system use or permitting for a property, the agent must make an adequate investigation of the facts before making any representations about the property.

T F 31. A short sale is a material fact, and therefore a listing broker must disclose this to the buyer and buyer agent.

T F 32. If a listing broker learns a short sale is required after a sales contract is signed, or if the property goes into foreclosure while under contract, the listing broker has a duty to inform the buyer.

SECTION FOUR: Agency & Compensation Issues

T F 33. Practicing dual agency lawfully is challenging because the sellers and buyers must agree to be represented in an adversarial relationship by the same agent. By entering into dual agency without the full understanding and consent of both clients, a broker may unfairly deprive those clients of the level of service they expect to receive.

T F 34. Sellers sometimes offer incentives in the form of cash, vacations, or other prizes to real estate agents, in addition to the sales commission, to promote the sale of their properties. Such incentives, or bonuses, are lawfully permitted so long as they are fully disclosed.

T F 35. A broker in a sales transaction cannot be compensated by his client unless that compensation is provided for in a written agency contract meeting the requirements of Commission rule.

T F 36. A pest control company solicits real estate brokers to join their "Preferred Broker Program." Among other benefits, the company offers all broker participants quarterly pest control services at their personal homes at no charge. In order to receive the free pest control, the broker must refer their buyer clients to the pest control company for the completion of lender-required pest inspections. This is a lawful referral of business.

T F 37. Real property may be offered as a prize in a raffle by certain organizations, but not individuals, provided the maximum appraised value of the real property to be raffled is $500,000.

SECTION FIVE: Closings & CFPB-HUD

T F 38. NC law requires brokers, 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.

T F 39. Lenders are permitted to provide the required Closing Disclosure to real estate agents.

SECTION SIX: Fraud & Scams

T F 40. Licensees should know now that even "little white lies" by a borrower on a mortgage loan application and supporting documentation constitutes mortgage fraud.

T F 41. Brokers should be wary of any down-payment assistance program in which the home seller makes a gift to a purported charity and the buyer receives a gift of roughly the same amount from the charity (minus fees and expenses) to use as a down-payment to buy the seller's house.

T F 42. Due to the proliferation of mortgage loan schemes, the NC Real Estate Commission has created a Financial Fraud Unit to investigate such cases and to work with state and federal law enforcement agencies.

T F 43. North Carolina Statutes govern every option contract executed along with a lease agreement and, among other things, the law dictates that every such option contract contain at least nine specific disclosures and also provides every purchaser a three-day right to cancel such an option contract.

SECTION SEVEN: Appraisal & BPOs

T F 44. There is no prohibition against real estate brokers contacting and "talking" to the appraiser of a property in which the broker represents one (or both) of the parties.

T F 45. A broker who performs a BPO for a fee must provide the BPO in writing, estimating only the "probable selling or leasing price" of a property (not the "value" or "worth" of a property), and the BPO must not be referred to as a "valuation" or "appraisal."

SECTION EIGHT: Commercial Practices

T F 46. As with residential brokerage, commercial brokers must review the Working with Real Estate Agents brochure with prospective buyers and sellers at first substantial contact.

T F 47. The Regulatory Affairs Division of the Commission sees many of the same compliance issues while investigating complaints or conducting audits in commercial practices as in residential practices.

SECTION NINE: Property Management

T F 48. Commission Rules requires brokers to enter into a written property management agreement before beginning to manage an owner-client's property, and the broker must operate within the authority granted by the agreement.

T F 49. The Landlord Tenant Act limits fees a landlord or his property manager may charge when pursuing evictions or monies owed by a tenant, determines the timing of landlord security deposit accounting to tenants, imposes duties on landlords to provide fit premises, and permits tenants to terminate leases early in foreclosure situations.

T F 50. Determining whether a tenant is "qualified" generally involves looking at a prospective tenant's income, credit history, credit score, employment history, rental history, criminal record, etc., and a property manager is obligated to take reasonable measures to ensure that all consumer information is disposed of in a manner that would prevent an unauthorized person from acquiring and using the information.

T F 51. While many property managers may attempt to pre-screen tenants to eliminate unqualified candidates early in the process, it is important that each interested person be provided with an application, and each applicant should receive an identical application form and be asked the same questions.

T F 52. HUD has determined that due to higher than average incarceration rates among certain races relative to their percentage of the total population, the use of criminal background checks to deny housing may actually cause a disparate impact on certain races and therefore be discriminatory.

T F 53. If you discover that the property owner, tenant, seller, or buyer that you represent intends to discriminate based on any of the protected classes, you must immediately consider terminating your agency agreement with that party or risk violating the law and losing your license.

T F 54. The Fair Housing Act (FHA) and the Americans with Disability Act (ADA) makes it illegal to discriminate against a person with a disability by refusing to make reasonable accommodations in rules, policies, practices, or services when it may be necessary to afford an equal opportunity to use and enjoy a dwelling. Making an exception to a no-pets policy for an Assistance Animal as defined in the Act has been held to be a reasonable accommodation.

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Notes

Section One:

Advertising

1. A broker should be careful not to advertise a property as having more bedrooms than the number permitted by the septic system permit.

ANS: **True** REF: Vol. 47, No. 1, May 2016
Septic Permits – A Refresher

The Real Estate Commission continues to receive complaints related to misrepresentations concerning bedrooms and septic permit disclosure despite the issue's coverage in *Update* courses and *Bulletin* articles. Brokers can be disciplined for making a willful or negligent misrepresentation, whether in listing advertisements or other representations.

This article reviews four types of septic systems: municipal, community, on-site, or the combination of on-site septic and municipal, and outlines considerations for brokers when preparing advertisements or disclosures.

Municipal Water or Septic System - A broker should accurately determine whether a property is connected to municipal water or is serviced by a septic system. Brokers in municipalities should not assume that septic issues are limited to rural homes; there are many older neighborhoods in cities where a homeowner may not have connected to the municipal system when given the opportunity.

If a property is in an older neighborhood or if there are red flags such as a depression in the yard, or stones marking a tank and the seller indicates that the home is served by the municipal system, a broker should verify that information. Even if a property is connected to a municipal system, the homeowner is typically responsible for the sewer line running from the street to the property. Damage to this line from tree roots or otherwise is not usually covered by homeowners' insurance. Verification of municipal connection can be obtained from either the city or county, depending on the property location. If the property is serviced fully by the municipality, the broker's investigation will be complete.

Community and Combination Systems - There may be a combination system, where the house's septic system is connected to a municipal system but water is not. Most owners know if they are connected to a community system that is regulated by the state (Environmental Health Section, a division of the NC Department of Health and Human Services) in conjunction with the county health department that maintains permit information. Community system drain fields are typically owned by the community's homeowners' association (HOA). The drain field site may be material depending upon its location, and should be determined through the seller, HOA or the county health department.

Combination systems with municipal system connection may no longer have a permit on file. Brokers should be aware that city or county responsibility ends where the septic system connects to the municipal system. Issues with a pump connected to the septic tank, root damage to pipes in the yard or any other problem that occurs on the owner's land will be left to the homeowner, potentially at considerable cost.

On-Site Septic Systems - If a broker learns that a property has an on-site septic system, a call to the county health department should normally provide the broker with the requisite septic permit information. Permits set a capacity (generally, two people per bedroom) which cannot be exceeded in the design parameter. Brokers should be aware that a permit may state other limitations such as prohibiting the use of a dishwasher or garbage disposal.

A broker should be careful not to advertise a property as having more bedrooms than the number permitted by the septic system permit. Although state law requires that on-site septic permits be maintained until they are no longer in use, there are a few counties where the records were not kept initially.

Issues in locating records can arise when the original septic permits recorded under the original builder or owner's name and that information is unknown. In those instances, given the difficulty of verifying the permitted number of bedrooms, a broker should research tax records. If the property appears to have four bedrooms but the tax records indicate three bedrooms, that could indicate a septic permit's limit. Ultimately, in cases when the permit cannot be located, brokers should disclose what they know: namely, that the property has an on-site septic system but the system permit was not located.

Advertising - When a septic system permit is available and indicates a capacity of three bedrooms, the broker may only advertise the property as a three-bedroom home. To knowingly advertise more bedrooms than permitted would be a willful misrepresentation.

One concern with misrepresenting a property as having more bedrooms than the system permits is that the system could be overused and eventually fail. The health department can then prohibit further use of the system in order to prevent possible contamination of groundwater and to protect public health. If the system is repairable, lower occupancy limits can be imposed.

The Commission regularly reviews cases where brokers knowingly advertise properties as having more bedrooms than the permit allows but try to qualify it. For example, a broker advertises that the property has six bedrooms but in the property remarks discloses that the septic permit allows only three bedrooms. Such advertising is still deceptive and encourages overuse of the system by suggesting allowable occupancy by more people than the septic system was designed to handle.

Complaints - When a broker has misrepresented either the type or capacity of the system, the buyers frequently file complaints with the Commission and may pursue the broker in civil court for their losses. Buyers' complaints cite septic system failures or discovery that their property is not usable as they intended, meaning certain improvements such as in-ground pools or building additions, are prohibited. Frequently, when a buyer attempts to resell the property, a new listing agent discovers the inaccuracy and the original three-bedroom home is now being advertised as a two-bedroom home. Thus, the owner may have a lower property value and difficulty attracting potential buyers. Resolution of these problems may be possible by expanding system capacity (assuming enough room) or connecting to a municipal system (if available and possible), but at a cost the buyer did not anticipate when purchasing the property. However, all too often, there is no way to fix the problem because access to a municipal system may not be possible or there may not be enough room for an expansion.

Brokers should take reasonable steps to ensure that they are discovering and disclosing the correct sewage system utilized by any home they are listing. If the home is connected to an on-site septic system, then the property should be represented as having the amount of bedrooms as indicated on the permit. Buyer's agents should be alert to any red flags and perform their own due diligence if there are concerns about the representations.

2. A broker's advertisement must NOT overstate or exceed the allowed limits and design parameters of the property's sewage disposal system or occupancy permitted by the local municipality.

ANS: **True** REF: Vol. 47, No. 3, May 2017

Checked Allowed Occupancy Limits Before Advertising Property

Each year, the Commission receives numerous complaints related to various types of misrepresentation by brokers. One common type of misrepresentation involves overstating the number of bedrooms or allowed occupancy limits of properties, whether they are being advertised for sale or for rent. Either way, a broker's advertisement must NOT overstate or exceed the allowed limits and design parameters of the property's sewage disposal system or occupancy permitted by the local municipality. In other words, be sure to check the limits imposed by the septic permit, specifically the number of bedrooms the septic permit allows, and occupancy limits of the local municipality.

When residential properties are built and served by on-site septic systems, the local permit department typically evaluates the site and determines the maximum number of bedrooms allowed based on the design of the system and the land's ability to percolate wastewater into the ground. That's why the evaluation was historically referred to as a "perc" test. The results of the test determine the maximum number of bedrooms allowed on the site.

Brokers must be aware of both bedroom and occupancy limitations in the sale, resale, and rental of properties with on-site sewage disposal systems. The Real Estate Commission expects all brokers to possess the skills and knowledge to accurately represent facts about such properties regarding the number of bedrooms and/or maximum occupancy. The septic permit generally can be checked by making a phone call to the local permit department or by checking the department's website. Checking the permit is especially important when there has been an addition or remodel to the property to increase the original number of bedrooms. A broker should not assume permits were issued for the construction. If the actual number of bedrooms in the property exceeds the number of bedrooms allowed on the septic permit, the listing broker may NOT represent the dwelling as having any more bedrooms than are indicated on the septic permit, even if there is a disclaimer made.

Many municipalities have occupancy limits for residential dwellings. For properties being advertised for rent, the occupancy level is generally calculated by multiplying the number of bedrooms on the septic permit by two, based on a maximum of two occupants per bedroom. The maximum is, of course, calculated regardless of the actual number of beds the landlord might have set up inside the dwelling. Therefore, claiming a three-bedroom property "sleeps 12" because it has six sets of bunk beds is a misrepresentation if the local municipality limits occupancy to two persons per bedroom. If the licensee overstates the maximum occupancy in a rental home, the tenants might over-occupy the dwelling and overload the septic system, causing the system to fail. Such system failure could result in not only the contamination of surrounding groundwater but also the potential condemnation of the property, not to mention costly repairs that would have to be made by the property owner. Brokers must take reasonable steps to discover and disclose material facts and to ensure everything being advertised is correct, including the septic information. That means checking the number of bedrooms on the permit and calculating the maximum occupancy based municipality requirements. Buyer's agents should also be alert to problems and red flags related to the septic system and septic permit, and whether the imposed limits match the actual number of bedrooms in the dwelling. It might be necessary for the buyer's agent to verify the information advertised by the listing agent, and to therefore potentially alert the buyer client of problems.

In some cases, the permit department might not keep records permanently or the records might not be available for other reasons. In that case, it is reasonable to advertise based on the existing number of bedrooms but with the disclosure that the permit records are not available and therefore certain assumptions have been made by the listing agent. Both listing and buyer agents should be able to explain to their clients the value of obtaining a septic permit and what information such permits provide. Disclosures must always be made so that the potential buyer is made aware of material facts before the potential buyer makes an offer.

CAVEAT: Real Estate License Law prohibits misrepresentation, omission, or concealment of material facts; a course of misrepresentation through false advertising; and improper, dishonest, or fraudulent conduct. Willful or negligent misrepresentation of the occupancy design limits of a property's on-site sewage disposal system violates the Real Estate License Law and may result in disciplinary action by the Commission.

3. Agents should be aware of the dangers of advertising occupancy levels for any property served by a septic system without first verifying the system's legal capacity.

ANS: **True** REF: Vol. 41, No. 2, October 2010
Bedrooms at the Beach – Adverting Occupancy

Every year the Commission receives complaints that brokers in the vacation rental business have represented that a cottage or cabin may be occupied by more people than the septic tank permit allows.

Of course, tenants complain when the waste lines back up or the septic system fails. Health officials become concerned when failures create unsanitary conditions and when property limitations allow no room for system expansion or repairs. Agents should be aware of the dangers of advertising occupancy levels for any property served by a septic system without first verifying the system's legal capacity.

Properties that are not served by municipal sewer systems are typically inspected by local health departments to assess the site's capacity for on-site sewage disposal (septic systems). An application is submitted for an improvement permit and the county issues a septic permit with a maximum number of bedrooms based on the site's capacity.

Occupancy levels are determined by the number of bedrooms allowed by the septic permit, with a maximum of two people per legal bedroom. Therefore, the septic permit is the key to identifying the total number of bedrooms and the total number of people that a particular sewage system can serve.

Brokers should understand restrictions on land usage for properties with which he/she is dealing. Brokers who advertise such properties must be careful not to overstate the number of legal bedrooms or the maximum occupancy.

Advertisements which say things like "three bedrooms and foldout sofa," "sleeps ten," and "two queens, two doubles, and bunk twins" all make representations about occupancy. Brokers should take care that their advertising does not promote a violation of health codes by directly or indirectly representing that a rental unit may be occupied by more persons than the septic tank permit will allow. An overloaded system can fail and lead to groundwater contamination, costly repairs, and even condemnation.

If a broker's advertisement of a property served by a septic system includes a maximum occupancy that exceeds the ability of the septic system as provided by the permit, the agent may have misrepresented the true condition of the property.

A broker should check the county records and disclose both the legal number of bedrooms and a maximum occupancy of no greater than the number determined by this method, regardless of the actual number of bedrooms or beds in the house.

Advertising a property as having more bedrooms than permitted, even with a disclosure that the septic permit states fewer bedrooms, may still be misleading and encourage illegal use of the property.

Sometimes the original septic permit for a property cannot be located. The health department can usually make a determination based on a new inspection. Licensees should also keep in mind the maximum occupancy must not be overstated as long as the house is serviced by a septic system, even when conversion to public sewer has been scheduled, but not completed.

4. A room in a house must have a "clothes closet" to be advertised as a bedroom.

ANS: **False** REF: Vol. 37, No. 2, October 2006
To be or not to be … A bedroom? That is the question!

Reports are that some brokers are mischaracterizing certain rooms as "bedrooms".

Specifically, in order to enhance the marketability of homes listed for sale, they are submitting information to multiple listing services and through advertising identifying as "bedrooms" rooms which were never designed or intended for such use.

As a result, prospective purchasers seeking homes with the number of bedrooms shown in the MLS are frustrated and angry when their agents show them homes where one or more of the "bedrooms" is clearly not suited for that purpose – even though the seller may have used the room as a bedroom.

The question then arises, "What is a bedroom?" Although there is no clear answer, there are some factors to consider when classifying a room as a bedroom:

Is there a clothes closet in or conveniently available to the room? However, since bedroom closets were not a common design feature in many older homes, do not disqualify rooms in these homes which do not contain closets if they were clearly intended to be used a bedroom.

Is there sufficient space in the room to accommodate standard bedroom furniture? 8' x 10' is suggested for a single bed, and 10' x 11½' for double beds.

Does the home comply with governmental regulations (septic tank requirements, fire and safety codes, etc.) pertaining to bedrooms? When in doubt, check with the appropriate local government agency.

To paraphrase a classic song, "A room is not a bedroom, just because there's someone sleeping there." So, save potential buyers and their agents time and trouble, and save yourself possible action from the Real Estate Commission by using your common sense and exercising reasonable judgement when determining whether a room is, for listing purposes, a bedroom.

NOT part of the above article:
The publication: North Carolina State Building Code: Existing Building Code – 2015 – states, in part:
Emergency escape and rescue openings. When the work being performed creates a bedroom, at least one sleeping room window or exterior door shall comply with Sections 805.11.1 through 805.11.3
Operation. Emergency escape & rescue openings shall be operational from the inside without the use of keys or tools.
Sill height. The opening shall have a sill height not greater than 44 inches measured from the floor.
Minimum size. The minimum net clear opening shall be 5.7 square feet. The minimum net clear opening width shall be 20 inches. The minimum net clear opening height shall be 24 inches. The clear opening dimensions shall be the result of normal operation of the opening.

Additionally, in an April 2011 NC REALTOR® article regarding this issue, the article states, in part, "… Under the NC Residential Building Code, if a room has at least 100 square feet, and at least 50% of the room has a ceiling height of greater than 7', it can be called a bedroom, provided, of course, the bedroom has a door or window leading directly to the outside"

5. The Real Estate Commission requires listing brokers to report square footage.
6. It is okay to use the square footage in tax records or an old appraisal as a source.
7. It is okay for a listing broker to get an appraiser to measure a property being listed.

ANS: 5: **False** 6: **False** 7: **True** (generally)
REF: Vol. 45, No. 3, February 2015

Your Square Footage Measurement Must Be Right When Listing a Property

The Commission regularly receives inquiries and complaints about the measuring of square footage in properties listed or being listed for sale. Accuracy in measuring is critical because the amount of space in a structure has a bearing on value and functionality and is a material fact. Thus, the task of assessing square footage should be one of the most important in the process of market evaluation.

Following are questions typically asked of Commission staff. Read these and the answers that follow to test and review your knowledge of this topic.

Q: Have there been changes to Commission rules on the reporting of square footage?
A: The Commission has no specific rules on this topic. However, it does have rules about misrepresentation which can result from inaccurate measuring. It also has educational information in the form of the Residential Square Footage Guidelines – a booklet which provides instruction in measuring different types of floor plans in residential properties – and content in postlicensing courses on the topic. All of this is available on the Commission's website, www.ncrec.gov. And, if questions still arise, you can call the Commission.

Q: I am the listing agent. Am I required to report the square footage?
A: The Commission doesn't require it, but if you decide to report the square footage, it must be correct. Furthermore, your MLS may require it. To avoid problems, obtain the correct square footage yourself or obtain the services of a licensed appraiser.

Q: Is it okay to use tax records of square footage as a source?
A: No. Review the tax records, but never rely on them for this information. If you find that the square footage of the property differs from the information on the tax records, there may be a permit or other issue to be resolved.

Q; If I do not measure the property myself, must I get an appraiser to do it?
A: No, but appraisers are generally a very good source because they are typically trained and experienced in measuring. The Commission will normally allow a broker to rely on a licensed appraiser's current measurement as long as that reliance is reasonable and there was no red flag to alert the broker to a problem. Regardless of who does the measuring, the broker should keep the measurements on file in the event of questions or problems arising.

Q: Is it okay to use an old appraisal?
A: No. Do not use an old appraisal or an old MLS listing description since there may have been changes to the property at a later date.

Q: What happens if I make a mistake in measuring, or report the wrong square footage for any reason?
A: According to NC General Statute 93A-6, the Commission has the authority to take disciplinary action against a licensee who makes any willful or negligent misrepresentation or pursues a course of misrepresentation through advertising or otherwise. Therefore, if the square footage is wrong, the listing agent and firm may be held responsible. In addition, the broker-in-charge is responsible for all advertising, so he or she may also be the subject of disciplinary action. The Commission looks at many facts when assessing these types of cases.

- Why was the square footage wrong?
- Who measured, and was he/she qualified?
- Can the measurements/sketch be reproduced by the broker?
- How much harm was done to the consumer?
- How far off were the measurements; was it a significant amount or negligible?
- Was the property unusually difficult to measure?
- Did the listing agent rely on square footage from tax records?
- Should the buyer's agent have recognized a significant difference and checked the measurements?
- When/why was the mistake made and was it corrected?

The bottom line, though, is that the listing broker, firm and broker-in-charge, and maybe even the buyer agent could be at risk of disciplinary action by the Commission for misrepresenting square footage.

Q: What should I do regarding areas of the house that do not have a permit, and how would I identify those areas?
A: When doing a walk-through of a house that a broker is listing for sale, the broker should be sure to look for any "red flags" indicating improvements to the property.

- Does the sunroom have a wooden deck floor?
- Does the third-floor bedroom appear to be finished to a lesser degree than normal?
- Does one room have baseboard heat instead of ducts?

These are all signs of potential additions and the broker should ask the seller about permits and additions and then verify the permit history of the property. Sometimes the permit department may not have records, but a broker must check if it's an issue and disclose the fact that there is no record of permits.

Q: Assuming I do discover an unpermitted section of the house, is it okay to include it in the overall square footage?
A: Include it separately and make the parties aware of it. As a listing agent, be sure not to misrepresent the property and/or mislead the buyer. The buyer needs to be made aware of the un-permitted section's size and location in the dwelling. It's best to provide written disclosure and maintain a copy in the file. The un-permitted section must be separately identified. Document your disclosures for future reference.

8. When listing and selling properties in residential subdivisions, especially newly developed subdivisions, brokers should check on the status of the streets (public vs. private), as all streets essentially begin as private streets and some eventually become public streets.

ANS: **True** REF: Vol. 46, No. 2, October 2015
Subdivision Street Disclosure Issues

When listing and selling properties in residential subdivisions, especially newly developed subdivisions, brokers should check on the status of the streets (public vs. private). Brokers should not assume that all streets are public. All streets essentially begin as private streets and some eventually become public streets.

A public street is one that was constructed in compliance with state (North Carolina Department of Transportation - NCDOT) standards and then was transferred to the NCDOT - usually upon the sale of a certain number of dwellings along the street or in the subdivision.

Upon acceptance of a street by the NCDOT, ownership and maintenance of the street will lie with the NCDOT. During the period between the construction of the street and the transfer of the street to the NCDOT, the developer and/or the lot owners are responsible for street maintenance. A street that is constructed to State standards, but falls into disrepair while waiting for the NCDOT to accept the street, may have to be repaired by the developer and/or residents before the NCDOT will accept it.

Private streets may or may not be constructed to state standards and the responsibility for maintaining them remains with the developer and/or the residents who live along the street. Persons who live on private streets that were not constructed in compliance with State standards would be wise to have a written road maintenance agreement signed by all of the property owners on that street.

Pursuant to North Carolina General Statute § 136-102.6(f), developers are required to give lot purchasers a subdivision street disclosure statement. This requirement applies to the first sale of a lot. Brokers who list lots for developers should remind the developers of the requirement.

There is no standard preprinted form for making this disclosure. Brokers assisting buyers of lots from developers should request a copy of the disclosure statement from the developer. Brokers who list and/or sell homes in relatively new subdivisions should inquire about the status of the roads, because the roads may not have been transferred to the NCDOT and a buyer may bear some or all of the responsibility for road maintenance until this transfer occurs.

The high cost of maintaining and repairing streets makes the status of a street a material fact. Over the years, the Commission has dealt with a number of complaints, usually from buyers who learned after their closings that the streets in their subdivision were private and that they would share in the cost of maintaining and repairing the roads.

In a few cases, buyers learned shortly after their closings that the neighborhoods were preparing to issue assessments to obtain the money necessary to repair the streets. In one case, the buyer of an unimproved lot in a 20-year old subdivision learned that the streets in his section of the neighborhood were private. Two years later, the streets had fallen into such disrepair that public school buses and emergency vehicles were unable to travel the streets.

Astute brokers will add “Verify street status” to their regular transaction checklist and verify the status of streets in order to better protect their clients. To verify that a street has been accepted into the State system, you may visit either the NCDOT website, https://apps.ncdot.gov/srlookup/, and enter the necessary information or go to www.ncdot.gov/doh/divisions/, hover over each division on the state map to determine the correct division for the county in which a road is located, click on the correct division and select “Directory” to contact someone within that division to confirm that a street has been accepted into the state system.

Verifying that a street has or has not been accepted into the State system will better protect your clients as well as reduce the incidence of complaints and the likelihood of disciplinary actions against brokers.

9. The mere presence of a radon mitigation system is not, in and of itself, a material fact.

ANS: **True** REF: Vol. 48, No. 1, May 2017

Revisiting Radon Gas and Radon Mitigation Systems

What is Radon Gas?

Radon is a colorless, odorless, radioactive gas which occurs naturally from the decomposition of uranium and is found in varying amounts in virtually all soils and in every state. It poses little to no health risk when allowed to dissipate in open air, but can present a significant health risk over time if it becomes trapped and accumulates in buildings. Radon gas rises through cracks and fissures in the earth's surface, homes through cracks or holes in the foundation or walls, in gaps around service pipes, around construction joints, and sometimes in water if the source is groundwater, rather than surface water.

What Level of Radon Gas is Safe?

Theoretically, *any* amount of radon poses some health risk since it is radioactive. The danger comes more from breathing radon. I f radon is in the groundwater, then the gas is released whenever water is used. Radon gas decays into radioactive particles which become trapped in the lungs and as they continue to decay, they release small bursts of energy which can damage lung tissue and lead to lung cancer. The Environmental Protection Agency (EPA) recommends that indoor radon levels not exceed 4 picocuries per liter (pCi/l) of air.

Is the Presence of Radon Gas a Material Fact that Must Be Disclosed?

If a broker knows that dangerous levels of radon are present in any structure which will be occupied regularly by people, then the broker must disclose that to all prospective buyers or tenants.

A broker is not expected to test all properties for radon. However, a broker listing a property should have the homeowner complete the Residential Property and Owners' Association Disclosure Form. Question 25 on that form deals with hazardous or toxic substances, including radon gas. If the broker has any reason to suspect that radon may be present at a hazardous level, the broker has a duty to inquire as to whether the property has been tested for radon. If the results of such a test were above the level recommended by the EPA, the broker has a duty to disclose this information to any prospective buyers. A buyer agent should always recommend to a buyer that the buyer have a radon test as a part of their due diligence, particularly if the broker knows that other buildings in the area have unusually high radon levels.

How Are Radon Levels Determined?

It is extremely easy to test for radon in a home or business. There are several "do-it-yourself" kits which may be purchased in hardware stores or from the EPA or over the internet and there are qualified testers trained to conduct such tests. A list of qualified testers may be obtained from the North Carolina Department of Environment and Natural Resources, Division of Radiation Protection at www.ncradon.org. Test kits can be ordered from the same website. There are both short-term and long-term tests available. Radon levels may vary from day to day and season to season and may be influenced by severe storms or high winds. Short-term tests are less likely to render an accurate picture of the year-round average radon level but do provide immediate feedback. They generally take a couple of weeks to get results. If the results are 4.0 pCi/l or above, it is recommended that a second test, either short-term or long-term be conducted. Long-term testing generally takes more than 90 days. Long-term tests will provide a more accurate reading of the year-round average radon level.

What if the Seller Installed a Radon Reduction or Mitigation System?

If a seller had a radon problem in the past, but installed a radon reduction system to remediate the problem and bring the radon within acceptable EPA levels, is the broker required to disclose the presence of the system? In the 2008-2009 Update Course, Commission staff stated that the system was installed to remedy an existing problem which could reoccur if the system failed to operate correctly and therefore the mere presence of the system should be viewed as a material fact and disclosed to prospective purchasers. However, since that time radon mitigation systems have become far more common and are often being installed in new construction homes with no history of radon gas. Such systems are often included as part of a green building program or as a feature in new homes since installation at the time of construction is much less expensive than installing an after-market system. In order to not stigmatize such homes as this feature becomes more prevalent, the Commission has since

revisited the issue and determined that the mere presence of a system is not, in and of itself, a material fact but the best practice for a listing broker is to disclose and let potential buyers make a fully informed decision before they go under contract. When a radon mitigation system is evident, buyer agents should inquire as to why a mitigation system was installed. And, buyers should be advised to have the property tested for radon gas and have the mitigation system tested to be certain it is functioning properly as part of their due diligence if they are interested in purchasing the home.

The North Carolina Radon Program at www.ncradon.org provides much helpful information about radon including a map showing various radon levels across the state.

10. A broker is required by Commission rule to enter into a written brokerage agreement with a seller-client before marketing the seller-client's property, and this includes the use of any “Coming Soon” marketing.

ANS: **True** REF: Vol. 44, No. 1, May 2013
New Brokerage “Coming Soon”

The Commission's Regulatory Affairs Division (formerly Legal Division) has experienced increased call volume recently regarding the use of Coming Soon sign riders attached to "For Sale" signs. The two primary questions asked by callers are, "Does 'Coming Soon' mean that the property is currently listed, but not yet available for showings?" and "Does it mean that the property is not yet listed, but will be listed soon?"

A broker is required by Commission rule to enter into a written brokerage agreement with a seller-client before marketing the seller-client's property. Thus, a broker is permitted to place a "For Sale" sign (with or without sign riders) on a property only if a written brokerage agreement is in effect that authorizes the placement of a sign on the seller-client's property.

If the seller-client wants the broker to begin marketing the property immediately to generate interest by prospective buyers, but the property is not yet ready to be shown, then this information should be specified in the brokerage agreement and in any advertising media, including an MLS system. If the seller is unwilling to enter into a written brokerage agreement, then the broker is prohibited from marketing the property in any manner including the placement of a "Coming Soon" sign.

There is another issue arising from the use of "Coming Soon" sign riders. Example: a broker places a "For Sale" sign with a "Coming Soon" sign rider on a property and then three weeks later, the broker replaces the "Coming Soon" rider with a "Sold In 2 Days" sign rider. The use of the "Sold in 2 Days" rider suggests that the property had only been listed for two days. If this is true, then the broker may have violated the Commission rule by placing the "For Sale" sign on the property before entering into a written brokerage agreement with the seller.

If the broker properly listed the property before putting the "For Sale" sign on the property, then it was a misrepresentation for the broker to put a "Sold in 2 Days" rider on the sign, because the property had been listed for approximately three weeks before a contract was signed. In this scenario, the broker could use a sign rider indicating "Sold In 3 Weeks" or "Sold 2 Days After Avail- able For Showings" (if this is a true statement).

Remember, before you place a "For Sale" or "For Rent" sign on any property, you must first enter into a written brokerage agreement with the property owner. As long as the agreement contains a definite expiration date and the anti-discrimination language specified in the Commission rule, the remaining terms of the agreement are negotiable by the broker and the seller-client. Moreover, as soon as a brokerage agreement expires or is terminated, you must cease all marketing efforts and remove all signs, lock boxes and other marketing materials.

When advertising with signs, newspapers, magazines or digital media (i.e. the MLS system, Web sites, etc.), brokers must exercise care to ensure that the advertising contains accurate information. While the Commission does not object to the use of sign riders including the "Coming Soon" sign riders, brokers must be careful to use them in a manner which is not misleading and which complies with the Commission's rules. Brokers are not eligible to receive compensation from transactions that arise from the improperly established agency relationships. Don't put your license or your livelihood in jeopardy by failing to comply with the rules.

11. My client wants to list now, but she doesn't want a lot of traffic in her home. I'd like to take the listing and place a "Coming Soon" sign in the yard, but not advertise the property in the MLS and only show it to a few buyers I know are interested in her type of property. This way I can generate leads without opening her home to a lot of traffic. My BIC said this is okay.

ANS: **False** REF: Vol. 44, No. 2, October 2013
'Coming Soon' Revisited

In the May 2013 issue of the Bulletin, an article appeared entitled New Brokerage "Coming Soon". The article addressed increased calls to the Commission regarding the use of "Coming Soon" sign riders attached to "For Sale" signs, and it generated so much conversation about issues stemming from this marketing tool that we felt it warranted a place in the Update Course as a follow-up article addressing a few lingering questions.

Q: I have a client who is ready to list, but needs to clean up the inside and make a few repairs. Can I list the property but not show it until it's ready, and can I place a "For Sale" sign in the yard with a "Coming Soon" sign rider to generate interest in the meantime?
A: Maybe. You must first enter into a written agency agreement with the owner that authorizes you to advertise the property. Once you have that, you can place a sign in the yard. If the property is not ready to be shown TO ANY potential buyers, you may attach a "Coming Soon" rider. Remember that your sign must comply with Rule A .0105 Advertising.

Q: My client wants me to list his home but he's not ready to sign a listing agreement yet. Can I advertise his property as "Coming Soon"?
A: Maybe. A broker is prohibited from advertising property belonging to another without first entering into a written brokerage agreement. The brokerage agreement must comply with the requirements of Rule A .0104, Agency Agreements and Disclosure, but the owner could limit the agreement to advertisement of the property as "Coming Soon" only. If that is the case, the broker may place a "Coming Soon" sign in the yard but may not place a "For Sale" sign, as the owner has not listed the property for sale. Under those circumstances, the broker may not advertise or disclose a list price and may not show the property to any potential buyers.

Q: My client wants to list now, but she doesn't want a lot of traffic in her home. I'd like to take the listing and place a "Coming Soon" sign, either as a rider to a "For Sale" sign or as an independent sign, in the yard, but not advertise the property in the multiple listing service and only show it to a few buyers I know are interested in that type of property. That way I can generate leads without opening her home to a lot of traffic.
A: No. Once the property is listed for sale, it should be available for viewing by any interested buyers unless legally and specifically excluded by the seller. For example, a seller may direct you to not advertise the property on a particular site or not to show the property to a specific person as long as the basis of the denial is not discriminatory. By limiting the market of potential buyers to those within a broker's firm or those with a business relationship to the broker or another broker, you may subject yourself to a claim of discrimination or even antitrust violations. In addition, you are likely doing a disservice to your seller client. Limiting potential buyers may also limit the potential selling price of the property. If you belong to a multiple listing service, you may be required to enter a new listing within a certain period of time. Post-dating a listing to avoid a problem with the MLS could be considered a misrepresentation. If you are a member of the North Carolina Association of REALTORS®, this type of conduct may constitute a violation of their Code of Ethics as well.

Remember, the goal is to sell the property under the most favorable terms for your client, not yourself. If your client isn't prepared to have buyers view the property, that means none, including your own or your buddy's. Please call the Regulatory Affairs Division at 919-875-3700 if you have further questions about this or any other topic.

Section Two:

Licensing Matters

12. The number one complaint the Real Estate Commission receives deals with trust monies.

ANS: **False** REF: Vol. 42, No. 1, May 2011
The Top Ten Complaints and How to Avoid Them

Each year, the Real Estate Commission receives as many as 1,000 –1,200 complaints against brokers from consumers, and in some cases, other brokers. Most are resolved without disciplinary action. Some go to hearing before the Commission, which may result in sanctions ranging from a reprimand to a license suspension or revocation.

The top ten complaints follow with suggestions as to how to avoid mistakes that may lead to disciplinary action.

ONE: Disclosure of Material Facts
Material facts fall into three general categories: facts about the property (leaky roof, cracked foundation, termite infestation, water intrusion, the presence of mold, etc.); facts relating to the property, such as zoning changes or the construction of a major roadway nearby; and facts that relate to a principal's ability to perform under the contract, such as a pending bank foreclosure or short sale situation.

Typical complaints of misrepresentation involve advertising a property for rent or sale with a greater number of bedrooms than is permitted by the property's septic permit, or advertising a larger living area for the property than was constructed pursuant to permit. Complaints sometimes involve hidden defects (cracked foundation or water intrusion resulting in mold) that were revealed by an inspection performed by a previous buyer.

To avoid complaints of misrepresentation or non-disclosure of material facts, you need to do your homework. Don't rely on information obtained from others – verify it through reliable sources. Also, check the accuracy of advertisements in print, on the MLS, or at a Web site.

A broker's duty to disclose material facts extends to his or her client, and to all parties involved in the transaction (including the lender in a short sale situation).

TWO: Mismanagement of Trust Accounts
The broker-in-charge is responsible for the proper handling of funds belonging to others, including the management of the trust account and trust account records. Although the broker-in-charge may delegate trust accounting duties, he or she remains ultimately responsible.

A broker-in-charge is responsible for maintaining a monthly trust account journal with a running balance, property ledgers for each sale transaction or lease, account reconciliations with bank statements and journal on a monthly basis, and a copy of the reconciliation worksheet with the trust account records. In many instances, where trust account violations have occurred, the investigation reveals that the broker-in-charge was not properly supervising those charged with bookkeeping duties, and was not regularly (preferably monthly) reviewing the trust account records.

Records must be retained for three years after all funds held in trust have been disbursed to the proper parties or until the conclusion of the transaction, whichever occurs later.

THREE: Disputed Deposits

A. **Earnest Money Deposits** - Commission rules require that, in the event of a dispute between a buyer and seller or landlord and tenant regarding the return or forfeiture of any deposit held by a broker, other than a tenant security deposit, the broker must hold the deposit in a trust account until a written release from the parties authorizes its disposition or until a court orders disbursement. The rule applies even where it appears clear to the broker that one party has no valid claim to the deposit. In lieu of retaining the disputed funds, a broker may deposit the funds with the Clerk of the Court at least 90 days after notifying the parties claiming ownership of the funds. Thereafter, it will be up to the parties to file a special proceeding with the Clerk of the Court to determine ownership of the funds. This procedure is described in the Offer to Purchase and Contract (Standard Form 2-T, rev. 1/2011) and enables brokers to educate their clients regarding handling of disputed deposits, and be less likely to face a complaint about the funds' return.

B. **Tenant Security Deposits** – Disputes concerning the disposition of a tenant security deposit are governed by the Tenant Security Deposit Act ("TSDA"), G.S. § 42-50 et. seq. When a dispute arises between a tenant and landlord, a property manager should follow the lawful directions of his or her client (the landlord) and disburse the security deposit accordingly.

The property manager is required to refund the balance not retained by the landlord to the tenant no later than 30 days following termination of the tenancy, together with an itemized list of damages charged against the security deposit. If the extent of the landlord's claim against the security deposit cannot be determined within 30 days following termination of the tenancy, the property manager must provide an interim accounting within 30 days, followed by a final accounting and refund of the balance within 60 days of the termination of the tenancy. Thereafter, a tenant must take the landlord to court to resolve the matter.

FOUR: Charges Against Tenant Security Deposits

The TSDA sets forth the maximum amount that may be imposed as a tenant security deposit, depending upon the duration of the tenancy, and further limits the items that may be covered. The deposit may not exceed an amount equal to two weeks' rent if a tenancy is week to week, one and one-half months' rent if a tenancy is month to month, and two months' rent for terms greater than month to month.

Items covered by the deposit include non-payment of rent, water and sewer service charges, damage to the premises, nonfulfillment of the rental period, unpaid bills that become a lien against the leased premises due to the tenant's occupancy, costs of re-renting the premises following a breach by the tenant, removal and storage of property after an eviction and related court costs. No other deductions are allowed.

Two common complaints against property managers involve charges for items such as cleaning carpets and appliances, and for re-renting the premises following a tenant's breach. The TSDA permits charges against the security deposit for property damage, but not for "ordinary wear and tear." Lease provisions imposing certain cleaning requirements on the tenant prior to vacating may not be enforced by charging the TSD and could require enforcement through a civil court proceeding. Much of the confusion related to improper charges for property damage can be eliminated by the proper use of property condition checklists.

FIVE: Short Sales

A short sale transaction constitutes a material fact that must be disclosed to potential buyers. For a detailed discussion, see the article on short sales in the *Real Estate Bulletin*, Vol. 42, No. 1, May 2011, pages 4-5.

SIX: Drafting Legal Documents

The Real Estate License Law prohibits brokers from drafting contracts, contract provisions, or any other legal documents, or from performing any other service constituting the practice of law as defined by G.S. § 84-2.1. While a broker may assist a client in filling out the standard forms approved by the N.C. Bar Association and N.C. Association of REALTORS ®, the broker must nevertheless avoid inserting complex contingencies into an Offer to Purchase and Contract or addendum. If a transaction requires more than can be inserted into the blanks of a standard form, a broker should refer the client to an attorney. Under no circumstances should a broker attempt to alter or combine approved forms that are not written to be used together. For example, don't combine an Offer to Purchase and Contract form with a standard residential lease form in an attempt to create a lease-purchase contract. In addition to engaging in the unauthorized practice of law, the broker will likely run afoul of recent legislation imposing strict requirements and restrictions on lease-purchase option agreements. Parties in lease-purchase transactions must be referred to private attorneys for document preparation and guidance.

SEVEN: Disputes Regarding Contract Acceptance

Negotiations leading to a contract can be fast-paced, to the extent that brokers find themselves communicating offers and counter-offers, as well as acceptances, orally. An example of such a situation occurs when an oral counteroffer is communicated to the buyers, who orally agree to the new terms. The acceptance is orally relayed to the sellers, who now mistakenly think they have a valid contract.

The Statute of Frauds requires that all contracts for the sale of land or for lease agreements exceeding three years be in writing and signed by the parties to be enforceable. In order for a valid contract to exist, all negotiated terms must be in writing and signed by the parties. Any changes must also be in writing and initialed by the parties.

A broker can best keep his or her clients informed of all communications material to negotiations between the parties by ensuring that offers, counteroffers, and acceptances are in writing and contain all necessary signatures. Oral agreements for the sale of real property are not binding.

EIGHT: Conflict of Interest

The Real Estate License Law prohibits brokers in a transaction from acting for more than one party without the knowledge of all parties for whom the broker acts. The most common complaints deal with dual agency, seller subagency, and special relationships between the parties.

With dual agency, an inherent conflict of interest exists because the broker is representing both the buyer and seller who have different and competing interests. To avoid a complaint of this type, Commission rules require that a broker provide a prospective client with the Working with Real Estate Agents brochure, and thoroughly review the types of agency and the broker's duties associated with each. The broker and prospective client must then agree as to whether the broker will work as a seller's agent, a buyer's agent, a seller's subagent, or a dual agent. To serve as a dual agent, the broker must first obtain written consent from all parties to the transaction.

Where a broker is working with a buyer who declines an agency relationship, the broker must disclose that he or she is working as the seller's subagent, and caution the buyer against revealing any confidential information. The seller's subagent can neither advise the buyer nor advocate on his or her behalf.

Brokers should also beware of conflict of interest issues that may arise in connection with the sale of the broker's own property. Although the broker is the seller, a prospective buyer may assume that the broker is representing the buyer's interests. This is especially true where the buyer had previously entered into an exclusive agency relationship with the broker prior to being shown the broker's listed property. **NOTE**: Effective July 1, 2015, Rule 58A .0104(o) was added: "A broker who is selling property in which the broker has an ownership interest shall not undertake to represent a buyer of that 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…"

NINE: Lack of Communication

A large number of complaints cite the broker's failure to communicate with his or her client. In sales transactions, sellers whose homes have remained on the market for prolonged periods express frustration at not being better informed regarding the broker's marketing strategies. Buyers note the lack of communication from their brokers concerning such matters as the outcome of property inspections or the progress in short sales of the lender approval process. Landlords complain about not being kept informed regarding marketing efforts to secure new tenants or property maintenance issues. But, by far the most frequent complaints we receive from brokers and consumers alike deal with the failure of other brokers to return phone calls or e-mails.

As a fiduciary, it is essential that you establish a method and frequency of communication that is responsive to your client's needs and preferences. As a broker, you should return telephone calls, e-mails, and other electronic communications promptly. If you are unable to respond promptly, due to a vacation or trip out of town, make sure that you have a back-up person to handle your calls in your absence and that you notify your broker-in-charge and your clients. Also, be sure to create an appropriate voice-mail message or automatic e-mail response to alert others trying to reach you.

TEN: Loan Fraud

Allegations of loan fraud often result from a broker trying to assist a buyer who is having difficulty qualifying for a loan in the amount needed to purchase a property. To help the deal close, the broker lends the buyer money for closing costs without notifying the lender. Alternatively, the seller may be asked to lend or "give" the buyer some money without telling the lender, since the lender has refused to allow any seller financing. Sometimes, the mortgage broker may ask the parties to pass money to the buyer as a "gift" outside of closing.

The rule of thumb is that any money which passes between the parties and third parties or even their brokers during the course of the transaction must be disclosed on the settlement statement (even "extras" paid for by the buyer to the builder over-and-above the contract price). The reason is that such payments may affect the loan-to-debt ratio used by the lender to determine creditworthiness. If you fail to disclose information to the lender, you may be committing loan fraud, which is a federal offense.

If in doubt as to whether a transaction is being handled correctly, contact an attorney or the Real Estate Commission.

13. Only cases involving sufficient, admissible evidence of a violation of the Real Estate License Law or the Commission's rules result in disciplinary action, and records of complaints filed against licensees are a matter of public record.

ANS: **True** REF: Vol. 44, No. 3, February 2014

What to Do When a Complaint Is Filed Against You

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...the Commission takes an objective, open-minded approach to investigating each complaint. Only cases involving sufficient, admissible evidence of a violation of the Real Estate License Law (Chapter 93A of the North Carolina General Statutes) or the Commission's rules result in disciplinary action.

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The Commission receives 800 to 1,400 complaints annually, covering every aspect of real estate brokerage plus unrelated issues such as criminal convictions. So, what should you do if a complaint is filed against you?

- First, don't panic. The Commission does not automatically assume that the allegation(s) in a complaint are true. Real estate brokers are considered innocent until proven guilty. However, to fulfill its mission to protect the interests of consumers, the Commission investigates each complaint to determine whether there has been any wrongdoing by a licensee.

- Second, if you receive a Letter of Inquiry from the Commission regarding a complaint, you must respond within fourteen (14) days of its receipt. If you need more time, contact the staff member who sent you the letter and ask for an extension of time to respond. Staff will usually be able to accommodate reasonable requests.

- Third, when responding to a Letter of Inquiry, provide a factual description of the transaction or incident described in the complaint and provide copies of relevant documents to support your statements. The Commission has the authority to expand investigations beyond the allegations described in complaints and may ask you for information and/or documentation regarding other aspects of a transaction or matter. You should fully answer the Letter of Inquiry before the deadline.

- Fourth, you may hire an attorney to represent you in responding to a Letter of Inquiry or when meeting with an Auditor/Investigator; however, it is not a requirement. If you are unsure about whether to obtain legal representation, you may want to discuss your situation with an attorney before deciding.

Cases which cannot be investigated by a Letter of Inquiry or where the broker fails to respond are assigned to a field investigator who performs face-to- face interviews, audits trust accounts and gathers information and documentation that may be needed to evaluate a complaint. In this type of investigation, the Auditor/Investigator typically will contact you to set up an interview.

After receiving your written response to the Commission's inquiry, it is evaluated it to determine any need for additional information and/or further investigation. Once the file provides a clear understanding of the facts, or in the case of a field investigation, after the report is completed, a decision is made to close the file with or without a warning or to forward the case to the members of the Commission to order its closing or to order an evidentiary hearing. Only Commission members can order a hearing against a broker or licensed firm. If the file is closed, you and the complaining witness will receive notification in writing of the decision.

When the Commission orders a hearing, the case is assigned to a staff attorney to prosecute on behalf of the Commission and you (or your attorney, if you have one) will be contacted to discuss your options for settling the matter.

If a settlement cannot be reached, then the Commission will hold the hearing, which is similar to a trial, except that the nine members of the Commission preside instead of a judge. After evidence is presented by the Commission's staff attorney and by you (or your attorney), the Commission members will decide whether the evidence warrants disciplinary action and, if so, the appropriate action (reprimand, suspension, or revocation).

All disciplinary actions are published in the Commission's Real Estate Bulletin, which is sent by mail or email three times annually, and distributed to the North Carolina Association of REALTORS®, the Better Business Bureau in the area where the violation occurred, and the local board.

The Commission retains records of complaints filed against its licensees, and under state law, those files are public records. In the event that someone contacts the Commission to inquire about complaints filed against a broker, the Commission's staff will report the number of cases and their disposition, and will provide copies if requested to do so.

When a case is closed without any disciplinary action, the Commission's staff informs callers that the evidence of a violation was insufficient to warrant disciplinary action and that the mere fact that a complaint was filed does not necessarily mean that a broker engaged in misconduct.

In summary, the Commission takes an objective, open-minded approach to investigating each complaint. Only cases involving sufficient, admissible evidence of a violation of the Real Estate License Law (Chapter 93A of the North Carolina General Statutes) or the Commission's rules result in disciplinary action. If a broker has not committed a violation, there is nothing to fear from a complaint. Moreover, conducting your business with a focus on integrity and customer service will go a long way toward protecting you from ever receiving a complaint.

14. Common knowledge may be defined as "knowledge that is widely or generally known to everyone or nearly everyone in a community" and, brokers are expected to possess such in the area(s) in which they work as a broker should become an expert on his/her market area.

ANS: **True** REF: Vol. 45, No. 1, May 2014

What is Common Knowledge?

One of the most frequent types of complaints the Commission receives from consumers alleges that material facts were omitted or misrepresented. As you know, a material fact is any information that would affect a reasonable person's decision to buy, sell or lease. Brokers are required to disclose material facts to all interested parties. Moreover, a broker representing the owner of a property offered for sale or lease has an added duty to discover as well as disclose material facts.

When investigating a complaint in which it is alleged that a broker omitted or misrepresented a material fact, the Commission assesses what the broker knew or reasonably should have known about the fact in question. To determine what a broker actually knew, we review transaction documents and written communications and interview persons involved either directly or indirectly with the transaction.

To determine what a broker reasonably should have known, we examine public records and ascertain whether the broker has taken relevant courses or has had access to publications, such as the Commission's Real Estate Bulletin, that would have educated the broker on the topic in question. We also consider whether the material fact was common knowledge.

What is common knowledge? It is knowledge that is widely or generally known to everyone or nearly everyone in a community. For example, it is common knowledge in the real estate brokerage community that a person must obtain a real estate license from the Real Estate Commission and maintain the license on current, active status in order to engage in real estate brokerage activities and be eligible to receive compensation for those activities.

In order to acquire common knowledge, brokers should thoroughly familiarize themselves with the area(s) in which they work. This may be accomplished by reading local newspapers, watching local TV news, conducting online research, attending continuing education courses, talking to other local brokers, etc. In other words, a broker should become an expert on his or her market area. This is important for all transactions, especially those in which the parties are not familiar with the area and brokers become the primary source of information.

Brokers who receive opportunities to handle transactions outside of their areas of expertise should either partner with or refer the opportunities to brokers with knowledge and experience in such areas. Brokers who undertake to handle transactions in unfamiliar areas will be held responsible for any adverse consequences that arise as a result of ignorance and/or incompetence. North Carolina General Statute §93A-6(a)(8) authorizes the Commission to pursue disciplinary action against a broker who is unworthy or incompetent and acts in a manner which endangers the public.

Brokers cannot use common knowledge as a defense for omitting material facts. In other words, a broker cannot claim that a prospective buyer or tenant should have known about a material fact in an attempt to relieve the broker of his or her duty to disclose it. Broker must disclose all material facts including those considered common knowledge. For the protection of the broker and all parties, it is best to make such disclosures in writing.

Prospective buyers, sellers, landlords and tenants depend upon their agents to inform and guide them in making good decisions. Brokers can only accomplish this if they acquire and then share relevant knowledge with their clients and customers. Brokers should therefore strive to be aware of common knowledge as well as all other property-specific and area-specific knowledge necessary to carry out their duties effectively.

Examples of Common Knowledge

- A plan by the North Carolina Department of Transportation ("NCDOT") to construct or widen a roadway that has been publicized on the NCDOT's website (www.ncdot.gov/projects/), in local newspapers, and/or on local TV:
- A city's plan to annex an area which will double the annexed area's property taxes and which has caused much debate in public hearings and in local media;
- The fact that when a strong Nor'easter hits some coastal communities, there is increased risk of beach erosion causing loss of dunes, street flooding, and damage to ocean-front homes;
- The fact that storm drainage system in a neighborhood is inadequate to handle the abundance of storm water produced by thunderstorms causing widespread flooding when the citizens in the neighborhood have filed a highly-publicized lawsuit against the city to get the city to take corrective action;
- The designation of a large commercial property as a Superfund site by the Environmental Protection Agency along with significant publicity that no cleanup efforts have been undertaken; and
- The location of a train station through which loud freight trains routinely pass during the early hours of the morning, where local residents have complained publicly for many years.

15. The Commission is a public/governmental agency, and therefore is required to make available to the public my name, email address, and other contact information.

ANS: **True** REF: Vol. 44, No. 2, October 2013

Commission Approves Licensee Data Policy

The Commission has approved a policy to segregate public and private licensee data, in response to the changes to the Real Estate License Law. Currently, email and delivery addresses, whether business or home, are considered to be public.

A method for retaining a personal email address that is not public record is being created. Licensees will be able to log into the Commission's Web site and use a new icon on their personal screen which will allow them to either add a "private" email address or move the existing email address to the "private" area.

The Commission will be the only organization that will use the "private" email address (for purposes such as renewal reminders, Bulletins, and important licensee notifications).

A licensee on inactive status, or on active status working from home, will still have their home address shown as their delivery address unless they change that address to a post office box. All information from the application of a new licensee will be considered private, again with the exception of the home address, until the applicant either provides a post office box or business address.

All pertinent Commission forms are being updated to permit the inclusion of two email addresses, public and private, should a licensee wish to provide them.

You Email Address: Public or Private?
Vol. 45, No 1, May 2014

You now have the option to designate your email address or addresses on file with the Commission as "public" or "private – for Commission use". Your "private" email address will be used by the Commission to communicate with you, and will not be disseminated to anyone. Your "public" email will be provided on request to others such as schools to send you CE information. To make your selection, log into and update your record.

16. Prior to conducting any real estate brokerage services, a real estate licensee must obtain <u>both</u> an individual and/or firm license from the NC Real Estate Commission and a state privilege license from the NC Department of Revenue.

ANS: **True** REF: Vol. 47, No. 2, October 2016
Privilege License vs. Broker License

And the difference is, a broker license is something every individual and business entity needs to perform real estate brokerage services like sales or property management in North Carolina. The broker real estate license for individuals and firms is administered by the Real Estate Commission and must be renewed yearly on or be- fore June 30 through the Commission. For more information on the broker and/or firm license go to the Commission's website, www.ncrec.gov.

A state privilege license is also required to do certain types of business activities within North Carolina. This license is personal and is not issued in the name of a firm or corporation. Individual real estate brokers are specifically required to obtain a privilege license under NCGS §105-41(a)(8); however, a licensed broker who is also a licensed appraiser is only required to get one privilege license which will cover both activities. The state privilege license is governed by the Department of Revenue and must also be renewed yearly by July 1. There are a few, very limited exemptions from the state privilege license requirement which can be found under NCGS §105-41(b). In order to apply for a privilege license, you must go to the Department of Revenue's website, http://www.dor.state.nc.us/downloads/ privilege.html. Once this state privilege license has been granted, you must pay an annual tax on July 1st. This tax is not prorated and there are penalties for failure to pay.

NCGS §160A-194, effective July 1st, 2015, limited the authority of cities to require an additional license for persons holding a license issued by an occupational licensing board. Brokers should still confirm with their city or county whether any other additional local permits are needed to conduct business in that location. Go to your city or county website for further information.

Remember: Before conducting real estate brokerage services you must: (1) obtain an individual and/or firm license from the NC Real Estate Commission; AND (2) obtain a state privilege license from the NC Department of Revenue. Once you have these licenses, mark your calendar to renew your broker license by June 30 of each year and to renew your privilege license and pay the yearly tax by July 1st.

17. Commission rules require the retention of all materials and statements used for the marketing and advertising of a listed property, including but not limited to, all Facebook, Twitter, Instagram and other social media posts that provide information regarding a listed property, and be prepared to reproduce legible hard copies of the posts upon request of the Commission.

ANS: **True** REF: Vol. 46, No. 1, May 2015

As Technology Changes, Records Retention Requirements Do Not

Whether communicating with clients and customers or updating property listings on the fly, today's tech-savvy brokers are taking full advantage of smartphone technology and social media in conducting real estate transactions. It is important for brokers to consider the implications that the Commission's records retention requirements have on the utilization of these tools, and to take the steps necessary to remain in compliance with Commission Rules and Real Estate License Law.

Commission Rule A.0108 requires that brokers retain records of all sales, rental, and other real estate transactions, and that they be able to produce those records for inspection and reproduction by the Commission without prior notice. Included in Rule A.0108 is a "catchall" provision requiring the retention of "any other records pertaining to real estate transactions."

Brokers who choose to use technology as a means of communication would be wise to retain all such communications related to a transaction, including emails and text messages - especially those that confirm that some act was or was not performed, that authorize the broker to undertake some act on behalf of a customer or client, or that disclose any material facts.

The challenge with text messages is not so much retaining them, but reproducing them at a later date. Many smartphones have applications that allow users to email text messages to themselves, and there are even applications that convert and save text messages as Microsoft Word documents.

Whichever method is chosen to save text messages, a broker must be able to promptly retrieve and produce hard copies when necessary, and the copies must be legible, and provide a clear communication trail. The sending and receiving parties should be evident in each message and when the message was sent and/or received. Also, where a series of messages was exchanged, the order in which the messages were sent should be apparent.

Retaining all communication exchanges as part of the transaction file will increase a broker's ability to defend against claims that the broker did or did not tell someone something, or that the broker was non-communicative during a transaction. If the broker is able to produce text messages proving that she was responsive to the client, the issue can be put to rest quickly and easily.

The catch-all provision in Rule A.0108 also requires the retention of all materials and statements used for the marketing and advertising of a listed property. It is therefore essential that a broker save all Facebook, Twitter, Instagram and other social media posts that provide information regarding a listed property, and be prepared to reproduce legible hard copies of the posts upon request of the Commission.

You may wish to consult with your firm's IT specialist for technical guidance on retaining and reproducing electronic communications and marketing materials. Additionally, feel free to contact the Commission with any questions you may have regarding records retention rules and requirements at 919-875-3700.

18. An unlicensed assistant may lawfully perform the following acts.

a. Submit listing and changes to MLS.
b. Obtain keys for listed properties.
c. Record and deposit trust monies.
d. Place "for sale" or "for rent" signs on property.
e. Show rental properties managed by the broker to prospective tenants.
f. Complete and execute preprinted form leases for rental property managed by firm.

ANS: **True for all** REF: Vol. 43, No. 2, October 2012
Unlicensed Assistants –
Drawing the Line Between What They Can and Cannot Do

There is a line between licensed and unlicensed in the world of real estate brokerage that requires the careful attention of brokers with unlicensed assistants who help them with their business and may work directly with buyers and sellers.

A complaint from a buyer or seller that the "broker" with whom they are working is not licensed as a broker is often followed by the actual broker explaining that the "broker" is really an unlicensed assistant.

The question then arises: Did the assistant cross the line between licensed and unlicensed when providing services requested by the client or the broker?

Because clients do not always know who is licensed in a brokerage office or precisely what rights a license confers, brokers should inform clients of the limits placed on their unlicensed assistants in providing services. Otherwise, there is considerable opportunity for confusion.

The best course of action is to explain matters to the client at the beginning of the relationship and, as an aid in doing that, provide the two lists below which draw that important line between what is allowable and what is not.

Unlicensed assistants MAY:
- Receive and forward phone calls, texts and emails to the employing broker or other licensees in a firm;
- Submit listings and changes to a MLS provider, but only if the listing or change is based upon data supplied by a broker;
- Assist a broker in compiling documents for closing;
- Research and obtain copies of documents in the public domain, such as the Registers of Deeds, Clerks of Court, or tax offices;
- Obtain keys for listed properties;
- Record and deposit trust monies under the close supervision of the office broker-in-charge (BIC);
- Type in offer to purchase, contract and lease forms with information provided by brokers;
- Check license renewal records and other personnel information pertaining to brokers at the direction of the BIC;
- Prepare commission checks and otherwise act as bookkeeper for the firm's operating account under the close supervision of the BIC;
- Place "For Sale" or "For Rent" signs on property at the direction of a broker;
- Order and supervise routine and minor repairs at the direction of a broker;
- Act as a courier at the direction of a broker;
- Coordinate or confirm appointments between brokers and other persons;
- Schedule appointments for showing properties listed for sale or rent;
- Show rental properties managed by the broker to prospective tenants;
- Complete and execute preprinted form leases for rental property managed by the firm.
- Answer basic questions from prospective buyers and others about listed properties if the broker has provided the information in promotional materials.

Only licensed brokers MAY:

- Show properties for sale to prospective buyers;
- Answer questions from prospective buyers and others about listed properties.
- Offer opinions as to the seller's or landlord's intentions about a listed property;
- Solicit listings or management contracts from prospective clients;
- Prepare information to be placed in promotional material or advertisements for properties for sale or lease;
- Discuss or explain listings, management agreements, offers, agency agreements, leases or other similar matters with persons outside the firm;
- Negotiate the amount of rent, earnest money deposits, due diligence fees or other contract provisions in connection with properties listed for sale or rent by the firm.

Finally, remember that if you are a broker-in-charge, you are responsible for all money being held in a trust account and the accuracy of all advertising. Brokers-in-charge should be closely supervising all actions in those areas, especially when those duties are performed by unlicensed persons.

19. A "full broker" that works alone, from home, and is not a BIC and has no BIC, may lawfully perform the following acts.

a. Solicit properties to list for sale or rent

b. Advertise or otherwise promote his/her real estate services

c. Regularly show properties to prospective buyers or tenants

d. Hold trust monies and/or manage trust accounts

e. List properties (owned by others) for sale or rent

ANS: **False for all** REF: Vol. 43, No. 3, February 2012
Limited Activities Available to Unaffiliated Brokers

What activities can a full broker engage in if the broker leaves a brokerage firm office and chooses to work alone from home without being designated as a broker-in-charge? The short answer is: very few. Assuming the license is active, permissible activities are limited primarily to:

- receiving referral fees from another broker or brokerage company,
- selling, buying or leasing property for himself or herself,
- representing someone as a buyer or tenant broker so long as the broker did not actively solicit the business. This most often occurs when the buyer/tenant is a relative or friend.

Pursuant to Commission Rule A.0110(a), a broker who chooses to function as a sole proprietor, but wishes to avoid acting as a broker-in-charge cannot:

- solicit business, advertise or otherwise promote his/her services,
- list properties (which inherently requires promotion),
- have other licensees affiliated with the broker's sole proprietorship,
- be responsible for holding any monies that must be deposited into a trust account.

Note that only sole proprietorships qualify for this exemption: a broker who chooses to receive income from referrals through his or her one-person licensed limited liability company or corporation must still have a broker-in-charge.

A broker-in-charge or affiliated full broker who leaves a firm to set up a sole proprietorship, for example by working from home in his or her own name, should notify the Commission in writing upon the severance of the affiliation. Such a broker may remain on active status at his or her home address without a broker-in-charge so long as the broker timely renews his or her license prior to June 30 and completes 8 hours of continuing education (including the mandatory Update course) by June 10 each year. On the other hand, provisional brokers must always have a broker-in-charge in order to be on active status — timely license renewal and continuing education is not sufficient so long as the license remains provisional. This means that a provisional broker cannot work from home as a sole proprietor.

Consider the following scenarios for an unaffiliated full broker with an active license but no broker-in-charge:

A) The broker is asked by her sister to list her sister's house for sale. Typically, brokers find it necessary to advertise whenever they represent a property owner, in order to attract a buyer or tenant. As a listing agent, the broker also may be called upon to hold any earnest money deposit. Thus, to take this listing, the broker must do any one of the following:
   - declare herself broker-in-charge of her sole proprietorship; or
   - create an entity, obtain a firm license and be broker-in-charge of her entity; or
   - refer the listing to another company and receive a referral fee; or
   - affiliate with a company/office if the broker wished to actively participate as an agent in the transaction.

B) The broker wants to represent herself in purchasing property and receive a portion of the commission. In this case, the broker does not need to have an active license to request and receive consideration because she is a party in the transaction (in this case, the buyer). As a party in the transaction, the buyer/broker is not engaged in brokerage, because she is not representing others. As such, she does not need a license to be paid. It is up to the listing company to decide whether it will share compensation with this buyer.

A common activity of brokers on active status who are not affiliated with an office and who choose not to declare themselves broker-in-charge is to refer parties to other licensees in exchange for a referral fee. As always, the broker making the referral must disclose to the prospect that the broker will earn a fee for the referral. It is recommended when negotiating referral fees that brokers put the terms of the referral agreement in writing. And, if the broker promotes his or her services as a referral agent by handing out business cards or maintaining a website soliciting consumers, then he or she must be a broker-in-charge.

On rare occasions, an unaffiliated non-BIC on active status acting as a sole proprietor may also act as a buyer agent. This is permissible IF the buyer client was not solicited in any way by the broker, and the broker does not handle any trust money in the transaction. Typically, the buyer will be a family member or friend who knows the broker has a license and who initiates contact with the broker. In this case, the broker is rendering brokerage services and must comply with all Real Estate License Law and Commission rules including maintaining transaction files, making appropriate agency disclosure and having a written agency agreement.

Practicing as a sole proprietor can sometimes be a challenge. But, a full broker (whose license is not provisional) does not have to affiliate with another broker to maintain his or her license on active status. The broker must simply timely renew the license and complete eight hours of CE each year (the Update course and an elective). So long as the broker remains a sole proprietor, the broker may engage only in the limited activity outlined above without being a broker-in-charge. Understand as well that this limited exception only applies to sole proprietorships, and not to any entity.

20. If the name of your sole proprietorship firm does not include your last name, then you must register the name of your firm with the Register of Deeds in the county where you intend to do business but there is no need to obtain a firm license from the Commission.

ANS: **True** REF: Vol. 43, No. 3, February 2013

How to Start a Real Estate Firm

[Note: This article is not intended to cover every possible issue that a broker will or should consider when starting a firm. It does provide guidance for many of the basic issues that will commonly arise.]

You are an active broker and have your broker-in-charge designation and have thought about starting your own firm for a long time and have decided that now is the time to do it. Here are some things to consider.

Types of Firms

Sole Proprietorship: If your firm will be a sole proprietorship, then no additional real estate license will be required. If the name of your firm will not include your last name, then you must register the name of your firm with the Register of Deeds in each county where you intend to do business and retain the Assumed Name Certificate(s) in your records. For example, if your name is Jordan Greentree and your firm name will be Greentree Properties, then you will not have to register your firm name with the Register of Deeds because the name of your firm includes your last name. However, if you desire to call your firm Awesome Real Estate Consultants, then you must register this assumed name at the Register of Deeds in the counties where you will engage in real estate brokerage services.

Corporation, Subchapter S-Corp, LLC, Partnership: If your firm will be a corporation, subchapter S-corp, or LLC, then you will need to contact the Corporations Division of the Secretary of State's office and set up the company. (See *Firm License Application* form for instructions on licensing a partnership.) After establishing the company with the Secretary of State (for which you may call upon the assistance of a lawyer), you must obtain a real estate broker license for the firm by submitting a firm license application to the Commission. Firm license application forms are available on the Commission's website. **If you are setting up a firm for the sole purpose of receiving sales commissions, you must still obtain a license for the firm before receiving any such sales commissions.**

Trust Accounts

If you intend to collect trust monies (i.e. earnest money, rents, security deposits, etc.), you must set up a trust or escrow account designated as such. This means that you must visit a federally insured depository institution lawfully doing business in North Carolina and set up a basic checking account in the name of your firm. The title or subtitle of the account must include the words, "Trust Account" or "Escrow Account", and these words must appear on the signature cards, checks and deposit tickets. The broker-in-charge of the firm must account for all trust account monies in accordance with Commission rules. This includes performing a complete trust account reconciliation on a monthly basis. If you have not taken the Commission's Basic Trust Account Course, we recommend that you do so before handling trust monies. You are not required to have a trust or escrow account unless you are holding trust monies.

Location

If you choose to operate your firm from your home or any non-commercial setting, make sure there are no zoning regulations or restrictive covenants which prohibit you from operating a real estate business from that location.

Signage

The Commission has no specifications for the size or shape of signs for a real estate office. For Sale and For Rent signs should clearly indicate the name of the firm so that prospective buyers and tenants will know that the sign and the telephone number on the sign belongs to a real estate broker.

Broker-in-Charge Declaration

If you actively engage in real estate brokerage activities, hold trust monies or have at least one associate, you must declare yourself Broker-In-Charge. You must have at least two years of real estate brokerage experience within the previous five years to be eligible to declare yourself broker-in-charge. You may do this by completing and submitting a Broker-In-Charge Declaration form available on the Commission's website (www.ncrec.gov). If you have set up your firm for the sole purpose of receiving sales commissions and have no associates or trust monies, then you are not required to declare yourself broker-in-charge.

Associates

If you hire a provisional broker to work at your firm, you must actively supervise him or her. Therefore, you must provide a work space from which the provisional broker can conduct his or her business under your supervision. If you hire a full broker to work at your firm, the full broker may conduct his or her business from any location provided, however, make sure that they deliver to you all agency agreements, transaction documents and trust monies in a timely manner. Full brokers must visit or at least communicate with their corporate offices on a regular basis to inquire about mail, because the Commission corresponds with active licensees at their business addresses. Make sure that any broker you hire has a current, active license.

Continuing Education & License Renewal

As a broker-in-charge, you will be responsible for assuring that every broker associated with your firm completes eight (8) hours of continuing education by June 10 of each year and renews his or her license by June 30 of each year. Brokers who allow their licenses to expire or become inactive must cease all real estate brokerage activities immediately.

Forms

The only trade or business forms provided by the Real Estate Commission are the Residential Property Disclosure Statement and the Working with Real Estate Agents brochure. All other forms are available through the North Carolina Association of REALTORS®. If you are not a member of NCAR, you may contact the North Carolina Bar Association for any forms they have jointly created or consult an attorney to draft any documents you need.

21. Each NC real estate firm must remain current, active, and in good standing with the NC Secretary of State and the Department of Revenue and, if a firm does not satisfy the requirements to remain in good standing with each, yet continues to act as real estate brokers, they may face disciplinary action by the Real Estate Commission.

ANS: **True** REF: Vol. 41, No. 1, May 2010

To Do Business in NC, Real Estate Firms Must Comply with State Laws

To do business legally in North Carolina, real estate firms (corporations, limited liability partnerships and limited liability companies) must remain current, active, and in good standing with the North Carolina Secretary of State and the Department of Revenue.

Firms may verify their compliance by visiting the North Carolina Secretary of State's Web site, www.secretary.state.nc.us/corporations, and searching their firm name. The site will note whether the firm is "Current-Active", whether there is a problem that needs to be addressed (e.g., "On Notice"), or if the firm has been suspended, cancelled or dissolved.

The Commission has instituted an ongoing audit of real estate firms to verify compliance and to assist those that have not fully met the state's requirements.

If firms do not satisfy requirements to remain in good standing yet continue to act as real estate brokers, they may face disciplinary action by the Real Estate Commission. Further, if a firm does not regain good standing within a reasonable period of time, its real estate license will be cancelled.

When license cancellation occurs, the following changes to licensee records and status are made:

(1) Brokers-in-charge lose their designation as brokers-in-charge (but not their eligibility to be re-designated);
(2) The licenses of provisional brokers with the firm are placed on inactive status; and
(3) The addresses of record of all brokers and provisional brokers affiliated with the firm are changed to their residence addresses.

If a company later satisfies the requirements of the Secretary of State and the Department of Revenue to do business in North Carolina, its qualifying broker must then file an application and pay a fee to the Real Estate Commission to reinstate its real estate firm license and must designate a broker-in-charge for each office.

Each broker-in-charge must then complete and file forms for each broker and provisional broker who wishes to re-affiliate with the company.

These procedures can be both time consuming and costly. Thus, be sure to keep your firm in compliance by timely filing annual reports with and paying fees due to the Secretary of State and Department of Revenue every year.

22. A broker may simultaneously have his/her license affiliated with more than one firm and, when brokers have multiple affiliations, they need to use business cards and forms that identify the correct real estate firm(s) with which the consumer is dealing.

ANS: **True** REF: Vol. 46, No. 1, May 2015

Who's Your Broker

When brokers have multiple firm affiliations, consumers can often be left wondering "Who's our broker?"

Say, for instance, that Broker A is affiliated with ABC Realty, Inc., a sales-only firm. Broker A wants to engage in property management. ABC Realty, Inc. gives Broker A permission to establish his/her own firm for property management and yet remain affiliated with ABC Realty, Inc., for residential sales. Broker A establishes XYZ Realty, LLC, becomes qualifying broker, broker-in-charge, and starts engaging in property management.

Months later, a tenant is unhappy with Broker A's disposition of the tenant security deposit and files a complaint with the Commission against Broker A and ABC Realty, Inc. The tenant named ABC Realty, Inc. in the complaint be- cause Broker A used ABC Realty's software program that auto-populates the firm name and address on the lease form.

The tenant has a reasonable belief that the rental property is being managed through ABC Realty, Inc. This could be a misrepresentation on the part of Broker A, not to mention a misuse of ABC Realty's software, and presents a problem for Broker A with both ABC Realty and the Commission.

When brokers have multiple affiliations, they need to use business cards and forms that identify the correct real estate firm with which the consumer is dealing.

Brokers-in-charge also need to be mindful of this issue. If you are a broker-in-charge and allow brokers with your firm to establish a separate firm, or affiliate with another existing firm, then make sure that they are not engaging in any other business under your firm name or using your trust account to handle monies that are related to a transaction with the other firm. Office policy should address whether brokers may have other affiliations.

There can be many reasons a broker might be affiliated with more than one real estate firm. Brokers just need to be sure that the documentation they are using indicates the correct firm affiliation for the transaction at hand, and that everyone knows which role the broker is performing for each transaction.

23. When a licensee is convicted of a misdemeanor or who has disciplinary action taken against him/her by an occupational licensing board, the licensee is required to file a report with the Real Estate Commission.

ANS: **True** REF: Vol. 41, No. 2, October 2010
Disclosing Criminal Convictions

So, you have a speeding ticket or impaired driving charge, an expired registration, or an assault charge. Commission rules require that you disclose certain types of convictions to the Commission, but which ones, how, and within what time period?

1. Before reporting, wait for final adjudication, which occurs following a plea of guilty or a finding of guilt by a judge or jury. Do not file a report before a judgment is entered against you to avoid a file being opened and a permanent record made of your report, which may be unnecessary if you are found not guilty or the matter is dismissed.

2. Non-moving violations, such as expired registrations, expired tags, etc., are not reportable offenses. Likewise, you are not required to report speeding convictions. All misdemeanor and felony convictions, however, must be reported. These include convictions for DWI or reckless driving, assault, larceny, etc. If you have questions about the reporting process, call the Commission's Legal Services Division.

3. Once you have entered a plea or otherwise have a criminal judgment against you, go to the Commission's Web site, *www.ncrec.gov* and, under "Forms," print the *Criminal Conviction / Disciplinary Action Reporting Form*. Please read the directions, which require you to provide a narrative in your own words explaining the incident and a CERTIFIED copy of the final order or judgment issued by the court. You have 60 days after conviction to file the form and supporting documentation with the Commission.

Once you have filed your report, the Legal Services Division will review it to determine if further action is necessary. You may be contacted to provide additional information. Just remember to respond quickly, fully and completely, so the matter can be handled in a timely manner. As with everything, full disclosure is always best.

Licensees Must Report Convictions

Commission Rule A.0113 requires any licensee who is convicted of a misdemeanor or felony or who has disciplinary action taken against him or her by an occupational licensing board to file a report with the Real Estate Commission. The reporting requirement includes conviction s for driving while impaired ("DWI"). The report must be filed within sixty (60) days of the final judgment or board action.

Section Three:

Broker Duties & Obligations

24. Any person that operates a "small Unmanned Aircraft System" (sUAS), a.k.a., a drone, for purposes of aerial photography in real estate must obtain a remote pilot certificate issued by the Federal Aviation Administration (FAA).

ANS: **True** REF: Vol. 47, No. 2, October 2012
Drones: Do's and Don'ts

On August 29, 2016, new federal rules went into effect for the operation of small Unmanned Aircraft Systems ("sUAS") in the National Airspace System ("NAS"). These rules, referred to as "Part 107", have been added to Title 14 of the Code of Federal Regulations, which governs aviation. These rules DO NOT apply to sUAS that are being flown strictly for hobby or recreational use which are considered Model aircraft. Part 107 regulations focus on the personnel, equipment, and operation of sUAS being flown in the NAS for anything other than hobby or recreational use. Such activities include research and development, aerial photography, education and academic uses.

Personnel
Under the new rules, a pilot's license is no longer required to operate sUAS. Now, a person can instead obtain a remote pilot certificate issued by the Federal Aviation Administration ("FAA"). To qualify for a remote pilot certificate, a person must: pass an initial aeronautical knowledge test, be vetted by the Transportation Security Administration ("TSA"), and be at least 16 years of age. Thereafter, a pilot must pass a recurrent aeronautical knowledge test every twenty-four (24) months. In lieu of taking the test, a person may demonstrate their aeronautical knowledge by holding an active pilot's license, completing a flight review within the previous twenty-four (24) months, and completing an online training course provided by the FAA. A person may not operate the sUAS if they know or have reason to know that they have a physical or mental condition that could interfere with its safe operation. The person operating the sUAS is required to understand airspace classifications and requirements.

Equipment
To be considered an sUAS, the aircraft must weigh less than fifty-five (55) pounds, including everything that is onboard or otherwise attached to the aircraft. Prior to operation, the sUAS must first be registered with the FAA. The operator must also keep up with the maintenance and repair schedule of the sUAS, is required to keep certain documents and records regarding the aircraft, and must make these documents and records available to the FAA upon request. Furthermore, the operator is required to verify that the aircraft is in a condition of safe operation prior to flight.

Operation
Most of the new rules deal with the operation of the sUAS. Some of these new rules are:

- During operation, the aircraft must remain within the pilot's visual line-of-sight, unaided by devices such as binoculars or telescopes;
- The aircraft should be operated during daylight hours;
- Maximum speed of the aircraft may not exceed 100 mph;
- The aircraft may not be flown above an altitude of 400 feet above ground level;
- There must be at least three (3) miles of weather visibility from the control station;
- No operation is allowed from a moving vehicle or aircraft;
- The pilot must not operate the sUAS in a careless and reckless manner;

- The sUAS may not carry hazardous materials;
- The sUAS may not operate over any persons not directly participating in the operation nor may it operate under a covered structure
- If operation results in serious injury, loss of consciousness, or property damage of $500 or more, the incident must be reported to the FAA within ten (10) days

Most of the restrictions above are waivable if the applicant demonstrates that the operation can safely be conducted under the terms of a certificate of waiver.

The above rules are some of the new provisions that are now in effect. For a complete summary of the rules, see: https://www.federalregister.gov/documents/2016/06/28/2016-15079/operation-and-certification-of-small-unmanned-aircraft-systems.

Caution to Brokers
Even though you may be licensed to operate the aircraft and it is properly registered with the FAA, you could still be violating local and State laws regarding privacy by operating the sUAS. Therefore, you should be knowledgeable about local and State laws regarding photography, transportation of goods, or any other intended uses of the sUAS.

25. A client may lawfully place a surveillance device in their home to monitor showings, inspections, etc., provided there is no audio turned on.

ANS: **True** REF: Vol. 45, No. 1, May 2014
The Use of Audio/Video Equipment During Showings

It seems that listing agents are being asked more frequently these days if sellers can keep some video or audio equipment "on" while their property is being shown.

Types of video or audio equipment include laptop computers, tape recorders, baby monitors, camcorders, and "nanny cams". The reasons that sellers give is that they want to protect their property and valuables from theft or destruction, or that they just want to hear what the potential buyers are saying about their house. A person who chooses to use such equipment must be very careful not to violate State or Federal law.

In 1968, the Federal government passed the Omnibus Crime Control and Safe Streets Act ("Omnibus Act"). Title III of this act speaks to wire and electronic communications and the interception of oral communications. The purpose of this Act is to protect an individual's right to privacy. Federal statute 18 USC § 2511 makes it unlawful for anyone to "intentionally intercept…any wire, oral, or electronic communication." Notice how the statute says nothing about "recording." That is because the statute prohibits the interception of oral communication whether it is recorded or not. This is a criminal statute, and a violation could result in a fine and up to 5 years in prison. There are some exceptions listed in the statute, but they mostly pertain to law enforcement. However, a person will not be in violation of this statute if State law allows them to hear an oral communication, when a party to the conversation has consented.

So, let's take a look at what North Carolina law says. General Statutes §§15A-286, et al. make up the Electronic Surveillance Act and reference and contain many of the same provisions found in the Federal Omnibus Act. This is a criminal statute, a violation of which is a class H felony. North Carolina also allows for a person, whose communication was intercepted, to sue the violator and get $100 per day for the violation, punitive damages, litigation costs, and attorney's fees. The statute only makes this a violation when one party to the communication has not consented.

Example 1: If you wanted to record a conversation between you and someone else, this generally would be allowed since you are a party to the communication and have consented to it being recorded. Even so, talk to your attorney before recording conversations.

Example 2: If your seller wanted to record a conversation between a potential buyer and their agent, this would not be allowed as the seller is not a party to that communication and the parties have not consented.

In 2002, the North Carolina Court of Appeals handed down a decision on the issues in Kroh v. Kroh. This was a case in which a married couple was separated and the wife decided to hide a video camera in the home to try and gather evidence for the divorce proceedings. The Court interpreted both the North Carolina and Federal laws discussed above and determined that the videotaping of the husband "did not violate the Electronic Surveillance Act unless such videotaping also included an audio recording". Kroh v. Kroh, 152 N.C. App. 147 (2002).

What does this all mean? These laws speak to oral or electronic communications and not video surveillance. Therefore, if you have a client who is adamant about placing a surveillance device in their home, advise them to ensure there is no audio turned on. They must also still be careful as to placement of the device (i.e. living room as opposed to bathroom) so as not to violate a person's privacy. They should not use non-recording audio devices such as baby monitors or walkie-talkies to try to figure out what people are saying about their property. As mentioned above, the fact that the devices do not record anything is immaterial. Violations of these laws are criminal and could land you or your client in jail and facing a hefty civil penalty.

Finally, the Commission recommends not using any device in the home as a means of trying to gain information on potential buyers or their agents. Such an attempt to gain potentially confidential information about a buyer would most likely be considered inappropriate at best, and has the potential to result in criminal or civil liability. Should you have any questions regarding this, please call the Commission at 919-875-3700.

26. Matters of survey, which relate to anything that could negatively affect the use of property being purchased, may be covered in a "lender's title policy", but generally do not protect the purchaser unless a survey (in the name of the purchaser) is performed prior to issuance of the policy.

ANS: **True** REF: Vol. 40, No. 2, October 2009
"Matters of Survey" Matter

There is a school of thought that it is not necessary to obtain a current survey when purchasing real estate--that title insurance and affidavits from sellers sufficiently protect the purchaser's interests or that the purchaser can simply rely upon a previous survey. However, real estate agents should be aware that purchasers face potential problems typically referred to as "matters of survey" when a current field survey of property is not performed.

Matters of survey relate to anything that could negatively affect the use of property being purchased. These include, encroachments across property lines or building restriction lines; fences/walls, landscaping features, wells, swimming pool decks; the location of utilities, access ways, etc., relative to easements, property lines or buildings; the existence of flood zones; and other similar matters.

It is possible that matters of survey may be covered in title insurance policies. But coverage that protects the purchaser's interests is unlikely to be included unless a survey is performed prior to issuance of the policy. "Lender's policies" may cover matters of survey without requiring a current survey, but they do not protect the purchaser. The risk associated with lenders' policies is often acceptable to the title insurer because claims from a lender are not likely to occur until the purchaser defaults on the loan.

In recent years, it has become popular to have the seller sign an affidavit effectively guaranteeing that no matters of survey negatively affect the property. However, in doing so, the seller may be unwittingly accepting some unwarranted risks of liability. The buyer may also be tempted to simply rely upon a survey document from a previous transaction, but such survey may not contemplate changes to the property since the earlier survey was performed.

Many people choose not to obtain a current survey because they believe it will delay closing the transaction. This may be true if it is not ordered from the surveyor until closing of the transaction is assured. However, if the purchaser decides that a current survey is desired, it can be ordered early enough so as not to delay the closing date.

An informed purchaser knows that an accurate, current survey will provide peace of mind that cannot be obtained from any other source.

27. The accuracy of any survey plat, as a snapshot in time, is only assured by the licensed surveyor on the date of performance of the survey.

ANS: **True** REF: Vol. 43, No. 1, May 2012
Beware of Use of Existing Surveys

Knowledge of survey plats is essential to your real estate practice. Prepared by Professional Land Surveyors (PLS) in North Carolina, survey plats are visual records of properties *at the time* the surveys were performed.

Whether you list a property or research one for a prospective buyer, you should caution your client to be certain that any existing plat prepared by a surveyor in the past is a true description of the property in the present.

The accuracy of any survey plat, as a snapshot in time, is only assured by the licensed surveyor on the date of performance of the survey. At any time, afterward, changes can occur, including, but not limited to:

- Alteration of property corners
- Encroachment of buildings or fences or other structures
- New easements
- Violations of current zoning laws
- Revised buffer and flood zones
- Sale of part of the property
- Reshaping of impervious surface area

Relying on plats that do not reflect changes occurring since the last survey has the potential to harm the purchaser of the property and the public. Historical survey plats, especially, are more likely not to provide the purchaser with the current accuracy of the boundaries or of any potential liabilities that may have evolved over time.

A map of survey must meet the North Carolina Board of Examiners for Engineers and Surveyors Board Rules, specifically 21 NCAC 56.1604 Office of Administrative Hearings, *www.ncoah.com/rules)* and, if the plat is going to be recorded in a county Register of Deeds office in a plat book, North Carolina General Statute 47-30 (North Carolina General Assembly, www.ncleg.net). The Board Rules and Statutes, including GS 47-30, are available from the Board's Web site at www.ncbels.org.

Survey plats can be prepared on three map sizes, 18" x 24", 21" x 30", and 24" x 36". At a minimum, each county Register of Deeds must accept the 18" x 24" size. Plats prepared to meet board rules do not have a size requirement, but the size of a map must permit all details to be legible on a copy. If a plat is going to be recorded as an attachment to a deed, the size requirement is no larger than 8½" x 14".

A sample GS 47-30 plat can be found at www.ncbels.org/forms/Sample_ *PLAT.pdf*.
For any questions or help when ordering or using surveys please contact the Board of Examiners for Engineers and Surveyors at (919) 791-2000 or visit the Web site at www.ncbels.org.

28. Brokers who represent prospective buyers and tenants should advise and encourage their clients to order inspections, tests and surveys for properties they wish to buy or lease and should never discourage a client from ordering an inspection, test or survey, even if it is not required.

ANS: **True** REF: Vol. 46, No. 3, February 2016
Handling Inspections: Guidelines for Brokers

Brokers who represent prospective buyers and tenants should advise and encourage their clients to order inspections, tests and surveys for properties they wish to buy or lease and may furnish them with lists of licensed, competent service providers to contact and hire.

A broker should never discourage a client from ordering an inspection, test or survey, even if it is not required. Inspections are an extremely important part of the purchase process for every buyer and in some commercial leasing transactions for tenants. Moreover, a prospective buyer's refusal to order an inspection in an effort to save money may have dire consequences in the long run.

Following are guidelines to consider in the management of the inspection process:

OBSERVATION - A broker should help a client understand that a home inspection is a visual inspection and not technically exhaustive. An inspector will be less likely to detect a defect that is not visible and cannot guarantee that a defect will not arise in the future from a hidden cause. An inspection, when conducted, is simply an observation of the condition of a property at that time.

BROKER PRESENCE - Ideally, a broker should be present for each inspection and encourage client presence as well to receive the inspector's explanations of findings. If a general inspector suggests that a more in-depth inspection is warranted, (i.e., for a defective heating/cooling system, mold, foundation cracks or other structural, mechanical, electrical or plumbing system defects, or any situation that could affect the health or safety of the buyer/tenant), then the broker should encourage clients to determine through additional inspections whether a serious problem exists and its potential resolution. Advise clients as well to complete inspections early enough during the due diligence period to give the seller/landlord an opportunity to respond to a repair request before the period expires.

DUE DILIGENCE PERIOD - If a client is unable to attend an inspection, the broker should assure client receipt of the full inspection report during the due diligence period. If it appears that the period will expire before the client can conduct all necessary inspections, the broker should advise requesting an extension of the period and possibly the closing date. If the property owner consents to an extension of the due diligence period (and the closing date), the extension should be written into the contract. If the property owner declines, then the client must decide whether to terminate the contract/lease.

OWNER INSPECTIONS - If a seller or landlord obtains an inspection and provides a report of it, a broker should nevertheless advise clients to strongly consider securing their own inspection to assure a qualified person makes a timely inspection. This guidance also applies when a general (home) inspector suggests further specialized inspections. The buyer/tenant generally will be better protected by hiring a specialized inspector instead of relying upon an inspector hired by the property owner.

CONFIDENTIAL REPORT - A home inspection report is usually considered confidential between the inspector and the client (i.e. the person for whom the inspection was performed). However, once the client or the client's agent gives a copy of the inspection report or a summary of the report to an opposing party or that party's agent, the document is no longer confidential.

OWNER REPAIRS - If a property owner performs requested repairs following an inspection, the buyer/tenant would be wise to order a re-inspection to verify that the repairs were actually and properly repaired. While the buyer/tenant will incur an inspection fee, it would be well worth the cost for peace of mind. A broker should obtain copies of all invoices for repairs and should use reasonable efforts to confirm that the persons who completed the repairs were properly licensed in their fields.

POST CLOSING REPAIRS – Brokers should encourage clients to insist upon the completion of all repairs prior to the closing/move-in date. If the parties agree that a repair will be made after the closing/move-in date, the buyer/tenant should insist upon written escrow agreement prepared by an attorney that includes a deadline for completing the repair, sufficient funds cover its cost, and the terms under which the escrowed money will be released.

BROKER DUTY TO INSPECT - When a broker lists a property for sale or lease, the broker has a duty to visually inspect it for defects since they may become material facts requiring disclosure unless corrected by the owner prior to listing. However, some defects including, but not limited to structural defects, high radon levels, the current or prior use of synthetic stucco and the presence of bacteria or toxins in well water must be disclosed by a listing agent even if the seller has taken steps to resolve or reduce the problem(s). This is due to the potential harm of these defects and the fact that there may not have been sufficient time or ability to determine if the repair truly fixed the problem. The buyer should be informed and able to have that repair evaluated. Similarly, brokers who represent buyers and tenants should also visually inspect properties and disclose to their clients any defects they observe and discuss whether further inspection by a professional is warranted.

For more comprehensive coverage of home inspections, licensees may review the 2001-2002 *Mandatory Update Course* manual and the Commission's brochure, *"Questions and Answers on: Home Inspections"*, available for viewing or purchase on the Commission's website, *www.ncrec.gov*. For questions not addressed by these publications, brokers may contact the Commission's Regulatory Affairs Division (919-875-3700) or the Home Inspector Licensure Board (919-662-4480). An article listing the types of inspections, testing and verifications available to buyers was published in the May 2015 issue of the *Real Estate Bulletin*.

Statutes, Rules and Useful Forms

• Home inspectors' inspection and reporting requirements are defined in Article 9F, Chapter 143, North Carolina General Statutes and in the rules, Title 11, Chapter 8, North Carolina Administrative Code. Knowledgeable brokers can help clients form reasonable expectations about the process and to identify features and structures that may be exceptions to a typical inspection. Access them on the Home Inspector Licensure Board's website, http://www.ncdoi.com/OSFM/Engineering_and_Codes/HILB.aspx.

• Professional Services Disclosure and Election forms for commercial (No. 585) and residential (No. 760) transactions, published by the North Carolina Association of REALTORS®, provide excellent tools for documenting inspections and adding specialized inspections and/or testing of any structure/feature not required such as an outbuilding or in-ground swimming pool.

NOTE: NO SUBSTITUTE FOR INSPECTION

BROKERS REPRESENTING BUYERS APPLYING FOR A VA LOAN SHOULD EXPLAIN THAT A VA APPRAISER WILL VISIT THE PROPERTY TO DETERMINE ITS VALUE, NOT ITS CONDITION. WHILE THE APPRAISER MAY IDENTIFY SOME DEFECTS AND THE BUYER'S LENDER MAY REQUIRE THE CORRECTION OF THOSE DEFECTS AS A CONDITION FOR LOAN APPROVAL, A VISIT BY A VA APPRAISER IS NOT NEARLY AS THOROUGH AS AN INSPECTION BY A LICENSED HOME INSPECTOR AND SHOULD NOT BE CHARACTERIZED AS BEING THE SAME. A VA APPRAISAL IS NOT A SUBSTITUTE FOR A HOME INSPECTION.

29. Even if a lender does not require a particular inspection or test, buyers should consider protecting their long-term interests, as an effort to save money and forgo inspections may cost the buyer much more than the cost of the inspection in the long run.

ANS: **True** REF: Vol. 46, No. 1, May 2015
Inspections: Varied Tests, Verifications, Property Evaluations Offer Many Choices for Prospective Homebuyers

The following is a list of inspections and verification measures that a prospective homebuyer should consider. Some lenders require certain inspections. However, even if a lender does not require a particular inspection or test, buyers should consider the following in order to protect their long-term interests. Declining an inspection in an effort to save money may cost the buyer much more than the cost of the inspection in the long run. This list is not exhaustive, but is intended to cover the most common inspections and verifications utilized by buyers.

Home Inspection –This is a general overview of the condition of a house. It is a visual inspection and is not exhaustive (i.e. it may not detect hidden defects). It does not provide a guarantee that defects will not arise in the future. Even buyers of newly-constructed homes should have home inspections. A residential home inspector must be licensed. Buyers should pay close attention to any recommendation by a home inspector for further, specialized inspections.

Wood-destroying insects – Every house should be inspected for insects that eat wood because the presence of such insects can damage or destroy a house. Evidence of a previous infestation of wood destroying insects may warrant an inspection by a general contractor or structural engineer to determine the extent of the damage.

Radon – This is a colorless, odorless, carcinogenic gas that rises through the soil and enters a house through the crawl space or concrete slab. There are several methods for testing for the presence of radon. The EPA has indicated that corrective action is necessary when the radon level inside a home is 4.0 pCi/L or higher as this can be harmful to one's health. Every buyer should consider having a radon test.

Survey – This will indicate whether there are any encroachments (e.g. fences, buildings, driveways, landscaping, etc.) by the subject property or adjacent properties.

Lead – Lead-based paint and lead pipes are the primary source of lead in homes. If a home was built before 1978, the seller must provide a lead-based paint disclosure. If a buyer has children, it may be wise to test the property for the presence of lead.

Mold – While mold is found everywhere and most types of mold are harmless, some types carry health risks. Also, persons with asthma and other respiratory health issues may be more sensitive to mold than the general population. If there is evidence of significant mold or if the buyer expresses a sensitivity to mold, an inspection by a qualified mold inspector would be wise.

Gas furnace – If the heat exchanger in the gas furnace is cracked, the furnace may produce carbon monoxide which can be fatal. A gas furnace should be inspected by a licensed HVAC firm.

Fireplace/Chimney – Fireplaces and chimneys should be inspected for cracks, creosote build-up and/or weak foundations that may allow the chimneys to lean away from the house creating gaps that enable moisture and pests to enter the gaps and the house. Also, don't forget to inspect flues for gas stoves and gas logs.

Moisture (crawl space, basement, roof leak, plumbing leak) – Moisture is a home's worst enemy. It promotes wood decay, mold and wood-destroying insects. Any evidence of moisture in a crawlspace or basement or stains on ceilings should lead to further examination.

Foundation cracks – This can be a sign of structural weakness caused by uneven settling of the soil under the house. The buyer should consider hiring a structural engineer to evaluate suspicious foundation cracks.

Septic systems – Check the septic permit for the specified number of bedrooms to make sure it meets or exceeds the advertised number of bedrooms and to locate the septic system on the property. If the area in which the septic system is located is wet or smells like sewage, the buyer should contact either the county environmental health department or a septic contractor to evaluate.

Wells – Test for contamination by bacteria, heavy metals, pesticides and other toxins. Drinking water containing any of these could be harmful to one's health. A buyer or buyer's agent may look at the water (Is it clear or brown?) and taste the water to help make the decision on how extensively to test the well water.

Underground fuel tanks – If a property depends upon well water and it has or previously had an underground fuel storage tank, it will be very important to determine whether there was any leakage from the tank. An unused tank should be removed or filled with sand to prevent collapse and the soil around the tank should be tested for fuel contamination.

City water/sewer – If a property is advertised as having "city water/sewer," it would be wise to contact the local utility provider(s) to confirm that the property is connected to city water and sewer services.

Fire – If there is information or evidence indicating that a fire occurred, the buyer should hire a structural engineer to evaluate the structural integrity of the house.

Cracked concrete slabs, driveways, patios – If a house is built on a concrete slab (instead of a crawl space) and the slab is cracked, a buyer should consider hiring a structural engineer to evaluate the crack. Minor cracks in driveways, sidewalks and patios are normal. However, if a crack appears to be wide or uneven in elevation, the buyer should consider hiring a structural engineer to evaluate.

Flooding issues – Is the property in a designated flood plain? If so, the lender may require flood insurance. If the property is not located in a flood plain, but is located near a drainage ditch or a body of water or, if the ground around the house slopes downward toward the house causing surface water to drain toward the house, then there could be a flooding or moisture issue that should be examined.

Homeowners' Association – Does an HOA exist? If so, who controls it, what is its financial condition, how much are the dues and what exactly do the dues cover?

Area – Prospective buyers and their agents should drive around the area, speak with neighbors, and check websites containing local information to identify potential problems regarding the property, neighborhood and general area.

Previous service/repair – If the seller or seller's agent indicates that something was serviced or repaired, it may be wise for the buyer to closely inspect the item to assure that it is in good working order and not in need of further service/repair.

Building permit – If a room has been added to the house or if a previously unfinished area was finished or if a new deck was constructed, a buyer would be wise to contact the county building inspection department to confirm that a building permit was obtained. The issuance of a permit ensures that the construction was done properly and approved by the county.

While all of the items in this list may not apply to every transaction, they provide a reasonable guide for prospective buyers and their agents to complete their due diligence and to help buyers determine whether to complete their purchases.

30. If a listing agent does not know for certain the correct facts about septic system use or permitting for a property, the agent must make an adequate investigation of the facts before making any representations about the property.

ANS: **True** REF: Vol. 38, No. 1, June 2007

Wastewater Regulations Can Impact Real Estate Licensees

Every year, several real estate brokers are disciplined for some form of concealment or misrepresentation of material fact relating to septic systems. In order to avoid being the subject of a complaint, you as a broker should be generally aware of the regulatory program for septic systems and also understand how the program is locally administered.

Presently in North Carolina, local county health departments administer a septic permit program under state regulation and supervision. Certain types of septic treatment solutions require a permit directly from a state agency, others from the county health department.

Once issued, a septic permit does not remain valid indefinitely. Although this was once true, in 1983, a three-year life was imposed on permits (later raised to five years). If a system was not installed during the three- (or five) year life of the permit, a new permit had to be obtained. The new permit was subject to whatever standards were in effect at that time - not standards that were in effect three (or five) years earlier when the original permit was issued, and there was no guarantee that a permit would in fact be available.

Recent legislation has eased this situation by requiring the health department to re-issue expired permits under certain circumstances. However, the re-issued permit generally will require the use of additional technology to improve system performance.

Similarly, the state can terminate a septic system permit for changed conditions on the property, including soil which is inadequate to support the system, use in excess of system design or permit, or false statements made to obtain a permit. Termination (or denial) of a permit renders a property unusable for residential and many commercial purposes. Therefore, the fair market value of a property is dramatically affected by the septic system permit availability and soil suitability.

What if a purchaser buys property for residential purposes and isn't told that it doesn't "perc"? North Carolina court decisions have compelled builders, lot sellers and developers to pay damages or re-purchase properties in some circumstances when those properties could not be used due to unsuitability for septic system installation or operation.

A broker who makes statements about a property with regard to septic system use must have an adequate factual basis for such representations. If a listing agent does not know for certain the correct facts about septic system use or permitting for a property, the agent must make an adequate investigation of the facts **before making any representations about the property**. Likewise, an agent working with a buyer must remain alert to any "red flags" in a transaction that might require the agent to undertake an independent inquiry into septic system use on a particular property.

Real estate brokers must be truthful in rental transactions as well as sales transactions. Septic permit regulations generally specify a design parameter of two persons *per bedroom listed on the permit* (not the number of rooms in which an owner or agent places beds or the number of beds actually in the property). Thus, when determining occupancy limits, a broker must use all necessary diligence to convey only correct information about permitted occupancy of a property served by a septic system even in a rental transaction, despite economic pressures to increase rental income by advertising higher occupancy levels. Because it is unlawful for an owner to use a property in excess of the occupancy limit imposed by a septic system permit, a licensee cannot willingly or negligently cooperate with the owner in flouting the permit limits.

When the land a broker offers for sale is a building site which must use a wastewater system requiring a permit, the broker should advise all parties to make an adequate investigation of the suitability of the property for a permitted system. A party to such a transaction who is making sale or purchase decisions based on the intended use of the property should be cautioned to determine not just the availability of a permit but to also determine whether the permit will meet the party's intended use of the property.

Caveat
As a real estate broker in sales and/or rental transactions, you must make every reasonable effort to ensure that your representations are correct concerning septic system permit availability and occupancy limits on properties served by septic systems. Relying on the representation of a property owner alone is not enough!

31. A short sale is a material fact, and therefore a listing broker *must* disclose this to the buyer and buyer agent.

ANS: **True** REF: Vol. 40, No. 1, May 2009
Getting Savvy About Short Sales

In today's economic climate, you may encounter sellers who owe more for their property than it is worth, i.e., they're "upside down" or "under water" on their mortgage. They may have more than one mortgage, a home equity loan, outstanding judgments and tax liens that must be dealt with before selling - one or all of which exceed the value of the property.

For sellers in financial distress, a "short sale" may help. A short sale occurs when a lender accepts a discounted payoff of the loan balance and gives up its interest in the property. In some cases, the seller is relieved of further liability; in others, the seller may still be indebted to the lender for the balance.

Lenders may agree to "short sales" to avoid the expense of a foreclosure, but often impose certain conditions:

- **Loan status**: Usually, the loan must be in default or imminent default; sometimes being "upside down" is enough.
- **Hardship:** Sellers must demonstrate that circumstances beyond their control prevent them from making their mortgage payments.
- **Financial Status:** Sellers must demonstrate insufficient resources to cover the loan amount.
- **Loan Fraud:** There must be no evidence of fraud in connection with the original loan. The lender is more likely to suspect fraud if default occurs within the first 12 months of the loan term.
- **Property Value:** The property must be appraised to determine the amount the lender will accept.

Although the buyer and seller have a contract, the seller's lender is in control in a short sale and can "just say no" to prevent it. Therefore, closing the sale is more uncertain than in ordinary transactions.

Listing Agent Responsibilities
Before you list a property, determine whether there is any possible need for a short sale, and be prepared to advise the seller about the process and consequences of one. While better than foreclosure, the seller's credit record will suffer. The process can take more time and the lender can simply stop it at any time. Suggest that the seller consider other options, including loan modification, refinancing, giving the lender a deed in lieu of foreclosure, or allowing foreclosure to occur. Recommend, prior to sale, consulting with the seller's attorney and financial and tax experts.

Consider the list price carefully: it cannot be so low that the seller's lender will reject it or it so high that buyers will lack interest.

Remember that because funds are "short," the seller may not be able at closing to pay third parties. Payments to lien-holders and other service providers, including yourself and maybe another broker, must be addressed. While foreclosure may wipe out some liens, a short sale requires negotiation with all lienholders.

A short sale is a material fact. As listing broker, **you must disclose this to the buyer and buyer agent.**

Short Sale Addendum - Listing Contract
Address in the listing contract a seller attempt at a short sale. The North Carolina Association of REALTORS® has developed a new *Short Sale Addendum to Exclusive Right to Sell Listing Agreement* which:
• requires the seller to work to obtain lender approval, including providing necessary financial information; and
• allows the listing agency to market the property as a short sale or pre-foreclosure property, to continue marketing while it is under contract and the lender is considering contract approval, and to disclose information to the lender and buyer agent.

Buyer Agent Responsibilities
When looking at properties and before making an offer, try to determine whether the property may be a short sale. The listing agent should disclose it, but if you have any doubt, ask for information about the status of the seller's loan, the possibility of a foreclosure action, and the seller's ability to convey the property free and clear of liens.

Be particularly attentive to property value, especially in a "soft" or declining market. An asking price below the seller's loan pay-off amount does not mean the property is worth it. Buyer agents should encourage clients to inspect the property to determine its condition, since a seller may not be financially able to make any repairs.

Some lenders in a short sale will not consider an offer until the buyer and seller have signed a contract. Make sure the buyer understands that once the contract is submitted, the lender may be slow to make a decision, require changes before approval, or even undertake foreclosure while considering it.

Short Sale Addendum - Offer
The North Carolina Association of REALTORS® has developed a *Short Sale Addendum* to the standard North Carolina *Offer to Purchase and Contract*. It includes contingencies that allow either party to cancel the deal if the lender rejects the short sale and the buyer to terminate the contract **at any time prior the lender's approval** by written notice to the seller. In either event, the buyer is entitled to the return of earnest money.

The addendum permits the seller to continue marketing the property and to communicate new offers to the lender. If those offers are higher than the contract price, the lender may reject the short sale contract in favor of a new offeror foreclose instead.

In Sum
Lenders are increasingly more likely to entertain the possibility of a short sale. However, because much of the decision-making rests with the seller's lender, such transactions entail significant risk, particularly for the buyer. Brokers should be certain to disclose to the buyer prior to contract if a short sale is necessary to accomplish the deal, use the standard addenda or have contract language drafted to specifically address the short sale, and allow plenty of time for the transaction to close.

32. If a listing broker learns a short sale is required *after* a sales contract is signed, or if the property goes into foreclosure while under contract, the listing broker has a duty to inform the buyer.

ANS: **True** REF: Vol. 41, No. 1, May 2011
Basic Short Sale Issues

With the decline in the economy over the last several years, the "short sale" transaction has increased in popularity. Licensees are listing a larger number of "short sale" properties and buyer-clients are seeking supposed bargains.

Brokers and buyers must remember that a seller is always free to sell their property for less than the remaining amount due on the seller's mortgage loan as long as the seller is able to come to closing with the difference in order to extinguish the mortgage lien. In general, that is known as a "short sale", but it does not require approval or participation by the seller's lender. For purposes of this article, a "short sale" transaction occurs when the seller's lender agrees to extinguish the lien for less than the amount due, allowing the seller to sell the property free and clear of the mortgage lien but without paying off the full balance due on the loan. There are several issues of which licensees should be aware in order to avoid short sale pitfalls.

THE LENDER MAY RELEASE THE LIEN BUT STILL HOLD THE SELLER LIABLE FOR THE REMAINING AMOUNT DUE ON THE LOAN (THE "DEFICIENCY").
Sellers in short sales must be made aware that they may be on the hook for any deficiency and just because a bank will allow the sale of the home does not mean that they will be left without owing the debt. A lender may accept the short sale amount and release the lien but refuse to consider it a full and final settlement of the debt. Brokers working with sellers should make certain the seller determines whether or not the lender will hold them liable for the deficiency before the short sale is completed. Conversely, if the lender agrees to forgive the remaining debt, the seller may face tax consequences because this debt forgiveness may be treated as income for tax purposes. Finally, a short sale transaction may affect the seller's credit score and ability to purchase another home for a period of time. Licensees should encourage sellers to discuss these issues in detail with their attorney and tax advisor before deciding to do a short sale. An attorney may be able to assist an owner in pursuing options other than a short sale (such as a loan workout, refinance, deed-in-lieu of foreclosure, bankruptcy, or loan modification).

AT WHAT POINT DOES A CONTRACT IN A SHORT SALE BECOME A BINDING CONTRACT?
The North Carolina Association of REALTORS ® has created a short sale addendum for both the standard form listing agreement and offer to purchase and contract. When these forms are used, lender approval is simply an additional contingency to the contract. At the point that both the buyer and seller have signed the contract and the seller's acceptance has been communicated to the buyer, the parties are in a binding contract subject to the contingency of the lender's approval of the short sale. Brokers representing sellers in a short sale situation where the standard form is NOT being used should advise their seller clients to have an attorney review the contract before they sign and be sure the seller can be released if the lender does not approve the short sale.

LENDER APPROVAL IS REQUIRED AND CAN BE COMPLICATED.
Each lender may have different document and eligibility criteria to determine whether a short sale transaction will be allowed. Generally, a lender will require proof that the borrower is incapable of paying off the loan and that the lender will fare better through a short sale than through the foreclosure process. Sometimes, being upside down on the loan (owing more on the loan than current fair market value) is enough, but the lender may still choose to evaluate the seller's financial circumstances to confirm that his or her resources are truly insufficient to cover the loan amount. Additionally, all debt and costs must be ascertained in order to determine the feasibility of a short sale. These debts include the amount of the delinquent loan, any home equity or other loans recorded against the property, past due HOA fees, and unpaid property taxes. The costs of the sale include any agreed closing costs (if allowed by the lender), escrow fees, and brokerage commissions. If a seller has more than one lien against the property, a short sale may require the approval of other lenders.

BROKERS SHOULD TRY TO IDENTIFY POTENTIAL SHORT SALE SITUATIONS PRIOR TO TAKING THE LISTING TO AVOID SURPRISES ONCE THE PROPERTY GOES UNDER CONTRACT.
Listing brokers must remember that it is a material fact that a seller cannot complete a transaction without doing a short sale and this must be disclosed to a buyer prior to contract even if the information may harm the seller's bargaining position. Similarly, if the listing broker learns a short sale is required after the contract is signed, or if the property goes into foreclosure while under contract, the listing broker has a duty to inform the buyer. Brokers should also remind sellers and buyers that short sales are uncertain. A lender is not obligated to approve a short sale transaction and may choose not to involve the seller or his listing broker in the decision-making process.

SELLERS AND BROKERS SHOULD BE ON THE LOOKOUT FOR SCAMS INVOLVING SHORT SALES.
These may include the buyer retaining a third party to negotiate a short sale, requesting that the seller execute a power of attorney for another party or not contact the lender themselves, large upfront fees, and guarantees to stop foreclosure. "Flopping" is a newly coined word for certain scams involving short sales. "Flopping" occurs when a seller or buyer (and/or his broker) convinces a lender to accept a short sale transaction while concealing from the lender the fact that another offer at a higher price is already lined up. The buyer then quickly resells the property for a profit. New regulations have been created to prevent flopping, including 90-day bans on resales.

LENDERS WHO AGREE TO A SHORT SALE TYPICALLY TRY TO HAVE A SAY IN THE AMOUNT OF BROKERAGE COMMISSION PAID AND MAY NOT ALWAYS BE WILLING TO APPROVE A SHORT SALE IF BROKERS TAKE THEIR USUAL FEE.
Listing brokers should be careful to accurately represent the commission they will pay to cooperating brokers and disclose that the amount of compensation may be adjusted based on the lender's requirements for approval of the short sale.

BUYER BROKERS SHOULD ADVISE BUYER-CLIENTS ABOUT THE PROCESS AND CONSEQUENCES OF A SHORT SALE.
A buyer broker should remember that just because the asking price of the property is below the payoff amount of the loan, there is no guarantee that the property is worth even the asking price. Brokers should take special care in assessing value in declining markets. In addition, a lender may not consider a short sale until a contract has been signed by buyer and seller. Once the parties submit a contract, the lender may take a long time to make a decision and may reserve the right to change the terms at the last minute. Moreover, a seller in a short sale transaction may not be financially able to make any repairs so the transaction is likely to be "as-is". The listing broker is allowed to continue marketing the property and may receive other offers which must be communicated to the seller and the seller's lender. Remember that the lender has a financial interest in the property and is being asked to take less than the amount owed. The lender therefore has the right to full disclosure of all offers. If another offer is more attractive in price or terms, the lender may not approve the first contract and require the seller to accept the later offer. Buyers must be patient, willing to wait, and understand that they could lose the property at any time before closing.

In summary, short sales involve significant risk to both sellers and buyers. Sellers may face many financial issues before, during and after the closing. The buyer must understand that not all short sale are bargains, short sales are generally not short transactions, and just because the parties have signed a contract does not mean that the buyer will get the house. Brokers should be well versed on these types of transactions before engaging in a short sale and should fully disclose all potential issues to their clients.

Section Four:

Agency & Compensation

33. Practicing dual agency lawfully is challenging because the sellers and buyers must agree to be represented in an adversarial relationship by the same agent. By entering into dual agency without the full understanding and consent of both clients, a broker may unfairly deprive those clients of the level of service they expect to receive.

ANS: **True** REF: Vol. 41, No. 2, October 2010
Dual Agency: When Is It Appropriate?

Agency Refresher - Clients may choose:

Exclusive Representation: Both the broker and the firm represent only one client in the transaction, to the exclusion of all others.

Dual Agency: The firm and its agents may represent both the buyer and seller in a transaction.

Designated Dual Agency: The firm represents both the seller and buyer via one agent designated exclusively as the seller's agent, and another agent designated exclusively as the buyer's agent, with each agent representing only the interest of their designated client.

In brief, dual agency is appropriate in a sales transaction only when it is agreed to – in writing - by fully informed sellers and buyers.

One of three types of agency representation (see box), dual agency arises when a firm is representing both the sellers and buyers in an in-house sale situation.

Practicing dual agency lawfully is challenging because the sellers and buyers must agree to be represented in an adversarial relationship by the same agent. A dual agent who must act with a combination of discretion and fairness that can be difficult to balance.

Although the laws and rules by which dual agency is practiced have not been reviewed to any significant extent by the courts, theoretically a dual agent owes the full range of agency duties to both principals. This creates practical problems for the dual agent regarding such matters as disclosure of material facts (especially confidential information about a client) and advocating for clients.

Thus, a broker's ability to provide full representation of the client may be compromised to some extent. By entering into dual agency without the full understanding and consent of both clients, a broker may unfairly deprive those clients of the level of service they expect to receive. Additionally, brokers can potentially have more exposure to claims of conflicts of interest when practicing dual agency.

To alleviate the conflicting responsibilities of dual agency, the North Carolina Association of REALTORS® has developed agency contract forms which place limits on the disclosure by a dual agent of information relating to any party's motivation, possible agreement to price, terms or other conditions, or any information identified as confidential. The contract forms also include an acknowledgment by the client that the agent will not act as an advocate for or exclusive representative of the client. Whether this form or another is used, all brokers are required by the Commission's rules to reduce their dual agency agreements to writing with the seller from the outset and with the buyer before one of the parties makes an offer.

Designated agency (a modified form of dual agency), is defined in rules adopted by the Real Estate Commission. It gives each client exclusive representation from an individual broker, while still allowing the firm to represent all of its clients. Remember, a broker-in-charge should never act as a designated agent in a situation where the other designated agent is a provisional broker under his or her supervision. The broker-in-charge loses his or her ability to supervise or assist a provisional broker in such a situation.

An agent who lists his or her own property, or property belonging to the firm, should refrain from acting as a dual agent when selling that property, as there are inherent conflicts of interest in offering one's own personal property for sale and then attempting to represent a buyer in the transaction as well.

What about the case of an unrepresented buyer or seller - can a broker work with him or her while solely representing another party? Yes, so long as the broker reviews and has the unrepresented party sign the *Working with Real Estate Agents* brochure, disclosing in writing that the broker will represent only his or her client (buyer or seller) in the transaction. Remember, there is no requirement that both the buyer and seller have broker representation in a transaction. An agent can work with an unrepresented buyer or seller as a customer, and still fully represent his or her client.

What if a previously unrepresented buyer or seller tells the listing broker that he or she would now like representation in an ongoing transaction where the listing broker has already disclosed that he or she represents only the interests of the seller? The broker's client may object, considering the information that the client has previously given the broker about his personal situation and/or desire for exclusive representation. If the parties do not consent to Dual Agency at that point, the listing broker should refer the unrepresented party to an outside broker/firm for buyer representation. All parties in the transaction deserve the best representation possible. Agents should remember to consider the interests of their clients first and determine which form of agency best suits their needs.

34. Sellers sometimes offer incentives in the form of cash, vacations, or other prizes to real estate agents, in addition to the sales commission, to promote the sale of their properties. Such incentives, or bonuses, are lawfully permitted so long as they are fully disclosed.

ANS: **True** REF: Vol. 38, No. 3, June 2008

Incentive Disclosure: Commission Reviews Compensation Rule

When market conditions make it more difficult to sell real estate, sellers sometimes offer incentives to real estate agents to promote the sale of their properties.

These "compensation incentives" may be in the form of cash, vacations, or other prizes. They are in addition to the sales commission or compensation the agent would otherwise receive from the sale and are usually given after the sale closes. They are especially popular among homebuilders to focus attention on their properties.

Real estate agents are permitted to receive compensation incentives so long as they are fully disclosed to their clients.

Responding to recent reports that some buyers are not being properly informed that their agents are being offered these special incentives, the Real Estate Commission formed an advisory committee consisting of real estate brokers, builders and consumer representatives to assist it in determining whether changes in its rules are needed to reasonably assure that real estate purchasers and sellers are properly informed of any compensation received by or offered to their agents from another party to the transaction.

The members of the Commission's *Incentive Disclosure Advisory Committee* were Kimberly D. Alston (Greensboro), William C. Bass (Asheville), Cindy S. Chandler (Charlotte), Tony H. Jarrett (Greensboro), C. Nash Lindsey, III (Fayetteville), P. Robert Measamer, Jr. (Fayetteville), Hampton Pitts (Raleigh), Page Robertson (Wilmington), James H. Sears (Gates), Grady F. Watkins, Jr. (Holden Beach), and Assistant Attorney General Harriet Worley. Special Deputy Attorney General Thomas R. Miller served as advisor to the committee and Executive Director Fisher facilitated the discussions.

After reviewing and discussing the relevant issues, the committee determined that proper disclosure of incentives of more than nominal value requires:

1. That the disclosure be in writing and preferably accompanied by an oral explanation of the incentive arrangement, that it be prominent, and that it be acknowledged by the agent's clients; but if the client fails to acknowledge the written disclosure, the broker may proceed with the transaction after noting this in his or her transaction records.
2. That the value of the incentive be disclosed and, if other than cash, a description of the incentive item and its monetary value stated.
3. That the disclosure by the agent be timely; i.e., preferably while showing properties for which an incentive is being offered, but in no event later than the making of the buyer's offer to purchase such properties.

The committee then concluded that, since the current Commission rule on disclosing the receipt of sales incentives does not require that the disclosure be made in writing nor does it address the timing or content of the disclosure, the rule should be amended to incorporate the disclosure elements it identified.

At its December meeting, after discussing the committee's report and recommendations, the Real Estate Commission initiated rulemaking to consider amending its Rule A.0109 governing the disclosure of compensation incentives. A rulemaking hearing will be held in the Conference Room of the Commission's Raleigh office on April 16 beginning at 10:00 a.m. during which the Commission will receive comments from interested persons concerning the proposed rule including any written comments received prior to the hearing.

Pending action by the Commission on the proposed rule change, licensees are reminded that they are required by current Commission rules to fully disclose to their clients any compensation incentive they are offered, and that federal law requires them to report on the HUD-1 form their "total sales/broker's commission" including any compensation incentives.

35. A broker in a sales transaction cannot be compensated by his client unless that compensation is provided for in a written agency contract meeting the requirements of Commission rule.

ANS: **True** REF: Vol. 41, No. 3, March 2011
Disclosing Compensation: When, Why and How

The License Law has always required brokers to disclose known conflicts of interest, and to avoid working on behalf of one party in a transaction without the knowledge of each party for whom the broker acts. Listing agents are required to set their compensation with their clients in the written listing agreement. Buyer agents must do the same in the Buyer Agency Agreement. From time to time, however, issues have arisen related to compensation and the appearance of impropriety in the manner in which licensees are often compensated.

In 2007, a newspaper article reported that certain buyer agents were receiving large bonuses from homebuilders/sellers as incentives to steer buyer clients to particular builders' properties. The brokers involved failed to disclose these bonuses to their buyer clients. This raised a concern that seller-paid incentives could cause brokers to direct their buyer clients to certain properties where the agent might receive extra compensation without the buyer's knowledge, rather than showing the buyer other properties that might also have suited the buyer's needs, perhaps at a lower price.

2007 Incentive Disclosure Advisory Committee

In response, the Commission formed an Incentive Disclosure Advisory Committee and charged it with determining whether changes in the Real Estate Commission's rules were needed to reasonably assure that real estate purchasers and sellers are properly informed of any compensation received by or offered to their brokers from another party to the transaction. The committee, which consisted of brokers, educators, attorneys, and a representative from the Consumer Protection Division of the Attorney General's office, found that there were promotions by builders and developers offering bonuses or special incentives to certain real estate brokers representing buyers without adequate disclosure to those buyers. These incentives ranged anywhere from $2,000 - $10,000 in cash, trips, or other prizes for selling particular properties. In most cases, the prices of the homes were increased to cover the cost of the bonus or incentive, meaning the buyers unknowingly paid the bonuses.

Sometimes the incentives were disclosed to the buyer, but in other instances, they were not. The committee recommended that the Commission's disclosure rule should be amended to clarify that:

- Disclosure of all compensation, including bonuses and incentives, should be made to the broker's client in writing, should be prominent, and should be acknowledged by the client;
- The value of any incentive should be disclosed and, if other than cash, described; and
- Disclosure should be timely (preferably while showing properties for which incentives are offered) but in no event not later than the time of offer.

After an investigation into the transactions that were the subject of the newspaper article, the Commission took disciplinary action against the brokers and firms involved for which sufficient evidence was discovered. The compensation disclosure rule, A .0109, was amended as a result of the committee's recommendations.

The rule as amended requires agents to do the following:

1. A broker in a sales transaction cannot be compensated by his client unless that compensation is provided for in a written agency contract meeting the requirements of Commission rule A.0104. Buyer agents and listing agents need written agency agreements in every transaction that provide for compensation.
2. A broker in a sales transaction cannot receive any compensation, incentive, or bonus of more than nominal value from any other party unless the broker provides full and timely disclosure of the payment or incentive, or the promise or expectation of such payment or incentive, to the broker's principal. This disclosure can be oral, but must be confirmed in writing before an offer is made or accepted by the principal.
3. Full disclosure requires a description of the compensation, incentive, or bonus, including its value and the identity of the party by whom it will or may be paid. The value can be expressed using a specific dollar figure, percentage or other mathematical formula. It is not sufficient to describe compensation as being any amount "up to" a certain amount, or "between" two figures. Disclosure is timely if it is made in sufficient time to aid a reasonable person's decision-making. To be timely to a buyer, the disclosure should be made at the time of showing if at all possible, but if not, at least prior to the submission of an offer.

The rule does not require a broker to disclose to a person who is not the broker's principal the compensation the broker expects to receive from the principal. It also does not require a broker associate, for example, to disclose to his or her principal the portion of compensation the broker-associate might receive from his employing brokerage firm.

The rule serves two policies. First, a consumer is entitled to know what the consumer will owe his own broker in connection with the consumer's real estate transaction. In addition, a consumer is entitled to know when his own broker is being paid by someone else in the transaction, and how much the broker is to receive if the consumer completes the transaction. If a broker stands to make a bonus if he sells a property in a particular subdivision, the buyer has a right to know and to decide whether or not the buyer wants to see homes outside the subdivision that might not offer the same bonus, but might be comparable and may be listed at a lower price.

How Do Brokers Disclose Compensation?
Whether the principal is a buyer or seller, compensation should be provided for in the required written agency agreement. If a buyer agent discovers a bonus or incentive is being offered on a property after the agency agreement has been executed, the disclosure can be made by any written means including email or subsequent written note.

Listing Agent Disclosure
Listing agents are required to have written agency agreements with their seller clients. The NCAR standard form listing agreement provides a place to disclose to the seller principal the listing broker's (firm's) compensation.

Buyer Agent Disclosure
The same is true for buyer agents. They are required to have written agency agreements with their buyer clients, and compensation can be disclosed in that agreement. NCAR has a standard exclusive buyer agency agreement that provides a place for disclosure of compensation. The form also indicates that the buyer agent may be offered additional compensation in the form of a bonus or incentive. The buyer agent or firm must still disclose the details of any bonus or incentive in writing prior to the time of the offer. NCAR has provided a new form for the disclosure of incentives or bonuses discovered after the agency agreement has been executed.

Subagents and Disclosure
What if you are handling the transaction for the buyer, but you are not a buyer agent, you are a subagent of the seller? No disclosure is necessary. Your principal is the seller, and he or she should have already received disclosure through the listing agent. If you have thoroughly discussed agency with the buyer, and the buyer has signed the *Working with Real Estate Agents* brochure which indicates you are a subagent of the seller, the buyer should understand that you do not represent him or her.

Dual Agency/Designated Agency
What compensation must a dual agent disclose? Remember that in most cases, the firm owns the listing and the buyer agency agreement, not the individual agents working the transaction. Disclosure to the seller is not an issue if it is done as part of the written listing agreement. Since the firm represents both the buyer and the seller, however, and since the firm is being paid by the seller, it must make a full compensation disclosure to its buyer client. This means the full amount of compensation or bonuses the firm is receiving from the seller.

Example: An agent working with a buyer may not know at the time of showing or at the time an agency agreement is signed with the buyer the full amount of commission on each property listed by the firm, plus any other incentives. Firms must make this information available to their brokers so disclosure can be made at the time of showing. If the information is not available at the time of the showing, the agent should make a good faith estimate of the firm's compensation and then follow up with full disclosure before an offer is made. If a broker assisting the buyer discovers a bonus is being offered at some point after the initial disclosure, the broker must disclose the bonus to the buyer immediately in writing. Emailing the buyer is a sufficient means of disclosure.

What About Special Types of Fees?
Example: A builder offers brokers incentives based on the number of properties sold. For example, when the individual broker sells 5 properties belonging to the builder, he receives a bonus of $5,000.00. The broker must disclose to his buyer client that the builder offers such an incentive, the amount of the incentive, and the fact that if the buyer purchases the property in question, the broker will either receive the bonus or have a future chance at receiving the bonus.

Example: A builder offers a firm incentives based on the number of properties sold. For example, when brokers with a certain firm sells 10 properties belonging to the builder, the firm receives a bonus of $10,000.00. If the firm represents the buyer either exclusively or in a dual agency situation, the firm must disclose the incentive arrangement with the buyer. An individual broker with the firm who knows or should know about the bonus is also required to disclose.

Example: A builder may pay a brokerage firm a fee for marketing a subdivision. These types of fees are sometimes paid to the brokerage firm at closing as each property sells. In such situations, a broker must disclose to his or her client that the firm receives fees for marketing the subdivision and that the fees are paid upon the closing of each property, and the amount to be paid based on the sale of the subject property.

Why Can't Brokers Just Disclose "Extra" Compensation in Addition to Their Commission?
In order to require only disclosure of "extra" compensation, the Commission would first have to establish what constitutes a base-rate of compensation. Since the Commission cannot set commission rates, nor can brokers lawfully agree among themselves as to a base-rate (because of federal anti-trust laws), it is impossible to require brokers to disclose only "extra" compensation. A broker could simply add the incentive to the base-rate in the transaction, call it all commission, and disclose nothing to the buyer.

2010 Incentive Disclosure Implementation Advisory Committee
In 2010, the Commission convened an Incentive Disclosure Implementation Advisory Committee to evaluate complaints and criticisms of the incentive disclosure rule and to recommend changes, if necessary, to disclosure requirements in dual agency transactions. The committee concluded that many brokers misunderstand the current disclosure rule and believe the rule is limited to a disclosure of additional or incentive compensation, and do not understand that in a dual agency situation, the firm must disclose total compensation to the buyer client. A majority of the committee concurred that full disclosure should remain the rule, including dual agency transactions, where the greater risks to the buyer also arise.

As with everything else, the amount of any incentive or bonus, whether cash or a non-cash item such as a trip, must be disclosed on the HUD-1 closing statement.

Potential for Disciplinary Action for Failure to Disclose Compensation
With all the disclosure requirements, the Commission will look at all the facts and circumstances surrounding a particular transaction before making a decision as to whether a broker acted inappropriately in disclosing compensation. Some of the factors that would be considered in connection with a complaint that a consumer was not given full and timely disclosure of the firm's compensation as required by the rule include:

- whether the broker gave the consumer a good faith estimate and how close the estimate was to the actual compensation paid;
- whether the broker had any reason to suspect the compensation might be different than disclosed;
- whether the compensation received was more, or less, than the amount disclosed;
- what systems were in place by the firm to make the information available;
- whether the broker utilized the firm's systems but, because of unusual circumstances, was unable to obtain the necessary information;
- whether the failure to disclose was exceptional, or the standard operating procedure of either the broker or the firm; and
- all other relevant facts and circumstances concerning the particular transaction.

The Commission will not generally impose discipline against a licensee who has made an error acting in good faith, particularly when the licensee has taken reasonable steps to obtain and disclose the correct information, and when any error was corrected without harm or significant risk to a member of the public.

36. A pest control company solicits real estate brokers to join their "Preferred Broker Program." Among other benefits, the company offers all broker participants quarterly pest control services at their personal homes at no charge. In order to receive the free pest control, the broker must refer their buyer clients to the pest control company for the completion of lender-required pest inspections. This is a lawful referral of business.

ANS: **False** REF: Vol. 47, No. 3, February 2017
RESPA ► Referrals ► You

A pest control company solicits real estate brokers to join what they refer to as a "Preferred Broker Program." Among other listed benefits of becoming a Preferred Broker, the company offers all broker participants quarterly pest control services at their personal homes at no charge. In order to receive the free pest control, the broker must refer their buyer clients to the pest control company for the completion of lender-required pest inspections.

The question posed to the Commission's legal staff was whether this type of program is in violation of the Real Estate Settlement Procedures Act (RESPA). RESPA prohibits kickbacks and unearned fees in any real estate transaction involving a federally related mortgage loan. The kickback provision is generally referred to as RESPA's "Section 8."

Section 8 prohibits anyone, including real estate brokers, from "… accept[ing] any fee, kickback, or thing of value…" as "…part of, a real estate settlement service involving a federally related mortgage loan…" 12 U.S. Code Chapter 27 § 2607(a).

A "thing of value" is any payment, advance, funds, loan, service, or other consideration with more than nominal value.

"RESPA also defines the term "Settlement service" as any service provided in connection with a real estate settlement for which the buyer or seller will pay. These services include, but are not limited to, the following:

- title searches,
- title examinations,
- the provision of title certificates,
- title insurance,
- services rendered by an attorney,
- the preparation of documents,
- property surveys,
- the rendering of credit reports or appraisals,
- pest and fungus inspections,
- services rendered by a real estate agent or broker,
- the origination of a federally related mortgage loan (including, but not limited to, the taking of loan applications, loan processing, and the underwriting and funding of loans), and
- the handling of the processing, and closing or settlement.

When a lender requires a buyer to have a pest inspection as part of the loan qualification process, the inspection is considered a settlement service. On the other hand, if a seller independently chooses to have a pest inspection as part of the listing process, and pays for that service separately from the settlement process, it is not related to the real estate settlement and is not considered a settlement service.

If a broker receives a quarterly pest control from the pest control company at no cost, a service that would typically have an associated cost, they have received a "thing of value." And if that broker receives that thing of value for referring a client to the pest control company to do a lender-required pest inspection, there is very likely a RESPA violation.

Even if the broker is referring a client to the pest control company for services unrelated to a closing and there is no apparent problem with RESPA, the broker must fully disclose their arrangement with the pest control company to their client per Commission Rule A .0109.

As you can see from the example above, whether a referral is prohibited under RESPA depends greatly on the specific transaction. If you are confronted with a business referral program, use the following fill-in-the-blank sentence as a test to determine whether the program may be in violation of RESPA: *As part of this program, I will receive _____, which will enrich or benefit me or my firm, in exchange for referring clients to _____ for services related to a real estate settlement.* If you can fill in these blanks, the safest course is to consider the program a no-go.

37. Real property may be offered as a prize in a raffle by certain organizations, but not individuals, provided the maximum appraised value of the real property to be raffled is $500,000.

ANS: **True** REF: Vol. 40, No. 2, June 2009
New Law Affects Property Raffles

The Real Estate Commission often gets calls from licensees and homeowners seeking alternative ways to bring about sales. One such method suggested by callers is to raffle a home. The seller would sell raffle tickets, the winning ticket-holder would receive the property, and the seller would receive the proceeds.

In the past, the answer was clear that under North Carolina law, no real estate could be offered as a raffle prize under any circumstance. However, in May 2009, the N.C. General Assembly amended N.C.G.S. §14-309.15 to allow real property to be offered as a prize in a raffle by certain organizations.

The maximum appraised value of the real property to be raffled is $500,000 for any one prize and the *(Continued from page 1)* total appraised value of all real estate prizes offered by one nonprofit organization may not exceed $500,000 in any one calendar year.

Licensees must note that the statute authorizes only nonprofit organizations or government entities to conduct raffles.

Sellers might ask if they would qualify if they donated a portion of the raffle proceeds to a charity. However, the statute provides that the proceeds of the raffle may not be used to compensate any person to conduct a raffle. The Commission, therefore, takes the position that *the seller may not receive any part of the raffe proceeds nor may a licensee receive any fee or commission from the raff e proceeds.*

A person conducting a raffle in violation of N.C.G.S. §14-309.15 shall be guilty of a Class 2 misdemeanor. Additionally, licensees and the public should be aware that there may be surprising tax consequences of winning a real estate raffle. Licensees should advise any participant in such a raffle to consult a tax advisor concerning the tax consequences to the winner. For example, in the current tax year, the home may be reportable as ordinary income, leading to a large income tax bill.

Further, when the winner decides to sell the home, he or she may encounter a large capital gains tax because the cost basis for the home will be the ticket price rather than the value of the home.

Section Five:

Closings – CFPB-HUD

38. NC law requires brokers, 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.

ANS: **True** REF: Vol. 46, No. 3, February 2016
TRID v. HUD-1 – What's a Broker to Do?

For any licensees who may have missed it, the new TILA-RESPA Integrated Disclosure Rules (TRID) became effective October 3, 2015. This has caused a lot of concern for brokers and closing attorneys in North Carolina, and has raised some questions as to how the Real Estate Commission might consider a broker's duty under G.S. §93A-6(a)(14) in light of the new federal law, as well as whether or not a statutory change might be necessary.

First, G.S. §93A-6(a)(14) states that the Commission has the authority to discipline a licensee if, following a hearing, the Commission determines that the licensee is guilty of "failing, 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." That duty remains unchanged. A broker must detail **for his client** all receipts and disbursements relating to the transaction **about which the broker knows or reasonably should know**. A broker is not expected to provide an accounting to a party who is not the broker's client, nor is the broker required to learn of items about which the broker does not know or reasonably should not know.

For example, a broker who knows that the seller paid the buyer a concession and that is not disclosed or that the buyer inspection costs are inaccurately stated cannot ignore those facts. However, a buyer's agent may not know or have reason to know that the seller hired a roofer to replace a shingle and that item is being paid as part of the closing.

The statute goes on to state "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." This has provided comfort to brokers and Commission staff alike in the past as it alleviated the broker's duty to prepare any accounting but still required the broker to review the statement prepared by the attorney for accuracy and to report any discrepancies the broker knew of or should have known about. With the exception of those inclined to commit loan fraud, the Commission has rarely had any occasion to use this particular section when considering whether or not to discipline brokers.

Some closing attorneys continue to produce a closing statement or ALTA settlement statement, a settlement statement in addition to the required disclosure statements. Others are preparing something similar. Remember that the law does not require review of the specific HUD-1 closing statement, only of a generic "closing statement." In cases where an attorney provides some form of closing statement, brokers may continue to rely on the attorney's document as long as they review it and report any errors. The confusion for brokers arises in situations where the closing attorney is not using the HUD-1 or any other familiar form of a closing statement in addition to the required closing disclosures. The closing disclosure for the buyer, and the closing disclosure for the sellers, when viewed together, are sufficient.

While the NCAR standard form contract now specifically authorizes the release of these disclosures to the parties and their brokers, in many cases, the broker is not provided with both sides for review.

What is a broker to do then?

Listing Agent Duties - TRID rules permit a settlement agent to provide the seller with a separate Closing Disclosure or with a copy of the Buyer/ Borrowers' Closing Disclosure as long as it contains all of the seller's transaction information. A broker representing the seller should review the disclosure and report any inaccuracies. The broker may or may not be given a copy of the buyer's disclosure. In that case, the broker is not obligated to disclose what the broker is not given. A broker may not refuse to look at the disclosure if offered or emailed to the broker, but if the broker is not provided with a copy of the buyer's disclosure, the broker must review the seller's disclosure and correct any errors contained therein. If a broker knows or reasonably should know of a receipt or disbursement related to the transaction that is left off of either disclosure, the broker must disclose the possibility of the receipt or disbursement as a material fact to the closing attorney and lender.

Buyer Agent Duties - If the settlement agent provides the seller with a separate Disclosure, then the settlement agent must also provide a copy of the Seller Closing Disclosure to the borrowers' lender, but not to the borrower. While the buyer agent may not necessarily see the Sellers' Closing Disclosure, the buyer agent may see a summary of the sellers' side of the transaction on page 3 of the buyer's Closing Disclosure, as with the current HUD-1. A broker representing the buyer may still rely on these, but should review the buyer's disclosure and the summary of the seller's side, and report any discrepancies or omissions. Again, the broker is not obligated to disclose information not provided.

The Commission will continue to monitor this process as it evolves, and if a statutory change is necessary, will proceed in that direction. For the time being, brokers should review the disclosures or closing statements they have access to, refrain from avoiding access when offered, and be sure to disclose any errors, discrepancies, or omissions of which they know or should have known.

39. Lenders are permitted to provide the required Closing Disclosure to real estate agents.

ANS: **True** REF: Vol. 47, No. 2, June 2016

CFPB to Ease Access to TRID Closing Disclosure

The Consumer Financial Protection Bureau CFPB) recently issued proposed amendments to its TILA-RESPA Integrated Mortgage Disclosure forms and rules, one of which is intended to clarify that lenders are permitted to provide the required Closing Disclosure to real estate agents.

The new disclosures (commonly referred to as "TRID", but dubbed "Know Before You Owe" by the CFPB) replaced the previous disclosure forms required in all "federally-related" mortgage transactions, including the "HUD-1" settlement statement, with the CFPB's residential mortgage Loan Estimate and Closing Disclosure forms.

Since the implementation of the TRID rules nearly a year ago, many real estate agents have experienced difficulties in obtaining copies of completed Closing Disclosure forms from lenders. The issue involves lender concerns about potential liabilities arising under the privacy provisions of the federal Graham-Leach-Bliley Act (GLBA), which prohibit lenders from disclosing customers' "nonpublic personal information" (NPI) to nonaffiliated third parties without providing customers with notice and an opportunity to opt-out of such disclosure.

[The Closing Disclosure has also raised questions in some state real estate regulatory jurisdictions whose licensing laws require brokers to ensure that transaction parties receive a closing statement. [See, *Real Estate Bulletin* February 2016]

In its proposed rulemaking notice the CFPB acknowledges that prior to implementation of the TRID rules, the Real Estate Settlement Procedures Act and its implementing regulations required settlement agents to issue a HUD-1 form to lenders, borrowers, sellers, and their agents. The CFPB also recognizes that many transaction participants rely on shared information to complete residential transactions; including real estate agents, loan officers, settlement agents and others. Consequently, the CFPB proposes to amend its rules to acknowledge that, in accordance with applicable exceptions to the privacy requirements of the GLBA, it is "usual, appropriate, and accepted" for creditors and settlement agents to provide the combined or separate Closing Disclosure to transaction parties and their real estate brokers or other agents. This will be accomplished by incorporating the CFPB's previous informal guidance on the subject into the official rule commentaries to clarify that the lender, at its discretion, "may make modifications to the Closing Disclosure form to accommodate the provision of separate Closing Disclosure forms to the consumer and the seller...". The commentaries will also explain the methods by which creditors can separate buyers' and sellers' information for that purpose.

Section Six:

Fraud & Scams

40. Licensees should know now that even "little white lies" by a borrower on a mortgage loan application and supporting documentation constitutes mortgage fraud.

ANS: **True** REF: Vol. 40, No. 3, January 2010
Borrower Beware

Many borrowers fudge a little when applying for a loan. The truth is, any lying on a real estate loan application is mortgage fraud.

Speaking about mortgage fraud, U.S. Attorney General Eric Holder said "these crimes have devastated and driven away many who were once willing to invest in our economy. They've robbed people of their homes and their economic security. They've depleted bank accounts and pension funds. In some places, they've dried up philanthropic giving and shuttered charities. They've placed unfair challenges before cash-strapped governments, local police departments, small businesses, and American workers and consumers."

Given the steep rise in foreclosures and bank failures from bad loans, and the resulting economic decline, licensees should know now that even "little white lies" constitute mortgage fraud.

41. Brokers should be wary of any down-payment assistance program in which the home seller makes a gift to a purported charity and the buyer receives a gift of roughly the same amount from the charity (minus fees and expenses) to use as a down-payment to buy the seller's house.

ANS: **True** REF: Vol. 37, No. 1, June 2006
Down-payment Gift Programs

The Internal Revenue Service has just issued a ruling (Rev. Rule 2006-27) on organizations that provide seller-funded down-payment assistance to home buyers.

Down-payment-assistance programs provide cash assistance to home buyers who cannot afford to make the minimum down payment or pay closing costs involved in obtaining a mortgage. Such programs can qualify as tax-exempt charitable and educational organizations when property structured and operated. In the ruling, the IRS provides detailed discussion of the guidelines-including two examples that meet and one that fails to meet the test for exemption.

The ruling makes it clear that seller-funded programs are not charities because they do not meet the requirements of section 501 (c)(3). Increasingly, the IRS has found that organizations claiming to be charities are being used to funnel down-payment assistance from seller to buyers through self-serving, circular-financing arrangements. In a typical scheme, there is a direct correlation between the amount of the down-payment assistance provided to the buyer and the payment received from the seller. Moreover, the seller pays the organization only if he sales closes, and the organization usually charges an additional fee for its services.

What happens when an organization does not qualify as a tax-exempt organization? No tax deduction will be allowed to the seller for a charitable contribution. The home buyers may not be able to include the amount of the assistance in the cost basis of their home. The assistance will probably no longer qualify as a third-party gift for the purposes of the buyer's loan application. Consequently, the lender will have to treat the payment as seller concession, deduct the concession for the value of the property and recalculate the buyer's loan-to-value ratio. If the buyer cannot come up with the required down-payment another way, his/her loan application will be denied.

Brokers are cautioned to be wary of any down-payment assistance program in which the home seller makes a gift to a purported charity and the buyer receives a gift of roughly the same amount from the charity (minus fees and expenses) to use as a down-payment to buy the seller's house. Such programs may not be what they claim to be and may violate the IRS ruling. Misrepresentation of such a program to a lender or party in a real estate transaction would be a violation of the North Carolina Real Estate License Law and may constitute loan fraud.

You can find the news release and the ruling at www.irs.gov/newsroom, click on "News Releases", then on "IRS Targets Down-Payment Assistance Scams", or https://www.irs.gov/charities-non-profits/questions-and-answers-down-payment-assistance-programs.

42. Due to the proliferation of mortgage loan schemes, the NC Real Estate Commission has created a Financial Fraud Unit to investigate such cases and to work with state and federal law enforcement agencies.

ANS: **True** REF: Vol. 41, No. 3, June 2010
Commission Creates Financial Fraud Unit

With the number of mortgage fraud investigations rapidly escalating, the Commission created a new Financial Fraud Unit to investigate these cases and to work with state and federal law enforcement agencies to bring appropriate cases for criminal prosecution.

Janet B. Thoren, the Commission's Chief Deputy Legal Counsel and a Special Assistant United States Attorney, will supervise the unit. Michael Gray, the Commission's former Chief Auditor/Investigator, has been designated as the Chief Financial Fraud Investigator. As an investigator with the Commission for the past 14 years, Mr. Gray focused almost exclusively on mortgage fraud cases since 2000. In addition, the Commission has employed D. Scott Schiller in the position of Financial Fraud Investigator. Mr. Schiller, a former Special Agent with the Internal Revenue Service Criminal Investigation Division, has an extensive background in criminal investigation and mortgage fraud.

The Financial Fraud Unit is responsible for investigating mortgage fraud cases involving real estate licensees and working with federal and state agencies to promote the criminal prosecution of those involved in mortgage fraud.

43. North Carolina Statutes govern every option contract executed along with a lease agreement and, among other things, the law dictates that every such option contract contain at least nine specific disclosures and also provides every purchaser a three-day right to cancel such an option contract.

ANS: **True** REF: Vol. 44, No. 3, February 2014
Commission Cracks Down on Firms Offering Illegal Leases, Credit Repair

The Commission recently investigated and disciplined two licensed real estate firms following receipt of complaints from consumers entering into certain residential leases.

The disciplined licensees all engaged in a business model that focused on an option to purchase agreement executed at the time of the lease. In both cases, tenant/buyers would make a significant down payment to obtain an opportunity to purchase the property within a certain time and for a set price.

As a rule, the tenant/buyers were unqualified for traditional financing, and were promised credit repair programs that would enable them to obtain financing when the time came to buy their home at the end of the lease term.

Problems arose for the formerly licensed firms when many tenant/buyers realized that their rental units were being foreclosed upon in the middle of their tenancy, making their option to purchase worthless.

Others discovered that promises made by the real estate firms regarding their credit repair services were untrue. After many months of following the advice of credit counsellors, these consumers found themselves just as unqualified to purchase their home as they were when they first began their tenancy.

These firms and their brokers are no longer licensed because they were ignorant of, or simply did not adhere to, the regulations and statutes governing option contracts and credit repair services.

As a caution to anyone participating in a real estate transaction involving option contracts or promises of credit repair, this article will touch on the uses, regulations, and pitfalls that arise when the lease with option to purchase scenario is utilized.

We'll also consider the credit repair services these firms offered and things to know if approached with questions from one of your real estate clients.

The Lease with an Option to Purchase
The tightening of residential mortgage lending following the recent economic downturn forced many homeowners to rent their homes when qualified buyers became scarce. Some builders and homeowners found tenants willing to pay an upfront, nonrefundable down payment to secure the right or option to purchase the property at a set price in the future. Such arrangements could legitimately provide the seller immediate cash and security in knowing that they had a good tenant in their home along with the expectation of a future closing.

Similarly, tenants who may have lost a job or gone through bankruptcy or a prior foreclosure were sometimes able to negotiate a competitive purchase price for a future closing, allowing them time to qualify for a mortgage.

In a typical, legitimate lease with option to purchase transaction, both the potential tenant-buyer and the seller risk losses in exchange for the promise of a future gain should the deal close. The tenant risks the non-refundable option fee, and the seller risks the possibility of a sale at a later date.

In the transactions investigated by the Commission, alleged "investors" offered to secure the tenant for the homeowner, and charged an upfront fee to the tenant for a future right to purchase the seller's home. In such cases, the "investor" risked nothing and had no motivation to ensure the success of the transaction or compliance with state laws. In fact, when a prospective purchaser defaulted under the option to purchase or lease, the "investors" kept the option fee, a new tenant was found and charged a new option fee also retained by the "investor." Therefore, failed transactions actually provided better opportunities for these "investors" to realize greater gains.

North Carolina General Statutes, Chapter 47G, govern every option contract executed along with a lease agreement. The law dictates that every such option contract contain at least nine (9) specific disclosures and details of the transaction. State law also provides every purchaser a three-day right to cancel such an option contract, and guarantees the right to a refund of any property exchanged or payments made by the purchasers if cancelled timely.

The seller is also required to record the option contract, or a memorandum of the same, in the office of the register of deeds in the county where the property is located. These are a few of the many statutory requirements in our State with which the disciplined real estate
firms failed to comply.

Credit Repair Providers

With very few exceptions, anyone offering credit repair programs must complete the promised programs prior to collecting or charging a fee. The firms that recently lost their licenses with the Commission charged upfront or monthly enrollment fees to participate in their advertised credit repair program.

The firms also falsely promised they could remove legitimate debts from consumer credit reports and gave deceptive advice on how to improve credit. While these guarantees were hollow, the promise of better credit was the hook for prospective purchasers who wanted to own a home now, but did not qualify for traditional financing.

There are two acts governing credit repair services in North Carolina. The first is the Federal Credit Repair Organizations Act, 15 U.S.C. 41, and the second is the North Carolina Credit Repair Services Act, N.C.G.S. § 66-220.

Both of these laws prohibit credit repair providers from making any statement or giving any advice that is untrue or misleading. They also require that credit repair companies make certain disclosures and give the opportunity to cancel a credit repair contract. Most importantly, the laws provide for civil liability for violations and protect consumers by making noncompliant contracts void.

When the Commission investigated the licensees offering credit repair, it found that not only were their services noncompliant with state and federal laws, but that the individuals were unaware of the strict regulation of their activities.

The Federal Trade Commission advises consumers that when they see the common claims and advertisements guaranteeing perfect credit in very little time, consumers should do themselves a favor, save the money, and avoid what's likely a scam. The only way to improve consumer credit is with time, effort, and a personal debt repayment plan.

Legitimate credit counselling providers are available through military bases, credit unions, non-profit groups, housing authorities, or consumer protection agencies.

There is also a list of government-approved organizations available at www.usdoj.gov/ust that work with folks prior to filing bankruptcy. As a broker, if you have a client who requests help repairing credit, be sure to caution them about potential scams and suggest they contact their financial institution or consult the above government-approved list of providers.

Section Seven:

Appraisal & BPOs

44. There is no prohibition against real estate brokers contacting and "talking" to the appraiser of a property in which the broker represents one (or both) of the parties.

ANS: **True** REF: Vol. 44, No. 2, October 2013
Can I Talk to the Appraiser?

There is NO prohibition against real estate brokers contacting and "talking" to the appraiser. However, there are clearly topics and facts that the appraiser CANNOT discuss or share with anyone other than the appraiser's client. (Typically, the client is the LENDER.)

Appraisers are highly regulated both on the state and federal levels. "Appraiser Independence" is the Law under Dodd-Frank (Wall Street Reform and Consumer Protection Act), and there are certainly circumstances where a broker can contact and "talk" to the appraiser. The national housing market downturn brought numerous regulatory changes to the real estate industry, including the entire appraisal process. Dodd-Frank legally sunset the Home Value Code of Conduct and required the Federal Reserve to amend the appraisal independence rules of Regulation Z of the Truth in Lending Act. The interim final rule effective April 1, 2011, applies to all consumer credit transactions secured by a consumer's principal dwelling. Fannie Mae and Freddie Mac servicing guidelines now reflect this rule. In addition, state laws and regulations require appraisers to comply with Uniform Standards of Professional Appraisal Practice (USPAP). Among many other things, this legislation and the accompanying rules include exactly what can be "asked" of an appraiser.

Recognize that the appraiser's function is to develop an independent, impartial and objective opinion of the value of the property for the lender to determine what the underlying collateral value is to base their financial lending decision on.

First, <u>the Ethics Rule of USPAP prohibits appraisers from "Disclosing"</u> 1) confidential information or 2) assignment results to anyone other than the "Client" (i. e.; entities or persons authorized by the client).

Secondly, language in Dodd-Frank states: "The requirements …. shall not be construed as prohibiting a ….. real estate broker, ….. or any other person with an interest in a real estate transaction from asking an appraiser to undertake one or more of the following: 1) Consider additional, appropriate property information, including the consideration of additional comps ….. to make or support an appraisal, 2) Provide further detail, substantiation, or explanation for the appraiser's value conclusion, 3) Correct errors."

This language does not allow a full blown "conversation" or "discussion" with the appraiser, but it does address the points that brokers can "ask" of an appraiser. However, this does imply that the flow of information is essentially one-way, from the broker to the appraiser. The broker CANNOT anticipate there will be any substantial "conversation" or "discussion" about the appraisal or conclusions.

It is unfortunate that some AMC's have instructed appraisers to significantly limit their interaction with otherwise interested parties to the transaction, creating much of the confusion on what type of contact and talk can be held with appraisers.

The most favorable "window-of-opportunity" to "talk" to the appraiser is as soon as the "appraisal inspection" is scheduled. There are many things that brokers and sellers can do to put the property in the best position possible for the most favorable appraised value outcome. The most important is providing as much accurate, current and detailed information on the subject property as possible. Most of that information can easily be provided through the local MLS (including as many photos as the MLS will allow), which is not only beneficial to the appraiser of the subject property but equally beneficial when the appraiser uses that same information as a future comparable and especially to potential buyers during their search process. This important information is the first opportunity for the listing broker to provide factual insight into the subject property and also disseminates the broker's unique knowledge of the local real estate market through supporting information and often supporting documentation.

Brokers are allowed to contact appraisers and provide additional Property information, including a copy of the sales contract for purchase transactions. Brokers may not intimidate or bribe an appraiser and an appraiser may not disclose confidential information about the appraisal or the assignment at any time.

Therefore, the "new-normal" is the development of an "appraisal package" on every property which comes under contract and subject to a mortgage. Make the "appraisers package" available at the property for the appraisal inspection, or meet the appraiser at the property so you can answer any questions, and inform the appraiser of the unique factual features of the property or neighborhood, and make sure you allow the appraiser the space and time to complete their inspection. The appraisers package could include plats, surveys, deeds, covenants, HOA documents, floor plans, specifications, inspection reports, neighborhood details, recent similar quality comparables, detailed list and dates of upgrades, remodels or repairs, recent CMA's, etc. Provide the seller/buyer a copy of the brochure developed by The Appraisal Foundation entitled "A Guide to Understanding a Residential Appraisal" available for download at *http://www.realtor.org/appraisal/a-guide-to-understanding-a-residential-appraisal.*

45. A broker who performs a BPO for a fee must provide the BPO in writing, estimating only the "probable selling or leasing price" of a property (not the "value" or "worth" of a property), and the BPO must not be referred to as a "valuation" or "appraisal."

ANS: **True** REF: Vol. 43, No. 2, October 2012

New BPO Laws, Rules Adopted – Effective October 1, 2012

The North Carolina General Assembly recently enacted important amendments to both the Real Estate License Law and the Appraisers Act regarding the extent to which a broker may perform a broker price opinion (BPO) or comparative market analysis (CMA) for a fee. The Real Estate Commission has adopted temporary rules implementing the License Law changes, **effective October 1, 2012.**

The Primary Law Changes

A **"non-provisional" broker** whose license is in good standing and on active status may prepare a broker price opinion (BPO) or comparative market analysis (CMA) and charge and collect a fee for the opinion. The BPO may now be performed 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** (i.e., a broker who has not completed all postlicensing courses and thereby removed his or her "provisional" status) may no longer perform a BPO or CMA **for a fee** for anyone. (The Appraisers Act previously allowed any real estate licensee to perform a CMA for a fee, but **only** for an actual or prospective client or for property involved in an employee relocation program.)

A broker who performs a BPO for a fee must provide the BPO **in writing,** estimating only the **"probable selling or leasing price"** of a property (not the "value" or "worth" of a property). The BPO must NOT be referred to as a "valuation" or "appraisal." A broker may NOT prepare a BPO for an existing or potential lienholder (e.g., mortgage lender) 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.

A "broker price opinion" and a "comparative market analysis" are defined as synonymous terms in both the Real Estate License Law and Appraisers Act.

Standards for Performing a BPO

The Commission's rules set out the standards for performing BPOs and require that the broker:

- have knowledge of, and access to, market data in the subject property's local area;
- exercise objective, independent judgment;
- inspect the subject property, unless the client expressly waives an inspection in writing;
- use methodology (analysis of comparable sales and/or income analysis) that is appropriate for the particular assignment;
- select comparable sold or leased properties and make necessary adjustments;
- include information about local market conditions and each method used in deriving the estimate of probable selling or leasing price; and
- explain the basis for any range in probable selling or leasing price when the higher figure exceeds the lower figure by more than ten percent.

Most of the standards addressed in the Commission rules for performing a BPO/CMA are *not new!* The Commission has for many years applied these standards to any CMA/BPO performed by a licensee, whether or not the CMA/BPO is performed for a fee, and these standards are required to be taught in pre-license and post-license courses.

BPOs/CMAs 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 the BPO law*. 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 the new Commission rules for guidance regarding the proper performance of a CMA/BPO.

Education on BPOs in Update Course, CE Electives and *Real Estate Manual*

The BPO law and rule changes are addressed in the current *Real Estate Update Course*, which licensees are urged to take as soon as possible. The *Update* coverage does not, however, attempt to address *how to properly perform a BPO/CMA.* For instruction on the proper performance of BPOs/CMAs, licensees are urged to attend a CE elective course on this topic that has been updated to reflect the recent law/rule changes. Updated coverage of proper performance of BPOs/CMAs will also be included in the next edition (2013-14 edition) of the Commission's *North Carolina Real Estate Manual* that will be available in January 2013. The complete law and rule changes may also be found on the Commission's Web site at www.ncrec.gov.

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Notes

Section Eight:

Commercial Practices

46. As with residential brokerage, commercial brokers must review the *Working with Real Estate Agents* brochure with prospective buyers and sellers at first substantial contact.

ANS: **True** REF: Vol. 44, No. 3, February 2014
Commercial and Residential Brokers Follow Same Laws, Commission Rules

Some commercial brokers have been surprised to learn that the Real Estate License Law (Chapter 93A of the North Carolina General Statutes) and the Commission's rules apply to commercial brokers as well as residential brokers. While there are some laws and rules that apply only in residential transactions, in general, most apply to both residential and commercial brokers alike. Here is a brief review of some important laws and rules that apply to everyone.

Any person or firm must first obtain a real estate license to engage in commercial or residential real estate brokerage activities. Commercial or residential real estate firms other than sole proprietorships must obtain separate firm licenses. An out-of-state broker who wishes to engage in commercial transactions in North Carolina may choose to either obtain a North Carolina broker license or a limited non-resident commercial broker license requiring affiliation with a resident North Carolina broker.

In both commercial and residential sales transactions:

- Brokers must review the *Working with Real Estate Agents* brochure with prospective buyers and sellers at first substantial contact. (Note: The brochure is not required for leasing transactions. Although the North Carolina Association of REALTORS® (NCAR) has created a form for use by its members in commercial leasing transactions, use of NCAR's form is not required by the Commission.)

- A commercial or residential *listing agent* must enter into a written listing agreement before beginning to market a seller's property, including placing a "For Sale" sign on a seller's property.

- A commercial or residential *buyer agent* must enter into a written buyer agency agreement no later than the point at which a buyer-client is ready to write an offer. Dual agency is permitted only after obtaining the advance, written authorization of all parties or sets of parties. Any broker who fails to properly establish his or her agency relationship in writing in a transaction is prohibited by law from receiving any compensation either directly or indirectly from the transaction. Similarly, in commercial or residential leasing transactions:

- Brokers who represent *landlords* must enter into written property management agreements before beginning to market or manage the landlords' properties.

- Brokers who represent a commercial or residential *tenant* must enter into a written agency agreement with the tenant no later than the point at which the tenant is ready to negotiate or sign a lease. Dual agency requires the advance, written authorization of all parties. Brokers, who represent landlords or tenants without written agency agreements, are prohibited from receiving compensation from those transactions.

Commercial and residential brokers must also handle trust monies in accordance with the Commission trust account rules, disclose material facts, retain transaction records for three years, and furnish all parties with copies of agency agreements and contracts.

This article is not intended to address all of the rules, but to remind both commercial and residential brokers of some of the Commission's requirements. When in doubt about any of the Commission's rules, brokers should contact the Commission's office and a member of our staff will be glad to provide more information and/or clarification.

Commercial, Residential Brokerage Fields Differ

If you are a residential broker without commercial brokerage experience or a commercial broker without residential brokerage experience, you will face considerable challenges if you choose to cross the professional line into the other realm.

Most of the real estate laws and Commission rules will apply, as the adjacent article explains, but the day-to-day conduct of business involving, say, a three-bedroom home compared with a three-story office building will differ greatly.

Any residential broker who wishes to venture into commercial real estate or vice versa, should consider partnering with an experienced broker in the new field to better learn both the business and how best to represent clients.

47. The Regulatory Affairs Division of the Commission sees many of the same compliance issues while investigating complaints or conducting audits in commercial practices as in residential practices.

ANS: **True** REF: Vol. 45, No. 3, February 2015
Top Ten Issues for Commercial Real Estate Brokers

The Regulatory Affairs Division of the Commission sees many of the same compliance issues while investigating complaints or conducting audits. The following list of compliance issues (and the Rule to which they relate) are common to most types of brokerage, but appear to be a particular concern for commercial brokers.

The *Working with Real Estate Agents* disclosure [Rule A.0104(c)].
Commercial agents can be sporadic with their use of this required disclosure; here are the basics:

- The rule requires brokers to provide and review the disclosure "at first substantial contact" with prospective buyers or sellers and to disclose or determine who the broker represents or could represent in the transaction. • Brokers are not required to review the disclosure with parties who are already represented by a broker, but must disclose in writing whom they represent.
- The disclosure is also not required in lease transactions, but the North Carolina Association of REALTORS® publishes a *Working with Real Estate Agents* disclosure for lease transactions and its use is encouraged.

Written agency agreement [Rule A.0104(a)].
The need for a written agency agreement is overlooked more often in commercial brokerage. The minimum requirements to adhere to:

- There is no "transactional brokerage" in N.C.; brokers either represent the buyer/tenant, the seller/landlord, or both, pursuant to a written agency agreement.
- When representing the buyer or tenant, the agency agreement must be in writing prior to making or receiving an offer to buy or lease.
- When representing the seller or landlord, the agency agreement must be in writing prior to offering the property for sale/lease.
- The minimum requirements for an agency agreement are that it must:
  - Provide for its existence for a definite period of time,
  - Include the agent's license number,
  - Include the nondiscrimination language prescribed in Rule A.0104(b).

Timely disclosure of representation [Rule A.0104(d-j)].
Most brokers are careful to inform the parties to a transaction who the broker represents, but commercial brokers often neglect to put this in writing. Always remember to:

- Disclose in writing to an unrepresented buyer/tenant that the broker represents the seller/landlord at first substantial contact. The *Working with Real Estate Agents* brochure is written to do this –use it.
- Disclose at first contact with a seller/landlord that the broker represents the buyer/ tenant, and do so in writing no later than with the submission of an offer.
- Get authorization from each party to practice dual agency in the agency agreement, and disclose the practice of dual agency in the same manner that you disclose representation to the seller and buyer above.

Timely disclosure of material facts [N.C.G.S §93A-6(1)].
Commercial brokers tend to see the discovery of material facts to be the job of the buyer/tenant and/or their agent. However, all brokers have a duty to make objective inquiries to discover material facts, and to verify information provided by the broker's client when it is reasonable to do so. Some of the basics to remember regarding disclosure of material facts:

- "Timely disclosure" is in time for a party or prospective party to a real estate transaction to make an informed decision to buy, sell or lease or to continue with a transaction.
- Generally, a party's motivations are not material, but facts relevant to the property or a party's ability to buy, sell or lease are material.

Disclosure of compensation to the agent's principal [Rule A.0109(c)(d)].
There is generally no duty for a broker to disclose his or her compensation to a party whom the broker does not represent. However, the total compensation a broker (or the firm) expects or receives is a material fact to that broker's client. Remember the following:

- Disclose to your client any offered/expected compensation, incentive or bonus in writing prior to your client making a decision to buy or sell.
- However, a broker is not required to disclose to anyone the broker's expected split of compensation with the broker's firm.

Deposit of trust money into a trust account (Rule A.0116(a)(b)). Commercial brokers acting as couriers of rent or other trust monies is a common issue. With the exception of option and due diligence fees, brokers are required to deposit all funds received in their fiduciary capacity into a trust account. The timing of such deposits are as follows:

- Earnest money or security deposits received in a form other than cash in conjunction with a pending offer to purchase or lease shall be deposited in a trust account no later than three days following contract acceptance.
- A broker may accept custody of a check made payable to the seller for an option or due diligence fee and deliver it to the seller according to the instructions of the buyer.

Representing a buyer in the purchase of property in which the broker has ownership interest [Rule A.0104(o)].
This has always been a conflict of interest, but now it is specifically prohibited by rule (as of July 1, 2015) 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 percent 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. Another broker with the firm may represent the buyer so long as that broker does not have an ownership interest and the buyer consents after full disclosure.

Broker purchasing his/her own listing [Rule A.0104(p)].
Another potential conflict of interest is specifically addressed by a new rule. A broker must disclose the inherent conflict of interest in writing to the seller and suggest the seller seek independent counsel. Prior to entering into an agreement to purchase, the broker must terminate the listing agreement or transfer to another broker affiliated with the firm who will not have an interest in the purchase.

Co-brokering with out-of-state brokers [Rule A.0109(g), A.1810].
Commercial brokers frequently work with out-of-state brokers representing buyers or tenants in N.C. transactions. N.C. brokers may pay a commission or fee to brokers licensed in other states so long as the foreign broker does not enter N.C. Foreign brokers practicing commercial real estate have two options for licensure in N.C.:

- Limited Nonresident Commercial License: Available to active, licensed brokers from other states by application; only for commercial brokerage.
- Nonresident License: Available to active, licensed brokers from other states by application and passing the "state" portion of the licensing exam; full brokerage privileges.

Record retention [Rule A.0108].
The Commission tends to see inconsistent record retention among commercial brokers with greater frequency. Rule A.0108 lists many of the documents that must be retained, but it is not exclusive. Brokers should retain *all* documents related to both failed and successful real estate transactions including offers, contracts, disclosure documents, agency and commission agreements and correspondence such as emails or texts. Remember the following:

- Records should be maintained for three years from the later of the closing of the transaction or the end of the agency relationship;
- Electronic records are sufficient so long as they are complete, are properly protected and can be made available without prior notice.
- Records help prove your side of the story.

The foregoing is only a basic treatment of these topics. If you have questions or concerns regarding compliance issues or wish to discuss a particular scenario with someone in the Regulatory Affairs Division, call the Commission at 919-875-3700 and ask to speak to an Information Officer or email us at regulatoryaffairs@ncrec.gov.

Section Nine

Property Management

48. Commission Rules requires brokers to enter into a written property management agreement before beginning to manage an owner-client's property, and the broker must operate within the authority granted by the agreement.

ANS: **True** REF: Vol. 41, No. 3, June 2011
Top Ten Issues for Property Managers

In the course of answering numerous telephone inquiries and investigating complaints led against brokers, the Commission's legal staff has identified some issues which, if handled properly, can help maintain good relationships between property managers and their owner-clients.

ONE: Have a written property management agreement and operate within the authority granted by the agreement. Commission Rule A.0104(a) requires a broker to enter into a written property management agreement before beginning to manage an owner-client's property. The agreement should include all terms and conditions including when rent proceeds will be sent to the owner-client, the extent of the background checks for prospective tenants, the frequency of inspections and authorization for repairs

TWO: Inquire about the status of the mortgage on rental property (if applicable). In today's economy, foreclosures have become common. Before accepting a rental property, a broker should ask the owner whether the mortgage is current, whether the rent proceeds will cover the mortgage payments and whether the owner has sufficient funds to cover the mortgage payments in the event that the rental property becomes vacant or the tenant stops paying rent.

THREE: Verify the qualifications (i.e. income, credit, rental history, etc.) of a prospective tenant before renting the property. Thorough background checks of prospective tenants may reduce the risk of nonpayment of rent, early termination of leases and property damage by tenants

FOUR: Perform move-in and move-out inspections and make periodic inspections during each tenancy. Document in writing and with photographs (when necessary) the condition of a rental property before and after each tenancy. This will help assign responsibility for damages to the property.

FIVE: Deposit all monies collected into a trust account before disbursing to owners, vendors or to yourself for management fees. Brokers are prohibited from depositing rent monies or security deposits directly into an owner-client's account. All monies collected by a broker in the course of managing an owner-client's property are trust monies and must be deposited into the broker's trust account.

SIX: Remit rent proceeds to owners in a timely manner. Brokers should allow sufficient time for rent checks to clear their respective banks and then promptly disburse rent proceeds to the owner-clients. The broker's policy should be clearly set forth in the property management agreement.

SEVEN: Keep owner-clients informed regarding tenant issues (i.e. non-payment of rent, damages, etc.) and financial issues. A broker should notify the owner-client immediately regarding repairs, nonpayment of rent and other serious issues affecting the rental property. Accurate monthly statements will provide the financial information needed by owner clients.

EIGHT: Maintain properties in safe and habitable condition and obtain authorization for repairs exceeding the amount set out in the management agreement. A property owner and his agent are responsible for maintaining residential rental properties in safe and habitable condition. This means that repairs, safety issues and conditions such as insect infestations should be addressed promptly. Property management agreements should indicate the extent of the broker's authority to take corrective action. If a broker agrees to contact an owner regarding corrections that will exceed a certain cost, then this agreement should be specified in the property management agreement.

NINE: Limit deductions from security deposits to those allowed by the Tenant Security Deposit Act and educate owner-clients to expect normal wear and tear. Brokers must use good judgment and be reasonable when determining whether to charge a tenant.

TEN: Retain copies of property management agreements and leases for three years from the date on which the broker stops managing a property. All information and documentation acquired by a broker during the course of managing an owner's property must be furnished to the owner if requested by the owner. A broker cannot withhold information or documentation from his client.

While this list is not intended to be all-inclusive, it addresses the issues most often raised by rental property owners and tenants. Paying attention to these issues will enable brokers to better represent their owner-clients, to be more responsive to tenants and lessen the risk that they will become the subject of an investigation.

49. The Landlord Tenant Act limits fees a landlord or his property manager may charge when pursuing evictions or monies owed by a tenant, determines the timing of landlord security deposit accounting to tenants, imposes duties on landlords to provide fit premises, and permits tenants to terminate leases early in foreclosure situations.

ANS: **True** REF: Vol. 42, No. 2, October 2011
Requirements to Remember in the Landlord Tenant Act

Many licensees are unaware that the Landlord Tenant Act limits fees a landlord or his property manager may charge when pursuing evictions or monies owed by a tenant, determines the timing of landlord security deposit accounting to tenants, imposes duties on landlords to provide fit premises, and permits tenants to terminate leases early in foreclosure situations. Since property managers often assist their landlord clients in complying with the law, an understanding of the requirements of the law is important.

Permitted Landlord Fees
In addition to allowable late fees, the law permits a landlord or property manager to charge a tenant in an eviction situation one of the following three additional fees pursuant to a written lease:

- Complaint Filing Fee – When a tenant is in default and sued for summary ejectment or money owed, but permitted by the landlord to cure the default, the landlord may charge the tenant a filing fee of $15 or 5% of the monthly rent, whichever is greater, even though the landlord dismisses the claim.
- Court Appearance Fee – When a landlord successfully sues a tenant in default in small claims court and the tenant does not appeal, the landlord may charge the tenant a fee of 10% of the monthly rent.
- Second Trial Fee – When a landlord successfully sues a tenant in default in small claims court and, if the tenant has appealed, and the landlord is also successful in district court, the landlord may charge the tenant up to 12% of the monthly rent. (Note that a property manager cannot act on behalf of a landlord at the district court level.)

Administrative fees in addition to court filing fees are no longer permitted when pursuing the eviction of a tenant or recovery of monies owed. Each of the defined fees is exclusive of the others and may only be charged in situations where the landlord has a written lease with the tenant. The law allows only one to be collected. The fee cannot be deducted from a subsequent rent payment and cannot be the basis of a default on the lease in a subsequent summary ejection action.

Security Deposit Accounting
The requirement that landlords account to tenants for security deposits within 30 days of tenancy termination was modified in 2009 to permit an interim report within 30 days and a final accounting within 60 days. The change provides additional time for landlords to obtain estimates and actual costs to repair any damage.

Under the statute, willful failure by a landlord to comply with the deposit, bond or notice requirements of the Tenant Security Deposit Act voids certain of the landlord's rights. If a tenant does not receive an accounting in a timely manner, the tenant can sue the landlord and, despite any legitimate claims for damages, win the right to have the entire security deposit returned in addition to charging the landlord for attorney fees. Licensees should make certain they send notices in a timely manner and document files carefully to avoid liability for themselves or their landlord clients.

Duty to Provide Fit Premises
An entirely new section added in 2009 requires landlords to remedy any "imminently dangerous condition" once they have actual knowledge of it, whether they have received notice of it from the tenant or not. If the tenant caused the dangerous condition, the landlord/agent may charge the tenant the "actual and reasonable" cost of repairs. The term "imminently dangerous condition" means any of the following:

- Unsafe wiring, flooring, steps, ceilings or roofs, or chimneys or flues
- Lack of potable water, operable toilet, operable bathtub or shower
- Lack of operable locks on all doors leading outside, broken windows or a lack of operable locks on all ground level windows
- Lack of operable heating facilities capable of heating living area to 65 when it is 20° outside (November 1 – March 31)
- Rat infestation as a result of defects in the structure
- Excessive standing water, sewage or flooding problems caused by plumbing leaks or inadequate drainage that contribute to mosquito infestation or mold

Landlords must also supply **carbon monoxide detectors** on each level of any residential rental unit that has:

- A fireplace
- A fossil fuel burning heater or appliance (i.e. coal, oil or natural gas)
- An attached garage

Responsibility for repairs, installation and replacement of batteries are the same as current laws regarding smoke detectors.

Foreclosure and Tenant Rights
Tenants residing in residential properties with less than 15 rental units and being sold in foreclosure have the right to terminate their lease upon 10 days' written notice to the landlord. While a broker has a duty to disclose that a property is in foreclosure, frequently the broker only becomes aware of it after the Notice of Sale has been posted at the rental unit. A notice that has been posted constitutes receipt. Once the Notice of Sale is received, the tenant has the right to terminate early. At that point, the landlord/agent must prorate the rent to the effective date of the termination and **cannot** hold the tenant liable for any other rent or damages due only to the early termination.

Brokers should be aware that state and federal statutes can change from year to year. Property managers in particular should stay up to date with the changing laws to best represent and protect their landlord or tenant clients. State laws and pending bills can be found on the North Carolina General Assembly website at www.ncleg.net.

50. Determining whether a tenant is "qualified" generally involves looking at a prospective tenant's income, credit history, credit score, employment history, rental history, criminal record, etc., and a property manager is obligated to take reasonable measures to ensure that all consumer information is disposed of in a manner that would prevent an unauthorized person from acquiring and using the information.

ANS: **True** REF: Vol. 45, No. 3, February 2015

Know How to Procure and Dispose of Tenant Background Information

One of the primary duties of a property manager is to procure qualified tenants for properties under management. Determining whether a tenant is "qualified" generally involves more than looking at a prospective tenant's income. It often involves looking at things like a prospective tenant's credit history, credit score, employment history, rental history, criminal record and more. Each of these factors can be important in making a decision to rent a property. The Federal Trade Commission's BCP Business Center (www.business.ftc.gov) has published the following articles which contain useful information on this topic for property managers: "Using Consumer Reports: What Landlords Need to Know," "A basic 'tenant' of credit reporting," and Disposing of Consumer Report Information? Rule Tells How."

More and more property managers are turning to consumer reporting agencies (CRAs) to obtain information about prospective tenants. Common types of CRAs include credit bureaus, tenant-screening services and reference-checking services. CRAs must comply with the Fair Credit Reporting Act (FCRA). Established in 1970, the FCRA is designed to ensure the confidentiality and accuracy of consumer credit information.

CRAs have a duty to inquire about the intended use of consumer information before actually providing the information. Use of consumer information for tenant-screening purposes is permissible. Using the information to spy on competitors, neighbors, and former spouses is prohibited.

If a property manager refuses to rent to a prospective tenant or changes the rental terms (e.g. increasing the rent, increasing the security deposit, requiring a co-signor, etc.) based even partially upon information in a consumer report, then the property manager must give the prospective tenant an "adverse action notice." Although giving an oral notice is permitted, written notice is better, because it provides evidence of compliance with the FCRA.

According to the FTC, an adverse action notice "… must include the name, address and telephone number of the CRA that supplied the consumer report, including a toll-free telephone number for CRAs that maintain files nationwide; a statement that the CRA that supplied the report did not make the decision to take adverse action and cannot give the specific reasons for it; and a notice of the individual's right to dispute the accuracy or completeness of any information the CRA furnished, and the consumer's right to a free report from the CRA upon request within 60 days."

Property managers and landlords who fail to comply with the FCRA can be sued in federal court. If a broker or landlord loses such a case, then he or she may have to pay court costs, the plaintiff's reasonable legal fees and punitive damages. For more information on the FCRA or for a copy of the Act, you may call 1-877-382-4357 or go online at www.ftc.gov/os/statutes/fcrajump.shtm.

Commission Rule A.0108 requires brokers to retain records of rental transactions for three years. If a tenant's rental application is rejected, then the broker should retain the tenant background information for three years from the rejection date. If a tenant's rental application is approved and the tenant enters into a lease, then the broker should retain the background information for three years following the termination of the tenant's lease.

When disposing of the information obtained from CRAs, landlords and property managers who acquired the information for business purposes must comply with the Disposal Rule which is enforced by the Federal Trade Commission. While the standard for proper disposal is flexible, property managers must take reasonable measures to ensure that all consumer information is disposed of in a manner that would prevent an unauthorized person from acquiring and using the information. For paper documents, shredding (so that they cannot be read or reconstructed) and burning are two methods of disposal that would satisfy the requirements for proper disposal. For digital information, destroying or erasing electronic files so that the information cannot be read is also acceptable.

While property managers may use CRAs as a tool for screening prospective tenants, they must exercise care to protect the information they obtain and to dispose of it in a manner that will prevent its use by unauthorized persons or for unauthorized purposes.

51. While many property managers may attempt to pre-screen tenants to eliminate unqualified candidates early in the process, it is important that each interested person be provided with an application, and each applicant should receive an identical application form and be asked the same questions.

ANS: **True** REF: Vol. 45, No. 2, October 2014
Screening Tenants in a Tight Rental Market

In a tight rental market, competition between multiple applicants for a single vacancy is becoming the norm rather than the exception. While this is good for the landlord, it places additional challenges on the property manager to properly screen prospective tenants with the goal of selecting the applicant who best meets the owner's requirements.

A thorough tenant screening increases the chances of procuring a tenant who will maintain the landlord's property and pay rent on time. In order to determine the minimum qualifications for a prospective tenant, the property manager must first determine the owner's needs and expectations. Typical issues to address include whether pets will be allowed, whether smoking will be permitted, and the number of permitted occupants. The property manager and landlord should also review the application form to ensure that it covers the essential questions. These and related questions should be resolved at the time the property management agreement is formed.

While many property managers may attempt to pre-screen tenants to eliminate unqualified candidates early in the process, it is important that each interested person be provided with an application regardless of their qualifications. Each applicant should receive an identical application form and be asked the same questions. Picking and choosing who receives an application form or providing different application forms to different applicants may violate state and federal fair housing laws. The property manager should take care to inform each applicant in writing regarding non-refundable application and "hold/reservation" fees, and what will be required for the formation of a binding rental agreement. In a situation where multiple applications have been submitted, each applicant should be informed of the existence of competing applications and the manner in which the applicants will be notified as to whether or not they were selected. The applicant should also be informed regarding the types of information that will be accessed during the screening process, such as credit reports, criminal history, rental history, employment verification and history, and personal references.

The property manager should also explain how the information obtained during the background check will be used in the selection process, and the type of information that might result in a rejection of the application, such as a low credit score or prior eviction. The tenant will have to provide written consent for the property manager to obtain some of the required information.

When the application has been submitted, the property manager's next task is performing the background check to verify the information provided by the applicant. A typical background check might include obtaining a credit report, criminal history, rental history, and employment verification.

After the background check has been completed, the property manager is ready to make a selection in accordance with the tenant qualifications agreed upon with the landlord. The selection process should be based on an objective and documented system to avoid possible fair housing issues.

Once the applications have been evaluated, the best qualified applicant should be notified of the deadline (e.g., within 72 hours of acceptance) for submitting the signed lease agreement, security deposit, and applicable pet fee. If the applicant fails to respond within the prescribed time limit, the next most qualified applicant would then be notified. While some property managers notify all qualified candidates, and award the rental to the first applicant to submit a signed lease agreement and security deposit check, such an approach invites claims of discrimination and may even result in a fair housing complaint.

The unsuccessful candidates should also be notified. If the applicants are otherwise qualified, the property manager can suggest other available rental properties for them to consider. If an applicant was rejected, the property manager may notify him or her of the basis of the rejection, such as poor credit score, adverse rental history, or unacceptable criminal history; however, such notification is not required. If the rejection was based on information obtained from a credit agency, the property manager will need to provide the applicant with information regarding the credit agency that provided the information in accordance with Fair Credit Reporting Act requirements.

Thorough tenant screening will benefit both the landlord and property manager. The selection of a reliable tenant who maintains the property will provide the landlord with a steady source of income and will reduce the time and energy expended by the property manager in servicing the account.

52. HUD has determined that due to higher than average incarceration rates among certain races relative to their percentage of the total population, the use of criminal background checks to deny housing may actually cause a disparate impact on certain races and therefore be discriminatory.

ANS: **True** REF: Vol. 47, No. 3, February 2017
HUD Issues Guidance on Use of Criminal Background Checks

Diligent property managers often run criminal background checks on prospective tenants before allowing them to lease a landlord's property. In April 2016, HUD issued guidance on how the Fair Housing Act ("the Act") impacts the use of such a background check by all providers of housing, including property managers. When designing a process for screening tenants, it is important for brokers to consider this guidance and how the use of such background checks might violate fair housing laws.

Before getting into the HUD guidelines, there are a few terms brokers should recognize and understand. The Act includes the following seven protected classes: race, color, religion, national origin, sex, disability, and familial status. A landlord or property manager may not discriminate against anyone in one or more of the protected classes. Another term, "disparate impact", is often used in housing discrimination cases and refers to a policy or practice that is neutral on its face, but its application actually has a discriminatory impact on a protected class.

The use of a criminal background check as part of a tenant screening process seems to be a neutral process as long as it is required of all potential tenants, not just certain ones selected by the landlord or property manager. However, HUD has determined that due to higher than average incarceration rates among certain races relative to their percentage of the total population, and when compared to incarceration rates of other races, the use of criminal background checks to deny housing may actually cause a disparate impact on certain races and therefore be discriminatory.

What does all of this mean for a landlord or property manager? First, criminal background checks should only be used for a non-discriminatory business objective, and there cannot be an alternative to the background check that is less discriminatory. There should be some evidence that the background checks actually accomplish the goal. Does a refusal to rent to individuals with criminal convictions actually mean fewer criminal acts or property destruction in the properties being managed? A blanket prohibition against anyone with any type criminal record likely would not survive a charge of discrimination. There are a couple of exceptions. The Fair Housing Act specifically states that landlords do not have to make housing available to persons with convictions for the manufacture or distribution of controlled substances. Just remember, though, other drug-related convictions are not specifically exempt from fair housing requirements. In addition, project-based HUD subsidized properties must prohibit anyone subject to a lifetime registration requirement under a state government sex offender registration program.

For anything outside the exceptions, HUD suggests that landlords and property managers should consider the following factors when using criminal background checks for prospective tenants:

- Do not consider charges or arrests that did not result in conviction. Arrest records should not be used as a basis for denying an applicant for housing. Such a record does not indicate that the applicant actually engaged in any criminal activity. Remember – innocent until proven guilty.
- Do not have a blanket policy against renting to anyone with any type of criminal conviction. Explain to landlord-clients the dangers of such a policy and advise them to use a more tailored approach.
- Consider the type of conviction. Look at the nature and severity of each conviction. A shoplifting conviction should not carry the same weight in a housing decision as a conviction for distributing cocaine. While fishing without a license is not good, an applicant participating in that type of activity will likely be a lesser risk to residents and property than someone selling drugs, which often brings more dangerous people and illegal drugs into the neighborhood.

- Consider the timing of the conviction. How long ago did the event happen and how long ago was the conviction? Research tends to show that the likelihood that a person with a prior criminal conviction will commit another offense decreases over time. HUD offers no insight into how long might be a reasonable period to consider, so consider a reasonable amount of time that you feel you can defend if challenged.
- Consider each offense individually. Create an assessment plan that is fair and takes into account mitigating factors such as the surrounding events, the age of the individual at the time, rehabilitation efforts, and the rental history of the individual. In other words, each instance should be reviewed on a case-by-case basis and narrowly tailor any refusals.

As a property manager, you have a duty to discuss these issues with your landlord clients and create a program that will help keep you and your clients out of trouble and will allow all housing applicants fair access to available housing. To see the HUD guidelines in full, use the link below.
https://portal.hud.gov/hudportal/documents/huddoc?id=HUD_OGC-GuidAppFHAStandCR.pdf

53. If you discover that the property owner, tenant, seller, or buyer that you represent intends to discriminate based on any of the protected classes, you must immediately consider terminating your agency agreement with that party or risk violating the law and losing your license.

ANS: **True** REF: Vol. 43, No. 1, May 2012
Practicing More Property Management?
Take Another Look at Fair Housing Law

If you find your real estate practice expanding into the management and marketing of rental properties and the securing of tenants for your owner clients, you should make it a point to refresh your knowledge of Fair Housing law.

Tenant rights and leasing and rental agreements are key areas of federal and state Fair Housing laws and an understanding of how the law treats them will enable you to provide your clients with appropriate counsel and to steer clear of possible legal issues.

The original Fair Housing Act (Title VIII of the Civil Rights Act of 1968) and the Federal Fair Housing Amendments Act of 1988, together, prohibit discrimination in the sale, rental or advertising of a dwelling on the basis of race, color, religion, sex, national origin, familial status (such as the presence of children under 18 years old and pregnant women), or handicapping conditions. The North Carolina Legislature enacted the State Fair Housing Act, found in Chapter 41A of the General Statutes, which conforms to federal law. It empowers the North Carolina Human Relations Commission to enforce the laws.

Take note that under these laws, whether you are involved with a sale or a rental, it is unlawful to take any action which results in discrimination *or to allow others to act* in such a manner.

Examples include:

- Refusing to rent or sell housing;
- Refusing to receive or transmit a bona fide offer to engage in a real estate transaction;
- Making housing unavailable;
- Denying a dwelling;
- Setting different terms, conditions or privileges for the sale or rental of a dwelling;
- Providing different housing services or facilities;
- Falsely denying that housing is available for inspection, sale, or rental;
- For profit, persuading owners to sell or rent (blockbusting); or
- Denying anyone access to or membership in a facility or service (such as a multiple listing service) related to the sale or rental of housing.

If you discover that the property owner, tenant, seller, or buyer that you represent intends to discriminate based on any of the protected classes, you must immediately consider terminating your agency agreement with that party or risk violating the law and losing your license. Intent has no impact on whether the broker is subject to penalty under the Fair Housing Act; the Human Relations Commission has sought civil damages and penalties against individuals whose conduct or statements merely implied or tended to suggest discriminatory intent.

Managing rental properties involves the accommodation of needs resulting from physical or mental disabilities. People with hearing, mobility and visual impairments, chronic alcoholism, chronic mental illness, AIDS, and mental retardation, disabilities that limit one or more major life activities, are protected under both state and federal statutes. Thus, it may be necessary for the property owner to modify a dwelling at the disabled person's expense or allow a disabled tenant to do so.

Modifications to accommodate tenant disabilities within a dwelling may require the tenant to restore the unit to the original condition if the modifications interfere with the landlord's or future tenants' use of the premises. External changes, however, such as a wheelchair ramp leading up to an entrance, are precluded from restoration when the lease or rental terminates.

It is unlawful to refuse to make reasonable accommodations in rules, policies, practices or services if necessary for the disabled person to use the housing. Below are a few important examples of necessary accommodations you may need to tell a landlord:

- A building with a no-pet policy must allow a visually impaired tenant to keep a guide dog. A therapy animal must be allowed to reside with a tenant who produces evidence of a prescription or note from their doctor or therapist regarding their need for the animal.
- An apartment complex that offers tenants ample, unassigned parking must honor a request from a mobility-impaired tenant for a reserved space near the tenant's apartment, if necessary, to ensure access.

Familial status is another protected class under the housing laws. Unless a community qualifies as housing for older persons, it may not discriminate based on familial status. This means you cannot discriminate against families in which one or more children under the age of 18 live with:

- A parent;
- A person who has legal custody of the child or children; or
- The designee of the parent or legal custodian, with the parent or custodian's written permission.

Familial status protection also applies to pregnant women and anyone securing legal custody of a child under 18. An apartment complex violates the law if it attempts to segregate families with children to a certain building or area in the complex.

Aside from the Acts and statutes cited earlier, two excellent sources of information and discussion of the Fair Housing law are: *North Carolina Real Estate Manual* Commission brochure: *Questions and Answers on: Fair Housing*

54. The Fair Housing Act makes it illegal to discriminate against a person with a disability by refusing to make reasonable accommodations in rules, policies, practices, or services when it may be necessary to afford an equal opportunity to use and enjoy a dwelling. Making an exception to a no-pets policy for an Assistance Animal as defined in the Act has been held to be a reasonable accommodation.

ANS: **True** REF: Vol. 47, No. 1, May 2016

NO DOGS ALLOWED:
The FHAA, the ADA, and exceptions to no-pet policies

Imagine you are a broker for a real estate firm managing a building of privately owned condominiums. One sunny afternoon, a woman comes into your office. Walking beside her on a leash is a small brown cat. The woman strolls up to your desk and asks if you have any units for rent. You tell her that there are some units for rent, but, nodding toward the cat, you mention that no units permit pets. The woman laughs and tells you Jasper, apparently the cat's name, is not a pet. She says that she has a condition that Jasper helps her with and asks that you make an exception to the no-pet policy. But as far as you can tell, the woman doesn't have any apparent disabilities.

Are you required to make an exception for Jasper? Can you ask the woman to take Jasper out of the rental office? And what questions can you ask the woman to determine if you must do so?

There is no shortage of confusion when it comes to answering these questions. And much of that confusion is due to differences in the two main laws that protect the rights of a person with a disability: the Fair Housing Amendments Act (FHAA) and the Americans with Disabilities Act (ADA). This article will provide guidance on how a broker should proceed when attempting to determine whether or not an exception to a no-pet policy must be made for a person with a disability.

FHAA Applicable Law

When it comes to making an exemption to a no-pet policy for a rental unit, be it an apartment, condominium, or house, the FHAA will be the applicable law in almost every case. The FHAA makes it illegal to discriminate against a person with a disability by refusing to make reasonable accommodations in rules, policies, practices, or services when it may be necessary to afford an equal opportunity to use and enjoy a dwelling. Making an exception to a no-pets policy for an Assistance Animal as defined in the Act has been held to be a reasonable accommodation, and "dwelling" has been very broadly defined and includes most types of housing, with a few very limited exceptions.

So, when Jasper's owner makes her request, you must consider two threshold questions before deciding whether or not you are required under the FHAA to make an exception to the no-pets policy: 1) does the woman have a disability? and 2) does the woman have a need related to her disability for the animal? If the answer to either of those questions is no, then you are not required to make an exception to the no pets policy. But if the answer to both of those questions is yes, then you and the landlord/owner are required to make an exception to the no-pets policy.

Much of the misunderstanding about the FHAA and the ADA arises from the fact that animals are considered differently under each. The FHAA requires reasonable accommodations for an "Assistance Animal." An Assistance Animal is an animal that provides assistance, performs tasks, or provides emotional support that alleviates symptoms or effects of a person's disability. To qualify as an Assistance Animal, there is no need for the animal to have any specialized training, which may come as a surprise to many brokers and landlords. It may also come as a surprise to some to learn that, under the FHAA, there is no restriction on the type of animal that can be considered an Assistance Animal. A person could have an emotional support dog, cat, or in theory even a kangaroo.

Ask Potential Renter

But what exactly can you ask the potential renter? If the person's disability is readily apparent and it is clear what function the Assistance Animal is providing, you may not ask for any more details and you should accommodate the request as your no-pets policy doesn't apply. For instance, if the person appears to be blind and the Assistance Animal is a seeing-eye dog, you must allow the dog, no questions asked.

If the person's disability is not readily apparent and the need for the Assistance Animal is not clear, you may ask the person to submit reliable documentation showing that they have a disability and that they have a disability related need for the assistance animal. So, back to Jasper and her owner, since the woman has no apparent disability and it is not clear what assistance Jasper is providing, it would be acceptable to ask her to provide a letter from a medical professional stating that she has a disability and Jasper alleviates one or more of the effects of the disability. But you may not ask for details about the person's disability, including what the disability is, nor require the person to provide detailed medical records. A note from a medical professional is all you should ask for. Likewise, if the disability is apparent, but the need for the Assistance Animal is not, you may ask for documentation showing the need for the Assistance Animal. But, again, you may not ask for details regarding the disability. You also may not ask how or if the Assistance Animal has been specially trained because no special training is needed for an animal to qualify as an Assistance Animal.

Therefore, if the woman provides you the requested letter, you will be required to make an exception to the no-pet policy, unless doing so somehow poses an undue financial or administrative burden (not likely), the animal poses a direct threat to the safety and health of others (possibly if it's a kangaroo), or the animal would cause substantial physical damage to the property. And, because under the FHAA Assistance Animals are not considered pets, you may not charge the woman a pet fee or deposit. But keep in mind that you may still charge the woman at the end of the tenancy for any actual damage caused by Jasper.

ADA Protection

So how does the ADA factor in? The ADA protects a person with a disability from discrimination in places of public accommodation. The office of a property management firm is a place of public accommodation, as are hotels, restaurants, stadiums, professional offices, gas stations, etc. An individual rental unit is not. Therefore, the ADA standards will apply to your decision whether or not to allow Jasper to be present in your rental office, but not when considering the woman's request for reasonable accommodation for a rental unit.

When the woman brings Jasper into your office, you may only consider two questions: 1) is Jasper a Service Animal that is required because of a disability? and 2) what work tasks has Jasper been trained to do? If the answer to either of those questions is no, then Jasper may be excluded. But if the answer to both of those questions is yes, then you are required to allow Jasper in the office.

Determining whether or not Jasper is a Service Animal is a little easier under the ADA. Unlike the expansive definition of an Assistance Animal in the FHAA, a "Service Animal" under the ADA may only be a dog and, in limited circumstances, a miniature horse, that is individually trained to perform specific tasks for the benefit of a person with a disability; the most common example being a seeing-eye dog. Many brokers are more familiar with the ADA's more restrictive requirements and mistakenly believe that the FHAA has the same standard. That is not the case. Jasper, being a cat, will not qualify as a Service Animal under the ADA and you would be within your rights to ask the woman to take Jasper back outside.

But let's assume for a minute that Jasper is a dog. If it is readily apparent that a dog is trained to do work or perform tasks for a person with an obvious disability, you may not ask about the person's disability or the dog's training. As in the FHAA example, if the person appears to be blind and the Service Animal is a seeing-eye dog, you must allow the dog to enter the office, no questions asked.

However, if it is not readily apparent that the dog is a Service Animal, the questions you may ask the person are much more limited than those allowed under the FHAA. You may ask if a dog is required because of the disability. A simple "yes" answer is sufficient; you may not ask for detailed information, not even the nature of the disability. You may also ask what the dog has been trained to do. The person should provide you with a description of what service the dog provides; however, you may not require the person to prove to you that the dog is registered, certified, trained, or licensed to be a Service Animal. If the person tells you that they need the dog because of a disability, and explains what the dog is trained to do, the dog may not be denied access to the facility unless it is out of control, not housebroken, or poses a direct threat to the health and safety of others.

The FHAA and the ADA are both laws protecting the rights of persons with disabilities. But knowing when and where each law applies can be tricky. Keep in mind the FHAA – the Fair Housing Amendments Act – applies to housing units and the ADA applies to anywhere the public can go. To protect yourself and the owners of any properties that you manage, always limit yourself to asking the questions permitted by each law. The FHAA allows you to ask: 1) Does the person have a disability? and 2) Does the animal provide assistance or support related to the disability? The ADA allows you to ask: 1) Is the animal a Service Animal required because of a disability? and 2) What work or tasks has the animal been trained to perform? And, under either law, if the person is able to answer both of those questions you are required to make an exception and allow an animal, even if you have an established no-pets policy.

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Between the Lines

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