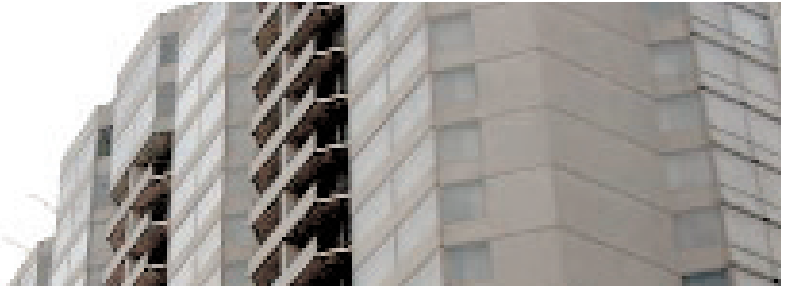


When the Price Isn't Right

How Inexperience Snared Two Real Estate Agents to the Tune of \$100,000



The Facts:

Risk Factor #1

The sellers were an elderly couple.

As such, they could bring suit under the Elder Abuse Statutes in their jurisdiction. Although they vary by jurisdiction, Elder Abuse Statutes generally provide broader remedies to the elderly, including demanding triple damages. Practically speaking, elderly clients will also generate greater sympathy from a judge or jury. Therefore, it's good risk management practice to exercise greater caution in documenting advice given to elderly clients so you can show clear and fair communication.

Risk Factor #2

The agents were inexperienced with commercial real estate.

This inexperience led to a crucial mistake: the failure to develop meaningful comparables to price the Johnsons' property

The NAR code of ethics and local board rules state that a Real estate agent shall not practice in areas outside their area of expertise. It is also good risk management practice to avoid unfamiliar transactions. Instead, refer clients to agents with the appropriate expertise. Another option is to work in partnership with an experienced agent until you have the right experience and knowledge yourself.

Risk Management Tip

If you are engaged only to list the property and not to assist the sellers in developing the listing price, then it's a good idea to document that and have your clients acknowledge it in writing.

Risk Factor #5

The agents used residential real estate forms in a commercial transaction.

Residential forms do not contain contingencies required in a commercial transaction including review of leases, rent control disclosures, etc. A more experienced real estate agent would have known the difference in the forms and most likely used the right one.

Mr. and Mrs. Johnson*, an elderly couple, wanted to sell their 8-unit apartment building. They contacted Joanne Greene of Winslow Real Estate to help them sell their property. Although she didn't have extensive experience with commercial transactions, Ms. Greene had previously been involved in a handful of commercial property transactions, so she agreed to take on the Johnsons as clients.

The Johnsons asked Ms. Greene for help concerning the listing price of the property. Ms. Greene checked the Multiple Listing Service and came up with another similar property that sold for \$1.5 million. She shared this listing with the Johnsons. Even though most commercial transactions are not listed on the MLS, Ms. Greene did not check with other commercial brokers.

In the meantime, one of Ms. Greene's colleagues at Winslow Real Estate, George Weathers, had met a couple looking to buy an investment property and complete a 1031 exchange to avoid capital gains taxes. Although Mr. Weathers had never been involved in a commercial real estate transaction, he agreed to represent the buyers, who offered the Johnsons \$1.2 million for the property. The Sellers countered with \$1.25 million and required the buyers take the property as-is. All offers and counteroffers were made on residential real estate forms.

A month later, the Johnsons discovered that similar properties were selling for 15-25% more than their listing price. They notified the parties that they were backing out of the contract. The buyers immediately filed suit against the Johnsons for specific performance, which asks a court of law to compel execution of the original contract. The Johnsons in turn filed suit against both real estate agents.

The Result:

The case was settled for \$85,000 in indemnity payments and \$25,000 in legal expenses. Key factors in the determination to settle the case was the obvious inexperience of the real estate agents in commercial real estate transactions and the age of the sellers.

*Names have been changed.

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Risk Factor #3

The agents did not disclose the dual-agency relationship.

By representing both sides of the transaction, Winslow Real Estate had a fiduciary duty to both the seller and the buyer. It is nearly impossible in the eyes of a jury to represent competing interests. Best risk management practices say to avoid dual agency transactions. If you do have one, inform your clients in writing and ask them to sign off that they understand and accept the dual agency relationship.

Risk Factor #4

The sellers were unaware that the buyers were involved in a 1031 exchange.

A 1031 exchange allows a buyer to avoid capital gains taxes by exchanging investment properties instead of selling and buying. However, to be a valid 1031 exchange, among other things, the sale and purchase of the two properties must be completed within six months.

Because of the 1031 exchange, the Johnsons' withdrawal from the contract caused significant damage to the buyers and gave them incentive to sue. A good risk management practice for a listing agent who knows the buyer is involved in a 1031 exchange is to communicate this fact to the seller as well as explaining what this means.

Special care should be taken by a Real estate agent when transactions involve 1031 exchanges. Realtors should advise in writing that the buyer consult with their accountant to assure they comply with the IRC 1031 rules to avoid any repercussions if the 1031 exchange doesn't work out. Also, the contract should include language addressing the seller's cooperation on the buyer's exchange. Consult your attorney for appropriate language.