

# LETTER of THE LAW

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SOLUTIONS THROUGH RESEARCH

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## CANONS of PROFESSIONAL ETHICS AND CONDUCT

**H**ow familiar are you with the Texas Canons of Professional Ethics and Conduct? Are the rules aspirational goals or realistic standards demanding compliance? How do they compare to the National Association of Realtor's (NAR) Code of Ethics?

Texas has five canons located in Title 22 of the Texas Administration Code, (TAC) Chapter 531. Each is appropriately named and, as of February 23, 1998, gender neutral. According to the canon entitled *Fidelity*, a licensee owes a client fiduciary responsibility while acting as an agent. Although the licensee's primary duty is to represent the client, other parties to a transaction must be treated fairly. Licensees must be faithful and observant to the trust placed in them, as well as scrupulous and meticulous in performing tasks. They also must subordinate personal interests to those of the client (Section 531.1).

The *Integrity* canon deals with misrepresentations. Licensees owe a special obligation to exercise integrity in discharging responsibilities. This may be accomplished with prudence and caution to avoid misrepresentation by words, deeds or omissions (Section 531.2).

The *Competency* canon obligates the licensee to be knowledgeable and educated about

market conditions affecting real estate on local, state and national levels. Licensees must exercise judgment and skill while performing their duties (Section 531.3).

The *Consumer Information Form 1-1* requires each active real estate broker to display prominently this form at each place of business (Section 531.18). This rule facilitates a Texas Real Estate Commission (TREC) directive to establish methods whereby disgruntled consumers and service recipients can obtain TREC's mailing address and telephone number in the event they wish to lodge a complaint.

As one might expect, the *Discriminatory Practices* canon parallels the Federal Fair Housing Act. No licensee shall inquire about or make a disclosure that indicates a preference, limitation or discrimination based on race, color, religion, sex, national origin, ancestry, familial status or handicap of an owner, previous or current occupant, potential purchaser, lessor or potential lessee of property. The term *handicap* includes anyone who has, had or may have AIDS, an HIV-related illness or HIV infection, as defined by the Centers for Disease Control of the United States Public Health Service (Section 531.19).

### A Closer Look at Canons

The first three canons (*Fidelity*, *Integrity* and *Competency*) were the initial rules formally adopted by TREC in the early 1970s and codified in 1976. The other two canons were adopted in 1990. The five rules bind all Texas real estate licensees.

Texas case law extends the application of the canons to all real estate contracts. A real estate broker was sued for breach of fiduciary duty (Section 535.1). The broker failed to tell the owner that her listed property had been posted for foreclosure. The broker contended that his conduct was governed exclusively by the listing agreement.

The court disagreed. Rules and regulations promulgated within an agency's authority have the force and effect of law. The law existing at the time of the transaction becomes part of the contract (*Kinnard v. Homann*, 750 S.W. 2d 30 [1988]).

Rarely will a licensee be sued solely for a breach of the canons, as occurred in the *Kinnard* case. Other laws embody the same rules, with more lucrative recoveries, such as the Deceptive Trade Practices Act. A breach of the statutes, Texas Real Estate Licensing Act (TRELA) or the common law forms the primary basis for most allegations. In fact, only three Texas appellate cases have included a breach of canons in the petition since 1980. The other two cases

include *West v. Touchstone*, 620 S.W. 2d 687 (1981) and *Kubinski v. Van Zandt Realtors*, 811 S.W. 2d 711 (1991).

In addition to civil liability, a breach of any TREL A provision or an order of the commission subjects the licensee to an administrative penalty not to exceed \$1,000 for each violation and a reprimand, suspension or revocation of license, according to TREC.

### NAR's Code vs. Texas Canons

NAR's Code of Ethics and Standards of Practice (the Code) are more extensive than the Texas Canons. They contain 17 articles covering three broad categories: Duties to Clients and Customers (Articles 1-9), Duties to the Public (Articles 10-14) and Duties to Realtors (Article 15-17).

The Code, as one might expect, is imposed only on NAR members who "... pledge to observe its spirit in all their activities and to conduct their business in accordance with the tenants . . . ."

However, it is important to note that not all Texas licensees are members of NAR.

### CODE-RELATED CASES

Has a Realtor been sued for violating the Code? Yes, but only 14 cases have reached the appellate level in the United States. And, only one involved a Texas controversy.

Several reasons explain the lack of appellate cases. First, most complaints are handled internally by the local boards and are never litigated. Realtors are required to place pertinent facts before the proper tribunals of local boards if

charged with unethical practices, according to Article 14.

If local boards cannot settle disputes between Realtors, Article 17 requires the complaint to be arbitrated according to the board's regulations. If the dispute is between Realtors and clients, again the dispute will be arbitrated if the clients agree to be bound by the decision.

Second, if litigation occurs, the case will not appear in a reporter system unless appealed above the basic trial court level (Texas District Court). In Texas,

licensees who are NAR members. Which standard applies when the Texas Canons and NAR's Code of Ethics conflict? Fortunately, no direct contradictions exist. However, one may require a higher standard of conduct than the other. For example, the Code imposes a duty to continue marketing a property after an offer has been accepted, yet this practice is not mandated by the Canons. However, any inconsistencies are ironed out in the new promulgated contracts.

The following is a brief summary of cases involving Code violations. Five cases involved disputes between Realtors, and five between the boards and Realtors. The remaining four cases were between clients and Realtors.

The five cases between Realtors centered around fee disputes. In two, the court had to decide which Realtor procured the first ready, willing and able buyer. In each case, the plaintiff contended the other

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the reporter system is the *Southwest Reporter*. Because of the time and legal expense involved, few controversies reach this level.

Third, if the controversy is litigated and a substantial sum of money is at stake, the client most likely will not sue for a breach of the Code. Many articles and standards of practice described in the Code are duplicated in the statutes, common law or TREL A. Given the choice, most clients proceed under the more lucrative avenues of recovery.

With this in mind, an interesting question emerges for Texas

Realtor sought an unfair advantage or did not treat all parties fairly (*Pearson-Cook Inc. v. Preferred Properties, Inc.*, 301 N.W. 2d 842 [1980], Michigan, and *Hines v. Darrow-Hilbreth Company*, 1991 W.L. 151516 [1991], Texas Unpublished Opinion).

In two of the other cases, different state courts rendered contradictory decisions based on similar facts (*Rogus v. Lords*, 804 P. 2d 133 [1991], Arizona, and *Jorgensen Realty, Inc. v. Box* [1985], Colorado). In *Rogus*, the court held that mutual membership in a board did not form a contractual relationship, allowing

a suit for breach of contract for violating the Code. In *Jorgensen*, the court held that the relationship between a voluntary association and its members is contractual. Members agree to submit to the rules of the association, including mandatory arbitration procedures set forth in the Code.

In the final suit between Realtors, the New Mexico Supreme Court held the Code provision requiring arbitration of disputes did not apply to Realtors of different firms (*Christmas v. Cimarron Realty Co.*, 648 P. 2d 788 [1982]).

The five cases between boards and Realtors focused on disciplinary proceedings. The first case involved the unauthorized practice of law, and the second, unauthorized soliciting of listings (*Allan Sobol Realty v. N.Y. State Assn. of Realtors, Inc.*, 652 N.Y.S. 2d 862 [1997], and *Costanzo v. Long Island Board of Realtors*, 532 N.Y.S. 2d 904 [1988]).

Two of the board cases centered on arbitration procedures. One questioned whether the arbitrator's decision was binding or merely a recommendation. The other held that the bylaws of the board constituted a valid contractual agreement to arbitrate. It did not, however, establish a contractual duty to petition the court to compel arbitration. This follows the precedent set in the *Jorgensen*

case discussed earlier (*Peterson v. Rose*, 33 Cal. Rptr. 868 [1963], California, and *King v. Larson Realty, Inc.*, 175 Cal. Rptr. 226 [1981], California).

In the final case involving a board, the Realtor asked the court to review the board's procedure used to revoke his membership. The trial court declined but the appellate court reversed. Because of the substantial economic control the board exerts over the defendant's ability to practice his profession, the court must review whether the action taken or proposed is substantially rational and procedurally fair (*Gaston Board of Realtors, Inc. v. Harrison*, 306 S.E. 2d 809 [1983], North Carolina).

**T**wo of the four cases between clients and Realtors were decided in Iowa. Both involved a suit for professional malpractice (negligence) for breaching the Code (*Menzel v. Dave Jones Realty*, 362 N.W. 2d 465 [1985] and *Crutchley v. First Trust and Savings Bank*, 450 N.W. 2d 877 [1990]). In *Menzel*, the court held that a violation of the Code is evidence but not conclusive proof of negligence. In *Crutchley*, the court followed the precedent set in *Menzel*.

In the third case, the Realtor was sued for failing to convey offers to the seller. In fact, the Realtor secretly competed with

potential purchasers for the property (*Nguyen v. Scott*, 253 Cal. Rptr. 800 [1988], California).

In the fourth case, the court was asked to decide if a breach of the Code constituted an illegal act. The court held it did not (*Biggs v. Marsh*, 446 N.E. 2d 977 [1983], Indiana).

### DRAWING CONCLUSIONS

It is difficult to reach any conclusions about these cases and their impact on future Texas decisions. Only one has been decided in this state. It was unpublished, and set no precedent. As for the remaining thirteen, Texas courts may examine the rulings, but not necessarily follow, if a similar dispute arises.

The two Iowa cases (*Menzel* and *Crutchley*) are important because they ruled a breach of the Code was evidence but not conclusive proof of negligence. The *Biggs* case is important because it held that a Code violation does not necessarily constitute an illegal act.

The *Rogus* case represents a major departure from all others. The court ruled that the Code set aspirational goals, not realistic ones. Further, it forms a non-contractual moral pledge among Realtors. Because no Code provisions provide specific enforcement of any ethical violations, one member cannot sue another for a breach. ☐

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