Theories of Real Estate Broker Liability: Arizona's Emerging Malpractice Doctrine

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There are certain well-developed rules[1] protecting sellers and buyers of real estate from the misconduct of brokers.[2] Generally these rules are based on the law of agency[3] or the law of torts.[4] Agency law may provide the basis for recovery by a principal[5] when the broker's conduct violates his duty as agent to his principal.[6] Tort law may provide the basis for recovery by any person who is a party to a transaction and who suffered damages as a result of a wrongful act or omission by the broker.[7]

In addition, Arizona brokers occupy an unusual position. By an amendment to the state constitution, brokers have been given a limited right to engage in the practice of law.[8] Because brokers have the au-

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1. Traditionally, recovery for real estate brokers' misconduct has been based on either the law of agency or the law of torts. See text & notes 37-41, 80-85 *infra*.

2. *See* ARIZ. REV. STAT. ANN. § 32-2101(25) (1976). A real estate broker is defined as a person, other than a salesman, who performs for another and for compensation, certain services as listed in the statute. *Id.* A broker is a person licensed as a broker under the statute. *Id.* § 32-2101(4). A real estate salesman is a person engaged to perform the services included under the definition of a real estate broker, but on behalf of a licensed real estate broker. *Id.* § 32-2101(27). For purposes of this Note, where the term "broker" is used, the term "salesman" may be substituted as well, except where the context refers to a broker specifically as an employer of salesmen.

3. See text & notes 15-18 *infra*. RESTATEMENT (SECOND) OF AGENCY § 1 (1957) defines agency as "the fiduciary relation which results from the manifestation of consent by one person to another that the other shall act on his behalf and subject to his control, and consent by the other so to act."

4. As a general definition, a tort is a civil wrong, other than a breach of contract, for which the aggrieved party can obtain damages through an action in the courts. W. PROSSER, HANDBOOK OF THE LAW OF TORTS § 1, at 2 (4th ed. 1971).

5. The principal is defined as "the one for whom action is to be taken." RESTATEMENT (SECOND) OF AGENCY § 1 (1957).

6. The duties of an agent to his principal are set forth in RESTATEMENT (SECOND) OF AGENCY §§ 376, 377, 379-81, 383, 387-91, 394-95 (1957). See also text & notes 37-73 *infra*.

7. *See* W. PROSSER *supra* note 4, § 30, at 143-44, § 105, at 685-86, § 106, at 695-99.

8. *See* ARIZ. CONST. art. 26, § 1 which provides:

> Any person holding a valid license as a real estate broker or a real estate salesman regularly issued by the Arizona State Real Estate Department when acting in such capacity as a broker or salesman for the parties, or agent for one of the parties to a sale, exchange,

thority to prepare legal documents, they are subject to certain duties with respect to such activity.[9] In a recent Arizona case, *Morley v. J. Pagel Realty & Insurance*,[10] a broker was found to have failed in his duty to advise his sellers as to the possible consequences of accepting an offer to purchase that did not provide for security of the unpaid balance.[11] The court discussed the broker's duties to explain the implications of legal documents that he has a right to prepare. In defining the extent of the broker's duty, the court limited this duty to the broker's client,[12] and also limited his duty to the explanation of "banal" advice.[13] However, the court also stated, quite broadly, without limitation to an agent's client and without limitation to "banal" advice, that brokers have a duty to explain the implications of documents that they now have a legal right to prepare; "failure to do so may constitute real estate malpractice."[14]

This Note will examine the traditional methods of recovery from brokers, including the law of agency and tort. Included in this examination will be the elements of each cause of action and the duties they impose on brokers. The events leading up to the passage of the referendum that granted the right to draft legal documents to brokers will be discussed, as will the possible ramifications of the constitutional amendment. Finally, the two possible interpretations of the constitutional amendment advanced in the *Morley* case will be analyzed. This analysis will include a look at the possible consequences of the case if interpreted in the more narrow sense, as well as the problems posed by the expanded obligations of brokers if the case is given a broad interpretation. The education required of brokers and salesmen will also be discussed, with an eye toward determining how such education prepares brokers to fulfill the obligations imposed by an expansive interpretation of *Morley*.

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or trade, or the renting and leasing of property, shall have the right to draft or fill out and complete, without charge, any and all instruments incident thereto including, but not limited to, preliminary purchase agreements and earnest money receipts, deeds, mortgages, leases, assignments, releases, contracts for sale of realty, and bills of sale.

This amendment was passed in response to a case in which the Arizona Supreme Court found that the enumerated activities, when engaged in by brokers, constituted the unauthorized practice of law. State Bar of Arizona v. Arizona Land Title & Trust Co., 90 Ariz. 76, 95-96, 366 P.2d 1, 14-15 (1961); *see* R. RIGGS, VOX POPULI: THE BATTLE OF 103 at 3 (1964).

9. *See* Morley v. J. Pagel Realty & Ins., 27 Ariz. App. 62, 65-66, 550 P.2d 1104, 1107-08 (1976); Gibson v. W. D. Parker Trust, 22 Ariz. App. 342, 345 n.4, 527 P.2d 301, 304 n.4 (1974).

10. 27 Ariz. App. 62, 550 P.2d 1104 (1976).

11. *See id.* at 65, 550 P.2d at 1107.

12. *Id.*

13. *Id.* Evidently, the court felt that the advice which should have been given to the seller in this case was so commonplace and ordinary that a broker who failed to provide such guidance should be liable to his principal. *Id.* at 65-66, 550 P.2d at 1107-08. However, it is not clear from the opinion whether the liability in this case was based on an agency principle or a negligence theory.

14. *Id.* at 66, 550 P.2d at 1108.

AGENCY

The principles of agency are often the primary grounds of recovery from a broker. The broker, as an agent, owes his principal a duty of utmost good faith, integrity, honesty, and loyalty,[15] as well as a duty of due care and diligence.[16] A suit against a broker based on an agency theory may be viewed as consisting of two basic steps: establishment of an agency relationship and determination of the duty breached by the agent.

Establishment of an Agency Relationship

Initially, the injured buyer or seller must establish the existence of the agency relationship.[17] Where the principal is the seller the agency relationship is usually established by the listing agreement.[18] In the

15. *See* Vivian Arnold Realty Co. v. McCormick, 19 Ariz. App. 289, 506 P.2d 1074 (1973). The court described the broker's duty as agent:

> The duties of a real estate broker as agent for a seller are well established. A real estate agent owes a duty of utmost good faith and loyalty to the principal, and one employed to sell property has the specific duty of exercising reasonable due care and diligence to effect a sale to the best advantage of the principal—that is, on the best terms and at the best price possible . . . . He is also under a duty to disclose to his client information he possesses pertaining to the transaction in question.

Id. at 293-94, 506 P.2d at 1078-79. *See also* RESTATEMENT (SECOND) OF AGENCY §§ 13, 380-81, 387, 395 (1957).

16. Vivian Arnold Realty Co. v. McCormick, 19 Ariz. App. 289, 293, 506 P.2d 1074, 1078 (1973). RESTATEMENT (SECOND) OF AGENCY §§ 377, 379, 383 (1957).

17. *See* Norville v. Palant, 25 Ariz. App. 606, 608-09, 545 P.2d 454, 456-57 (1976), where the seller failed to prove the existence of the agency relationship, even though he assured the broker that he would compensate her upon consummation of the transaction. The broker was found to be the agent of the buyer rather than the seller.

18. A listing agreement is a contract employing the broker as agent for the seller and authorizing him to solicit purchasers under given terms and price. Such contracts may read as follows:

> 1. In consideration of your acceptance of this listing, and your promise to endeavor to effect a sale or exchange of this property, I or We, as owner, appoint you as our Agent or Broker and give you the sole exclusive and irrevocable right to sell or exchange and represent the subject property as set forth in the foregoing listing data, together with the remarks set forth therein.
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> 2. . . . I . . . agree to furnish marketable title by policy of title insurance. . . .Upon presentation of offer of purchase in compliance with the above terms accompanied by earnest money deposit in the form of cash, check or note subject to collection, in the amount of 10% of the selling price or the down payment whichever is less. . . I . . . agree to execute an acceptance of said offer. You are hereby authorized to accept said earnest money deposit on my . . . behalf and to deposit same in your trust account or with an escrow agent upon my or our acceptance of the purchaser's offer.
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> 3. This contract is to remain in full force and effect and be irrevocable by me . . . to and including the ____ day of _____ 19__ and I . . . agree to pay you a brokerage fee of ____% of the above gross price, or any other consideration agreed to by me . . . (1) in the event you procure a bona fide offer from a purchaser ready, willing and able to purchase said property at the price and upon the terms above set forth, or (2) in the event a sale or exchange is made by me . . . directly or through any other source or if said property is transferred, conveyed, leased or withdrawn from sale without your written approval or (3) in the event a sale or exchange is made within __ days after the expiration of this listing contract to any person to whom the property has been shown by you or any licensed broker, and whose name has been submitted to me or any of us in writing during the term of this listing. . . .
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> 4. In case a deposit is forfeited, one-half of same, or __% of the sales price, whichever is less, shall be paid to you, and the balance to be paid to me or us.

absence of a written listing agreement, courts have differed as to what circumstances give rise to an agency relationship between brokers and either buyers or sellers.[19] The existence of a confidential relationship between the broker and his client has been sufficient to establish an

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. . .

6. To orderly disseminate this listing information and encourage the cooperation of other brokers as subagents, you are directed to submit this listing to MULTIPLE LISTING SERVICE OF TUCSON, INC., for reproduction and distribution to it's [*sic*] members. . . .

7. I authorize you to cooperate with subagents in accordance with state statutes and the rules and regulations of the state real estate department. . . .

. . .

9. In the event that any broker, subagent, Multiple Listing Service of Tucson, Inc., or any shareholder thereof shall be liable or shall suffer loss or liability by reason in whole or in part of any incorrect statements in the above listing data or remarks, or of owner withholding pertinent information therefrom, I or We do hereby agree to indemnify such broker, subagent, Multiple Listing Service of Tucson, Inc., or any shareholder thereof to the full extent of such loss or liability if any, together with all costs, expenses, and attorney's fees of any claim in connection therewith asserted against such broker, subagent, Multiple Listing Service of Tucson, Inc., or any shareholder thereof.

. . .

I . . . as the Listing Broker, hereby agree to endeavor to effect the sale or exchange in accordance with the terms and conditions above set forth, agree to submit this listing to the MULTIPLE LISTING SERVICE OF TUCSON, INC., and agree to be bound by all of the terms of the within listing contract.

. . .

This Listing agreement is similar to one commonly used in Tucson, Arizona at the time this Note was written.

In Warren v. Mangels Realty, 23 Ariz. App. 318, 533 P.2d 78 (1975), the court held that the buyer could not prove any agency relationship with the broker because the listing contract made the broker the agent of the seller, and an agent cannot be the agent for both parties without the knowledge and consent of both parties. The seller never consented to an agency relationship between the buyer and the broker. *See also* Norville v. Palant, 25 Ariz. App. 606, 609, 545 P.2d 454, 457 (1976). *But see* Brean v. North Campbell Prof. Bldg., 26 Ariz. App. 381, 548 P.2d 1193 (1976). In *Brean*, the broker was found to be the agent of the buyer, not the seller, even though the seller and broker had entered into a listing contract known as an "open listing." *Id.* at 385, 548 P.2d at 1197. An open listing is usually an agreement to pay a commission to the broker in the event he obtains a ready, willing, and able buyer. The broker's obligation does not include submission to any multiple listing service or dissemination of the information to other brokers. Often, the broker is not even obligated to use his "best efforts" to effect a sale. However, such an agreement does act as a commitment by the seller to pay the broker a commission if he brings him a buyer in complete accordance with the terms of the listing. Under the terms of an open listing, even in the event a sale is made, a seller is generally not obligated to the listing broker unless the broker is also the selling broker, or at least the "procuring cause" of the sale. Consequently, a seller may enter into open listings with a number of brokers, any one of whom could earn the entire commission. Additionally, even if the property is listed on an open basis, the seller can usually sell the property himself with no obligation to any broker. In contrast to the open listing, the exclusive listing imposes an obligation on the seller to pay a commission to the broker in the event of any sale or transfer. The obligations of the broker then are apparently minimal under the "open listing" agreement. In *Brean*, the broker first contacted the buyers and searched for appropriate properties for them. In that search for suitable land, the broker contacted the seller, who showed an interest in selling. The initial contact with the seller was made on behalf of the buyer, and the agency relationship with the buyer therefore existed prior to this contact, and thus precluded the agency relationship with the seller. *Id.* at 382, 385, 548 P.2d at 1194, 1197.

19. An oral agreement may also form an agency relationship. Miller v. Boeger, 1 Ariz. App. 554, 405 P.2d 573 (1965). The court held that a "limited agency relationship [was] initiated at the time the defendants [sellers] gave to the real estate agent an oral listing . . . ." *Id.* at 557, 405 P.2d at 576. An agency relationship may also be implied from the conduct of the parties. *See* Anderson v. Thacher, 76 Cal. App. 2d 50, 65, 172 P.2d 533, 541 (1946). *See* RESTATEMENT (SECOND) OF AGENCY §§ 15-16 (1957), which states the agency relationship exists only if there is manifestation of consent to the relationship by both agent and principal. No consideration is required.

agency relationship.[20] However, both seller and buyer may claim such a confidential relationship, and generally the broker can be the agent of only one party to a transaction.[21]

In many real estate transactions, there are two brokers involved. One of the brokers is the "listing broker"[22] and the other broker is the "selling broker."[23] When this is the case, the agency relationship is usually established between the seller and the listing agent through the listing contract, an agreement that acts as an employment contract for the listing agent.[24] An agency relationship between the seller and the selling broker is often created by express language in the listing agreement.[25] The clause that creates this agency relationship expressly authorizes or requires the listing agent to utilize the services of other

20. *See* Anderson v. Thacher, 76 Cal. App. 2d 50, 68, 172 P.2d 533, 543 (1946). The court stressed the confidence placed in the agent by the principal, thereby imposing a fiduciary relationship on the agent. Such a relationship prohibits the agent from taking advantage of the principal in furtherance of his own interests. *Id.* at 68, 172 P.2d at 543. *See* RESTATEMENT (SECOND) OF AGENCY § 15 (1957) which states that the agency relationship may be created by the manifestation of consent by both parties to the relationship. Perhaps the principal's placement of confidence is a manifestation of consent, and the agent's acceptance of that confidence is a manifestation of his consent.

21. *See, e.g.*, Brean v. North Campbell Prof. Bldg., 26 Ariz. App. 381, 385, 548 P.2d 1193, 1197 (1976); Norville v. Palant, 25 Ariz. App. 606, 609, 545 P.2d 454, 457 (1976); Warren v. Mangels Realty, 23 Ariz. App. 318, 321, 533 P.2d 78, 81 (1975); RESTATEMENT (SECOND) OF AGENCY §§ 387, 391, 394 (1957). *See also* ARIZ. REV. STAT. ANN. § 32-2153(A)(4) (1976) (a broker's license may be suspended or revoked if the broker represents more than one party to the transaction without the knowledge and consent of all parties.)

22. The broker termed the "listing broker" is the broker who has obtained the listing from the seller and has actually contracted with the seller as agent. Normally, a confidential relationship has developed between the seller and the listing broker by the time the contract has been executed. The listing contract in itself is evidence that the seller has placed the entire obligation of the sale of his property in the hands of a broker, in whom he has faith and confidence. In many instances, the terms of the listing contract are negotiated over a period of time, and after substantial investigation by the broker into such factors as market conditions, financing available, and, sometimes, a formal appraisal or valuation of the property. See also the model listing set forth in note 18 *supra*.

23. A selling broker is the broker who obtains the offer to purchase from the buyer. The selling broker and listing broker can be one and the same; however, in most cases involving residential sales, there are two brokers involved. This type of transaction is often called a "cooperative" transaction and is usually accomplished through the Multiple Listing Service (or Multi-List as it is called in some areas).

24. See note 22 *supra*.

25. RESTATEMENT (SECOND) OF AGENCY §§ 5, 77, 142 (1957). See ¶¶ 6-7 of the listing agreement, note 18 *supra*. *See also* Frisell v. Newman, 71 Wash. 2d 520, 522-23, 429 P.2d 864, 869 (1967), where the selling broker held an interest in the corporation that was the purchaser, and failed to disclose the interest to the seller. The court allowed an action in rescission based on the breach of fiduciary duty. *Id.* at 529, 429 P.2d at 866, 869. In Reich v. Christopulous, 123 Utah 137, 256 P.2d 238 (1953), the court held that the agency relationship was created with the subagent by the Multiple Listing agreement. *Id.* at 140, 256 P.2d at 239. That portion of the listing agreement upon which the court relied in the *Reich* opinion was similar in language to the agreement set forth in note 18 *supra*. Similarly, in Wendt v. Fischer, 243 N.Y. 439, 442-44, 154 N.E. 303, 303-05 (1926), due to the broker's non-disclosure, he was held liable to the seller for the amount of his commission. The facts the broker failed to disclose were that he was record owner of stock in the corporate purchaser and also held a management position in the corporation. The court found him liable even though the seller suffered no damage, the broker held no beneficial ownership interest in the corporation, he acted in good faith, and the profits went to another. But the court relied on the reasoning that only by such rigidity of enforcement could the principle of undivided loyalty be preserved. *Id.* at 442-44, 154 N.E. at 303-05.

brokers as subagents.[26] Therefore, any broker who is not the listing broker but is attempting to effect a sale of the property in cooperation with the listing agent is considered a subagent.[27] Consequently, when the listing contract contains such a provision, the selling broker has the duties of agency imposed upon him as a subagent of the listing broker.[28] In essence, the selling broker, as subagent, is the agent of the seller. This subagency relationship with the seller, which generally precludes an agency relationship with the buyer,[29] seems to be ignored by, if not unknown to, many selling agents.[30] In addition, most buyers are probably unaware of its existence much less its legal ramifications. In practice, if the selling broker ever meets the seller,[31] it is usually either when showing the property to a prospective purchaser or upon presentation of a purchase offer to the seller. However, the selling broker's relationship with the buyer is quite different. Often, the broker has been in the company of the purchaser for many hours and has conducted some fairly confidential interviews with the prospective purchaser.[32] Given such extensive contact with the buyer, and such minimal contact with the seller, the buyer is justified in believing that the agent will do his best to obtain the property for the buyer at the

26. See ¶¶ 6-7 of the listing agreement, note 18 *supra*.

27. First Church of the Open Bible v. Cline J. Dunton Realty, Inc., 19 Wash. App. 275, 279, 574 P.2d 1211, 1214 (1978). RESTATEMENT (SECOND) OF AGENCY §§ 5, 77 (1957).

28. *See* note 27 *supra*. *See* Frisell v. Newman, 71 Wash. 2d 520, 529, 429 P.2d 864, 869 (1967). "A subagent is a person appointed by an agent empowered to do so, to perform functions undertaken by the agent for the principal, but for whose conduct the agent agrees with the principal to be primarily responsible." RESTATEMENT (SECOND) OF AGENCY § 5 (1957). A subagent is an agent of both the agent and the principal. *Id.* at comments b, d. A subagent is an agent of both the agent and the principal and has a fiduciary duty to that principal. *Id.* at comment d. *See id.* at comment b, illustration 5.

29. Because the existence of the agency relationship imposes fiduciary duties on the agent, the agent must perform his duties "solely for the benefit of" his principal. RESTATEMENT (SECOND) OF AGENCY §§ 13, 387 (1957). Hence, in a situation where two parties' interests are adverse, the agent's duties are to benefit his principal, not the other party. *Id.* If the agent were to be the agent for both parties to a single transaction, the performance of this duty becomes difficult due to the inherent conflict of interest. *See* text & notes 20-21 *supra*.

30. Selling agents are rightly charged with knowledge of the contents of the listing agreement, as all members of multi-list co-ops use the same listing forms. However, the agents are not generally aware that the sub-agent clause imposes duties of agency upon them, nor what those duties are. The general impression seems to be that the sub-agent clause allows the selling agent the right to earn a commission on a transaction with that seller.

31. When the seller is not the occupant of the house, as when it is either rented to tenants or vacant, the selling broker usually has no contact with the seller. Therefore, it is possible, and often happens, that the selling broker does not have any direct contact with the seller prior to presentation of the offer to purchase. In many cases, as where the seller is relocated and out of town, the selling broker may not have any direct contact with the seller at all, and all negotiations are made through the listing broker.

32. The way in which a residential sale is frequently made is that the broker receives an inquiry from a potential buyer based upon an ad, or a referral from a friend or former client and attempts to locate a suitable house for this new client. The prospective purchaser must discuss his financial capabilities and credit rating in detail with the broker, his desires as to size, location, style and financing. The purchaser usually then relies on the broker to find a suitable home within his budget and normally at the best possible price for the purchaser. This process of searching and house hunting may take days, weeks, or even months and the broker and purchaser may be in each other's company for many hours.

lowest possible price and on the most advantageous terms.[33] Of course, for the agent to attempt to do so is a violation of the agent's duty to the seller.[34] However, it would be unrealistic to expect the buyer to feel that a broker who has worked with him extensively is attempting to obtain the highest possible price for the seller, which, in actuality, is the agent's duty.[35]

Once the agency relationship is created,[36] the law imposes several

33. For a discussion of the relationships between broker, buyer, and seller, and the expectations of the parties, see Comment, *A Reexamination of the Real Estate Broker-Buyer-Seller Relationship*, 18 WAYNE L. REV. 1343, 1353 (1972). This article suggests that the selling broker, when in a two-broker transaction, should be found to be the agent of the buyer rather than the seller. The author uses the reasoning that the buyer's expectation is that the selling broker is his agent, and agency law should reflect the expectations of the parties. The consequences that may result from such a change may not be entirely beneficial to the buyer. With the seller-selling agent relationship established, the seller may become liable to the buyer in tort for any misrepresentations of his agent through the ratification doctrine. *See* RESTATEMENT (SECOND) OF AGENCY §§ 82, 92-93, 98-100, 218 (1957). Such liability allows the remedy of rescission against the seller. If there is no agency relationship between the seller and the selling broker, but the agency relationship is between the buyer and the selling broker, this remedy of rescission is no longer available to the buyer because the ratification doctrine would not be applicable, and the buyer's only recourse may be a suit against the broker for damages. In such a situation, the finding of agency between buyer and selling broker may be more harmful to the buyer than beneficial, because the buyer would lose his action for rescission and restitution against the seller. *See* RESTATEMENT (SECOND) OF AGENCY §§ 82, 92-93, 98-100, 218 (1957). Furthermore, if the agent breaches his fiduciary duty to his principal, one of the remedies available to the principal is the return of compensation paid. If the selling broker is the agent of the buyer, it could be argued that the buyer did not pay any compensation to the agent, because the agent was paid by the seller through the listing broker. Again, the finding of an agency relationship between the selling broker and the buyer may not enhance the buyer's legal position.

34. Marmis v. Solot Co., 117 Ariz. 499, 503, 573 P.2d 899, 903 (Ct. App. 1977) (both listing and selling agents have an "overriding obligation to their seller to obtain the highest and best price for the listed property."). See text & notes 20-21, 28-29 *supra*.

35. *Id.* Both the listing agent and the selling agent may be present when the offer is presented to the seller. In such circumstances, the listing agent's role generally appears to be to represent and protect the interest of the seller. The selling agent's apparent role is not so well-defined. In an attempt to consummate a sale, the selling broker may appear to advocate acceptance of the buyer's offer. Such a position would appear to be a representation of the buyer's interests more than the seller's.

36. The broker's defense to the claim of agency has often been to claim that the relationship between the agent and the plaintiff was that of a middleman, rather than an agent or to claim an agency relationship with the other party to the transaction. *See, e.g.*, Norville v. Palant, 25 Ariz. App. 606, 608-09, 545 P.2d 454, 456-57 (1976) (in an action by the seller for breach of fiduciary duty, the court found that the broker was the agent of the buyer and, therefore, was not liable to the seller); McConnell v. Cowan, 44 Cal. 2d 805, 810-11, 285 P.2d 261 265 (1955); Anderson v. Thacher, 76 Cal. App. 2d 50, 67, 172 P.2d 533, 542-43 (1946) (broker unsuccessfully claimed middleman status). To be a middleman, the broker must have no discretion and must not be involved in any of the negotiations. In *Anderson*, the court described the role of a middleman as follows: "A broker acts as a middleman when his duty is simply to bring together two or more people who desire to exchange their property and whose entire duty is performed when he has brought the respective parties together . . . ." 76 Cal. App. 2d at 67, 172 P.2d at 542-43. Therefore, a middle man's activities must be limited to no more than merely putting the parties in touch with each other. "If the broker is involved in promises of service, representations, preparation of escrow documents, advice, and assistance, the broker is an agent and not a middleman." *Id.* The reasoning behind this limitation on involvement in negotiations is that a middleman must not be in a position to sacrifice the interest of one party for the benefit of the other. It would seem that in practice, the status of middleman would be achieved only when the person claiming to be a middleman is acting as a "broker's broker." A broker's broker situation arises when the broker who is acting as a middleman puts the seller's broker-agent and the buyer's broker-agent in touch with each other. This seems to be the only situation where a broker would neither influence any party to the transaction nor have any discretion at all.

duties on the broker. These agency duties will now be examined.

Duties of the Broker-Agent

The law of agency imposes on the agent the duty of utmost good faith, integrity, honesty, and loyalty in his transactions with his principal.[37] It is well established that a broker, as an agent, is held to this standard.[38] The breach of this duty is found in a broker's failure to disclose pertinent facts to his principal,[39] in a broker's failure to exercise due care and diligence on behalf of his principal,[40] and in a broker's lack of good faith.[41]

Duty to Disclose

An agent is under a duty to disclose any material fact known to the agent, which, if known to the principal, would possibly influence the principal's decision on the subject matter of the agency agreement.[42] Liability for such nondisclosure has been found in an agent's failure to disclose the value of the surrounding property,[43] failure to disclose a personal relationship with the buyer,[44] and failure to disclose all offers

37. RESTATEMENT (SECOND) OF AGENCY §§ 376-77, 379-81, 383, 387-91, 394-95 (1957).

38. *See, e.g.*, Hassenpflug v. Jones, 84 Ariz. 33, 36, 323 P.2d 296, 298 (1958); Haymes v. Rogers, 70 Ariz. 408, 411, 222 P.2d 789, 790 (1950); Vivian Arnold Realty Co. v. McCormick, 19 Ariz. App. 289, 293-94, 506 P.2d 1074, 1078-79 (1973); Batson v. Strehlow, 68 Cal. 2d 662, 674-75, 441 P.2d 101, 109-10, 68 Cal. Rptr. 589, 597-98 (1968); Merksy v. Multiple Listing Bureau of Olympia, Inc., 73 Wash. 2d 225, 228-30, 437 P.2d 897, 899 (1968).

39. *See, e.g.*, Kruse v. Miller, 143 Cal. App. 2d 656, 659, 300 P.2d 855, 857 (1956) (court relied on the agent's failure to disclose to the seller the misrepresentation made to the purchaser to find the breach of duty); Anderson v. Thacher, 76 Cal. App. 2d 50, 69, 172 P.2d 533, 543 (1946) (agent's non-disclosure of his relationship to the purchaser); Frisell v. Newman, 71 Wash. 2d 520, 529, 429 P.2d 864, 869 (1967) (non-disclosure of subagent's interest in the corporate purchaser). *See also* RESTATEMENT (SECOND) OF AGENCY § 381 (1957).

40. Baird v. Madsen, 57 Cal. App. 2d 465, 474-75, 134 P.2d 885, 890-91 (1943) (broker abandoned negotiations with an offeror who later purchased directly from the seller, the court found a breach of duty which precluded the broker's recovery of the commission). *See* Vivian Arnold Realty Co. v. McCormick, 19 Ariz. App. 289, 294, 506 P.2d 1074, 1079 (1973) (no breach of the agent's duty because the broker's efforts were at all times aimed toward effecting a sale); Lyon v. Giannoni, 168 Cal. App. 2d 336, 339, 335 P.2d 690 693 (1959) (broker who persuaded the purchaser to buy elsewhere was found to have breached the duty imposed by agency. *See* RESTATEMENT (SECOND) OF AGENCY § 377 (1957).

41. *See* Haymes v. Rogers, 70 Ariz. 408, 409-11, 222 P.2d 789, 789-91 (1950), where the Arizona Supreme Court initially found a representation that the seller would accept less than the listed price to be a breach of duty as a matter of law. Upon rehearing, the court held that such a representation would be a breach of duty only if done in bad faith. 70 Ariz. 408, 410-11, 222 P.2d 789, 790-91 (1950).

42. *See, e.g.*, Mason v. Bulleri, 25 Ariz. App. 357, 359, 543 P.2d 478, 480 (1975) (information regarding the purchaser's financial condition that prevented him from completing the sale was material); Kimmell v. Clark, 21 Ariz. App. 455, 455, 520 P.2d 851, 851 (1974) (material fact not disclosed was the purchaser's relationship to the agent); Wendt v. Fischer, 243 N.Y. 439, 442-44, 154 N.E. 303, 303-05 (1926) (broker failed to disclose an ownership share of the purchasing corporation, liable even though acted in good faith); Moore v. Turner, 137 W. Va. 299, 315-16, 71 S.E.2d 342, 351-52 (1952) (failure to disclose comparable sales prices barred recovery of the commission by the broker).

43. *See* Moore v. Turner, 137 W. Va. 299, 315-16, 71 S.E.2d 342, 351-52 (1952).

44. *See* Iriart v. Johnson, 75 N.M. 745, 748-49, 411 P.2d 226, 227-28 (1966) (broker failed to

to purchase.[45] Consequently, the agent has a duty to inform his seller of any relationship with the purchaser, either as a relative or as a partial beneficial owner of a corporate purchaser.[46] An agent has also been held liable for failure to inform the seller that the purchaser had given the agent the earnest money check under the condition that the agent "hold" the check.[47] Furthermore, failure to disclose an offer higher than the one presented has been deemed equivalent to an affirmative representation that no such offer exists and is in itself a misrepresentation to the principal.[48]

These standards suggest that any information pertaining to the transaction would be considered pertinent and potentially influential to the principal and, thus, must be disclosed to him by the agent. This information includes any circumstances affecting the buyer's ability or desire to perform, any facts influencing the seller in his determination of a fair price, or influencing his decision as to whether to accept or reject a particular offer, or to attempt a compromise through a counteroffer. Other pertinent information includes any circumstances influencing the agent's opinion as to the benefits of a particular transaction for the seller, such as a close relationship to the purchaser, or an interest other than an interest in a commission.

Duty of Reasonable Care and Diligence

The agent's duty to exercise due care and diligence is imposed not only by the law of agency,[49] but also in many cases by the contract between the agent and his principal.[50] The standard of due care has been clarified as the duty the agent owes to his seller to effect a sale to

disclose to trust beneficiary that he was acting as the purchaser). The court emphasized that the broker need not have gained an advantage to be held liable for such nondisclosure. *Id.*

45. *See* Simone v. McKee, 142 Cal. App. 2d 307, 312, 298 P.2d 667, 671 (1956) (agent failed to disclose to the seller a more favorable offer than the one presented for acceptance). The court said that such a "[f]ailure to disclose . . . is equivalent to the affirmative representation that no other offer existed." *Id.* at 312, 298 P.2d at 671.

46. A failure of an agent to inform the seller of his partial interest in the corporate purchaser is a violation of the duty to disclose. For example, in Frisell v. Newman, 71 Wash. 2d 520, 429 P.2d 864 (1967), the court ruled that the subagent had the burden of establishing the informed consent of the principal to the subagent's beneficial ownership of a share of the corporate purchaser. *Id.* at 529, 429 P.2d at 868. The court held that even though the relationship was discernible from the sale documents, the subagent did not satisy the burden of proving complete disclosure. *Id.*

47. *See* Reich v. Christopulos, 123 Utah 137, 142-44, 256 P.2d 238, 240-41 (1953), where the court seemed to believe that the seller might not have accepted the purchaser's offer if he had been aware of the condition.

48. *See* Simone v. McKee, 142 Cal. App. 2d 307, 312, 298 P.2d 667, 671 (1956) (failure to disclose the higher offer gave rise to damages normally awarded under the tort theory of misrepresentation as well as punitive damages). See discussion at text & notes 87-117 *infra*.

49. RESTATEMENT (SECOND) OF AGENCY §§ 379-80 (1957).

50. *See, e.g.*, Vivian Arnold Realty Co. v. McCormick, 19 Ariz. App. 289, 293-94, 506 P.2d 1074, 1078-79 (1973); Lyon v. Giannoni, 168 Cal. App. 2d 336, 341-42, 335 P.2d 690, 692 (1959); Baird v. Madsen, 57 Cal. App. 2d 465, 474, 134 P.2d 885, 890 (1943). *See also* RESTATEMENT (SECOND) OF AGENCY § 377 (1957).

the best advantage of his principal.[51]

A variety of fact situations have given rise to claims against brokers based on the agent's duty of reasonable due care and diligence. Such a breach has been found when an agent failed to make the contract clear and understandable to the seller, who consequently misunderstood the amount he would receive as proceeds of the sale.[52] Similarly, the duty was breached where a broker failed to advise his client to secure a note for the balance of the sales price with a mortgage or deed of trust against the sold property.[53] Due diligence also imposes a duty to describe the desireable features of the seller's property.[54] For example, a failure to advise prospective purchasers of the advantageous financing available, and for showing other property in the area in an attempt to induce prospective purchasers to purchase such other property has been held to be a breach of the duty of due diligence.[55]

Duty of Good Faith

The agent's duty of good faith has been mentioned in several cases, and has been the basis of recovery in one case.[56] Although "good faith" is not defined in the cases or the *Restatement of Agency*, it has been mentioned as a specific duty that an agent owes to his principal.[57] Good faith is defined in the Uniform Commercial Code as "honesty in fact in the conduct or transaction concerned."[58] However, this definition is merely a minimum standard of conduct.[59] This is illustrated in the U.C.C. section on sales[60] where a merchant is held to a higher standard of good faith than a non-merchant.[61] A merchant is charged with a duty of honesty in fact plus a duty to observe "reasonable commercial standards of fair dealing in the trade."[62]

It seems reasonable that an agent, whose relationship with his principal is fiduciary in nature, would be held at least to a standard comparable to that imposed on a merchant in his dealings with mem-

51. *See, e.g.*, Vivian Arnold Realty Co. v. McCormick, 19 Ariz. App. 289, 293-94, 506 P.2d 1074, 1078-79 (1973); Lyon v. Giannoni, 168 Cal. App. 2d 336, 339, 341, 335 P.2d 690, 692-93 (1959); Baird v. Madsen, 57 Cal. App. 2d 465, 474-75, 134 P.2d 885, 890 (1943).

52. *See* Reese v. Harper, 8 Utah 2d 119, 124, 329 P.2d 410, 413 (1958), where the broker was found to have failed to discharge his duty of reasonable diligence and care where the seller mistakenly thought he was getting $15,000 more than the contract actually provided for.

53. *See* Morley v. J. Pagel Realty & Ins., 27 Ariz. App. 62, 65-66, 550 P.2d 1104, 1107-08 (1976).

54. *See* Mallalieu-Golder, Inc. v. O'Neal, 16 Pa. D. & C. 2d 594, 595-96 (1959).

55. *Id.*

56. Haymes v. Rogers, 70 Ariz. 408, 411, 222 P.2d 789, 790 (1950).

57. *Id.*

58. U.C.C. § 1-201(19) (1972 version).

59. *See id.*

60. *Id.*, Article 2.

61. *Id.* § 2-103(1)(b).

62. *Id.*

bers of the public and potential customers. From *Haymes v. Rogers*,[63] the inference may be drawn that the duty of good faith may be merged with the duty of loyalty[64] to require the agent to put his principal's interests above the interests of all others, including himself.[65]

The good faith requirement of the agent has been used as a basis for recovery in circumstances where the agent represented to prospective purchasers that the seller would sell for less than the listed price.[66] Many of the cases based on agency discuss bad faith, but also have elements of non-disclosure or misrepresentation.[67]

Duty of Loyalty

The duty of loyalty owed to the principal by his agent requires that the agent act in his principal's best interest at all times.[68] This duty precludes the agent from acting for a party with interests adverse to his principal's without the latter's knowledge and consent,[69] from acting for himself without his principal's knowledge and consent,[70] and from acting for any other with conflicting interests without his principal's knowledge and consent.[71] Thus the duty of loyalty was breached by an agent when he attempted to obtain an offer from a prospective purchaser by explaining the seller's reason for wishing to sell quickly[72] because such facts may have caused the prospective purchaser to take advantage of the principal.[73]

Advantages and Disadvantages of An Agency Theory

The benefit of basing an action on the law of agency is that there

63. 70 Ariz. 408, 222 P.2d 789 (1950).

64. See text & notes 68-73 *infra*.

65. Haymes v. Rogers, 70 Ariz. 408, 409-10, 222 P.2d 789, 790 (1950).

66. *Id.* *See* Marmis v. Solot Co., 117 Ariz. 499, 503, 573 P.2d 899, 903 (Ct. App. 1977).

67. *See* Jennings v. Lee, 105 Ariz. 167, 171, 173, 461 P.2d 161, 165, 167 (1969); Simone v. McKee, 142 Cal. App. 2d 307, 312, 298 P.2d 667, 671 (1956) (agent did not disclose a higher offer); Iriart v. Johnson, 75 N.M. 745, 748-49, 411 P.2d 226, 227-28 (1966); Frisell v. Newman, 71 Wash. 2d 520, 529, 429 P.2d 864, 868 (1967).

68. *See* RESTATEMENT (SECOND) OF AGENCY §§ 387-91, 394-95 (1957). *See also* Beckwith v. Clevenger, 89 Ariz. 239, 360 P.2d 596 (1961), in which the court found a breach of duty by the agent when he disclosed to the purchaser the seller's anxiety to sell due to poor health, and held that the breach precluded the broker from recovering a commission. *Id.* at 241-42, 360 P.2d at 597-98.

69. *See* Warren v. Mangels Realty, 23 Ariz. App. 318, 321, 533 P.2d 78, 81 (1975). ARIZ. REV. STAT. ANN. § 32-2153(A)(4) (Supp. 1978-79) requires only that the parties have knowledge *or* consent to the broker acting for more than one party to a transaction. See RESTATEMENT (SECOND) OF AGENCY § 391 (1957).

70. *See* RESTATEMENT (SECOND) OF AGENCY § 389 (1957). *See also* Frisell v. Newman, 71 Wash. 2d 520, 526, 429 P.2d 864, 868 (1967).

71. RESTATEMENT (SECOND) OF AGENCY § 394 (1957). This requirement is particularly pertinent when an agent is acting as selling broker and listing broker. See the discussion of possible conflict of interest which may be inherent in such a situation in Comment, *A Reexamination of the Real Estate Broker-Buyer-Seller Relationship*, 18 WAYNE L. REV. 1343, 1351-53 (1972).

72. *See* Beckwith v. Clevenger, 89 Ariz. 238, 241-42, 360 P. 2d 596, 597-98 (1961).

73. *Id.* at 242, 360 P.2d at 598.

need not be a showing of actual damages in order to obtain relief.[74] However, there is a significant disadvantage to an action based on agency. Only the principal may recover from the agent for breach of the agent's duty since certain duties owed to a principal by his agent are not owed to a third party participating in the transaction.[75] Thus, the broker's liability to his principal depends upon establishment of the agency relationship.

In contrast, the broker's liability based on tort does not require establishment of an agency between the plaintiff and the broker.[76] In the absence of the agency relationship, an aggrieved party to a transaction may recover under a tort theory, such as misrepresentation or neg-

74. Only a breach of the agent's duty must be proved to establish liability. Wendt v. Fischer, 243 N.Y. 439, 442-44, 154 N.E. 303, 303-05 (1926); Reich v. Christopulos, 123 Utah 137, 144, 256 P.2d 238, 241 (1953). However, when no damages are proven, the recovery seems to be limited to the compensation paid to the agent, unless the agent acted as a buyer or seller. If the broker has acted as a buyer or seller, without the knowledge and consent of his principal, the aggrieved principal may pursue an action for rescission and restitution in addition to the recovery or denial of compensation. *See* Frisell v. Newman, 71 Wash. 2d 520, 529, 429 P.2d 864, 869 (1967). Such a rescission is allowed if the agent did not disclose that he was acting as a principal for his own account in addition to serving as agent for one party to the transaction even if the principal suffered no actual damages, as was the situation in *Frisell*. In the event that the agent/purchaser no longer owns the property, but has resold with a "secret profit," the principal may recover the amount of that secret profit through the remedy of a constructive trust. *See* Anderson v. Thacher, 76 Cal. App. 2d 50, 69, 172 P.2d 533, 543 (1946) (court allowed recovery of secret profits); Iriart v. Johnson, 75 N.M. 745, 749-50, 411 P.2d 226, 228-29 (1966) (seller recovered the commission paid as well as $100,000 in secret profits made by the broker who acted as an undisclosed purchaser); RESTATEMENT (SECOND) OF AGENCY § 388 (1957). This reasoning has also been applied to the situation where the purchaser, who is not the agent's principal, sues the broker for secret profits, as in the case of Harper v. Adametz, 142 Conn. 218, 223-25, 113 A.2d 136, 139 (1955). In this case, the court relied on the presence of deliberate deceit to allow recovery by the purchaser. This recognizes the possibility that the broker could be liable to both the buyer and seller in the same transaction for the amount of profit he made if he deceived the buyer and breached his duty of loyalty to the seller. In *Harper*, the buyer's requisite damages were measured as the deprivation of his bargain. *Id.* at 224-25, 113 A.2d at 138.

When the purchaser is neither agent, nor principal, but a third party to the transaction, he may still choose to rescind due to the agent's wrongful acts. Jerger v. Rubin, 106 Ariz. 114, 116, 471 P.2d 726, 729 (1970). If an action to rescind is successful, or if the seller consents to rescission due to the broker's wrongful acts, then the seller-principal has a claim against his agent. *See id.* at 118, 471 P.2d at 730 (1970) (court granted the seller recovery of the commission paid to the agent due to the subsequent rescission based upon the agent's misrepresentation to the purchaser); Mattieligh v. Poe, 57 Wash. 2d 203, 205, 356 P.2d 328, 330 (1960) (purchaser demanded rescission and the seller recovered from the agent the commission as well). *See also* Kruse v. Miller, 143 Cal. App. 2d, 656, 660-61, 300 P.2d 855, 856 (1956) (such a violation precludes the agent's retention of the commission paid for the transaction). The court's reasoning in *Kruse* was that a failure of the agent to inform his principal of the misrepresentation that was the ground for rescission, or any other wrongful act that would justify rescission, is a violation of the fiduciary duty owed to the principal by the agent.

75. *See* RESTATEMENT (SECOND) OF AGENCY §§ 328-32 (1957). The non-principal party to the transaction can recover from the principal under the theories of agency such as the ratification doctrine discussed in note 37 *supra*. Hence, the law of agency can provide the buyer with a basis of recovery from the seller. *See* RESTATEMENT (SECOND) OF AGENCY § 339 (1957) (a third party to the transaction—the non-principal party—can rescind the sale when the property is in the agent's possession). Such an action requires a showing of more than a breach of the duty of agency, because the agent does not owe such a duty to the third party. See text and notes 15-41 *supra*. To obtain rescission in such an action, there must be an element of misrepresentation, see text & notes 80-85, 100-02 *infra*.

76. *See* W. PROSSER, *supra* note 4, § 30, at 143-44, § 105, at 685-86, § 106, at 695-99.

ligence. Proof of nine factors is required for a successful claim of misrepresentation,[77] and failure to establish any one of the factors defeats the plaintiff's claim.[78] On the other hand, a claim in negligence involves merely a showing of a duty, a breach of that duty, and resulting damages.[79] The courts seem to be elevating the standard of performance required of real estate brokers so that application of a negligence theory to real estate transactions is a developing area. The trend is toward requiring brokers to possess and use knowledge and skill for the benefit of all parties to the transaction, not only for the benefit of the principal. This trend is illustrated through an examination of tort law in the context of real estate transactions.

TORT

Either party to the transaction, seller or buyer, may recover from the broker under a tort theory[80] since the law of agency does not shield the agent from liability in tort to a third party.[81] The basis for recovery is often either misrepresentation[82]or negligence.[83] Although a misrepresentation by an agent to his principal, whether buyer or seller, would also involve a breach of the fiduciary duty imposed by the law of agency,[84] if liability is established under a tort theory, all damages proximately flowing from the tortious act of the broker are recoverable.[85]

77. *See* Carrell v. Lux, 101 Ariz. 430, 434, 420 P.2d 564, 568 (1966); discussion of misrepresentation at text & notes 86-95 *infra*.

78. *See* the discussion of misrepresentation, text & notes 86-95 *infra*.

79. *See* the discussion of negligence, text & notes 125-27 *infra*.

80. *See, e.g.*, Brown v. Coates, 253 F.2d 36, 38-39 (D.C. Cir. 1958) (seller recovered for misrepresentation, with the court partially relying on breach of the agent's fiduciary duty and the duty imposed by statute); Roy H. Long Realty Co. v. Vanderkolk, 26 Ariz. App. 226, 228, 547 P.2d 497, 499 (1976) (seller recovered from the broker for a negligent misrepresentation); Simone v. McKee, 142 Cal. App. 2d 307, 312, 298 P.2d 667, 671 (1956) (court found an affirmative tortious misrepresentation in the broker's failure to disclose an offer higher than one presented); Spargnapani v. Wright, 110 A.2d 82, 83 (Mun. Ct. App. Dist. Col. 1954); Schecter v. Brewer, 344 S.W.2d 784, 793 (Mo. App. 1961).

81. *See* RESTATEMENT (SECOND) OF AGENCY § 343 (1957).

82. *See, e.g.*, Brown v. Coates, 253 F.2d 36, 40-41 (D.C. Cir. 1958); Spargnapani v. Wright, 110 A.2d 82, 83 (Mun. Ct. App. Dist. Col. 1954); Schecter v. Brewer, 344 S.W.2d 784, 787 (Mo. App. 1961).

83. *See* Morley v. J. Pagel Realty & Ins., 27 Ariz. App. 62, 65, 550 P.2d 1104, 1107 (1976) (broker's failure to advise his seller to secure the unpaid balance of the sales price with a mortgage on the property). *See also* Poniatowski v. Griffiths, 91 N.J.L. 663, 665, 103 A. 192, 192-93 (1918) (agent negligently purchased the wrong lot for his buyer).

84. *See* RESTATEMENT (SECOND) OF AGENCY §§ 380-81 (1957); text & notes 37-48 *supra*.

85. *See, e.g.*, Timmsen v. Forest E. Olson, Inc., 6 Cal. App. 3d 860, 872, 86 Cal. Rptr. 359, 366 (1970); Harper v. Adametz, 142 Conn. 218, 222-23, 113 A.2d 136, 138 (1955) (buyer's damages measured by the "deprivation of the bargain" where broker made a secret profit); Poniatowski v. Griffiths, 91 N.J.L. 663, 665, 103 A. 192, 193-94 (1918) (through agent's negligence, the client bought the wrong lot and built a house on lot not owned; such loss was recoverable as damages naturally flowing from negligence); Iriart v. Johnson, 75 N.M. 745, 749-50, 411 P.2d 226, 228-29 (1966) (seller recovered the commission paid to the broker as well as the secret profit that the broker had made for himself on the transaction).

Misrepresentation

To assert a successful claim of tortious misrepresentation against a broker, a buyer must show nine factors:[86] first, a representation;[87] second, its falsity;[88] third, its materiality;[89]fourth, the agent's knowledge of its falsity, or ignorance of its truth;[90] fifth, the agent's intention that the purchaser act on the representation;[91] sixth, the purchaser's ignorance of the falsity of the representation;[92] seventh, the purchaser's reliance on its truth;[93] eighth, the purchaser's right to rely on the representation;[94]and ninth, injury proximately cased by the misrepresentation.[95]

Misrepresentations to the seller may be misrepresentations as to the value of property being given up or received in an exchange,[96] misrepresentations as to the factual circumstances upon which a seller might rely in making a decision,[97] or misrepresentations as to the sales prices of comparable properties.[98] A seller may also recover damages for misrepresentations made by the broker to the buyer that cause the buyer to rescind or take other action against the seller.[99]

86. Arizona refers to nine elements required for a successful claim while other states embody the same elements in a shorter list. Arizona's nine elements are listed in Carrel v. Lux, 101 Ariz. 430, 434, 420 P.2d 564, 568 (1966). The five factors that constitute actionable misrepresentation in several other states are first, a representation or non-disclosure of fact materially affecting the value or desirability of the property. Second, the buyer must prove the broker's knowledge of the falsity of the representation or a lack of information sufficient to make such a representation (or that the information was unknown to the buyer or beyond the reach of the buyer). Third, the purchaser must show that the broker intended to induce the buyer to buy. Fourth, the buyer must show that he was induced to act by reason of the misrepresentation or non-disclosure. Fifth, there must be resulting damages proved. These five elements are found in Lingsch v. Savage, 213 Cal. App. 2d 729, 738, 29 Cal. Rptr. 201, 206 (1963); and Harper v. Adametz, 142 Conn. 218, 223-24, 113 A.2d 136, 138-39 (1955).

87. Carrel v. Lux, 101 Ariz. 430, 434, 420 P.2d 564, 658 (1966).

88. *Id.*

89. *Id.*

90. *Id.*

91. *Id.*

92. *Id.*

93. *Id.*

94. *Id.*

95. *Id.*

96. *See* Smith v. Carroll Realty Co., 8 Utah 2d 356, 358-59, 335 P.2d 67, 68-69 (1959) (agent advised his client that the property being received in an exchange transaction was worth $15,500 when the actual value was only $7,000 to $8,000). The court in *Smith* relied on the agent's failure to fulfill his duty to exercise reasonable skill and diligence. The court's analysis sounded more like an agency theory of liability, despite the agent's misrepresentation. *Id.*

97. Quistgard v. Derby, 114 Cal. App. 2d 271, 273-74, 250 P.2d 2, 3-4 (1952) (broker told his seller that he had obtained the approval of the sale from the beneficiary of the second deed of trust, when in fact no such approval had been obtained).

98. Moore v. Turner, 137 W. Va. 299, 315, 71 S.E.2d 342, 351 (1952).

99. *See* Jerger v. Rubin, 106 Ariz. 114, 115-17, 471 P.2d 726, 727-29 (1970), where the salesman's representation that he had been negotiating with a potential resale client, which would enable the plaintiff-purchaser to sell off a portion of the parcel he was buying, was sufficient to give the purchaser the right to elect rescission against the seller. The damages suffered by the seller due to the rescission were recoverable from the broker. *See also* Kruse v. Miller, 143 Cal. App. 2d 656, 660-61, 300 P.2d 855, 858 (1956), where the court found the broker liable to the seller for damages suffered when the purchaser rescinded due to misrepresentations made by the broker that the lot was not a "filled lot." The court reasoned that the agent violated his duty to inform his principal by failing to inform him of the misrepresentation. *But see* Brean v. North Campbell

Misrepresentations are more likely to be made to the buyer since, in the usual case, it is the agent's duty to describe the property and make certain representations in an attempt to procure a sale for the benefit of the seller.[100] Since the broker is usually the agent of the seller, and dual agency is strongly discouraged,[101] the buyer can rarely rely on the fiduciary duty of agency for recovery.[102]

The cases do not seem to make a distinction between liability based on innocent misrepresentations, negligent misrepresentations, or intentional misrepresentations.[103] The broker is held liable for any misrepresentation, even though he is relying on information supplied to him by the seller.[104] An example of an innocent misrepresentation resulting in liability is where a broker makes a reasonable claim as to the quality of construction or performance capabilities of the mechanical fixtures, believing it to be true.[105] Negligent misrepresentation was held actionable where the agent told a prospective buyer that there was only one encumbrance on the property when in fact there were two.[106] Similarly, in an Arizona case, negligent misrepresentation was the basis for recovery against an agent who signed a sales agreement that acknowledged receipt of the buyer's earnest money deposit, when in fact the agent had not received the deposit.[107] Intentional misrepresentations occur in contexts similar to those from which negligent misrepre-

Prof. Bldg., 26 Ariz. App. 381, 385, 548 P.2d 1193, 1197 (1976) where the court held that the agent was not liable to the purchaser for the error in size. The court found that the broker was the agent of the purchaser not the seller and that the representations made, which were false, were actually made by the seller and not by the purchaser's agent.

100. *See* Jerger v. Rubin, 106 Ariz. 114, 119, 471 P.2d 726, 731 (1970); Carrel v. Lux, 101 Ariz. 430, 440, 420 P.2d 564, 574 (1964); listing agreement set forth in note 18 *supra*.

101. ARIZ. REV. STAT. ANN. § 32-2153(A)(4) (1976) (broker's license may be suspended or revoked if broker represents more than one party to a transaction without knowledge and consent of all parties); RESTATEMENT (SECOND) OF AGENCY §§ 389, 391, 394 (1957).

102. See discussion regarding the establishment of the agency relationship at text & notes 17-36 *supra*.

103. *See* W. PROSSER, *supra* note 4, § 105, at 685-87; *See also* Roy H. Long Realty Co. v. Vanderkolk, 26 Ariz. App. 226, 228, 547 P.2d 497, 499 (1976), where the court stated that even though negligent misrepresentation is actionable, the law of negligence rather than the law of fraud applies.

104. For example, in Barnes v. Lopez, 25 Ariz. App. 477, 480-81, 544 P.2d 694, 697-98 (1976), the court found both the seller and the broker liable for a misrepresentation of the existing zoning. The court said the misrepresentation was fraud even if merely an affirmation of erroneous zoning information on the listing.

105. For example, a broker's claim that the buyer could "heat [the house] for $100 a year" when in fact the boiler was broken was a sufficient misrepresentation to make the broker liable to the buyer. Spargnapani v. Wright, 110 A.2d 82, 83 (Mun. Ct. App. Dist. Col. 1954).

106. Wilson v. Hisey, 147 Cal. App. 2d 433, 438, 305 P.2d 686, 690 (1957).

107. *See* Roy H. Long Realty Co. v. Vanderkolk, 26 Ariz. App. 226, 228-29, 547 P.2d 497, 499-500 (1976); *accord*, Merkley v. MacPherson's, Inc., 69 Wash. 2d 776, 777, 420 P.2d 205, 206-07 (1966) (sales agreement showed receipt of a promissory note that the broker failed to obtain). In both cases, the measure of damages was determined by the liquidated damages provisions of the sales agreements, and the brokers were held liable to the sellers for one-half the amount of the earnest money that was to be obtained. Roy H. Long Realty Co. v. Vanderkolk, 26 Ariz. App. at 229, 547 P.2d at 500; Merkley v. MacPherson's, Inc., 69 Wash. 2d at 780, 420 P.2d at 208.

sentations arise.[108] For example, intentional frauds were found where the representation made was in a description of the soil condition of the property,[109] where the misrepresentation was a statement regarding the zoning of the property,[110] and where the agent incorrectly represented the status of negotiations with a prospective purchaser.[111]

In practice, misrepresentations are frequently made in response to prospective buyers' inquiries regarding the facts pertaining to particular properties.[112] In many instances, the broker must rely on representations made to him by the seller concerning the condition of the property;[113] however, this does not relieve the broker of liability to the purchaser.[114] Consequently, even if the broker believes that the representation is true, based on statements made by the seller, the broker may be liable if the representation is in fact false.[115] Therefore, since

108. The element of the broker's intention, which is required for a successful action against a broker for misrepresentation, has been easily established in most cases. *See* Carrel v. Lux, 101 Ariz. 430, 439, 420 P.2d 564, 573 (1966); Barnes v. Lopez, 25 Ariz. App. 477, 480, 544 P.2d 694, 697 (1976); Wilkie v. Coinway, Inc., 257 Cal. App. 2d 126, 136, 64 Cal. Rptr. 845, 851 (1967); Hall v. Wright, 261 Iowa 758, 772, 156 N.W.2d 661, 669 (1968). When the representation is made in the description of a parcel of real property, the intention to induce the prospective purchaser to buy is assumed. Carrel v. Lux, 101 Ariz. 430, 439, 420 P.2d 564, 573 (1966). The broker's motive of monetary gain to be realized from a consummated transaction is sufficient to support a finding that the agent intended that the purchaser rely on his representations. *Id.*

109. *See* Kruse v. Miller, 143 Cal. App. 2d 656, 658-59, 300 P.2d 855, 857 (1956).

110. *See* Barnes v. Lopez, 25 Ariz. App. 477, 480, 544 P.2d 694, 697 (1976).

111. *See* Jerger v. Rubin, 106 Ariz. 114, 115-16, 471 P.2d 726, 727-28 (1970).

112. Buyers frequently ask many questions concerning the property. The selling broker, in attempting to answer these questions, relies most often on the information supplied to him by the listing broker or seller. If the property being shown is listed with a multiple listing organization, the fact sheets are circulated throughout the membership with all pertinent information supplied by either the seller or the listing broker. In a community such as Tucson, the membership relying on this information could exceed 1,200 agents. If an error has been made, or a representation of the seller accepted without verification, this misrepresentation could be made continually by all agents showing the property based on such a fact sheet. It seems that these agents are placed in a position similar to that of an endorser or warrantor of information, unless they expressly disclaim knowledge of the truth of any of the representations.

113. Diligent brokers will inquire of their client-sellers as to the condition of heating and cooling equipment, hot water heater, appliances included in the sale, roof, plumbing, insulation, and electrical systems, and, in the case of income property, income and expense figures. It is normal practice to rely on the seller's representations regarding these matters unless there is reason to doubt the seller's truthfulness. Rarely are these representations included in the listing agreement, unless it is a representation that something has recently been replaced. A broker should, and usually does, verify all information to the extent possible. Information on such matters as sewer connection, lot size and/or acreage, property taxes, legal description, school district, assessments, and encumbrances are generally a matter of record.

114. The elements of a cause of action based upon misrepresentation are stated at text & notes 86-95 *supra*. It is apparent that an agent's ignorance of the truth, *i.e.*, lack of knowledge of the truth or falsity of the statement, is sufficient to satisfy the "scienter" requirement. First Church of the Open Bible v. Cline J. Dunton Realty, Inc., 19 Wash. App. 275, 280, 574 P.2d 1211, 1214 (1978).

115. *Id.* In such a case, however, the agent may have a claim against the seller, or his primary agent, for indemnity, provided there is such a provision in the listing contract. *See* RESTATEMENT (SECOND) OF AGENCY § 256 (1957). For an agent to recover based on indemnity, he must show that his reliance on the principal's representations was justifiable. Barnes v. Lopez, 25 Ariz. App. 477, 482, 544 P.2d 694, 699 (1976) (broker was denied indemnity due to his own misconduct); First Church of the Open Bible v. Cline J. Dunton Realty, Inc., 19 Wash. App. 275, 281-82, 574 P.2d 1211, 1215-16 (1978) (broker must exercise due care to be excused as justifiably ignorant); RESTATEMENT (SECOND) OF AGENCY § 256 (1957).

an independent investigation by the broker is generally not feasible, except as to information that is a matter of record,[116] a cautious broker makes few representations to the buyer, leaving the buyer on his own to evaluate the property.[117] A less cautious broker may be of more service to the buyer, as he may pass on to the buyer representations made by the seller that could prove valuable to the buyer's evaluation process. Ideally, a broker should be able to disclaim liability for representations originating with the seller, provided a buyer fully understands who is responsible for the representations and who bears the ultimate liability in the event the representations are false.

Brokers have relied on various defenses in an attempt to avoid liability for misrepresentations. Lack of privity of contract has been ineffective as a defense.[118] Similarly, a disclaimer of warranties, such as an "as is" clause in the sales agreement, has no effect as against a representation or even against a non-disclosure.[119] Furthermore, the broker's attempt to prove lack of reliance is generally not successful, since a buyer or seller usually has the right to rely on representations made by a broker.[120]

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116. For information that may be verified from the public record, see note 113 *supra*.

117. It is preferable to inform prospective purchasers that the seller's representations are merely that, the unverified representations of the seller. This would avoid the problem of being accused of asserting any of the seller's representations as a fact. It would be most preferable to make this disclaimer in writing to the purchaser to avoid litigation on the issue of who said what, and what was heard by the other party.

118. *See, e.g.*, Lingsch v. Savage, 213 Cal. App. 2d 729, 736, 29 Cal. Rptr. 201, 205 (1963); Nathanson v. Murphy, 132 Cal. App. 2d 363, 368, 282 P.2d 174, 178 (1955); Wittenberg v. Robinov, 9 N.Y.2d 261, 263-64, 173 N.E.2d 868, 869, 213 N.Y.S.2d 430, 431 (1961) (agent was liable because he was *not* a party to the contract which contained a disclaimer of representations clause).

119. Lingsch v. Savage, 213 Cal. App. 2d 729, 742, 29 Cal. Rptr. 201, 208-09 (1963); Crawford v. Nastos, 182 Cal. App. 2d 659, 665-66, 6 Cal. Rptr. 425, 429 (1960), where the buyer recovered damages for representations regarding a well, even though the contract contained language that the buyer had inspected the property and accepted it in an "as is" condition. The court reasoned that the buyer was under no duty to investigate. *Accord*, Smith v. Rickards, 149 Cal. App. 2d 648, 308 P.2d 758 (1957), where the court allowed the purchaser to rescind despite the language of the contract stating that the purchaser was not relying on any representations. *Id.* at 653-54, 308 P.2d at 761-62.

A broker is under a duty to disclose to the buyer knowledge of defects materially affecting value or desirability where such defects are not known to or observable by the buyer. Lingsch v. Savage, 213 Cal. App. 2d 729, 735-36, 29 Cal. Rptr. 201, 204-05 (1963).

120. *See* Barnes v. Lopez, 25 Ariz. App. 477, 480, 544 P.2d 694, 697 (1976) (purchaser was entitled to rely even if the facts were a matter of public record); Wilkie v. Coinway, Inc., 257 Cal. App. 2d 126, 137, 64 Cal. Rptr. 845, 852 (1967); Anderson v. Thacher, 76 Cal. App. 2d 50, 70-71, 172 P.2d 533, 544 (1946) (seller is entitled to rely on the premise that the broker is acting entirely in his interest); Foxley Cattle Co. v. Bank of Mead, 196 Neb. 1, 4, 241 N.W.2d 495, 497 (1976). *See also* ARIZ. REV. STAT. ANN. § 32-2153(A)(1) (1976) (which provides that any substantial misrepresentation is grounds for suspension, revocation, or denial of a real estate license).

It has been held that a purchaser has the right to rely on a broker's representations when the buyer lacks equal facilities for learning the truth, when the facts are peculiarly within the knowledge of the speaker and difficult for the hearer to ascertain without expert help, or where the misrepresentations relate to latent defects. Schecter v. Brewer, 344 S.W.2d 784, 788 (Mo. App. 1961). This standard is too strict and does not give the buyer sufficient protection. The Arizona standard protects the buyer to a greater degree. In *Barnes*, the buyer's reliance was justified even though the facts were not peculiarly within the speaker's knowledge, nor difficult to ascertain without expert help, nor pertinent to a latent defect. 25 Ariz. App. at 480, 544 P.2d at 697. The

Brokers have also attempted to avoid liability by asserting the "ratification doctrine" as a defense.[121] However, although the ratification doctrine imposes liability upon the seller for the agent's misrepresentation when the seller refuses to rescind or make an adjustment,[122] it does not relieve the agent of liability;[123] it merely makes the seller jointly liable with the agent. A broker may not escape liability by virtue of the seller's joint liability.[124]

Negligence

A broker may be negligent in a variety of ways.[125] To establish a successful claim of negligence against a broker, the plaintiff must show that the broker owed him a duty to conform to a certain standard of conduct and that the broker failed to conform to that standard.[126] The tort of negligence differs from the tort of misrepresentation in that it can cover a broader variety of activities. A broker can be negligent without making any representations. The tort of negligence also differs from an action based on an agency in that the plaintiff in a negligence action need only allege that the broker owed him a duty of due care, not the fiduciary duty of loyalty, good faith, and diligence.[127]

In many cases where the court has determined that the broker is liable for negligence, elements of misrepresentation, breach of agency, or bad faith were also involved.[128] Liability has been based on negli-

seller and broker were both held liable for a misrepresentation as to the existing zoning, which is a matter of public record. *Id.* at 480, 482, 544 P.2d at 697, 699.

121. *See* RESTATEMENT (SECOND) OF AGENCY §§ 82, 92-93, 98-100, 143, 408, 416 (1957). The doctrine of ratification applies to cases where an agent makes false representations while acting for his principal, the seller, and the aggrieved buyer demands rescission from the seller. If the seller refuses to rescind, he ratifies the false representations, thereby becoming liable to the buyer for damages resulting from the misrepresentations. The buyer may choose to force rescission in equity, or sue for damages. The reasoning behind the ratification doctrine is that a seller may not retain the benefits of a transaction and disclaim liability for the agent's misrepresentations, which were the procuring cause of those benefits. *See* Carrel v. Lux, 101 Ariz. 430, 439, 420 P.2d 564, 573 (1966).

122. *See* discussion at note 121 *supra.*

123. *See* Carrel v. Lux, 101 Ariz. 430, 442, 420 P.2d 564, 576 (1966) (seller's ratification of a broker's misrepresentation does not relieve the agent of liability, but makes the seller jointly liable with the agent); RESTATEMENT (SECOND) OF AGENCY §§ 348, 360 (1957).

124. Carrel v. Lux, 101 Ariz. at 442, 420 P.2d at 576. If the seller's refusal to rescind is based on the agent's claim that no misrepresentation has been made, when in fact the agent makes a false representation, the agent becomes liable to the seller for causing the seller damages due to his refusal to rescind. RESTATEMENT (SECOND) OF AGENCY § 416 (1957).

125. W. PROSSER, *supra* note 4, § 30, at 143.

126. The elements of a cause of action for negligence are as follows:

> 1. A duty, or obligation, recognized by the law, requiring the actor to conform to a certain standard of conduct, for the protection of others against unreasonable risks.
> 2. A failure on his part to conform to the standard required. . . .
> 3. A reasonably close causal connection between the conduct and the resulting injury. . . .
> 4. Actual loss or damage resulting to the interests of another.

Id.

127. *See* text & notes 37-41 *supra.*

128. *See, e.g.*, Roy H. Long Realty Co. v. Vanderkolk, 26 Ariz. App. 226, 228, 547 P.2d 497,

gence where the broker-agent failed to obtain a promissory note for his principal, the seller, as represented in the sales agreement.[129] Such a situation involves a negligent misrepresentation.[130] In Arizona, the court has specifically stated that the law of negligence will be applied in a case of negligent misrepresentation, rather than the law of misrepresentation and fraud.[131] In California, also, the law of negligence has been applied in a case of negligent misrepresentation.[132] In *Wilson v. Hisey*,[133] for example, the court found that the broker's failure to advise the buyer to obtain a title search was not, by itself, an act of negligence; however, when coupled with a misrepresentation regarding the status of the title, the broker's ommission constituted a lack of reasonable care and diligence in the exercise of his duty.[134] Negligence, when used in the context of professional conduct, is often referred to as "malpractice."[135] A recent Arizona case marked the emergence of a new and potentially far-reaching concept of malpractice for real estate brokers.[136]

Real Estate Malpractice

Arizona has adopted, by referendum, a constitutional amendment that allows real estate salesmen and brokers to prepare legal documents, without charge, incident to a real estate transaction.[137] The referendum was overwhelmingly passed by the electorate on November 6, 1962.[138] In an effort to get the proposition before the people[139] and approved by the general electorate, an extensive campaign was waged

499 (1976) where the circumstances involved negligent misrepresentation by the agent to his principal. For similar circumstances and result, see Merkley v. MacPherson's, Inc., 69 Wash. 2d 776, 779-80, 420 P.2d 205, 207-08 (1966).

129. In both the *Long* and *Merkley* cases, there was an agency relationship and a representation on the sales agreement. In *Long*, the court specifically relied on the law of negligence rather than misrepresentation or breach of an agent's fiduciary duty. 26 Ariz. App. at 228, 547 P.2d at 499; Merkley v. MacPherson's, Inc., 69 Wash. 2d at 779-80, 420 P.2d at 207-08.

130. *See* text & notes 106-07 *supra*.

131. Roy H. Long Realty Co. v. Vanderkolk, 26 Ariz. App. 226, 228, 547 P.2d 497, 499 (1976).

132. Wilson v. Hisey, 147 Cal. App. 2d 433, 438-39, 305 P.2d 686, 689-90 (1957). The failure of the broker to recommend to the lessees that they should obtain a title search, along with a representation that there was only one encumbrance of a certain amount against the property was considered to be negligence, not fraud.

133. 147 Cal. App. 2d 433, 305 P.2d 686 (1957).

134. *Id.* Failure to exercise reasonable care has established liability regardless of the reason for the failure to use such care. Mattieligh v. Poe, 57 Wash. 2d 203, 205, 356 P.2d 328, 330 (1960). Even when the broker made a gratuitous offer to perform some service, if it was not done with care, liability based on negligence could result. *See* Lester v. Marshall, 143 Colo. 189, 195, 352 P.2d 786, 790 (1960).

135. W. PROSSER, *supra* note 4, § 32, at 161-62.

136. Morley v. J. Pagel Realty & Ins., 27 Ariz. App. 62, 66, 550 P.2d 1104, 1108 (1976).

137. ARIZ. CONST. art. XXVI, § 1, set out in full at note 8 *supra*.

138. R. RIGGS, VOX POPULI: THE BATTLE OF 103 at 34 (1964).

139. For a proposition to be placed on the ballot for the general election, the petitions in favor of placing it on the ballot must contain the signatures of 15% of the total number of votes cast for governor in the last general election. ARIZ. CONST. art. XXI, § 1.

by supporters of the proposition, many of whom were real estate agents. The referendum proposition was prompted by the State Bar's successful attempt to severely limit the real estate licensees' ability to draft many documents associated with transactions involving real property.[140]

In 1953, Ashby Lohse, the chairman of the Arizona State Bar's Unauthorized Practice of Law Committee, filed suit against a broker alleging the unauthorized practice of law.[141] A short while later, the State Bar filed a similar suit against the Arizona Land Title Company.[142] The cases were consolidated and heard together in 1957.[143] The trial court ruled in favor of the position taken by real estate agents and title companies in finding that the preparation of documents incident to real estate transactions was a necessary and proper incident of their businesses and thus did not constitute the unauthorized practice of law.[144] The reasoning used was that it was not specifically prohibited by statute, did not violate public policy, and was a custom of long standing.[145]

In 1961, the Arizona Supreme Court decided the issue in favor of the State Bar.[146] The court found that the preparation of legal documents by title companies was the unauthorized practice of law, unless the title company had a direct interest in the obligations and rights created under the document.[147] The court acknowledged that any person has always been able to represent himself, and that title companies were not unable to act on their own behalf.[148] However, this limitation allowed title companies only to draft documents relating directly to their obligations and rights under the title policies. All documents affecting the rights of parties other than the title companies were outside

140. Although the listing agreement is a contract that determines legal rights and obligations of the parties, it was permitted under the reasoning that the broker was a principal to that agreement, and he can contract for his personal services. *See* State Bar of Arizona v. Arizona Land Title & Trust Co., 91 Ariz. 293, 295-96, 371 P.2d 1020, 1022 (1962); R. RIGGS, *supra* note 8, at 3.

141. State Bar of Arizona v. Arizona Land Title & Trust Co., 90 Ariz. 76, 79-80, 366 P.2d 1, 3 (1961); R. RIGGS, *supra* note 8, at 13-14.

142. State Bar of Arizona v. Arizona Land Title & Trust Co., 90 Ariz. 76, 79-80, 366 P.2d 1, 3 (1961); R. RIGGS, *supra* note 8, at 13-14.

143. R. RIGGS, *supra* note 8, at 14.

144. State Bar of Arizona v. Arizona Land Title & Trust Co., 90 Ariz. 76, 80-81, 366 P.2d 1, 4 (1961).

145. *Id.* The real estate broker did not respond because his specific case had been found to be the unauthorized practice of law. Even though the court had found that real estate agents could practice law in a limited manner, his activity did not fall within those limitations. *Id.* at 81-82, 366 P.2d at 4-5. The act complained of was not sufficiently related to his activities as a broker, and he also received compensation for the particular service he performed. Since he was not a member of the Arizona Association of Realtors, the association did not intervene, nor did any other organization. *See* R. RIGGS, *supra* note 8, at 14-15.

146. State Bar of Arizona v. Arizona Land Title & Trust Co., 90 Ariz. 76, 94-97, 366 P.2d 1, 14-15 (1961).

147. *Id.* at 92-93, 94-97, 366 P.2d at 12, 14-15.

148. *Id.* at 92-93, 366 P.2d at 12.

the authority of the title companies. Included in the unauthorized category were all deeds, mortgages, satisfactions of mortgages, liens, and other escrow papers and loan documents.[149] Brokers were similarly limited to drafting agreements affecting the broker's rights and duties directly, such as listing agreements and employment agreements.[150] Brokers requested the court to reconsider and clarify this limitation as it pertained to them, insisting that without the right to draft the preliminary sales agreements, their businesses would suffer irreparably.[151]

Even before the rendition of a supplemental decision in May of 1961, the Arizona Association of Realtors started a campaign to get the proposition for the constitutional amendment before the people.[152] However, some relief from the court's first opinion was provided by the supplemental decision authorizing brokers to make a contract, between themselves as agents and their principals, embodying the terms of sale acceptable to the sellers. Then they could get the buyer to sign this agreement as an acceptance of the seller's offer.[153] When this decision was handed down, the Realtors had already built up such momentum on the referendum effort that they continued that course of action.[154] Their labors were rewarded with the adoption of Article XXVI, §1 of the Arizona Constitution which reads:

> Any person holding a valid license as a real estate broker or a real estate salesman regularly issued by the Arizona State Real Estate Department when acting in such capacity as broker or salesman for the parties, or agent for one of the parties to a sale, exchange, or trade, or the renting and leasing of property, shall have the right to draft or fill out and complete, without charge, any and all instruments incident thereto including, but not limited to, preliminary purchase agreements and earnest money receipts, deeds, mortgages, leases, assignments, releases, contracts for sale of realty and bills of sale.[155]

149. *Id.* at 93, 366 P.2d at 12-13.

150. *Id.* at 94-95, 366 P.2d at 14.

151. R. RIGGS, *supra* note 8, at 15-16.

152. *Id.* at 22-23. For a detailed account of the campaign strategies and expenses of both sides, see *id.* at 18-33.

153. State Bar of Arizona v. Arizona Land Title & Trust Co., 91 Ariz. 293, 295-96, 371 P.2d 1020, 1022 (1962). This method of obtaining an offer from a buyer would be extremely awkward. The agent would have to have the original listing contract in his possession while negotiating an offer with the buyer. If the buyer's offer differed from the terms contained in the listing contract, this method would be unworkable, since the broker would be unable to alter or modify the listing contract without the seller's consent. *See id.* Furthermore, if the seller was offering the property with alternative terms, such as cash to the existing mortgage, or with the option of the buyer to procure his own financing, the buyer's acceptance of his offer to sell would be difficult to obtain on the same agreement and still avoid ambiguity and substantial modifications in the original contract.

154. R. RIGGS, *supra* note 8, at 16, 18-19.

155. In State Bar of Arizona v. Arizona Land Title & Trust Co., 90 Ariz. 76, 95, 366 P.2d 1, 14 (1961), the court said the legislature cannot infringe upon the inherent power of the courts to determine who may practice law. In the disbarment case of *In re* Greer, 52 Ariz. 385, 81 P.2d 96

This provision of the constitution has imposed duties as well as privileges upon brokers. In an important decision, *Morley v. J. Pagel Realty & Insurance*,[156] the Arizona Court of Appeals relied on this provision to impose a duty on real estate agents to explain the consequences of the use or non-use of certain documents.[157] In this case, after listing the house for the seller, the broker obtained an offer to

(1938), the court discussed the right to practice law as a privilege, over which the court has always had the final determination as to what conditions are required and who has complied with those conditions. While it acknowledged the legislature's right to set minimum requirements, and the court's obligation to respect this minimum, the *Greer* court said it could demand more than the minimum. *See id.* at 390, 81 P.2d at 98. Similarly, in State Bar of Arizona v. Arizona Land Title & Trust Co., 90 Ariz. 76, 366 P.2d 1 (1961) the court explicitly said the legislature "cannot infringe on the ultimate power of the courts to determine who may practice law." *Id.* at 95, 366 P.2d at 14 (citing *In re* Greer). According to the court in *Greer*, the source of the court's power to govern the practice of law is "inherent" and not jurisdictional. Consequently, there is "no jurisdictional requirement when the proceeding is based on the inherent power of the court and not upon some statutory ground." *Id.* at 390, 81 P.2d at 98.

The question then becomes, whether the constitutional amendment by referendum is a legislative act, and if so, whether it is a valid legislative act.

Under ARIZ. CONST. art. 4, pt. 1, § 1, the legislative power is delegated by the people to the legislature, with reservation by the people of the power to propose constitutional amendments independently of the legislature. In Adams v. Bolin, 74 Ariz. 269, 284, 247 P.2d 617, 627 (1952), the court stated the legislative power of the State of Arizona is vested in the legislature and the people, and may be exercised by both. It seems clear that a referendum by popular vote is a legislative mechanism. *See id.*; ARIZ. CONST. art. 4, pt. 1, § 1. *See also* ARIZ. CONST. art. 2, § 33 (the granting of rights through the constitution shall not be construed to deny others retained by the people).

The question whether the people have the power to legislate authorization for brokers to practice law in a limited manner set out in the constitutional amendment has no clear answer. In the *Adams* case, where an injunction was sought to prohibit the filing of petitions for a referendum, the court said the authority of the legislature is absolute, except as prohibited by, or repugnant to, other provisions of the state constitution, United States Constitution, or federal laws. 74 Ariz. at 281, 247 P.2d at 625. Also in the *Adams* case the court said, "in the absence of express statutory power, the courts are without jurisdiction to interfere, whether by injunction or otherwise, with the exercise of the legislative function . . . ." *Id.* at 285, 247 P.2d at 628. ARIZ. CONST. art. 3, on the other hand, prohibits the legislature from exercising judicial powers.

The court has claimed the ultimate and exclusive power to determine who can practice law in the courts. *See* Arizona v. Arizona Land Title & Trust Co., 90 Ariz. 76, 80-81, 95, 366 P.2d 1, 4, 14 (1961); *In re* Greer, 52 Ariz. 385, 389, 81 P.2d 96, 98. The combination of these principles indicates that, although the court has no jurisdiction to interfere with a referendum, it has inherent power to determine who may practice law, and such power does not depend on jurisdictional requirements. The court has not decided the issue as to which power shall prevail when the ultimate legislative power of the people infringes upon the inherent power of the court. It could be reasoned that since the court's power over the practice of law is not granted by statute or constitution, the legislative power of the people can be utilized to grant authority to brokers to engage in the limited practice of law. This argument is supported by the language in *Adams*, 74 Ariz. at 281, 283, 247 P.2d at 625-26. However, it might be argued that the power to control the practice of law is inherent in the judicial function, and thus protected by the constitution's separation of powers provisions from infringement by the legislature. This argument is also consistent with the language in *Adams. Id.* However, art. 2, § 32 of the Arizona Constitution states: "Provisions of this constitution are mandatory unless by express words they are declared to be otherwise." Since there is no express statement that art. 26, § 1 is not mandatory, it must be enforced by the courts. *See* Schock v. Jacka, 105 Ariz. 131, 134, 460 P.2d 185, 188 (1969); State v. Nabours, 79 Ariz. 240, 243, 286 P.2d 752, 754 (1955). In *Nabours*, the court stated that "the word 'mandatory' as used in the constitutional provision is defined as a command and hence obligatory, with which we must implicitly follow and obey." 79 Ariz. at 243, 286 P.2d at 754.

It seems clear then that art. 26, § 1 is mandatory and enforceable and validly grants to real estate brokers the rights stated therein.

156. 27 Ariz. App. 62, 550 P.2d 1104 (1976).

157. *See id.* at 66, 550 P.2d at 1108.

purchase from the ultimate buyer. The offered price was $15,000, with $2,500 as a down payment and the balance of $12,500 by promissory note. The obligation evidenced by the note required regular monthly payments to be made to the sellers. In the offer, there was no provision for securing the note with a deed of trust or mortgage against the property. Shortly after closing the transaction, the purchasers resold the property for cash, thereby delivering the house free and clear of encumbrances to a subsequent purchaser. After the house was in the hands of the second purchasers, the original buyers defaulted on the note to the sellers and went into bankruptcy. The sellers were without recourse to the property, and could not collect from the original purchasers due to their insolvency and, therefore, chose to pursue the broker for breach of duty and negligence based on his failure to advise them to secure the unpaid balance of the purchase price with a security instrument encumbering the property.[158] This was not a case of the broker making an error in the technical use of legal documents. It was a case of the broker failing to exercise skill and knowledge by failing to advise his client of the possible consequences of proceeding with the sale in a certain manner, and failing to advise the client to protect his investment by securing the promissory note with the sold property.

In describing the broker's duty, the court in *Morley* said a broker "must employ all his professional ability and knowledge to make sure the *client* understands the facts that will materially affect his desire to sell in accordance with the terms of a purchase offer."[159] The case can be read two ways, either broadly or narrowly. The court apparently wanted the case to be applied narrowly and limited the holding to the situation presented by the facts of the case.[160] This interpretation is supported by language indicating that the obligation of the agent to explain is owed only to his client[161]—in this case, his principal. The broker's defense was that such advice would be the unauthorized practice of law. The court disposed of this argument by stating that "the giving of such banal advice . . . creates no danger to the public."[162] This language implies that only the giving of advice based on commonplace knowledge, rather than on special skill and professional training is not the unauthorized practice of law.

However, the court has opened the door to a much broader interpretation. The court went on to say:

> Having achieved, by virtue of [Article XXVI, §1] the right to prepare

158. *Id.*
159. *Id.* at 65, 550 P.2d at 1107 (emphasis added).
160. The court said, "[o]ur holding today is a narrow one and should not be read to extend beyond the situation presented by the facts of this case." *Id.* at 65-66, 550 P.2d at 1107-08.
161. *See id.*
162. *Id.*

> any and all instruments incident to the sale of real property, including promissory notes, real estate brokers and salesmen also bear the responsibility and duty of explaining to the *persons involved* the implications of these documents. Failure to do so may constitute real estate malpractice.[163]

This statement implies a duty to explain to any party to a transaction, not only to the agent's client. This statement does not seem to limit the agent's duty to an explanation based only on commonplace knowledge, but seems to extend that duty to include an explanation of all pertinent implications of the relevant real estate documents.[164]

The differences between the narrow and broad readings are that the narrow reading of *Morley* indicates that the duty to explain runs only to the client of the broker, as in the agent-principal relationship, whereas the broad language used by the court appears to extend the duty to all persons involved in the transaction, which is a group certainly containing non-clients. The narrow reading limits the advice that the broker is authorized to give to that which is "banal," such as commonsense advice to get a mortgage or other security instrument, whereas the broad reading imposes a duty on brokers to explain the implications of all documents that they are empowered by the constitutional amendment to draft.

The existence of these two interpretations raises several problems. The relationships among the broker, his principal, and third parties must be examined in light of the two interpretations of *Morley*. Furthermore, if the *Morley* case is to be interpreted in the broad manner, then the education and expertise of brokers becomes important.

The obligation imposed on brokers by *Morley* is not clear.[165] The narrow view of the *Morley* duty, requiring only that brokers give "banal advice . . . which creates no danger to the public,"[166] would seem to encompass matters of common knowledge in the real estate business. The broad interpretation requires brokers to exercise professional skill and knowledge in explaining the implications of legal documents the broker prepared or merely had the right to prepare.[167] This broad interpretation may require that the agent advise his principal to use certain documents that would be to his principal's best advantage in a transaction. The distinction between these two possible interpretations of the broker's obligation becomes particularly important when at-

163. *Id.* at 66, 550 P.2d at 1108 (emphasis added).
164. For a discussion of the educational requirements, knowledge, and skill of practicing real estate brokers, see text and notes 179-200 *infra*.
165. *See* Morley v. J. Pagel Realty & Ins., 27 Ariz. App. 62, 65, 550 P.2d 1104, 1107 (1976).
166. *Id.*
167. *Id.* at 66, 550 P.2d at 1108.

tempting to determine which parties to the transaction are beneficiaries of this duty.

The law of agency imposes the duties of loyalty, honesty, integrity and reasonable due care and diligence on the agent.[168] These duties are owed by the agent solely to his principal.[169] Where the agent is a broker and acts as the intermediary-negotiator between a buyer and seller, he can fulfill all these traditional duties to his principal, regardless of whether the principal is the buyer or the seller, without violating any traditional duty of honesty and fairness to the other party.[170] Given the two possible interpretations as to who is to benefit from the *Morley* duties, the agent's duty to the non-principal regarding legal documents may now be different. Perhaps now the broker must also provide to non-principals guidance and expertise beyond what would be required by honesty and fair dealing. There can be no argument that an agent cannot behave honestly and with due care to all parties to a property transaction without violating his duty to his principal.[171] The problem arises when analyzing the duty of loyalty.

It has been said that a servant cannot be loyal to two masters.[172] This is especially true when the two masters inevitably possess conflicting interests. If *Morley* is read narrowly and the duty extends only to the agent's principal, there is no conflict with the law of agency. If, however, the *Morley* obligation is read broadly, and the beneficiaries of this obligation include all "persons involved"[173] in the transaction, then a conflict arises. If the broad *Morley* obligation includes requiring the broker to advise the parties to the transaction as to which documents are to the best advantage of each party, it is apparent that advising the buyer to use documents less beneficial to the seller would violate the broker's duty of loyalty to the seller, assuming the seller was the broker's principal. For example, a deed of trust, with redemption provisions that appear to be more lenient to the purchaser, in that the purchaser can reinstate the deed of trust by bringing the payments up to date prior to sale, may not be in the best interests of the seller. The

168. See discussion of agency at text & notes 37-41 *supra*.

169. *Id.*

170. *Id. See also* Comment, *A Reexamination of the Real Estate Broker-Buyer-Seller Relationship*, 18 WAYNE L. REV. 1343, 1350-53 (1972).

171. An agent's duty to his principal does not require that he deal dishonestly or unfairly with any other party. *See* ARIZ. REV. STAT. ANN. § 32-2153(A)(1-5) (1976); ARIZ. ADMIN. R. & REG. tit. 4, § R4-28-17(A), at 21 (1975) [hereinafter cited as ARIZ. R. & REG.] (requiring honesty and fair dealing with the public without regard to the principal-agent relationship.).

172. If two principals have interests adverse to each other, an agent cannot fulfill his obligation of loyalty to both. In other words, an agent cannot act "solely for the benefit of" his principal, when an act that benefits one party is to the detriment of the other. *See* Marmis v. Solot Co., 117 Ariz. 499, 502-03, 573 P.2d 899, 902-03 (Ct. App. 1977). *See also* ARIZ. REV. STAT. ANN. § 32-2153(A)(1-5) (1976); ARIZ. R. & REG., *supra* note 171, § R4-28-17(A), at 21; RESTATEMENT (SECOND) OF AGENCY §§ 387, 389-94 (1957).

173. Morley v. J. Pagel Realty & Ins., 27 Ariz. App. 62, 66, 550 P.2d 1104, 1108 (1976).

seller may be best served by the use of a mortgage with foreclosure and default provisions precluding a reinstatement of the payment provision by the purchaser. Such provisions, if strictly enforced by the seller, are extremely harsh to the purchaser. Therefore, if the *Morley* obligation requires the broker to give advice as to which documents to use, rather than merely the possible consequences of not using certain types of documents, it is clear an agent may actually compromise his duty of loyalty to his principal in giving such advice to the non-principal party to the transaction. However, if the *Morley* duty only requires "banal" explanation of the documents to the parties involved, an agent can perform this disclosure function without impairing his duty of loyalty to his principal.[174] It is possible however, that a mere explanation of the documents may be insufficient to prevent consequences such as occurred in *Morley*.[175] The court expressly stated, by way of dicta, that the agent "bears the responsibility and duty of explaining . . . the *implications* of these documents."[176] The agent seems to owe his principal more. The language that seems limiting in *Morley* can be reconciled with the broader language in the case if interpreted to mean that a broker owes all persons involved a duty of disclosure and explanation as to the implications and consequences of certain legal documents, while he owes his principal even more, *viz.*, a duty to advise the principal as to the most appropriate and advantageous documents to be used in the transaction.[177] In fulfilling this duty to his principal, the agent must use diligence and care, and call upon all his professional skill and expertise.[178]

If the broker's duty is more extensive than the "banal advice"

174. The facts in the *Morley* case would be helpful to illustrate a possible interpretation of the way in which this duty could be fulfilled. The broker in *Morley* presented an offer to his seller in the amount of $15,000 with a $2,500 down payment. The balance of the purchase price of $12,500 was to be payable as follows:

> $12,500.00 by buyers executing in favor of sellers a demand note payable at not less than $100.00 per month. Buyers reserve the right to pay more than $100 per month on said note without penalty. Interest rate on the note will be 8%. The note will be all due and payable 10 years from date of closing.

27 Ariz. App. at 63, 550 P.2d at 1105. If the duty is interpreted as being narrow, perhaps that duty could have been fulfilled by merely stating the details of the note, and that the note is the document creating the obligation to pay. If this is all that is required, the situation that arose in *Morley* would not be a violation of any duty. If, as suggested in *Morley*, the advice must include the implications of the lack of security, then to give this advice to a non-client could very well violate the duty of loyalty to the principal.

175. *See* note 174 *supra*.

176. Morley v. J. Pagel Realty & Ins., 27 Ariz. App. 62, 66, 550 P.2d 1104, 1108 (1976) (emphasis added).

177. However, it is possible that the simple act of explaining to a non-client the implications of a particular document may in effect be advice as to the desirability of a course of action. If so, the duty of loyalty to the principal may be breached by the explanation to the non-principal party. To hold a broker liable for such a breach seems unjust, as it would be penalizing the broker for dealing fairly and openly with the non-principal party, as required by ARIZ. REV. STAT. ANN. § 32-2153(A)(5-6)(1976) and ARIZ. R. & REG., *supra* note 171, § R4-28-17(A), at 21.

178. *See* RESTATEMENT (SECOND) OF AGENCY § 379 (1957).

mentioned in *Morley* and is more like that of a lawyer, the question that suggests itself is whether the education of brokers and salesmen is adequate to prepare them to discharge this duty. Every applicant for an original license as either a salesman or a broker must provide evidence to the Commissioner of Real Estate that he has completed the required educational course.[179] The Real Estate Commission has adopted rules and regulations[180] setting forth the required curriculum of the salesman's forty-five hour course[181] and the broker's ninety hour course.[182] Although the number of hours recommended by the department for each subject is advisory only, the subjects outlined in the rules are required,[183] as is the total number of hours of classroom instruction.[184]

The subjects required for the broker's ninety hour course of instruction are exactly the same as those required for the salesman's course except for the requirement of one additional topic relating to the operation of a real estate office and several areas that could be considered specialties.[185] The topics receiving the most emphasis in both the brokers' and salesmen's courses are property and estates,[186] contracts,[187] encumbrances and burdens on title,[188] and valuation and ap-

179. ARIZ. REV. STAT. ANN. § 32-2124(B)-(C) (1976).

180. *Id.* § 32-2107(E) (1975) grants the power to the commissioner to adopt rules and regulations as may be necessary to carry out the provisions of the statutes. Rule R4-28-01 is the rule adopted by the commissioner setting forth the requirements for the real estate school curricula. ARIZ. R. & REG., *supra* note 171, § R4-28-01, at 1-16.

181. *See* ARIZ. REV. STAT. ANN. § 32-2124(B) (1976) which requires that an applicant for an original salesman's license is required to attend 45 hours of classroom instruction. The curriculum that is required for the salesman's course is set forth in ARIZ. R. & REG., *supra* note 171, § R4-28-01)(C), at 1-8.

182. *See* ARIZ. REV. STAT. ANN. § 32-2124(C) (1976) which requires that an applicant for an original broker's license is required to attend 90 hours of classroom instruction. The curriculum required for the course is set forth in ARIZ. R. & REG., *supra* note 171, § R4-28-01(D), at 9-16.

183. ARIZ. R. & REG., *supra* note 171, § R4-28-01(E), at 16.

184. ARIZ. REV. STAT. ANN. § 32-2124(B)-(C) (1976).

185. The required general topics are set forth in ARIZ. R. & REG., *supra* note 171, § R4-28-01(C)-(D), at 1-16 for both salesmen and brokers. There are 18 general topics for salesmen and 19 for brokers.

186. ARIZ. R. & REG., *supra* note 171, § R4-28-01(C), at 1-8 suggests allocation of seven hours to the topic of property and estates for salesmen and subsection D of the same rule suggests an allocation of nine hours for broker applicants. The sub-topics included in this general category cover property law, estates and interest in real property, fee simple estates, life estates, leasehold estates, landlord-tenant, types of tenancy, kinds of leases, forcible entry and detainer, concurrent estates, joint tenancy, tenancy in common, community property, and rights and duties of cotenants. *Id.*

187. ARIZ. R. & REG., *supra* note 171, § R4-28-01(C)-(D), at 1-16 suggests allocation of seven hours to the topic of contracts for salesmen and nine hours for brokers.

188. ARIZ. R. & REG., *supra* note 171, § R4-28-01(C)-(D), at 1-16 sets out the required coverage under encumbrances and burdens on title, with seven hours suggested for salesmen and nine hours suggested for brokers. Under the three main categories, liens, easements, and deed restrictions, the main emphasis is on liens. The curriculum requires coverage of mechanics liens, tax and judgment liens, mortgages, deeds of trust, priorities, clauses that are often included in such security instruments, implications of buying or selling "subject to" or "by assumption," general versus specific liens, voluntary versus involuntary liens, and enforcement of liens.

praising.[189]

In light of the possible interpretations of the *Morley* case,[190] the instruction required of new licensees seems to be adequate.[191] When considering the fact situation in *Morley*, an agent, having attended a course of instruction as required by the rules, should have sufficient knowledge to advise a client, or other person involved, as to the implications of the documents required for the transaction. The course of instruction includes consideration of various types of liens and encumbrances on title, including mortgages and deeds of trust.[192] The course also requires that students be taught the purpose of these security instruments, the necessary parties to these instruments, the actual documentation required, characteristics, benefits, limitations on use, and foreclosure methods for each type of security instrument.[193] This information would certainly be sufficient to give a broker the necessary educational background to advise a client as to the "implications"[194] of the documents.

Another area of law covered by the broad language at the end of the *Morley* decision[195] is contracts.[196] The comprehensive curriculum set forth under the contracts category[197] includes elements of contracts, such as offer and acceptance, consideration, capacity of the parties, lawful object, writing, form of contract, status of contracts, *i.e.*, valid, void, voidable, express versus implied contracts, executed versus executory, contract interpretation, parol evidence, materiality, remedies for breach, types of contracts, and the Statute of Frauds.[198] Again, this material seems to be sufficiently comprehensive to provide the broker with a sufficient understanding of contract law to allow him to prevent damages to the persons involved in a transaction resulting from faulty contract drafting. The broad interpretation of *Morley* seems justified when

189. ARIZ. R. & REG., *supra* note 171, § R4-28-01(C)-(D), at 1-16 requires coverage of a topic called valuation and appraising. The suggested time for this topic is three hours for salesmen and nine hours for brokers. Included in this section are market value versus price or cost, methods of appraising, market data, income approach, cost, depreciation, and economic principles of valuation.

190. See text & notes 156-78 *supra*.

191. Prior to 1968, no instruction of any kind was required of applicants for original licenses. ARIZ. REV. STAT. ANN. § 32-2124 (1976) (historical note). However, the 1968 amendments requiring the education applied only to new licensees; therefore the brokers and salesmen that were already licensed were not required to obtain this training. *Id.* However, ARIZ. REV. STAT. ANN. § 32-2130(A) (1977) requires that all renewal applications be accompanied by proof of attendance at real estate-oriented educational sessions approved by the commissioner. Many of the schools that offer the instruction for the original license course also offer the continuing education courses.

192. ARIZ. R. & REG., *supra* note 171, § R4-28-01(C)(6), at 5; *Id.* § R4-28-01(D)(6), at 12.

193. *Id.*

194. Morley v. J. Pagel Realty & Ins., 27 Ariz. App. 62, 66, 550 P.2d 1104, 1108 (1976).

195. *Id.* See text & notes 163-67 *supra*.

196. See note 194 *supra*; ARIZ. CONST. art. XXVI, § 1, set out in full at note 8 *supra*.

197. ARIZ. R. & REG., *supra* note 171, at § R4-28-01(C)(4), at 4; *Id.* § R4-28-01(D)(4), at 11.

198. *Id.*

reviewing the educational requirements established by the state for brokers and salesmen.

If we assume the *Morley* case imposes the broad duty on brokers to explain implications of all documents that brokers are allowed by the constitutional amendment to prepare, the educational requirements seem to provide the brokers with adequate knowledge and understanding of all the documentation that would ordinarily be used in a transaction.[199] However, most brokers still tend to rely on the expertise of title companies to prepare all documents with the exception of the preliminary deposit receipt and sales agreement.[200]

If *Morley* is given a narrow interpretation, in that the broker's duty extends only to his "client," the non-client party to the transaction may be deprived of the benefit of the broker's education and expertise.[201] If the non-client party is not a permissible beneficiary of the *Morley* doctrine,[202] and also not a permissible beneficiary of agency law,[203] he is left to the law of torts for his protection.[204] This would mean that the only duties the broker owes to the non-client are due care and honesty.[205] It has been stated that the purpose of state licensing statutes is to protect the general public from unscrupulous and unqualified real estate brokers.[206] Since the state has required a degree of

199. See text & notes 192-98 *supra*.

200. The fact that the title companies continue to engage in activities that may constitute the unauthorized practice of law was the subject of an article in the Arizona Bar Journal. The article noted that in the sixteen years since the passage of the constitutional amendment allowing real estate brokers to prepare legal documents incident to real estate transactions, title companies have been the actual source relied upon in many cases by brokers and even attorneys. *See* Unauthorized Practice of Law Committee, State Bar of Arizona, *Real Estate Instruments—Who is En"title"d to Prepare Them*, 13 ARIZ. B.J., Feb. 1978, at 30. The Unauthorized Practice of Law Committee of the State Bar has held several meetings to formulate a position for the State Bar as to the procedures in which the title companies participate. In an opinion setting forth the State Bar's interpretation of the current status of the law, many of the activities, such as preparation of deeds, mortgages, mortgage releases, etc., are deemed to fit within the State Bar's definition of the practice of law. *Id.* at 31. The title companies agreed that preparation of these documents constitutes the practice of law; however, they refused to abide by the opinion. This refusal seems to be partially based on anti-trust considerations prompted by Surety Title Ins. Agency, Inc. v. Virginia State Bar, 431 F. Supp. 298 (E.D. Va. 1977). *See id.* at 30-31. The Arizona State Bar plans to seek a judicial determination of the status of the title companies' activities and an injunction to prevent further unauthorized practice of law, if it is determined that such activity is being undertaken. *See id.* at 31. The opinion also sets forth services that the title companies could provide and that would not be considered the practice of law. *Id.* at 34.

201. See text & notes 202-09 *infra*. Since the *Morley* situation seemed to be one where there was only one broker acting as negotiator between the buyer and seller, the court's use of "client" could be ambiguous. In *Morley*, there is no doubt that the broker was an agent for the seller. Therefore, the seller was the "client" of the agent. However, in a cooperative sale with two brokers involved, the term "client" could be interpreted to mean the buyer when used in reference to the selling broker. This could give rise to the situation where the selling broker is the subagent for the seller, with the *Morley* obligation to his "client"—the buyer. For a discussion of a subagent's duty, see text & notes 32-44 *supra*.

202. See text & notes 159-61 *supra*.

203. See text & notes 17-36 *supra*.

204. See text & notes 80-85 *supra*.

205. See text & notes 80-134 *supra*.

206. *See, e.g.*, Whitaker v. Arizona Real Estate Bd., 26 Ariz. App. 347, 349, 548 P.2d 841, 843

competence of brokers, as evidenced by the educational prerequisites and license examinations,[207] it is reasonable to conclude that the public is to benefit from these statutory requirements.[208] There is no distinction between the broker's principal or a non-principal in any discussion of the intended beneficiaries of the statutes.[209] Therefore, it would appear that even the non-principal of the agent should benefit from the skill, knowledge, and expertise required by statute of all those allowed to engage in the real estate brokerage business in Arizona. To require brokers to explain the implication of all legal documents in the transaction to non-clients as well as to clients would merely require the broker to exercise his expertise and skill in conformity with the probable expectations of non-clients,[210] as well as the clients. Such a duty to the non-client does not impair any of the agent's duties to his principal, including the duty of loyalty. Even if the existing, traditional methods of recovery available to the non-client of the broker are adequate to protect him, it would be desirable to assure his complete understanding of all documentation. The broad interpretation of *Morley* would have this effect.

Conclusion

Although the law of agency imposes high standards of conduct upon real estate brokers for the benefit of the principal,[211] it does not address the problem of the standard of conduct of a broker absent the agency relationship. If there is no agent-principal relationship, an aggrieved party must rely on a standard of conduct as established under tort law principles.[212]

In the context of a real estate transaction, the possible actions in tort are misrepresentation and negligence. The elements of a misrepresentation claim are well settled; however, the standard of care for negligence or "malpractice" claims seems to be a developing area of the law, as evidenced by the court's opinion in *Morley*.[213]

The broad interpretation of *Morley* would require the agent to exercise his expertise for the benefit of all parties to the transaction, not

(1976); Realty Executives v. Northrup, King & Co., 24 Ariz. App. 400, 402, 539 P.2d 514, 516 (1975); Farragut Baggage & Transfer v. Shadron, 18 Ariz. App. 197, 200, 501 P.2d 38, 41 (1972).

207. *See* ARIZ. REV. STAT. ANN. § 32-2124(C) (1976) (requiring applicants for original brokers' licenses to show proof of attendance for 90 hours of classroom instruction and to pass an examination); *id.* § 2130(A) (Supp. 1977-78) (requiring applicants for renewal of brokers' licenses to show proof of attendance at 24 hours of classroom instruction); ARIZ. R. & REG., *supra* note 171, § R4-28-01(D), at 9-16.

208. *See* cases cited note 206 *supra*.

209. *Id.*

210. See text & notes 32-35 *supra*.

211. *See* text & notes 37-73 *supra*.

212. *See* text & notes 80-135 *supra*.

213. See text & notes 156-78 *supra*.

only for the principal. If limited only to principals, the case merely strengthens already existing agency law. Because the court used the words "client" rather than "principal" and "malpractice" the case seems to obviate an argument that the duty is limited to principals. It implies the duty extends beyond the laws of the agency. Assuming an interpretation broader than existing agency law, the extent of the duty imposed, as well as a determination of the beneficiaries of that duty, shall remain uncertain until defined in subsequent decisions by the court.

The more a non-principal party can require a broker to use his expertise, skill and experience on his behalf, the closer the broker comes to breaching the duty of loyalty to his principal. With those competing interests considered, it would seem that the broker's duty to the non-principal party would be basically a disclosure obligation. Obviously, it is desirable for all parties to a transaction to have a complete and thorough understanding of all the documents involved as well as the possible legal ramifications of the choice of documents. As has been determined in other areas of consumer transactions,[214] public policy supports a full and complete understanding of all aspects of a transaction by all the parties to the transaction.

If the broker's duty to the non-principal party is primarily a disclosure function, then his duty to his principal should be even greater. Because the principal has placed his confidence in his agent, the agent should be required to do his absolute best, drawing upon all his knowledge, expertise, experience, skill, and resources to perform his services to the best of his ability solely for the benefit of his principal. This duty may be summarized in the term "loyalty."

It is possible for an agent to fully disclose all pertinent facts to the non-principal and even educate the non-principal to a certain degree without breaching his duty of loyalty to his principal. However, it will be a fine line that a broker will have to walk. It cannot be reasonably argued that standards requiring a broker to keep the non-principal party ignorant as to the legal effects of the documents of a transaction would be desirable. Such behavior would violate the standards of fair dealing, full disclosure, and public policy.

In summary, *Morley* can and should be interpreted in such a manner as to impose duties on the broker that will benefit all the parties to real estate transactions. This interpretation would be in harmony with

214. *See* 15 U.S.C. §§ 1601-1613, 1631-1644, 1661-1665 (Supp. 1978) (Truth in Lending Law requires extensive disclosure in consumer credit transactions); 15 U.S.C. §§ 77a-77aa (1976) (Securities Act of 1933 requiring expansive disclosure of financial and business conditions of corporations that are offering securities to the public).

agency law, tort law, and public policy as expressed in the statutory educational requirements.