CANADIAN REGULATORS GROUP

Supplementary Paper No. 1

AGENCY LAW AND REAL ESTATE BROKERAGE:

CURRENT ISSUES

A Review of the Case Law and Some Industry Practices

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EXECUTIVE SUMMARY

Introduction (Section 1)
This report primarily reviews current issues in agency law and the real estate brokerage industry brought disclosed by cases from the thirteen provinces and territories in the last ten years. Some comments are also made concerning certain industry practices.

Terminology (Section 2)
The terminology used by the industry, legislation and the courts to describe the various actors in real estate transactions and their relationships differ. Thus, key terms used in the report are defined and their synonyms (where relevant) are provided.

Brokers As Fiduciaries (Section 3)
Brokers, when acting as agents, have been traditionally held to owe their clients fiduciary obligations. But it has been recognized that not all agents need be fiduciaries where the critical elements of such relationships are absent. These elements are a discretionary power in a person to affect the interests of another who is in a position of vulnerability and who is relying on the former to protect their interests.

At its heart, fiduciary relationships entail that brokers owe their clients a duty of utmost loyalty, to avoid all conflicts of interest and to act only in their clients' interests. In particular, this means that brokers must protect any confidential information obtained from clients, refrain from making any secret profits (including, directly or indirectly, buying or selling any property clients owns or are interested in purchasing) at the expense of his or her clients. Thus, the dual agency relationship raises particular problems for brokers.

Brokers can avoid liability for a *prime facie* breach of their fiduciary obligations if they completely disclose the conflict of interest and obtain their clients' consent to engage in otherwise prohibited conduct.

Representative Capacity of Brokers (Section 4)
Brokers normally represent one party to a transaction (either the buyer or the seller). However, a broker's representative capacity is primarily a question of law and not one of intention; consequently, brokers may unknowingly enter into agency relationships, especially dual agency relationships in particular cases. Thus, while the move towards disclosure of representative capacity is a positive one, such disclosure is insufficient in itself to overcome potential problems raised by dual agency.

The growth in buyer agency in the industry is also a positive development but is again a potential source of problems where a broker represents competing buyers or seeks remuneration from the seller.

The issue of dual agency continues to be a source of concern to the industry as it can arise: where an individual broker represents both parties to a transaction; and, also where the parties are represented by employees of the same firm or different firms under MLS arrangements. In these latter instances, the problem is caused by two presumptions: first, that members of a firm share information and advice and thus all are presumed to have knowledge of confidential information

concerning the firm's clients; and second, that the knowledge of an agent is imputed to the principal. However, the case law suggests that not all dual agency relationships need attract fiduciary obligations; and developments in other fields suggest that brokerage firms may be able to implement policies and procedures ("Chinese Wall") to protect confidential information provided by clients.

Duty and Standard of Care (Section 5)
It is well accepted that brokers owe clients and customers a duty of care and must exercise their chosen profession in accordance with set standards that have their basis in industry practice. The standard is an objective one – that of the reasonable broker –and is applicable to all, though a higher standard is expected of those who posses or purport to posses special expertise. Where questions arise as to how a reasonable broker would have conducted himself or herself, recourse may be had to expert testimony and the rules and by-laws of the industry. The pervasiveness of the duty and standard of care does not appear to be fully understood by industry members given the number of cases in which non-compliance has been alleged by a client or customer.

It is well known the brokerage firms are vicariously liable for the misconduct of their employees. However, in recent cases "direct" liability has been imposed on firms for failing to adequately supervise and monitor their employees and to have in place policies and procedures to prevent harm to clients and customers.

While "exclusion clauses" in contracts may provide brokers and their firms some protection from liability it still remains to be seen whether brokerage firms can avoid vicarious liability through employment of brokers as "independent contractors.

Duty of Disclosure (Section 6)
In the course of their profession, brokers are required to disclose information to clients and customers. To clients, brokers are required to disclose all relevant information that they might posses about the property, the transaction and a third party with whom a client is dealing with.

Brokers' obligation of disclosure to customers is narrower than that they owe to clients. In fact it is identical with their client's obligation of disclosure. Clients and, by extension their brokers, must disclose to customers all material latent defects in a property. Material latent defects are a subclass of those defects that cannot be discerned through a reasonable inspection of the property. They are those defects that render the property dangerous or potentially dangerous to the occupants; render the property unfit for habitation; render the property unfit for the purpose for which the buyer is acquiring it where the buyer has made this purpose known to the seller or the broker; concern local authority and similar notices received by the seller that affect the property; or, concern the lack of appropriate municipal building and other permits.

Given the limited duty of disclosure of clients and their brokers, property disclosure statements are problematic since they require clients to disclose more than they are legally obliged to disclose to buyers. Thus, where brokers ask their clients to complete such statements serious questions arise as to whether brokers are acting in their clients' best interests.

Governance Framework (Section 7)
Most legislation governing brokers and their industry reflects previous practice where brokers where perceived to be the seller's agents. Thus, the legislation does not deal effectively with, for example, buyer agency and dual agency. A detailed review of the legislative framework will be

the subject of an upcoming report.

The move to self-regulation in the industry is a positive one. While governing bodies have the power to regulate members of the industry, in general, they lack the power to affect the common law and statutory rights and obligations of members, clients and customers.

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1. INTRODUCTION

As the title suggests this report focuses on *current issues* in agency law and the real estate brokerage industry (hereafter "the industry"). These issues have been identified primarily through a review of cases over the past decade. In addition, a number of issues arising from a preliminary review of provincial legislation (statutes and regulations) governing the industry are indicated, as are some other issues inherent in certain industry practices.

Comments on the Case Law

To identify relevant case law an electronic search was conducted in all provinces and territories (hereafter "provinces") for cases decided over the past decade involving industry members that raised, explicitly or implicitly, agency issues, or touched on their practices. The search disclosed 419 cases. This figure represents, what may be described as, the "tip of the iceberg" of legal disputes involving industry members since, on the one hand, not all cases are "reported" and, on the other, the search gives no indication of the number of legal "disputes" involving industry members that are settled out of court.

It may be of interest that a search for cases involving other categories of agents and brokers (e.g. insurance agents, stock brokers, etc) disclosed far fewer reported cases. This accord with an earlier comparative survey that was conducted of agency litigation in Canada, namely, that the preponderance (over 80%) of agency litigation involves members of the industry.

In the following discussion, not every case disclosed by the search is referred to because not all were helpful: some involved preliminary or procedural issues; others did not contain a full statement of the facts; yet others contained very little discussion of relevant legal principles. In addition, it should be noted that no attempt is here made to treat:

- *Commission cases*: those primarily concerning disputes as to entitlement to commission (of which there have been approximately 90 in the last decade). These cases offered little, if anything, new to the principles governing brokers entitlement to commission;
- *Licensing cases*: those where the central issue was the need for, or absence, of an appropriate license; and
- *Disciplinary cases*: cases dealing with disciplinary proceedings against industry members, unless a case had something of significance to add to the agency issues dealt with in this report.

Finally, to avoid cluttering the body of this report with references, the cases to which reference is made herein are to be found in footnotes.

Current Issues

The issues that appear from the case law to be current are, in most instances, not new – they are, with some exceptions, recurring issues that may be grouped together under four broad themes:

- *Brokers as fiduciaries* - under which are considered the essential elements of fiduciary relationships, and fiduciary duties and their relevance to industry members;
- *Representative capacity of brokers* - under which are treated the issues of disclosure, purchaser agency and dual agency;
- *Duty and standard of care* - under which are considered the duty of care brokers owe

to clients and customers, the standard of care with which they must comply, how the standard is determined, the scope of the standard, and avoidance of liability for violations of the standard;

- *Duty of disclosure*: under which are treated the duty of disclosure (other than the fiduciary duty of disclosure) brokers owe to clients, on the one hand, and customers, on the other, and the potential implications of the use of property disclosure statements.

In the final section of this report, certain issues suggested by the current legislative and regulatory frameworks of the industry are briefly mentioned.

It should be noted that a number of current issues facing the industry will be dealt with in subsequent reports, that is, issues that may arise from:

- the legislative framework;
- industry by-laws and rules regulating the conduct of members as agents;
- the standard forms used in the industry; and
- the move to self-regulation.

2. TERMINOLOGY

Before turning to the substance of this report, a word need be said about the *terminology* used in the case law, by the industry and in this report. This is necessary because, notwithstanding the acknowledgement that industry members are agents governed by the law of agency, rarely does one encounter use of traditional agency terminology (that of agent, principal and third party) in the legislation, rules, by-laws and codes of ethics to which industry members are subject. Moreover, whereas industry members use the terms most familiar to them (buyer and seller, client and customer, purchaser or buyer agency, and the like), lawyers and judges use those most familiar to them (purchaser and vendor, principal and third party, listing agent or broker and selling agent or broker, and the like). This is not surprising, but for those not intimately familiar with industry terminology, on the one hand, and legal terminology, on the other, there is a risk of misunderstanding.

Thus, while it is a positive move on the industry's part to develop a uniform set of industry terms to facilitate communication between members, and between provincial governing bodies and their members, it may take some time for such terminology to gain currency in the law. In part, this is because the law governing the real estate brokerage industry is seen as but part of the broader field of law governing real estate transactions, that is, the law of vendor and purchaser as it is frequently called; in part, because industry terminology is not (yet) commonly encountered in the legislation regulating the industry; and, in part, because of the law's fondness for tradition. Further, to add to the potential for misunderstanding, even where terms are defined, say, in legislation, similar terms are not always given identical definitions in all provinces.

In light of this, in what follows, an attempt has been made to use industry terminology to identify the actors and other relevant matters. Thus:

Agency

"Agency" simply describes the relationship that exists "between two persons, one of whom [the

principal] expressly or impliedly consents that the other [the agent] should act on his behalf, and the other of whom similarly consents so to act or so acts."[1]

Agency agreement

"Agency agreement" is used to denote the representation agreement, entered into between a broker or brokerage firm and client, that establishes the relationship of agency between them. This term includes listing, buyer agency and dual agency agreements. (However, these latter terms will be used where greater specificity is required by the context.)
***NOTE*:** As is discussed below [section 4.2], an agency agreement may be entered into expressly by a broker and client, or its existence may be implied from the particular facts of a case.

Broker

Although traditionally "broker" and "agent" are not synonymous terms, they are used interchangeably in the case law that deals with industry members. However, for the sake of clarity, the term brokers is used herein to describe industry members – after all, real estate brokers, are always brokers, though they may not always act as agents, in the legal sense of the term, in every transaction.

***NOTE*:** According to *Black's Law Dictionary* (7th ed.) a "*broker*" is as "an agent who acts as intermediary or negotiator between prospective buyers and sellers; a person employed to make bargains and contracts between other persons in matters of trade, commerce and shipping;" and a "*broker-agent*" is a "person who acts as an intermediary ... and as representative of one of them." In other words, brokers act essentially as middlemen, whereas broker-agents and agents act as representatives of a party to a transaction. It would thus appear that the term that may best describe industry members is that of "broker-agent." The reality, however, is that once the term agent is linked to broker, all of the duties and obligations inherent in agency attach to the broker.

Brokerage firm

"Brokerage firm" is used to designate real estate brokerage firms, the entities that employ industry members whether they are brokers or salespersons.

***NOTE*:** Where an individual industry member employed by a brokerage firm enters into an agency agreement with a client, in law the agreement is with the brokerage firm - and it is the firm (small or large) that is the client's agent, and it is the firm and all its employees who, *prima facie*, are deemed to owe duties and responsibilities to the client. But, in fact, the individual broker can be viewed both as the agent of the firm, who enters into agency agreements with clients as a representative of the firm, and as the agent of the client.

Buyer agency

"Buyer agency" (or "purchaser agency") describes the situation where a broker expressly or by implication (assumed buyer agency) has as client a buyer in a transaction.

Client

"Client" is used to identify a broker's principal, that is, the person with whom the broker or brokerage firm has entered into an agency relationship. A client may be a seller or buyer.

Customer

"Customer" is used to identify the third party, the "outsider" to a particular agency relationship. However, a customer to one broker may be the client of another. A customer may be a seller or

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[1] *Bowstead on Agency*, 15th ed. (1985).

buyer.

Dual agency

"Dual agency' identifies those situations in which a broker or brokerage firm represents both seller and buyer in a transaction. Dual agency may arise by express agreement or its existence may be implied from the particular facts of a case.

***NOTE*:** The term "limited dual agency" is not used in this report as its meaning is not readily apparent from the disclosure forms or the case law. In a dual agency situation [as discussed below in section 4.3.1] it is a broker's capacity to act as a agent for each of the competing clients that is limited; it is not the dual agency itself that is limited. Similarly, if the term is meant to suggest that the dual agency relationship is a non-fiduciary relationship [as discussed below in section 4.3.4], it is misleading because it is, again, a broker's capacity to act as agent that is limited; it is not the dual agency itself that is limited.

Salespersons

"Salespersons" are persons who are employed, appointed or authorized by brokerage firms or brokers to trade in real estate. Unlike brokers, they are deemed by statute to lack the capacity, *inter alia*, to trade in real estate on their own account.

***NOTE*:** There are few references to salespersons in this report. This is not because they are not significant actors in the industry – indeed they are the "hub" of many transactions. Rather, the lack of specific reference to them is because, from an agency law perspective, salespersons owe the same duties and responsibilities as brokers or brokerage firms owe to clients and customers; and their misconduct engages the liability of their employers in the same manner as that of brokers. Thus, unless otherwise indicated, what is said about brokers applies equally to salespersons.

3. BROKERS AS FIDUCIARIES

The Supreme Court of Canada has observed that:[2]

> There are few legal concepts more frequently invoked but less conceptually certain than that of the fiduciary relationship. In specific circumstances and in specific relationships, courts have no difficulty in imposing fiduciary obligations, but at a more fundamental level, the principle upon which that obligation is based is unclear. Indeed, the term "fiduciary" has been described as "one of the most ill-defined, if not altogether misleading terms in our law ....

3.1 Agents - Presumed Fiduciaries

Nevertheless, the Supreme Court has recognised that there are certain classes of relationships, of which agency relationships are one, which are assumed to give rise to fiduciary obligations. Thus, in any consideration of the obligations of brokers the starting premise must be that "there is no doubt that in most, perhaps almost all, situations, real estate [brokers] owe their [clients] a fiduciary duty."[3]

But, the presumption that brokers are fiduciaries is a rebuttable one, it now being accepted that

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2 *Lac Minerals Ltd.* v. *International Corona Resources Ltd.* (1989), 61 D.L.R. (4th) 14 (S.C.C.).

3 *Phillips* v. *R.D. Realty Ltd.*, [1995] O.J. No. 2746 (Gen. Div.) aff'd [1996] O.J. No. 3074 (C.A.).

the mere "fact that a person wears the badge of 'agent' does not automatically subject him or her to fiduciary responsibility towards his or her [client]."[4] Rather, the case law makes clear that:

> the question of whether a fiduciary duty is owed cannot be answered by simply looking at the formal legal label attached to the relationship between the parties .... [I]t is necessary to examine the substance of the relationship between the party alleged to owe a fiduciary duty and the party claiming the benefit of that duty.[5]

Still, it must be stressed that, in light of the presumption that brokers are fiduciaries, it is for brokers to discharge the onus of proving that in the circumstances of the transaction they were not in a fiduciary relationship with the client; it is not for the client to establish that the relationship was one attracting fiduciary obligations.

Consequently, in discussing the issue of brokers as fiduciaries regard will be had:

- to the identifying characteristics of fiduciary relationships;
- to the duties inherent in such relationships; and
- to the matter of the duration of fiduciary relationships.

3. 2. Essential Elements of Fiduciary Relationships

What are the essential elements of fiduciary relationships which, if shown to be absent in a particular, case may transform the *prima facie* fiduciary relationship of brokers into a non-fiduciary relationship. These elements are:[6]

1. The fiduciary has scope for the exercise of some discretion or power.
2. The fiduciary can unilaterally exercise that power … so as to affect the beneficiary's legal or practical interests.
3. The beneficiary is peculiarly vulnerable to or at the mercy of the fiduciary holding the discretion or power.

Unhelpfully, in the same breath, courts have observed that the mere absence of one or more of these elements will not necessarily lead to the conclusion that a particular relationship is not fiduciary in nature.

Nevertheless, the "common thread that unites this body of law" has been said to be "the measure of the confidential and trust-like nature of the particular advisory relationship, and the ability of the plaintiff to establish reliance in fact."[7] Consequently, the key ingredient to the existence of fiduciary relationships appears to be whether clients repose trust and confidence in brokers and rely on their advice, thus making clients dependent on and vulnerable to brokers.[8] Indeed, it has

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4 *Rawlinko* v. *Blair* (1998) 17 R.P.R. (3d) 91 (Ont. Gen. Div.); and see *Knoch Estate* v. *Jon Picken Ltd.*(1991) 18 R.P.R. (2d) 250 (Ont. C.A.) and *Alwest Properties Ltd.* v. *Roppelt*, [1998] A.J. No. 1401 (Q.B.).

5 *Phillips* v. *R.D. Realty Ltd.*, [1995] O.J. No. 2746 (Gen. Div.) aff'd [1996] O.J. No. 3074 (C.A.). See also *Rattan* v. *Mangar*, [1994] O.J. No. 866 (Gen. Div.).

6 *Frame* v. *Smith*, [1987] 2 S.C.R. 99. See also *Lac Minerals Ltd.* v. *International Corona Resources Ltd.* (1989), 61 D.L.R. (4th) 14 (S.C.C.); *Rattan* v. *Mangar*, [1994] O.J. No. 866 (Gen. Div.); *Rawlinko* v. *Blair* (1998), 17 R.P.R. (3d) 91 (Ont. Gen. Div.); *Bryson* v. *Mila*, [1994] O.J. No. 2685 (Gen. Div.); *591971 Saskatchewan Ltd.* v. *Martin Developments ltd.*, [1998] S.J. No. 738 (Q.B.).

7 *Hodgkinson* v. *Simms*, [1994] 3 S.C.R. 377.

8 *Hodgkinson* v. *Simms*, [1994] 3 S.C.R. 377; *Lac Minerals Ltd.* v. *International Corona Resources Ltd.* (1989), 61 D.L.R. (4th) 14 (S.C.C.). And see *Mucci* v. *C.M.F. Realty Ltd.*, [1999] O.J. No. 2700 (S.C.); *Sandhu* v. *Sheill*, [1996] B.C.J. No. 507 (C.A.).

been observed that this ingredient is present, and a fiduciary relationship arises, as soon as brokers receive confidential information from a seller (say, the lowest price that the seller will entertain) or a buyer (say, the highest price that buyer is prepared to pay).[9]

If this "common thread" is the determinant of the existence of a fiduciary relationship, it is indisputable that many, if not most, agency relationships are fiduciary in nature since clients do disclose confidential information to and repose trust and confidence in their brokers.

In concluding this section, it must be noted that a fiduciary relationship may exist even where brokers:

- have not entered into express agency agreements with sellers or buyers, for in fiduciary relationships, as in the case of agency relationships [as discussed below section 4.2], the law will impose such a relationship on brokers where it is warranted by the facts of the case;[10]
- are acting gratuitously for their clients;[11] or
- are engaged in joint ventures with their clients.[12]

3.3 Fiduciary Duties

As is well known, persons in fiduciary relationships owe their clients, what are termed, fiduciary duties. But, what is not so well understood is that not all duties owed by fiduciaries are fiduciary duties. Some of these duties - such as, those to exercise reasonable care and skill in the performance of their functions and the attendant duty of disclosure [discussed below in section 5 and 6 respectively] - are owed by all professionals who act in an advisory capacity, whether or not they also act as fiduciaries. This does not always appear to be appreciated with some counsel and courts taking the position, incorrectly, that all breaches of duty by fiduciaries are breaches of fiduciary duties.

Strictly speaking, the fiduciary duties owed by brokers are all encapsulated in the basic principle that they must always act in their clients' best interests. More specifically, fiduciaries must never permit their own interests, or the interests of third parties, directly or indirectly, to come into conflict with the interests of their clients absent their clients' fully informed consent to such conflict.

Some of the various manifestations of this overarching duty are outlined below.

3.4. Conflict of Interest Situations

Conflicts of interest, real and potential, arise is a range of situations. Those disclosed in the recent case law are not new and most are obvious; but they, nevertheless, are worth identifying.

3.4.1 *Dual agency*

Whenever brokers or brokerage firms act for both parties to a transaction a conflict of interest

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9 *Anderson* v. *Peters*, [2000] M.J. No. 563 (Q.B.).
10 *Ibid.*
11 *Ibid.*
12 *Mr. T. International Agencies* v. *Deol*, [1999] B.C.J. No. 2400 (C.A.); *Verma* v. *Zinner*, [1994] A.J. No. 816 (C.A.).

prima facie will arise between sellers and buyers whose interests are diametrically opposed. This particular situation is dealt with in greater detail below [in section 4.3].

3.4.2 *Purchase by brokers of clients' properties*

Whenever listing brokers, or co-operating brokers under an MLS agreement, seek to buy their clients' properties, whether directly or indirectly through nominees, and whether for re-sale or for personal use, a conflict arises between brokers' and clients' interests.[13]

A conflict of interest will also be present where other persons, to whom brokers are related, personally or through business, seek to acquire clients' properties.

It should be noted that it has even been suggested that in such situations brokers should withdraw from the agency relationship; and that their industry associates who are aware of the circumstances may incur liability if they fail to advise them to withdraw.[14]

3.4.3 *Purchase by brokers of properties in which clients are interested*

A similar conflict of interest arises whenever brokers in buyer agencies seek to buy the properties in which their clients are interested, whether the property is acquired directly or indirectly through nominees, and whether for re-sale or for personal use.[15]

Again, a conflict of interest will also be present where persons to whom brokers are related, personally or through business, seek to acquire clients' properties.

3.4.4 *Disclosure of confidential information*

As noted above, fiduciary relationships are inherently confidential in nature. Consequently, brokers are under a duty to preserve the confidentiality of any information that may be used to the disadvantage or prejudice of their clients' interests.[16]

In this context, the term "confidential information" is not restricted to personal information concerning a client. It essentially embraces any information concerning the client, the property or the transaction that is not required by law to be disclosed but which, if disclosed, could be used by a customer to the disadvantage of a client.

Thus, brokers representing sellers or buyers must not provide customers with information affecting their clients or the properties in question, which could be advantageous to customers in their negotiations with brokers' clients other than information they are permitted by their clients, or required by law, to disclose. It is, in part, for this reason that the use by sellers' brokers of property condition statements is potentially problematic [as is discussed in greater detail below in section 6.3].

Finally, it is obvious that brokers cannot personally use confidential information to the prejudice of their clients' interests.

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13 *David Manning Family Trust* v. *Country Brook Estates Ltd.*, [1996] B.C.J. No. 1752 (S.C.).; *Struthmann* v. *Routly*, [1994] O.J. No. 1535 (Small Claims Ct.); *Bryson* v. *Mila*, [1994] O.J. No. 2685 (Gen. Div.); *Bryson* v. *Mila*, [1994] O.J. No. 2685 (Gen. Div.); *Tuli* v. *Re/Max Apex Realty Inc.*, [1995] O.J. No. 3789 (Gen. Div.); *Homelife Romano Realty Ltd.* v. *Castelluzzo*, [1996] O.J. No. 4474 (Gen. Div.).

14 *Bodnar* v. *Real Estate Council of British Columbia*, [1994] B.C.J. No. 2742 (C.A.).

15 *Anderson* v. *Peters*, [2000] M.J. No. 563 (Q.B.); *G.L. Black Holdings Ltd.* v. *Peddle*, [1998] A.J. No. 1488 (Q.B.) aff'd [1999] A.J. No. 1083 (C.A.).

16 *MacAuley* v. *LeClair*, [1998] O.J. No. 1918 (Gen. Div.).

3.4.5 *Secret profit*

Brokers, when acting as fiduciaries, are prohibited from making any secret profits or, indeed, receiving any form of remuneration or reward from anyone but their clients in the absence of the fully informed consent of their clients to the receipt of such payment. This prohibition extends to the receipt of:

- commissions from the other party to a transaction, a situation which creates potential difficulties for brokers in buyer agency and dual agency relationships;[17]
- referral fees or gifts from third parties (contractors, lending institutions, other brokers, lawyers and the like) for referring clients to them for particular purposes.[18]

It would appear that the prohibition on secret profits extends to payments received from third parties:

- whose services are necessary for the satisfactory consummation of the transaction itself (e.g. lenders, appraisers, building inspectors, lawyers, etc.); and
- who provide what may be described as incidental services (e.g. building contractors, landscapers, interior decorators, moving companies, etc.).

It is suggested that the acid test for determining what constitutes a secret profit is: would the payment have been earned by the broker but for the existence of the broker-client relationship in the circumstances of the case? If the answer is no, then the payment is likely to be considered a secret profit for which the broker is accountable to the client.

3.5 Fiduciary Duty of Disclosure

The foregoing *prima facie* breaches of brokers' fiduciary obligation, always to act in their clients' best interests, are nevertheless permitted if brokers have fulfilled their fiduciary duty of disclosure.

Thus, when a conflict of interest, real or potential, arises brokers must be able to prove that:

- they have made full and fair disclosure of all relevant facts respecting the subject matter of the contract which would be likely to influence the conduct of their clients; [19]
- their clients have agreed to continue with the transactions notwithstanding the conflict; and
- the eventual transactions entered into by their clients are "righteous ones" in all the circumstances, that is, they are transactions that would have been undertaken by parties at "arm's length."[20]

From this, it would appear that mere disclosure alone is not sufficient. Nor is it sufficient to have clients simply sign an acknowledgement of disclosure form, even if accompanied by explanatory materials. Brokers must also be able to show that their clients understood:

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17 *Cross Creek Timber Traders Inc.* v. *St. John Terminals Ltd.*, [2002] N.B.J. No. 77 (Q.B.).

18 *Re/Max Loyalsit Realty Ltd.* v. *Spence (c.o.b. Robert Spence Construction)*, [1993] O.J. No. 1539 (Gen. Div.); *Klingspon* v. *Royal LePage Real Estate Services Ltd.*, [1993] O.J. No. 1439 (Gen. Div.).

19 *Charles Baker Ltd.* v. *Baker*, [1954] O.R. 418 at 432 (C.A.) per McKay J.A. And see, e.g., *Krassman Realty Ltd.* v. *Paragon Realty Ltd.* (1983), 45 A.R. 64 (Q.B.); *Proulx* v. *Gardiner Realty Ltd.* (1982), 40 N.B.R. (2d) 529 (Q.B.); *D'Atri* v. *Chilcott* (1975), 55 D.L.R. (3d) 30 (Ont. H.C.).

20 *Charles Baker Ltd.* v. *Baker*, [1954] O.R. 418 at 432 (C.A.) per McKay J.A.; *Gornergrat Developmeents Ltd.* v. *Vanro Properties Inc.*, [1995] O.J. No. 1116 (Gen. Div.).

- the nature of the conflict;
- what was being proposed by the broker; and
- the implications of giving their consent.

Thus, brokers have to be able to satisfy the courts:

- in the cases of dual agency relationships [discussed below in section 4.3.4], that their clients fully appreciated all of the implications inherent in such a relationship and nevertheless consented to enter such a relationship; and
- in the case of the use of property disclosure statements by sellers' brokers [discussed below in section 6..3.2], that the clients were fully aware of their limited obligation of disclosure, the legal implications of such statements and, yet, nevertheless, consented to complete the statements.

It should be noted that, at common law, the disclosure imposed on fiduciaries may be satisfied either in writing or orally; however, to minimize the possibility of disputes it is advisable that such disclosures always be in writing.

Moreover, it must be kept in mind, that brokers' duty of disclosure in particular situations, and the form such disclosure must take, has been embodied in the provincial statutes regulating the industry. This is especially the case where brokers seek:

- directly or indirectly, to purchase their clients' property for resale by the brokers - not only must their status as their representative capacity but a range of other pertinent information (all provinces);
- directly or indirectly, to purchase their clients' property for personal use (some provinces); and
- to sell their properties to clients (few provinces).

In addition, in at least one province (British Columbia), brokers must, by statute, disclose to their clients the source of all commissions received.

The statutory obligation of disclosure attaches to brokers even though at the time of making an offer or contracting they were not officially designated as brokers but become so designated prior to completion of the transaction.[21]

Finally, on this point, it must be remembered that none of the current statutory disclosure requirements replace or diminish the fiduciary duty of disclosure; and that the latter, in many instances, is more onerous than the former. Thus, compliance with both statutory and fiduciary duties of disclosure is required.

3.6 Termination of Fiduciary Relationships

The fiduciary relationship of broker and client persists until the agency agreement expires or the purpose of the agency has been accomplished (i.e. the transaction is completed). Therefore, where a broker has obtained an offer that has been accepted by the client the fiduciary relationship remains in effect until the transaction is completed[22] or the agency agreement

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21 *Alert Products of America Corp.* v. *Parksville Apartments Ltd.*, [1993] B.C.J. No. 1605 (S.C.).

22 *Reidy Motors Ltd.* V. *Grimm*, (1996) R.P.R. (2d) 251 (Alta. Q.B.).

terminates.

However, even when an agency agreement and, thus, the fiduciary relationship between broker and client has been terminated, some fiduciary duties persist thereafter - thus, for example, on termination of an agency relationship, brokers cannot use confidential information acquired while representing a client for their own or a third parties benefit.

4. REPRESENTATIVE CAPACITY OF BROKERS

Under this heading are discussed a range of current issues relating to the representative capacity of industry members; not all are new issues by any means. These issues are:

- the move to disclosure of brokers' representative capacity;
- the move to "official" recognition by the industry of buyer agency; and
- the continuing, indeed perennial, issue of dual agency.

4.1 Disclosure of Representative Capacity

The move towards requiring brokers to disclose in writing who is their client (be it the seller, buyer or, in a dual agency situation, both), is a positive development. It has been made an industry requirement in British Columbia and Nova Scotia. However, it should not be made a pre-condition to recovery of remuneration in all cases as there can be situations in which a seller or buyer may be unwilling to enter into an agency agreement with a broker, yet seek to take advantage of the broker's efforts on their behalf. This, for example, is recognised by the Nova Scotia legislation.

The advantage of such disclosure is that both clients and customers are put on notice as to who brokers represent and, thus, the level of service that may be expected of them by each. Similarly, the disclosure should also serve to direct the mind of brokers as to who are their clients and, therefore, whose interests should be of paramount importance to them and, particularly, to whom they owe fiduciary obligations. Disclosure, thus, should reduce disputes as to the existence of agency relationships,[23] and who brokers are representing in particular transactions.[24]

However, the cases suggest that it is not properly understood by industry members that a mere declaration, written or oral, is not determinative of the representative capacity in which they are acting. As has been observed, the capacity in which brokers act, and who they represent, are questions of fact to be determined in the circumstances of each case.[25] What brokers may intend, indeed, what brokers may have told the parties to a transaction, is not determinative. It is how brokers act and how their acts are perceived that is determinative.[26] Nor is the label attached by sellers or buyers to their relationship with brokers conclusive where their representative capacity

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[23] *Sandhu* v. *Sheill*, [1996] B.C.J. No. 507 (C.A.).

[24] *Struthmann* v. *Routly*, [1994] O.J. No. 1535 (Small Claims Ct.); *Howe* v. *635362 Ontario Ltd.*, [1997] O.J. No. 370 (Gen. Div.); *Eastercrest Developments Ltd.* v. *Jakovljevic*, [1997] O.J. No. 4139 (Gen. Div.); *Anderson* v. *Peters*, [2000] M.J. No. 563 (Q.B.)

[25] *Rawlinko* v. *Blair*, [1998] O.J. No. 1315 (Gen. Div.); *R.K. Holdings Corp.* v. *Koyl Commercial Real Estate Services Ltd.*, [2000] S.J. No. 109 (Q.B.); *Toll* v. *Marjanovic*, [1002] O.J. No. 70 (S.C.J.); *Vincent* v. *Lanoue*, [1994] O.J. No. 2925 (Den. Div.).

[26] *489212 Ontario Ltd.* v. *Participative Dynamics Inc.* (1994), 38 R.P.R. (2d) 32 (Ont. Gen. Div.) aff'd [1997] O.J. No. 3856 (C.A.).

is called into question.[27]

Thus, it is possible for brokers to be viewed as agents in transactions even though they are ignorant of their representative status because, while agency must generally derive from the consent of the parties:[28]

> the consent need not necessarily be to the relationship of principal and agent itself (indeed the existence of it may be denied) but it may be to a state of fact upon which the law imposes the consequences which result from agency.

In light of this, it is apparent that the mere disclosure of representative capacity will not insulate brokers from the problem of dual agency [discussed below in section 4.3]. What is needed is for brokers also to act in conformity with their disclosure and avoid conduct that may provide the basis for the argument that they have become the agent of the customer in a particular case.

Moreover, the disclosure by brokers of their representative capacity must be timely, that is, before they have led the seller or buyer to believe that the broker is acting as their agent and before any potential conflicts of interest have arisen. Thus, in light of the indicia of fiduciary relationships, discussed above, the disclosure should be made before a party has conveyed any confidential information to the broker; once this has occurred a broker may have little option but to elect to represent that party as the broker may well be deemed to be in a fiduciary relationship with that party from that point in time.[29]

More basically, timely disclosure of representative capacity is required because the party who is not represented by the broker must have a meaningful opportunity to consider the disclosure and to make a decision as to whether to retain another broker or advisor before proceeding with the transaction.[30]

In addition, the disclosure when made must be complete and not misleading; thus, it is not enough for a broker, acting as dual agent, simply to advise each client the broker is acting as that client's agent if the fact of the dual agency itself is not disclosed.[31]

However, it may here be noted that recent cases suggest that an agency relationship will not be established:

- with a seller simply because it is the seller who pays a broker's commission;[32]
- with a customer simply because a broker conveys information and documents from the customer to a client.[33]

Similarly, as noted above, just because a broker is deemed to be the agent in the circumstances of a case, "does not automatically subject him or her to fiduciary responsibility towards his or her [client]."[34] But the burden of proving the non-fiduciary nature of the relationship rests on the

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27 *Abdullah* v. *Bro*, [2000] O.J. No. 4165 (S.C.).
28 *Branwhite* v. *Worcester Works Finance Ltd.*, [1969] 1 A.C. 552 at 587 (H.L.).
29 *Anderson* v. *Peters*, [2000] M.J. No. 563 (Q.B.).
30 *Mucci* v. *C.M.F. Realty Ltd.*, [1999] O.J. No. 2700 (S.C.).
31 *Siculiana Holdings Inc.* v. *J.Goia Holdings Inc.*, [1994] O.J. No. 2571 (Gen. Div.).
32 *MacCauley* v. *Leclair*, [1998] O.J. No. 1918 (Gen. Div.); see also *Cross Creek Timber Traders Inc.* v. *St. John Terminals Ltd.*, [2002] N.B.J. No. 77 (Q.B.); *Stacey* v. *Sigmund*, [1995] B.C.J. No. 721 (S.C.).
33 *Sandhu* v. *Sheill*, [1996] B.C.J. No. 507 (C.A.).
34 *Rawlinko* v. *Blair* (1998), 17 R.P.R. (3d) 91 (Ont. Gen. Div.); *Knoch Estate* v. *Jon Picken Ltd.* (1991), 18

broker.

4.2 Buyer Agency

The paradigm agency situation is one in which one party (say, the seller) appoints an agent to represent its interests in a transaction and the other party (say, the buyer) appoints another agent to represent its interests, with each party remunerating only their respective agent. This situation, though not unknown in the industry, was, for many decades, not common. Most often it was the seller's broker (or another broker deriving authority through the seller's broker under an MLS arrangement - that is, a co-operating agent or sub-agent) who also dealt with the purchaser. However, the last decade has witnessed a shift towards the agency paradigm in the industry; but often the paradigm is still not fully achieved since buyers' brokers often look to sellers, or sellers' brokers, for their remuneration.

Nevertheless, the growth in buyer agency is a positive one that addresses the criticisms levelled at brokers dealing with buyers:[35]

> It has been said that the position of the real estate agents in showing properties to prospective purchasers is a difficult one because they are, in fact, the agents of the vendor. To say that is "difficult" would be an understatement. The entire process is almost insidious in the way that it operates; in no other area of commercial transaction is the consumer so badly served because there is no one representing his interest. There is a clear conflict of interest the minute a realtor acts as a selling agent and all of the plain language contracts, exculpatory clauses, assumptions, waivers or restrictions on liability will not reduce the fiduciary relationship that exists between the real estate agent and potential purchasers when there is reliance placed upon that realtor. The purchasers go to an agent with their specific requirements and the agent proceeds to search for a house to meet those specifications. In the process, a level of trust develops to the point where the purchasers believe they have an advocate on their side. They allow the realtor to draw up the offer and rely on her to ensure that all of their concerns are covered in the agreement. They do not perceive themselves in a situation where they have to check the accuracy of the realtor's representations because they consider her to be their agent looking out for their interests. That system works provided no problems occur. If they do, the realtor backs away, relies on the contract and attempts to minimize any agency relationship with the purchasers because the realtor says she was always acting for the vendor. It was clear to me that Ms. Walls would have said anything to make this sale. As the realtor, she assumed a professional advisory role with the purchasers, "her clients" as she called them; they relied upon her.

This change in practice within the industry poses no problems in and of itself; but it does present two potential pitfalls for the unwary, and it raises a point to ponder.

4.2.1 *Source of remuneration*

The first potential pitfall is posed by the practice of sellers being responsible for the commission of both their own brokers and the buyers' brokers. This practice conflicts with the basic agency principle that agents cannot seek or receive remuneration from anyone other than their clients without the latter's fully informed consent. Thus, where buyers' brokers look to sellers (or their brokers) for remuneration they must ensure that they have their buyer-clients' fully informed consent to pursue this course of action. Such consent as a general rule should be forthcoming since their clients are relieved of the burden of directly remunerating their brokers. Moreover, as noted above, case law now suggests that the mere fact that it is the seller who pays a broker's

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R.P.R. (2d) 250 (Ont. C.A.); *Alwest Properties Ltd.* v. *Roppelt*, [1998] A.J. No. 1401 (Q.B.).

[35] *MacDonald* v. *Gerristen*, [1994] A.J. No. 468 (Q.B.). And see *Wypych* v. *McDowell* (1991), 11 R.P.R. (2d) 89 (Ont. Dist. Ct.).

commission does not in itself make the broker the seller's agent.[36]

Indeed, it may now be possible to argue that there is a custom in the industry, well known to the public, that in the normal course of business, sellers are responsible for commissions unless a contrary agreement is reached between buyers and their brokers. After all, it is patently unreasonable for buyers to expect their brokers to represent them totally "free of charge."

4.2.2 *Competing buyers*

The second potential pitfall arises where a buyer's broker has two or more buyers as clients who become competitors for the same property – a situation which may be encountered with greater frequency with the growth in buyer agencies.

This situation presents a problem similar to, though not identical with that encountered with dual agency. The problem in both situations flows from the basic fiduciary principle [discussed above], that brokers cannot let another's interests come into conflict with their clients' interests without the latter's fully informed. While buyers' brokers in these circumstances are not dual agents (i.e. do not represent both seller and buyer in a transaction), they nevertheless represent two or more buyer-clients who are in direct competition with each other for the same property. The propriety of buyers' brokers so acting, to the best of my knowledge, has yet to be commented on by the courts; although the courts have sanctioned brokers simultaneously representing two independent sellers of abutting properties of similar descriptions.[37]

However, the two situations are not analogous:

- *Concurrent representation of two or more sellers*: In such a situation it is in the broker's interests to serve loyally each of the sellers since the broker stands to earn a commission on each sale. Moreover, brokers' and sellers' interests coincide – they are both seeking the highest possible price for the properties - the higher the price, the higher the return for both seller and broker.
- *Concurrent representation of two or more buyers*: The same cannot be said where a broker concurrently represents two or more buyers interested in the same property. Here the potential for conflict of interest is acute - only one of the competing buyers will be able to acquire the property. It is highly unlikely that the buyers will both have available the same financial resources and it would be in the broker's interest to favour the buyer prepared to pay the highest price since the higher the price paid for the property, the higher the broker's commission. Indeed, it would be in a broker's interest to provoke a bidding war between the purchasers.[38] In either event, of course there would be a breach of the broker's obligation to negotiate the lowest possible price for the principal.

It remains to be seen how the courts will dispose of this issue when they are confronted with it. Nevertheless, it would be prudent for brokers only to act as agents for competing buyer-clients if they have the fully informed consent of their clients to pursue this course of action.

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[36] *MacCauley* v. *Leclair*, [1998] O.J. No. 1918 (Gen. Div.).

[37] *Kelly v. Cooper*, [1993] A.C. 205 (P.C.).

[38] There is a decision that suggests that a seller's agent should not "conduct a sort of auction" where there are more two or more buyers interested in the seller's property: see *Selmax Realty Inc.* v. *Peter Marchese Homes Ltd.*, [1995] O.J. No. 1035 (Gen. Div.). Little attention was paid to what was in the seller's best interests in this case, the court focussing more on the interests of the purchaser who made the first offer.

4.2.3 *Remuneration by commission*

The point for reflection raised by the development of buyer agency is this: to the extent that buyers' brokers remuneration, whether paid directly by the client or by the seller's broker, is represented as a percentage of, and therefore linked to, the sale/purchase price of a property, there is an incentive, no doubt resisted by most industry members, not to get the best possible, that is the lowest, price for the client (which, after all, is not necessarily the highest price the client has declared it is prepared to pay for a property), as this translates into a smaller commission for the broker. Consequently, the method of determining the remuneration of brokers in buyer agencies may need to be re-visited.

(While on the matter of remuneration by commission, it should be noted in passing, that it has also been suggested that it could be tempting for a seller's broker to undervalue a client's property as it would lead to a quick and certain sale and, consequently, a commission for the broker.[39] Indeed, the industry practice of remuneration by commission, a practice through which only two brokers (the seller's and the buyer's brokers) and their firms stand to receive any remuneration from a transaction, makes for a highly competitive environment in which less successful members may well be tempted to overlook the rules of the game - a "game" in which, essentially, the winner takes all. To some, therefore, the ends may well be seen as justifying the means - this is particularly true with dual agency.)

4.3 Dual Agency

It is evident from the case law that dual agency is a continuing concern for the industry. This form of agency representation arises when brokers or brokerage firms are found to be representing as clients both sellers and buyers in the same transactions.

As with agency relationships in general, the courts will impose a dual agency relationship where such relationship is warranted by the facts of a particular case. Thus, the existence of a dual agency relationship is not contingent on:

- the existence of an intention in brokers or their clients to establish such a relationship;
- knowledge in brokers or their clients of the existence of such a relationship; nor
- brokers being remunerated by both parties to transactions.[40]

Indeed, as is shown below, dual agency is inherent in a number of situations common in the industry.

However, there have been some positive developments in this field that may be helpful in reducing litigation of the issue. Moreover, it must be kept in mind that dual agency is, of course, not prohibited by the law; rather it is permitted but held in suspicion and severely regulated.

In the ensuing discussion of dual agency regard is had to:

- the problems inherent in this form of agency;
- the situations in which dual agency arises;
- whether fiduciary obligations are inherent in all agency relationships; and
- the means by which brokers and brokerage firms may seek insulate themselves against

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39 *Cox* v. *Martin*, [1997] B.C.J. No. 1690 (S.C.).

40 *Abdullah* v. *Bro*, [2000] O.J. No. 4165 (S.C.). See also *Raso* v. *Dionigi* (1993), 12 O.R. (3d) 580 (C.A.).

the accusation that they are in breach of their fiduciary obligations.

4.3.1 *The problem with dual agency*

Although dual agency is not unique to the industry, it raises a significant problem peculiar to it. The cause of that problem is simple - brokers, unlike some other categories of professional agents, represent parties whose interests are invariably diametrically opposed in the negotiation of transactions in which few, if any, terms and conditions (from the amount of the deposit and price to date of possession) are pre-determined and unalterable. Sellers look to their brokers to obtain the highest possible price and the terms which best accommodate their interests and needs; whereas buyers look to their brokers to negotiate the lowest possible price and the terms which best accommodate their interests and needs. Neither sellers nor buyers look to brokers merely to mediate what the brokers personally believe to be a "fair" or acceptable deal between them. Consequently, if brokers act as dual agents, absent compliance with their fiduciary duty of disclosure [discussed below in section 4.3.4], they permit a conflict of interest to arise between the interests of sellers and those of buyers.

Moreover, embedded in the fiduciary nature of brokers' relationships with clients are the obligations:

- always to act in the best interests of clients;
- of undivided loyalty to clients; and
- of obedience, always to follow clients' instructions provided they are legal.[41]

It is evident from these duties, owed to both clients in dual agency relationships, that brokers are in, what can be described as, a "Catch-22" situation. It is an untenable situation for, as observed in one case,[42] brokers cannot simultaneously fulfill these duties for competing parties. They cannot both act as dual agents and be the loyal, obedient and trusted advisor of both clients, providing the level of professional and confidential service that each would be entitled to expect if the broker were the agent solely for one or the other.

Indeed, brokers in dual agency relationships are, essentially, akin to "middlemen" (or "brokers" in the narrow sense of the term [noted above in section 2: Terminology]. They have three basic options, all of which demand of them neutrality, impartiality and objectivity:

- they may simply bring sellers and buyers together to negotiate their own deal, and act merely as conduits for information and notices that each party wishes to be conveyed to the other, but otherwise preserving the confidentiality of all other information (except that they are required to disclose by law) and playing no other significant role in the transaction;
- they may purport to act as agents for both sellers and buyers on the understanding that certain information concerning sellers and buyers will remain confidential, but all other information received from or concerning a party or the property will be fully disclosed to the other; or
- brokers might purport to act as agents for both sellers and buyers on the understanding that all advice provided, and information received by the broker will be fully disclosed to the other party – or, as one dual agency acknowledgement form states:

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[41] It has been stated that if the client's instructions are unlawful, a broker cannot merely ignore those instructions; rather the broker should terminate the agency relationship: see *Glasner* v. *Royal LePage Real Estate Services Ltd.* (1993), 28 R.P.R. (2d) 72 (B.C.S.C.).

[42] *Warberg* v. *McFadzean* (unreported decision of Alta. Q.B. No. 9608-00465 (April 2, 2001)). This decision is also discussed in REEOIC, *Risk* (2002, No. 15:2, pp. 4-5) and AREIX, *Newsletter* (February, 2002, No. 15).

> When representing both [seller and buyer] the seller's agent will have duties of good faith, obedience, honesty, competence, full disclosure and accountability to both of you and a prospective buyer(s).
>
> (It should be noted that this statement, in so far as it requires brokers to be obedient to both seller and buyer, is asking brokers to do the impossible.)

Of the foregoing options, the first is to be preferred if both clients are to start their negotiations on an equal footing. The reason for this is that a broker, or brokerage firm [as discussed immediately below], who becomes a dual agent invariably starts as the sole representative of either the seller or the buyer who will usually have disclosed confidential information to the broker. The broker is then presented with the opportunity to also represent the other party (and, of course, to earn a full commission). At this point, the fully informed consent of both clients must be obtained and they must be advised of the role the broker elects to play as dual agent. Thus,

- If the broker elects the first option, the confidential information obtained from the initial client will remain confidential, as must all information received from both clients unless they instruct the broker otherwise.
- If the broker elects the second or third option, the broker will then have to disclose to the second client the confidential information received from the initial client (other than that expressly excluded in the second option). However, the second client, having been put on notice that all information conveyed to the broker must also be conveyed to the other party, may wisely refrain from disclosing any confidential information. The second client, thus, will enter the dual agency relationship in a more advantageous position armed with information concerning the first.

Moreover, brokers must be aware that in the latter two options, and whether or not they in fact communicate information to the parties, each party nevertheless is deemed to have knowledge of all information received by the broker from the other on the strength of the principle that notice to an agent is deemed to be notice to the client. Brokers, thus, expose themselves to liability for non-disclosure if they fail to convey to each client the information received from or concerning the other.[43]

However, regardless of how brokers see themselves as acting in a particular dual agency relationship, to avoid liability for breach of their fiduciary obligations, they must obtain the fully informed consent of both parties to that relationship; and, then act strictly in accordance with the role they have elected to play showing neither party favour.

4.3.2 *Dual agency situations*

The situations in which dual agency is encountered are not new. Dual agency arises in the following situations:

Single Broker, Dual Agency

Dual agency relationships involving individual brokers may arise in two circumstances:

- Concurrent representation of both seller and buyer in a transaction; or
- Sequential representation of, say, seller then buyer in two transactions.

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[43] *Koczulab* v. *Madill*, [1993] O.J. No. 1719 (Gen. Div.); *Winland* v. *Kolakis*, [1998] A.J. No. 236 (Q.B.); *Abdallah* v. *Bro*, [2000] O.J. No. 4165 (S.C.).

Concurrent representation

Dual agency through the concurrent representation of both seller and buyer in the same transaction is the most egregious form of dual agency encountered in the cases.[44]

Sequential representation

Dual agency through the sequential representation of parties, perhaps, is not as common but may nevertheless be encountered on the facts of a particular case. The key issue in determining the existence of dual agency in these cases, it is suggested, is the nature of the relationship that existed between the broker and a party in the first transaction. Thus, for example:

- Where a broker acts as listing agent for seller A on a sale to buyer B, and then becomes the listing agent on the sale of buyer B's current property, the broker will not be deemed, without more, to be in a dual agency relationship with seller A and buyer B.[45]
- But, where a broker acts as listing agent for seller A's property and then seller A becomes interested in buying C's property that is also listed with the broker, for the purposes of this second transaction it is highly unlikely that the broker can shed the role of A's agent and treat A as a customer rather than as a client. The initial agency relationship established between the broker and A is likely to be transported into the subsequent transaction' with the result that the broker would be in a concurrent dual agency relationship by having A (now a buyer) and C (the seller) as clients.

However, given that the existence of both agency and dual agency relationships is "fact sensitive," it is difficult to provide clear and comprehensive guidelines that will permit brokers to determine when, in instances of sequential representation, a dual agency will arise. Thus, in case of doubt, it is advisable for brokers to obtain the parties' consent to a dual agency relationship to minimize the risk of subsequent disputes.

"In-firm" transactions

It must be recalled that when sellers or buyers enter into express or implied agency agreements with brokers, the agreements, in law, are not with the individual brokers but with the brokerage firms who employ them. The agency agreement effectively makes the entire sales staff of the brokerage firm agents of the clients. This is so, even though none in the firm but the individual seller's or buyer's broker, as the case may be, and the firm itself, receives any remuneration on the successful completion of a transaction.

The major difficulty that is caused in these circumstances arises from the presumption that professionals who work for the same firm share each other's confidences with the result that knowledge of confidential matters is therefore imputed to other members of the firm. A presumption that may, nevertheless, be rebutted [as is discussed in section 4.3.3].

In light of the foregoing, a dual agency will be presumed to arise where sellers and buyers are represented by:

- different brokers working out of the same branch of a brokerage firm ("*individual representation, same branch*");[46] or

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[44] *Koczulab* v. *Madill*, [1993] O.J. No. 1719 (Gen. Div.); *Howe* v. *635362 Ontario Ltd.*, [1997] O.J. No. 370 (Gen. Div.); *Houweling* v. *Imperial Equestrian Centre Ltd.*, [2001] B.C.J. No. 2424 (S.C.); *Abdallah* v. *Bro*, [2000] O.J. No. 4165 (S.C.); *Winland* v. *Kolakis*, [1998] A.J. No. 236 (Q.B.); *Siculiana Holdings Ltd.* v. *J. Gioia Holdings Ltd.*, [19940 O.J. No. 2571 (Gen. Div.); *Toll* v. *Marjanovic*, [2002] O.J. No. 70 (S.C.).

[45] *Sowiak* v. *Cartright*, [2000] A.J. No. 1669 (Prov. Ct.).

[46] *489212 Ontario Ltd.* v. *Participative Dynamics Inc.* (1994), 38 R.P.R. (2d) 32 (Ont. Gen. Div.) aff'd [1997]

- different brokers working out of different branches of a brokerage firm (*"individual representation, different branch"*);
- different employees (say a broker and an appraiser or building inspector) of a multi-service firm (*"individual representation, different service"*).

M.L.S. transactions

These are transactions in which sellers have authorized the listing broker (i.e. brokerage firm) to utilize the services of co-operating brokerage firms, members of the MLS, in marketing their properties. Traditionally, the terms of the MLS commonly make these co-operating firms the sub-agents of the seller and, as a consequence, all of the sales staff of these firms will also be viewed as the sub-agents of the seller. Thus, where the buyer is represented by a broker employed by a co-operating firm, a dual agency will again be created since that firm and its employee are also legally the agents of the seller.

The traditional understanding of the role and representative capacity of the selling broker has been questioned in a number of cases,[47] but it has also been subscribed to in others.[48] Despite this apparent conflict, there have been other developments that have helped clarify the role and the nature of the obligations owed by selling brokers under MLS arrangements.

4.3.3 *Are all dual agency relationships fiduciary in nature?*

The short answer to this question is, no. However, it must be recalled that there is a presumption that brokers in all agency relationships are fiduciaries; thus, they are obliged to establish, on the facts of a particular case, that they were not acting as fiduciaries.

The presumption has been successfully rebutted in a number of cases by co-operating brokers under MLS arrangements; also there is case law that suggests that it may be rebutted in the "in-firm" dual agency situations through the construction of what are termed "Chinese Walls" [discussed below].

Selling Brokers under MLS Arrangements

Recent case law has helped to clarify the role and obligations of the selling broker when acting as a co-operating broker under a MLS agreement.[49] As noted, such brokers have traditionally been viewed as dual agents owing fiduciary obligations to each of the clients (the seller and the buyer). While on the balance recent cases still support the view that a co-operating broker in these circumstances remains a sub-agent of the listing broker, they hold that if the co-operating broker is the buyer's agent, the co-operating broker does not necessarily owe fiduciary obligations to the seller. That is, the cases recognize that there may be a dual agency in *form* but, most importantly, not in *substance*.

However, to determine whether such is the situation in a particular case, it is necessary to

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O.J. No. 3856 (C.A.); *Knoch Estate* v. *Jon Picken Ltd.* (1991), 18 R.P.R. (2d) 250 (Ont. C.A.), aff'g 5 R.P.R. (2d) 207.

47 *Knoch Estate* v. *Jon Picken Ltd.* (1991), 18 R.P.R. (2d) 250 (Ont. C.A.), aff'g 5 R.P.R. (2d) 207, *Pai* v. *Freimuts* (1993), 28 R.P.R. (2d) 115 (Ont. Gen. Div.); *Wypych* v. *McDowell* (1991), 11 R.P.R. (2d) 89 (Ont. Dist. Ct.).

48 *Barrett* v. *Reynolds*, [1997] N.S.J. No. 494 (S.C.); *Knoch Estate* v. *Jon Picken Ltd.* (1991), 18 R.P.R. (2d) 250 (Ont. C.A.), aff'g 5 R.P.R. (2d) 207.

49 *Knoch Estate* v. *Jon Picken Ltd.* (1991), 18 R.P.R. (2d) 250 (Ont. C.A.), aff'g 5 R.P.R. (2d) 207, *Pai* v. *Freimuts* (1993), 28 R.P.R. (2d) 115 (Ont. Gen. Div.); *Wypych* v. *McDowell* (1991), 11 R.P.R. (2d) 89 (Ont. Dist. Ct.); *Barrett* v. *Reynolds*, [1997] N.S.J. No. 494 (S.C.).

examine the relationship that exists in fact between the seller and listing broker, on the one hand, and the co-operating broker, on the other, to determine whether the indicia of a fiduciary relationship are present. If the relationship is limited in scope (the co-operating broker has no access to confidential information affecting the seller, must deal only with the listing broker and the like), and there is no opportunity for the co-operating broker to exercise some discretionary power over the seller, the co-operating broker owes the seller no fiduciary obligations though a sub-agent of the seller in the formal sense. This conclusion will not be effected even if the co-operating broker remains the seller's sub-agent for administrative purposes, such as presenting offers to purchase to, receiving notices for, and making representations that may bind, the seller.

To conclude on this point, it is worth reiterating that, since brokers acting as agents are presumed to be fiduciaries, co-operating brokers carry the onus of establishing that their agency relationship in a particular case was not of a fiduciary nature. To facilitate the discharge of this onus it would be advisable for MLS arrangements to have clear policies and guidelines with respect to the roles of listing (sellers') brokers and co-operating (buyers') brokers.

"Chinese Walls"

The term "Chinese Wall" was coined to describe the arrangements implemented by multi-service financial institutions in the United States to prevent the flow of information between departments that represented different clients with competing interests. The wall comprises policies, procedures and enforcement mechanisms designed to ensure that employees working in different departments do not communicate with, or to, their colleagues in other departments any information which, if disclosed, could be prejudicial to their clients' interests.

The use of Chinese Walls by real estate brokerage firms has not been considered by the courts in Canada; however, their use in other contexts (legal and accountancy firms) has been considered.[50] A central issue confronting the courts in these cases is the presumption that professionals, who work for the same firm, albeit in different branches, share each others' confidences (with the result that knowledge of confidential matters is, therefore, imputed to other members of the firm). The question the courts had to consider was: could this presumption be rebutted through use of Chinese Walls? The cases suggest suggested that, in some circumstances, this is possible.

Consequently, it may be reasonable to assume that the courts would also countenance the use of these mechanisms in other professional contexts, particularly those involving concurrent representation (as in the "in-firm" and MLS transactions outlined above).

Erecting a "Chinese Wall"

What then are the factors that are relevant in determining the acceptability and effectiveness of a Chinese Wall?

First, it would appear that each broker would have to give a solemn undertaking not to disclose any confidential information concerning the client to the broker representing the other party. That is, "a cone of silence," to use a term coined by the Supreme Court of Canada,[51] would have to be imposed.

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[50] *MacDonald Estates* v. *Martin*, [1991] 3 S.C.R. 1235; *Drabinsky* v. *KPMG* (1998), 41 O.R. (3d) 565 (Gen. Div.) aff'd 10 C.B.R. (4th) 130 (Civ. Ct); *Prince Jefri Bolkiah* v. *KPMG*, [1999] 1 All E.R. 517 (H.L.).

[51] *MacDonald Estates* v. *Martin*, [1991] 3 S.C.R. 1235.

Second, a brokerage firm would have to put in place policies, procedures and enforcement mechanisms to ensure that firm members representing clients with conflicting interests do not communicate with or to their colleagues (directly or indirectly, advertently or inadvertently), any information which, if disclosed, could be prejudicial to the interests of the clients. Moreover, it must be kept in mind that the probable effectiveness of any particular Chinese Wall will turn on the court's assessment of the effectiveness of the screening procedures adopted in light of the facts and circumstances of each particular case.

Elements of a "Chinese Wall"

With this in mind, what follows is a list of some of the factors identified in the literature as relevant in determining whether a Wall may effectively be erected in a firm. These factors are:

- the size of the firm (the smaller the brokerage the more difficult it may be to build an effective wall);
- the extent of its departmentalization (are brokers representing buyers and sellers in distinct departments);
- the number of branch offices (are the brokers representing the buyer and the seller based in different branches);
- physical separation of brokers in an office (what are the chances that confidential conversations will be, advertently or inadvertently, overheard by the Aother side@);
- internal procedures for the handling of files, data and confidential information (is access restricted?; if so, how, to whom, to what degree?);
- support personnel (do brokers share the services of the same support personnel);
- opportunities for personal contact (are the brokers likely to come into contact (socially or professionally?) other than in relation to the transaction at issue creating the risk that they may inappropriately "talk shop");
- sharing of commissions by the brokers (will the brokers benefit from each others activities – an element that raises a particularly difficult issue in light of the fact that it is the seller who tends to pay the entire commission).

Additional Considerations

In addition, it is suggested that for a Chinese Wall to be acceptable and effective the following conditions must also be met:

- *Timely Erection*: Chinese Walls have to be erected in a timely manner, that is:
  - before the creation of the risk that confidential information may be inadvertently disclosed; and
  - before a dual agency situation arising.
- *Education*: Firms must educate their employees concerning the Wall:
  - its elements;
  - the reasons for its presence; and
  - the consequences of its breach.
- *Full Disclosure*: Brokerage firms and brokers would have to disclose fully to clients:
  - the existence of the Wall;
  - the elements of the Wall;
  - the reason for its creation (to ensure that each client will still benefit from "arm's length" representation and the preservation of each broker's fiduciary obligations of obedience, loyalty and confidentiality);
  - the risks that it entails (that the Wall is not an impermeable barrier to the flow of

information and may be breached, intentionally or unintentionally); and
    - the names of the employees with whom the client can safely communicate.
- *Client Consent*: After full and complete disclosure has been made of all facts that might influence a client's decision as to whether to accept such representation, each client's consent to the arrangement must be obtained.
- *Independent Advice*: Perhaps clients should also be given the opportunity, if not advised, to obtain independent advice as to the implications of dual agency representation behind a Chinese Wall.

4.3.4 *Disclosure of dual agency*

The duty of brokers to disclose dual agency relationships to their clients is but one aspect of their fiduciary duty of disclosure [discussed above in section 3.5]. Disclosure of the dual agency must be made to both clients, and the fully informed consent of both must be obtained.

Thus, the following observations by the court in one case, concerning the rationale for disclosure of dual agencies, must be qualified:[52]

> [A] vendors' agent may deal with purchasers directly without the agent becoming the agent of the purchasers, or as a dual agent .... The purpose for the dual agency provisions are to protect the vendors. In the normal course the agent obtains a listing agreement from the vendors. The Code makes it the duty of the agent to obtain an acknowledgement from the vendors when the agent proposes to act on behalf of the purchasers. The reasoning appears obvious .... [P]urchasers are usually aware the agent is already acting for the vendors. If the agent proposes to act for the purchasers then ... [there is] imposed upon the agent the requirement that the vendors be given notice of and consent to their agent acting for the purchasers as well.

It is undeniable, as observed in this passage, that disclosure and consent are required to protect the interests of brokers' existing clients (be they seller or buyer) where brokers also seek to represent the other parties to transactions. However, a broker's obligations of disclosure are not exhausted once disclosure is made to the initial client. Disclosure to, and consent of the "new client" are also required. Both clients have to be fully aware not only of the existence of a dual agency, but also of the full implications of representation by a dual agent.

Consequently, merely asking one or other client to sign a dual agency acknowledgement, even if accompanied by explanatory documentation, may not suffice if the acknowledgement and documentation does not inform the clients of:[53]

- the full implications of that relationship (including, in a "single broker, dual agency," that the broker stands to receive a full commission); and,
- perhaps, the implications and benefits of sole representation and the parties' entitlement there to.

The consent of both clients to a dual agency relationship with a broker must be a fully informed consent because clients have the right to make a fully informed choice as to the nature of the representation they wish to receive.

Finally, the disclosure must be timely and, preferably, be made before either client has disclosed confidential information to the broker. If brokers have been entrusted with confidential

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52 *Sowiak* v. *Cartwright*, [2000] A.J. No. 1669 (Prov. Ct.).

53 *Columbus* v. *Mehner*, decision of the Alaska Supreme Court. This case, discussed in (202) 15:2 *Risk* pp. 4-5, provides a good discussion of the scope of a dual agents obligations of disclosure.

information before the possibility of a dual agency arose then, depending on the role the broker elects to play as dual agent [discussed above in section 4.3.1], they may be obliged to advise the clients who have entrusted them with the information that it will have to be disclosed to the brokers' other clients.

5. DUTY AND STANDARD OF CARE

It is indisputable that brokers owe both clients and customers a *duty of care* to conduct themselves in accordance with the *standard of care* that is expected of industry members in dealing with clients and customers. Failure to fulfil this duty exposes brokers to liability for professional negligence.

5.1 Differential Duties of Care

The duty owed by brokers to clients is broader than that owed to customers.

5.1.1 *Duty to clients*

To clients the duty of care extends to everything brokers do, or should do, in the performance of their mandates. As stated in one recent decision:[54]

> [T]he real estate agent is often the only professional advisor on ... [a] purchase and sale. Typically lawyers are not retained until ... the agreement has been signed by both sides. Because agents take on this advisory role, they must be held accountable for failing to protect their clients against the special risks of a transaction.

While this comment was directed at Ontario practice, it is generally applicable in all provinces.

5.1.2 *Duty to customers*

The duty of care owed customers by brokers is more limited since brokers are not, or should not be, the professional advisors of customers – to so act would place them in a dual agency relationship. Rather, brokers essentially owe customers the obligations:

- of honesty;
- of reasonable care and skill in ensuring the accuracy of information conveyed to customers; and
- of reasonable care and skill in performing any particular functions that they have expressly or impliedly undertaken to perform on behalf of a customer (e.g. to convey information or an offer from customer to client, amend a form to accord to customer's intentions, etc.).

Of these obligations to customers, that relating to disclosure of information is dealt separately below [in section 6.2].

5.2 The Standard of Care

To determine whether brokers have discharged their duty of care it is necessary to measure their conduct against a standard, the standard of care, expected of them. That such a standard exists is

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[54] *Wong* v. *407527 Ontario Ltd.*, [1999] O.J. No. 3377 (C.A.).

indisputable. Thus, it should come as no surprise that, the argument advanced on behalf of a broker, to the effect that "there was absolutely no evidence of a standard of care of a real estate agent in British Columbia and, accordingly, there can be no finding of negligence,"[55] was not accepted by the court.

However, the cases do suggest that not all brokers are aware:

- of the standard by which the propriety of their conduct is measured;
- that it is not always a simple task to ascertain whether a broker has met the appropriate standard in a given situation; or
- the range of matters to which their duty, and standard, of care applies.

In this part a review is provided of the general obligation of industry members to exercise reasonable care and skill in their dealings with clients and customers. Separate regard is had to brokers' duty of disclosure to clients and customers of defects in the various attributes of a property [see section 6].

5.2.1 *What is the standard of care*

It is generally accepted that the standard of care expected of brokers is to exercise such skill, care and diligence in the performance of their functions as is usual and necessary for the proper conduct of the business in which they are employed or is reasonably necessary for the proper performance of the duties undertaken by them.[56] The standard, therefore, is:[57]

> that of the reasonably careful person in the circumstances of the defendant [industry member] .... [The] standard of conduct is determined by taking into account both the practical realities of what ordinary [industry members] do and what judges believe they ought to do. It is not, however, a standard of perfection.

In general, therefore, the standard of care is determined through regard to how ordinary and prudent members of the industry or, as observed in one case,[58] how "knowledgeable and well trained" brokers, would conduct themselves in the same or similar circumstances to those in which an industry member's conduct has been put in question. That it is an industry-based standard is evident from the cases where, for example, the courts have stated that brokers are not building envelope specialists,[59] or surveyors,[60] and should not be expected to conform to their standards.

Objective standard

The standard is an objective standard and, with one exception, is applicable to all brokers. Thus, for example, no allowance is made for:

- beginners in the industry;[61]
- lack of experience in some aspect of the industry or with a particular class of transaction;
- brokers who act gratuitously in transactions;[62]

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55 *Cox* v. *Martin*, [1997] B.C.J. No. 1690 (S.C.).
56 See generally *Barker* v. *100 Mile Realty Ltd.*, [2000] B.C.J. No. 417 (S.C.); *Abbey Blinds Inc.* v. *Mikesh*, [1996] B.C.J. No. 920 (S.C.).
57 Osborne, P. *The Law of Torts* (2000) pp. 26, 27.
58 *Vokey* v. *Edwards*, [1999] O.J. No. 1706 (S.C.).
59 *Fee* v. *Currie*, [1999] B.C.J. No. 3097 (Prov. Ct.).
60 *Colbourne* v. *Comerford*, [2001] N.J. No. 334 (Prov. Ct.).
61 *Johnstone* v. *Dame*, [1995] B.C.J. No. 2637 (S.C.).
62 *Spencer* v. *Invidiata*, [1994] O.J. No. 2189 (Gen. Div.).

- the fact that brokers have done their personal best in the circumstances; or
- the fact that brokers are unaware that their conduct deviates from the industry norm.

The exception is, if brokers possess, or hold themselves out as possessing, special expertise or experience, the standard is determined through reference to a smaller reference group. It is no longer a general industry standard; rather the reference group becomes how prudent brokers similarly skilled would have conducted their affairs.[63]

Errors of judgement

However, as noted above, the standard is not one that demands perfection from industry members.[64] Thus, it has been observed "brokers are not omniscient;"[65] nor do they need to be prescient.[66] Moreover, it is recognized that real estate appraisal is an inexact science.[67] Errors of judgement and mistakes are allowed provided that they are errors and mistakes that the reasonable and prudent industry member would make. Nevertheless, the reality is that while such errors and mistakes will not result in the imposition of liability they will often result in litigation and thus have attendant "costs" (in terms of time, energy, stress, reputation, legal fees, etc.) for industry members involved.

5.2.2 *Ascertaining compliance with standard*

Despite the fact that the standard of care against which the conduct of brokers is measured is based on a standard derived by ascertaining how reasonable and prudent members of the industry would have conducted themselves, expert evidence is not always required to determine this matter. Thus, for example, the courts have observed that:

- where a broker's conduct is particularly egregious expert evidence is not required;[68] and
- in certain cases, it is reasonable for a court to infer that reasonable industry members would have conducted themselves differently in the circumstances of the case.[69]

Expert testimony

Nevertheless, recent cases suggest greater use is being made of industry experts in seeking to establish how reasonable and prudent brokers would have acted in particular circumstances.[70] Indeed, in some instances, courts have acknowledged that such evidence is necessary to enable them to determine what are the industry norms.[71] Thus, it has been stated that:[72]

> … unless conduct is particularly egregious, the court likely requires expert evidence of the usual or customary standard in the real estate industry regarding:
> a) the kind of information that must be checked or verified by realtors, where it has not been demonstrated

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63 See e.g., *Harela* v. *Powell*, [1998] O.J. No. 2989 (Gen. Div.).
64 See e.g., *669283 Ontario Ltd.* v. *Reilly*, [1996] O.J. No. 273 (Gen. Div.).
65 *Colbourne* v. *Comerford*, [2001] N.J. No. 334 (Prov. Ct.).
66 *West Coast Engineering Ltd.* v. *Homelife Benchmark Realty Corp.*, [1994] B.C.J. No. 1935 (S.C.).
67 *Alwest Properties Ltd.* v. *Roppelt*, [1998] A.J. No. 1401 (Q.B.); *Phelan* v. *Realty World-Empire Ltd.*, [1994] B.C.J. No. 752 (S.C.).
68 *Walls* v. *Ross*, [2001] B.C.J. No. 1641 (Prov. Ct.).
69 *Rankin* v. *Menzies*, [2002] O.J. No. 51 (S.C.).
70 *Walls* v. *Ross*, [2001] B.C.J. No. 1641 (Prov. Ct.); *Nicholson* v. *Forster*, [1994] S.J. No. 655 (Q.B.); *669283 Ontario Ltd.* v. *Reilly*, [1996] O.J. No. 273 (Gen. Div.); *Fee* v. *Currie*, [1999] B.C.J. No. 3097 (Prov. Ct.); *Anderson* v. *Peters*, [2000] M.J. No. 563 (Q.B.).
71 *Cheung* v. *Sutton Group Broadway Realty Ltd.*, [1994] B.C.J. No. 1599 (Prov. Ct.); *Walls* v. *Ross*, [2001] B.C.J. No. 1641 (Prov. Ct.).
72 *Walls* v. *Ross*, [2001] B.C.J. No. 1641 (Prov. Ct.).

that the realtor had cause to doubt the information;
b) a duty to take positive steps to confirm the nature, identity and extent of the property they advertise, including any duty to recommend a purchaser secure a plot plan or survey; and
c) a duty to recommend that the purchaser secure an inspection regarding the soundness of premises, including any structural defects.

However, it must be noted that expert evidence will not necessarily be determinative of the standard to be expected of the reasonable and prudent industry member because:

- experts sometimes counsel perfection,[73] a standard few, if any, in any walk of life measure up to; or
- the industry practice attested to by the expert may itself be found to be deficient as, for example, where it was held that an established industry practice of communicating only written, not oral, offers to sellers was unreasonable.[74]

Industry By-laws, Rules, etc.

In addition to expert evidence, one finds in some cases reliance being place on industry by-laws, rules and codes of ethics in determining whether brokers have departed from industry norms in particular cases.[75] Such reliance is to be expected given that it is normal to infer that reasonable and prudent brokers would conduct themselves in conformity with these industry standards, and failure to do so suggests unacceptable conduct.

However, it must be borne in mind that mere compliance with such industry norms and standards may not, in it self, be sufficient. Thus, the existence of a statutory requirement to deliver to sellers all written offers, did not preclude the existence of a common law duty also to communicate to them all oral offers.[76] Similarly, it has been suggested that while the property condition disclosure requirements of industry governing bodies are of interest, they neither define nor exhaust a broker's duty of disclosure.[77]

The increased recourse to experts and industry by-laws, rules and codes of ethics is to be expected given the greater professionalization of, and the shift to self-regulation in, the industry.

5.2 Illustrations of Violations of the Standard

No attempt is here made to list all of the situations in which brokers have been held liable to their clients or customers for failure to live up to the standard of care expected of them; rather the list below is illustrative.

In addition reference is made to certain situations in which the courts have imposed direct, not just vicarious, liability on brokerage firms for the misconduct of brokers – a new development.

5.2.1 *By brokers*

The cases are replete with illustrations of what the courts consider reasonable and prudent

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73 See *669283 Ontario Ltd.* v. *Reilly*, [1996] O.J. No. 273 (Gen. Div.).
74 *Krasniuk* v. *Gabbs*, [2002] M.J. No. 13 (Q.B.).
75 See e.g. *Sowiak* v. *Cartwright*, [2000] A.J. No. 1669 (Prov. Ct.); *Spencer* v. *Invidiata*, [1994] O.J. No. 2189 (Gen. Div.); *1019216 Ontario Inc.* v. *Wolkowicz*, [2000] O.J. 3267 (S.C.); *Martin* v. *Mayo*, [1997] B.C.J. No. 1926 (S.C.).
76 *Krasniuk* v. *Gabbs*, [2002] M.J. No. 13 (Q.B.).
77 See e.g., *Pavenham Development Corp.* v. *Sladen*, [1997] B.C.J. No. 2103 (S.C.).

brokers would do. Thus, for example:

- Reasonable brokers are aware of the limits of their expertise:
  - in the drafting of documents;[78]
  - in particular classes of transaction;[79] and,
  - consequently, when it is appropriate for them
    - to personally seek advice; or[80]
    - to recommend that a client or customer seek legal advice[81] - although there appears to be no general duty to recommend that legal advice be sought.[82]

- In the preparation of contracts and other documents reasonable brokers ensure that:
  - any document or clause they draft is adequate to meet its purposes;[83]
  - the appropriate documents are delivered to the parties;[84]
  - contract terms are not inappropriately waived by a client[85] or customer;[86]
  - clients and customers are aware of the implications of documents presented to them for signature;[87]and
  - clients do not accept more than one binding offer at a time.[88]

- Reasonable brokers also have knowledge of such matters as:
  - the zoning of property where relevant to a transaction;[89]
  - local improvement levies (especially if aware improvements by municipalities);[90]
  - the GST implications for sellers of commercial property.[91]

- Reasonable brokers, moreover, do not fail:
  - to conduct a title search of a property for, as one court observed, "I do not understand how a seller's agent can reasonably discuss a house with prospective purchasers without doing a title search. Aside from ownership, what about encumbrances on the title?;"[92]

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78 *Wong* v. *407527 Ontario Ltd.*, [1996] O.J. No. 1030 (Gen. Div.) aff'd [1999] O.J. No. 3377 (C.A.).

79 *Pacifico Publico Management Ltd.* v. *Heer*, [1996] B.C.J. No. 467 (S.C.); *Samson* v. *Lockwood*, [1995] O.J. No. 3616 (Gen. Div.).

80 *Wong* v. *407527 Ontario Ltd.*, [1996] O.J. No. 1030 (Gen. Div.) aff'd [1999] O.J. No. 3377 (C.A.); *Pacifico Publico Management Ltd.* v. *Heer*, [1996] B.C.J. No. 467 (S.C.).

81 *Burchell* v. *Vincent*, [1994] N.S.J. No. 315 (S.C.); *Wong* v. *407527 Ontario Ltd.*, [1996] O.J. No. 1030 (Gen. Div.) aff'd [1999] O.J. No. 3377 (C.A.).

82 *Passmore Gates Development* v. *Chung*, [1996] O.J. No. 1932 (Gen. Div.).

83 *Vokey* v. *Edwards*, [1999] O.J. No. 1706 (S.C.); *Athwal* v. *Sidhu*, [2002] B.C.J. No. 1596 (S.C.); *Zeidler* v. *Henley & Assoc. Realty Ltd.*, [1993] B.C.J. No. 512 (S.C.); *Ragunath* v. *Krause*, [1993] O.J. No. 2117 (Gen. Div.).

84 *Kwok* v. *Griffiths*, [1996] B.C.J. No. 84 (S.C.); *Abdallah* v. *Bro*, [2000] O.J. No. 4165 (S.C.).

85 *Winsham Fabrik Canada Ltd.* v. *Re/Max All Stars Realty Inc.*, [2001] O.J. No. 1478 (S.C.).

86 *Kotowich* v. *Petursson*, [1994] M.J. No. 60 (Q.B.).

87 *Heffernan* v. *Black*, [1995] O.J. No. 1219 (Gen. Div.); *Burchell* v. *Vincent*, [1994] N.S.J. No. 315 (S.C.); *Zeidler* v. *Henley & Assoc. Realty Ltd.*, [1993] B.C.J. No. 512 (S.C.).

88 *Forgan* v. *Lovatt*, [2001] M.J. No. 495 (Q.B.).

89 *Redmond* v. *Densmore*, [1997] N. J. No. 190 (C.A.).

90 *Vokey* v. *Edwards*, [1999] O.J. No. 1706 (S.C.).

91 *Top Realty (GP) Ltd.* v. *388204 Alberta Ltd.*, [2000] A.J. No. 843 (Prov. Ct.); *Sainbury* v. *Nanaimo Realty Ltd*, [1993] B.C.J. No. 1032 (S.C.).

92 *De Sena* v. *Allure Homes Ltd.*, [2002] A.J. No. 752 (Q.B.) See also *MacDonald* v. *Gerristen*, [1994] A.J. No. 468 (Q.B.). This obligation, however, may be restricted to provinces that have a land titles system.

- to conduct a local taxation search;[93]
- to ascertain existence of property disclosure statements and deliver copies to clients;[94] and
- to follow instructions when provided.[95]

- Reasonable brokers do not simply rely on information:
  - supplied by the listing broker regarding important material attributes of property;[96]
  - supplied by the vendor if the information appears questionable or affects an important issue;[97]
  - for brokers are not mere conduits of information.[98]

- Reasonable brokers will verify the accuracy of information when:
  - it is to be used as part of the listing information to market a property;
  - it is usual and customary for brokers to check the information in question (here expert evidence may be required to determine what is usual and customary);
  - there is reasonable cause to doubt the accuracy of the information provided; and
  - they are, or should be, aware that the particular information is of importance in the transaction.[99]

- Finally, the reasonable broker leaves adequate instructions for office staff with respect to on-going transactions when absent from the office for a period of time.[100]

It is evident from a number of the illustrations that all brokers must possess a certain degree of specialized knowledge to meet the attributes that are ascribed to the reasonable and prudent industry member, even if the knowledge is only required to know when to recommend that a client or customer seek legal or other expert advice in a transaction.

5.2.2 *By brokerage firms*

A development in the case law, though not yet a "trend" given the few cases on the issue, concern claims against brokerage firms for failure to have in place policies and systems to minimize clients' and customers' exposure to sub-standard behaviour by the firm's employees. For example:

- in one case, a brokerage firm was found negligent for not providing appropriate supervision for its brokers and failing to have a policy requiring its brokers to insert waiver or disclaimer clauses in property marketing brochures;[101]

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93 *Anchor Fence Inc.* v. *Polaris Realty Inc.*, [1994] A.J. No. 482 (Q.B.).
94 *Vokey* v. *Edwards*, [1999] O.J. No. 1706 (S.C.); *Pavenham Development Corp.* v. *Sladen*, [1997] B.C.J. No. 2103 (S.C.).
95 *McDowell (c.o.b. Rural Realty and Consulting)* v. *Nykoliation*, [2000] M.J. No. 403 (Q.B.).
96 *Fletcher* v. *Hand*, [1994] A.J. No. 531 (Q.B.); *Winsham Fabrik Canada Ltd.* v. *Re/Max All Stars Realty Inc.*, [2001] O.J. No. 1478 (S.C.).
97 *789538 Ontario Ltd.* v. *Gambin Associates*, [1997] O.J. No. 4691 (Gen. Div.); *Johnstone* v. *Dame*, [1995] B.C.J. No. 2637 (S.C.).
98 *Brown* v. *Fritz*, [1993] B.C.J. No. 2182 (S.C.).
99 *Winsham Fabrik Canada Ltd.* v. *Re/Max All Stars Realty Inc.*, [2001] O.J. No. 1478 (S.C.).
100 *Scarponi* v. *Rotella*, [1995] O.J. No. 1333 (Gen. Div.).
101 *Samson* v. *Lockwood*, [1995] O.J. No. 3616 (Gen. Div.).

- in another case, a brokerage firm was held liable for not having in place a system for the orderly transfer of transaction files while its employees were on vacation, which system would act as a fail-safe mechanism to prevent wrongdoing by clients or customers.[102]

It is foreseeable that such direct liability of brokerage firms may be extended to include the absence of firm policies and practices designed to protect clients where its employees:

- function as dual agents;
- purchase clients' properties;
- sell to clients their properties;
- make a secret profit, etc.

The implication of such cases for brokerage firms is significant since the liability of the firm is direct and personal to the firm. It is the firm that is deemed guilty of misconduct, unlike the situation of vicarious liability where a firm is financially answerable for an employee's wrong-doing. Where firms are held personally (directly) liable, they have no right to indemnification from their employees for any damages the firms may have to pay - a right that exists where firms are held vicariously liable for the misconduct of employees.

Finally, on the issue of the liability of brokerage firms, the suggestion has been made that where a broker, as seller, uses the services of his or her brokerage firm to market his or her property and the broker is guilty of misconduct in dealing with the buyer, the firm may be held vicariously liable to the buyer for its employee's misconduct.[103] This is a novel, but a not an unexpected, twist, given that the broker in marketing the property is acting in a dual capacity, that is, as both seller and broker.

5.3 Avoiding Liability

5.3.1 *Exclusion clauses*

A number of cases have dealt with the question: may brokers invoke the protection of any *exclusion clause* that may be found in the agreement of purchase and sale entered into between seller and buyer. In the past the general approach was to deny brokers the protection of such clauses because of the doctrine of privity of contract – brokers not being party to the agreement could not take advantage of its terms.[104] Some recent cases, however, suggest that where the exclusion clause expressly mentions brokers they may be protected by it.[105]

However, the protection afforded by exclusion clauses is limited:

- it only extends to the seller's broker;[106]
- it only provides protection for certain misrepresentations made to the customer; and
- it is inoperative in cases of fraud by a broker.[107]

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102 *Scarponi* v. *Rotella*, [1995] O.J. No. 1333 (Gen. Div.).
103 *Belzil* v. *Bain*, [2001] A.J. No. 1350 (Q.B.).
104 *Brown* v. *Fritz*, [1993] B.C.J. No. 2182 (S.C.).
105 *478649 Ontario Ltd. (c.o.b. Green Acres Estate)* v. *Corcoran*, [1996] O.J. No. 1779 (Gen. Div.); *Anchor Fence Inc.* v. *Polaris Realty Inc.*, [1994] A.J. No. 482 (Q.B.); and see *Brown* v. *Fritz*, [1993] B.C.J. No. 2182 (S.C.).
106 *Anchor Fence Inc.* v. *Polaris Realty Inc.*, [1994] A.J. No. 482 (Q.B.).
107 *Belzil* v. *Bain*, [2001] A.J. No. 1350 (Q.B.); *Reidy Motors Ltd.* v. *Grimm* (1996), 50 R.P.R. (2d) 251 (Alta. Q.B.); *Burreddu v. Palace Property Services Ltd.*, [1995] O.J. No. 69 (Gen. Div.).

Any protection afforded brokers by exclusion clauses extends to their brokerage firms who would otherwise have been vicariously liable for the their misconduct. But an exclusion clause will not protect a brokerage firm where it is the firm that is found to have been personally (directly) negligent [as discussed immediately above].

5.3.2 *By independent contractor designation*

Some brokerage firms have sought to employ industry members as independent contractors rather than as employees, agents, etc. One of the benefits sought by firms through this relationship is avoidance of the doctrine of vicarious liability for it is generally acknowledged that the doctrine is inapplicable to the "employment" relationship that exists between an employer an independent contractor.

But it must be noted, firms may incur personal (direct) liability if they are negligent in their choice of the independent contractors who work for them, or in retaining the services of independent contractors who they know, or should know, are incompetent or otherwise unfit to serve as members of the industry.

However, while it has been accepted in some cases that the brokerage firm-broker relationship may be that of employer and independent contractor for purposes of determining their rights and obligations *inter se*, recent case law suggests that:

- that the employment of brokers as independent contractors may in fact violate the legislative parameters of the employment relationship that must exist between brokerage firms and brokers;[108] and,
- that, even if brokers may be employed by firms as independent contractors, the firms will not avoid liability under the doctrine of vicarious liability if clients and customers of the firm are unaware of the nature of the employment relationship between the firm and its "employees."[109]

With respect to this second point, in one case in which the brokerage firm sought to avoid its vicarious liability for the misconduct of an employee on the basis that the latter was an independent contractor, the court observed, that the brokerage firm:[110]

> did not disclose to its customers that its agents were independent contractors rather than employees, nor was this distinction or its consequences apparent to potential customers. [Therefore it] cannot rely on this distinction to avoid liability [and the firm's] liability should be the same as that of an employer in similar circumstances.

Consequently, the court stated, a brokerage firm cannot seek to "hide behind the terms of its contract [with its employees] ... when those terms were not published to its potential customers" because:

> sales representatives have the apparent authority to act on behalf of the listing broker in obtaining listing agreements, obtaining offers to purchase, receiving deposits to be held in trust and giving receipts for those

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[108] *F.W.C. Land Company Inc. (Receiver Manager of)* v. *Turnbull*, [1997] B.C.J. No. 1985 (S.C.); *Homelife/Realty (Victoria) Ltd. (Receiver Manager of)* v. *Canada (Minister of National Revenue, Taxation, Customs and Excise – M.N.R.)*, [1993] B.C.J. No. 2922 (S.C.).

[109] *Choi* v. *Sutton Group Central Realty Inc.*, [1998] O.J. No. 269 (Gen. Div.); *Caron* v. *Alllport*, [1995] O.J. No. 4220 (Gen. Div.).

[110] *Choi* v. *Sutton Group Central Realty Inc.*, [1998] O.J. No. 269 (Gen. Div.).

> deposits. [The firm] clearly entrusted these duties on its behalf to [its representative]. In the absence of full disclosure by the [employer] of the agent, the sales representative's "scope of authority" and what is in the "course of employment" must be viewed from the subjective perspective of the outsider customer, acting reasonably, rather than the perspective of the [employer] or its agent who are privy to an undisclosed agreement.

Nevertheless, if firms are permitted to employ brokers as independent contractors, this case suggests that if clients and customers are aware that the broker with whom they are dealing is an independent contractor and the implications of this designation, a brokerage firm may avoid liability for the broker's misconduct. Whether this will be borne out by subsequent litigation, remains to be seen.

However, even if brokerage firms may employ brokers as independent contractors, it is unlikely that such employment relationships may be established between firms and salespersons who, by statute, are prohibited from trading in real estate on their own account.

5.3.3 *Usual course of business*

Brokerage firms may avoid vicarious liability by showing the act performed by the employee is not one that industry members would usually undertake in the performance of their mandate.[111] That is, the firm must show that the act was not one that falls within the usual course of employment of brokers. However, where brokers merely violate express instructions issued by their brokerage firms (e.g. not to fraudulently or negligently misrepresent properties) in performing acts that they normally perform, the firms are not shielded from liability.[112] Consequently, this line of defence is of limited utility to brokerage firms.

However, it must be remembered that when brokerage firms are held vicariously liable for the misconduct of their employees they have the right to be indemnified by the employees concerned for any loss the firm suffers.

6. THE DUTY OF DISCLOSURE

An ongoing issue in the case law is that of the scope and intensity of brokers' duty of disclosure to clients, on the one hand, and customers, on the other. Several challenges must be faced in attempting to elucidate the parameters of this duty, namely:

- the absence of any clear discussion in the case law of the comparative intensity of the duty of disclosure owed to clients and owed to customers;
- the lack of clear discussion in the case law of a broker's duty of disclosure to customers in light of their seller-clients' limited duty of disclosure to buyers, an issue of particular relevance to the use of property disclosure statements by sellers' brokers;
- the presence in the case law of what appear to be broad statements concerning brokers' duties of disclosure to buyer-customers, statements that can only be fully understood by taking into account the context in which they were made and other relevant case law; and
- apparent confusion between brokers' general duty of disclosure (a duty imposed on all professional advisors whether or not they are also fiduciaries); and brokers' fiduciary duty of disclosure [discussed above in sections 3.5 and 4.3.4]. Breach of the former duty

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111 *McGowan* v. *Campbell*, [1999] B.C.J. No. 166 (C.A.).
112 *Caron* v. *Alllport*, [1995] O.J. No. 4220 (Gen. Div.).

> will result in liability only on proof of loss by clients; whereas liability for breach of the latter may be imposed whether or not a client has suffered loss.[113]

These challenges are largely due to the fact that the courts are restricted to deciding cases on the strength of the legal arguments presented by counsel. Rarely do courts engage in general expositions of the law relevant to the broader issues that may be raised by cases but that are not addressed by counsel. Thus, a case often proffers guidance as the scope of brokers' duty of disclosure only in the particular circumstances of that case, but it does not help inform general principles. Therefore, it is necessary to try and discern the general law on the issue of disclosure from the many cases in which it has been considered.

Consequently, in this section of the report regard is had separately to brokers:

- duty of disclosure to clients;
- duty of disclosure to customers; and
- duty of disclosure and property disclosure statements.

Brokers' fiduciary duty of disclosure has already been discussed above.

6.1 Disclosure to Clients

The obligation of brokers to clients, be they sellers or buyers, is clear: it is to make full disclosure of everything known to them respecting the subject matter of the transaction or the customer that would be likely to influence the conduct of their clients,[114] even if the broker might disagree with the information.[115]

A necessary corollary of this duty is that brokers must exercise reasonable care and skill in ensuring the accuracy of the information conveyed and in keeping themselves informed of matters that may be of concern to their clients. (It may be noted that in dual agency situations, depending on the role they have chosen to play [discussed above in section 4.3.1], brokers must fulfil this duty to both seller and buyer.)

6.2 Disclosure to Customers

The obligation of brokers to customers, be they sellers or buyers, is not as broad as that owed to clients. Nevertheless, one encounters observations in the case law that appear to suggest the contrary. For example:

- the obligation of brokers to customers is "a general duty to disclose all material facts known to [them] which could affect the [customers'] willingness to enter into a contract of purchase and sale;"[116]
- that "it is now clear that the law ... is such that [sellers] are required to disclose latent defects of which they are aware. Silence about a known major defect is the equivalent of

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113 See e.g., *Verma* v. *Zinner*, [1994] A.J. No. 816 (C.A.).

114 *Rec Holdings Co.* v. *Peat Marwick Thorne*, [1997] B.C.J. No. 1640 (S.C.); *Morton* v. *Francis*, [1994] O.J. No. 1664 (Gen. Div.); *Bayes* v. *Century 21 Valley Realty Ltd.*, [1999] O.J. No. 2673 (S.C.); *Fee* v. *Currie*, [1999] B.C.J. No. 3097 (Prov. Ct.); *Rattan* v. *Mangar*, [1994] O.J. No. 866 (Gen. Div.); *Redlick* v. *Chatybok*, [1996] M.J. No. 149 (C.A.).

115 *Cox* v. *Martin*, [1997] B.C.J. No. 1690 (S.C.).

116 *Fee* v. *Currie*, [1999] B.C.J. No. 3097 (Prov. Ct.).

an intention to deceive;"[117]
- that a broker's failure to disclose a material fact is fraud.[118]

Such statements may be understood by some as suggesting that brokers (and sellers) are under a duty to disclose all to a customer. But that is not the case; their obligation only extends to the disclosure of *material* facts or *major* defects, not *all* facts and defects.

Thus, at present, at least, as is discussed below, brokers owe no general obligation of disclosure to customers, analogous to that they owe to clients, to make full disclosure to customers of everything known respecting the subject matter of the transaction or the client that would likely affect effect a customer's judgement.

6.2.1 *Brokers' duty co-extensive to that of clients*

When brokers act in a representative capacity as agents, in the absence of a clear statutory rule or judicial pronouncement to the contrary, their obligation of disclosure to customers is co-extensive with the obligation of disclosure owed by their clients to customers. To impose on brokers a more extensive duty of disclosure would be to compel them to also act in the customers' best interests and, thus, in breach of the fiduciary owed their clients to always act in their best interests.[119]

However, this requires that brokers be aware of the scope of a client's duty of disclosure, particularly where the client is the seller. What then is the scope of a sellers' duty of disclosure to buyers?

6.2.2 *Application of caveat emptor*

In answering the above question, one must start with the realization that, according to the Supreme Court of Canada, "the common law doctrine of *caveat emptor* has lost little of its pristine force in the sale of land ...."[120] This doctrine, however, "does not mean that buyers must 'take a chance;' it means [they] must 'take care'."[121]

In light of the continued application of the doctrine of *caveat emptor* to real estate transactions, what then are the defects that must be disclosed by sellers to buyers? In brief, they are:
- *latent*, not *patent*, defects;[122]
- latent defects that reasonable persons would agree are material in the circumstances of a particular case;
- not all defects that a particular buyer, often with the benefit of hindsight, might deem to be material for "to allow defects to be determined by individual preferences would open the floodgates of litigation by remorseful [buyers] and create an impossible standard of disclosure for [sellers]."[123]

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117 *Jung* v. *Ip* (1988), 47 R.P.R. 113 (Ont. Dist. Ct.).
118 Manitoba, *Real Estate Brokers Act*, s. 1; Saskatchewan, *Real Estate Act*, s. 2.
119 See e.g. *MacAuley* v. *LeClair*, [1998] O.J. No. 1918 (Gen. Div.).
120 *Fraser-Reid* v. *Droumtsekas*, [1980] 1 S.C.R. 720. And see *Morris* v. *Hitchen*, [1998] N.J. No. 134 (Prov. Ct.).
121 *Wallis* v. *Russell*, [1902] 2 Ir. R. 585 (Ireland C.A.).
122 *Belzil* v. *Bain*, [2001] A.J. No. 1350 (Q.B.); *Tony's Broadloom & Floor Covering Ltd.* v. *NMC Canada Inc.*, (1996), 141 D.L.R. (4th) 394 (Ont. C.A.); *44601 B.C. Ltd.* v. *Ashcroft (Village)*, [1998] B.C.J. No. 1964 (S.C.); *Davis* v. *Stinka*, [1995] B.C.J. No. 1256 (S.C.); *Moore* v. *Page*, [2002] O.J. 2256 (S.C.); *Fischer* v. *Faucher*, [1993] B.C.J. No. 2005 (Prov. Ct.).
123 *Summach* v. *Allen*, [2002] B.C.J. No. 200 (S.C.).

6.2.3 *What are material latent defects?*

A review of the case law pertinent to the law of vendor (seller) and purchaser (buyer), demonstrates that sellers and, by extension, their brokers, have a duty to disclose to a buyer a range of material defects that are both latent and material and, of course, known to them.

Latent defects are those defects which are not discoverable through the exercise of reasonable vigilance in the course of an inspection of a property; whereas *latent material defects* are both not discoverable and:

- render the property dangerous or potentially dangerous to the occupants;[124]
- render the property un-fit for habitation;[125]
- render the property unfit for the purpose for which the buyer is acquiring it where the buyer has made this purpose known to the seller or broker;[126]
- concern local authority and similar notices received by the seller that affect the property;[127]
- concern the lack of appropriate municipal building and other permits.[128]

Patent defects, on the other hand, are defects that would be discovered through the exercise of reasonable vigilance in the course of an inspection of a property. Buyers are deemed to be aware of such defects whether or not they in fact inspect the property or have it inspected on their behalf. While it is clear that there is no duty on sellers and their brokers, to disclose patent defects, sellers and their brokers cannot hide from, or otherwise mislead buyers as to the existence of such defects.[129]

6.3.4 *Disclosure options*

Sellers and, by extension, their brokers, must disclose latent material defects of which they are aware. With respect to other defects known to them, they cannot fraudulently or negligently misrepresent property. Thus, when asked by customers for information concerning matters that do not qualify as latent material defects, sellers and brokers are not obliged to provide it; rather, sellers and their brokers have several options:[130]

- they can refuse to provide the information and suggest that the buyer ascertain it for themselves;
- they can provide the information but attach a disclaimer as to its accuracy, putting customers on notice that they need to verify the information for themselves; or
- they can provide the information without qualification.

If sellers and their brokers choose the final option they must conform to the standard of care demanded of members of the industry [discussed above in section 5] in ensuring the accuracy and completeness of the information conveyed to the buyer.[131]

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124 *Fournier* v. *van der Laan*, [1997] N.B.J. No. 96 (Q.B.).

125 *Moore* v. *Page*, [2002] O.J. 2256 (S.C.); *Pavenham Development Corp.* v. *Sladen*, [1997] B.C.J. No. 2103 (S.C.).

126 *Tunner* v. *Novak*, [1993] B.C.J. No. 505 (C.A.); *Summach* v. *Allen*, [2002] B.C.J. No. 200 (S.C.).

127 *Phung* v. *Pshebnicki*, [1999] A.J. No. 1432 (Prov. Ct.); *Pavenham Development Corp.* v. *Sladen*, [1997] B.C.J. No. 2103 (S.C.).

128 *Jakubke* v. *Sussex Group*, [1993] B.C.J. No. 1036 (S.C.); *Pearce* v. *Chacon*, [1997] B.C.J. No. 29 (S.C.).

129 *Anderson* v. *Kibzey*, [1996] B.C.J. No. 30008 (S.C.); *Edwards* v. *Crocker*, [1998] B.C.J. No. 1241 (S.C.).

130 *Hedley Byrne & Co.* v. *Heller & Partners*, [1964] A.C. 465 (H.L.).

131 *Burke* v. *Chung (c.o.b. Ben's Vegetable Produce)*, [1995] B.C.J. No. 38 (S.C.); *Burreddu v. Palace Property Services Ltd.*, [1995] O.J. No. 69 (Gen. Div.); *Redmond* v. *Densmore*, [1997] N.J. No. 190 (C.A.); *Fletcher* v. *Hand*, [1994] A.J. No. 531 (Q.B.); *Spilker* v. *Clayton-Carroll*, [1997] B.C.J. No. 678 (S.C.); *Finstad* v. *Nelson*,

6.3 Duty of Disclosure and Property Disclosure Statements

There appears to be growing use of property disclosure statements (hereafter "PDSs") in the marketing of property. The use of these statements is a relatively recent industry innovation. These statements, essentially, ask sellers to disclose all *patent* and *latent* defects, and other matters, affecting their properties, of which they may be aware. As stated in one case,[132] these statements are:

> a form of disclosure ostensibly used to provide potential [buyers] with information about the property. The questions posed [in the statements] to the [seller] ... are those which a knowledgeable, diligent and serious potential [buyer] would normally ask.

In British Columbia particularly, PDSs have been the source of considerable litigation between sellers and buyers, litigation often also involving the seller's and/or buyer's broker. It is probable that the use of PDSs will be the cause of continuing litigation of which industry members must be aware.

While this industry practice may be seen by brokers as being consistent with their duties, it is suggested that the practice raises significant questions as to its compatibility with the sellers' and, by extension, their brokers, duties of disclosure to buyers [discussed above]. Moreover, it must be stressed that an industry practice cannot in itself alter the legal rights and responsibilities of sellers and buyers or those of brokers.

Thus, in considering the use of PDSs by industry members it is important to keep in mind both:

- the obligation of brokers to exercise care and skill in advancing the interests of their clients; and
- the limited duty of disclosure that sellers' brokers owe to customers given they are:
  - acting as agent for a seller-client; and
  - that their duty of disclosure to buyer-customers, in the absence of legislation or clear and binding judicial pronouncement to the contrary, is co-extensive with the duty of disclosure owed by their clients to customers.

Consequently, in the following discussion, regard is had to the use of PDSs:

- first, by buyers' brokers; and
- second, by sellers' brokers

6.3.1 *PDSs and buyers' brokers*

Where buyers' brokers request sellers to complete a PDS buyers' brokers are, of course, acting in the best interests of their clients and seeking to discover as much information as possible that may be relevant to their clients' decisions.

Of course, sellers are not obliged to complete PDSs, provided they otherwise comply with their limited duty of disclosure. In such situations, buyers and their brokers are left to conduct their own inspections and otherwise satisfy themselves as to the state of the property.

The important fact, however, is that the use of PDSs by buyers' brokers raise no adverse agency law issues for them as they are acting in their buyer-clients' best interests by seeking to obtain as

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[1993] A.J. No. 377 (Prov. Ct.); *Kotowich* v. *Petursson*, [1994] M.J. No. 60 (Q.B.).

[132] *Rampersad* v. *Rose*, [1997] O.J. No. 2012 (Gen. Div.).

much information as possible in the circumstances so that their clients may make informed decisions.

However, if sellers do provide PDSs, then buyers' brokers' obligations to their clients are not discharged merely by delivering the statements to their clients. The case law suggests that they should advise their clients of:

- the continued relevance of the doctrine of *caveat emptor*;[133]
- the limited utility of these statements as contractual documents;[134]
- the limited utility of the statements as they attest only to sellers' current knowledge about their properties and not necessarily about the actual state of the properties;[135]
- the fact that there may be defects of which the sellers may be unaware;
- any apparently incorrect or questionable responses by sellers;
- the need for further inspection and inquiry by the buyer or appropriate experts;
- the need for brokers to personally verify certain information to ensure the statement's accuracy when a reasonable broker would do so;[136]
- the need for the insertion of appropriate warranties if particular attributes of the property are of concern to the client.

6.3.2 *PDSs and sellers' brokers*

Sellers' brokers, who request their clients to complete PDSs, may do so for one or both of two purposes:

- to determine for themselves the condition of their clients' property and other relevant matters so that they are in a position to respond, if they choose, appropriately to inquiries by potential customers; and/or
- to provide the statements to potential customers or their brokers.

For Information of Broker

Where sellers' brokers have their clients complete PDSs for their sole use, no adverse agency law issues arise provided, of course, they exercise reasonable care and skill in verifying their clients' responses to the questions in the statement when necessary.

Although, it must be kept in mind that in a dual agency situation, once a PDS is completed by a seller-client, and even if the broker obtained the statement initially for self-information, the broker may be obliged to deliver it in a timely manner to the broker's buyer-client, since the broker has "duty to ... provide [the buyer] with all the information ... given [the broker] about the property."[137] The foregoing statement must be treated with care as its application will turn on the role the broker is playing as dual agent [see discussion above in section 4.3.1]. Moreover, it cannot be read as imposing a duty on all sellers' brokers to provide buyers with PDSs since this would be inconsistent with the principles governing the duty of disclosure of sellers and, by extension, their brokers.

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133 *Taschereau* v. *Fuller*, [2002] M.J. No. 300 (Q.B.); *Lind* v. *MacLead*, [1997] B.C.J. No. 3134 (S.C.); *Davis* v. *Kelly*, [2001] P.E.I.J. No. 123 (S.C.).

134 *Arsenault v. Pedersen et al*, [1996] B.C.J. No. 1026 (S.C.); *Terbeek* v. *Newsome*, [1999] P.E.I.J. No. 66 (S.C.T.D.); *Davis* v. *Stinka*, [1995] B.C.J. No. 1256 (S.C.) *Malenfant* v. *Janzen*, [1994] B.C.J., No. 2373 (S.C.); *Rooney* v. *Neuman*, [1997] A.J. No. 470 (Prov. Ct.); *Csada* v. *Williams*, [1998] S.J. No. 909 (Prov. Ct.).

135 *Zaenker* v. *Kirk*, [1999] B.C.J. No. 3033 (S.C.); *Lind* v. *MacLeod*, [1997] B.C.J. No. 3134 (S.C.).

136 *Mateazzi* v. *Mateazzi*, [1997] B.C.J. No. 2137 (Prov. Ct.); *Johnstone* v. *Dame*, [1995] B.C.J. No. 2637 (S.C.).

137 *Pavenham Development Corp.* v. *Sladen*, [1997] B.C.J. No. 2103 (S.C.).

For Information of Buyer

Use of PDSs by sellers' brokers for the purpose of delivery to buyer-customers, clearly poses significant agency law issues in light of the limited duty of disclosure owed by sellers and, by extension, their brokers, to customers notwithstanding that it has been observed that PDSs:[138]

> are clearly drawn in a manner offering more protection to [seller] than to a purchaser and in an manner to provide a sales person or vendor with an air of rectitude which might not on all occasions be deserved -- even given the cautionary line: "Buyers are urged to carefully inspect the property and, if desired, to have the property inspected by an inspection service of their choice".

Even though PDSs may be biased in favour of sellers, their use poses potential problems if only because the statements do not sufficiently clearly, if at all, advise clients:

- of the continued relevance of *caveat emptor*;
- that they are not legally obliged to disclose patent defects;
- that they are only legally obligated to disclose material latent defects;
- what constitute material latent defects;
- of the importance of accuracy and completeness if they chose to complete the statement;[139]
- of the fact that once disclosure is made there arises a continuing duty of disclosure;[140]
- that, even though the statements are not necessarily contractual documents, they nevertheless constitute representations and may be used by buyers as a basis for an action for negligent misrepresentation;[141]
- that completion of the statement does not relieve clients from their duty of disclosure to buyer-customers.[142]

While a number of these issues have not yet been considered by a court, it is suggested that it is only a matter of time before they are. For in requiring sellers to complete PDSs without an awareness of the full implications of these statements, it is difficult to see how it can be said that brokers are acting in the best interests of their clients. It is true that, in some ways, the exercise is in the interests of sellers in that it should make them aware of relevant aspects of the condition of their properties and alert them to the type of questions likely to be asked by buyers.

However, for sellers' brokers to provide these statements to buyers, is to:

- ask sellers to volunteer information to buyers, much of which information sellers are not legally obliged to volunteer; and
- place buyers in an advantageous bargaining position being armed as they are with a list of all known defects, patent and latent.

Moreover, it must be kept in mind that, in reality, many buyers are not sufficiently knowledgeable or diligent to ask for all of the information disclosed on these statements and, if buyers' brokers wish to ask these questions, they can request sellers complete the statement.

It may be that, in practice, sellers' brokers orally provide their clients with information as to the

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138 *Arsenault v. Pedersen et al*, [1996] B.C.J. No. 1026 (S.C.). See also *Curtin* v. *Blewett* (1999), 28 R.P.R. (3d) 115 (B.C.C.A.); *Best* v. *Lavoie*, [1999] B.C.J. No. 1383 (S.C.); *Chamberlain* v. *Jenner*, [1997] B.C.J. No. 184 (S.C.).

139 *Ward* v. *Smith*, [2001] B.C.J. No. 2371 (S.C.).

140 *Johnstone* v. *Dame*, [1995] B.C.J. No. 2637 (S.C.); *Rooney* v. *Neumann*, [1997] A.J. No. 470 (Prov. Ct.).

141 *Davis* v. *Stinka*, [1995] B.C.J. No. 1256 (S.C.); *Dirksen* v. *Au*, [1996] B.C.J. No. 2738 (Prov. Ct.).

142 *Pavenham Development Corp.* v. *Sladen*, [1997] B.C.J. No. 2103 (S.C.).

full implications of PDSs, noted above. However, written disclosure would be more effective to minimize the risk of allegations that brokers have breached their duty, *inter alia*, to always act in their clients' best interests and to disclose all matters (i.e. the full implications of PDSs) that may affect their clients' judgements in determining whether to complete a statement.

6.3.4 *PDSs – Some general issues*

In addition to the foregoing issues, the case law also suggests that brokers, whether representing sellers or buyers, must:

- if they play a role in the completion of the statements, exercise reasonable care and skill in ensuring their accuracy;[143]
- be alert for changes in, or new, information and ensure that PDSs reflect current knowledge concerning the property;[144]
- investigate certain responses to questions in the statement, if there is some evidence that would put a reasonable broker on notice that the response provided is not reasonable.[145]

7. GOVERNANCE FRAMEWORKS

Industry Legislative Framework

An initial review of the legislative frameworks (statutes and regulations) governing the industry discloses that, with few exceptions, they still reflect the era in which the popular and legal perception was that brokers were agents (or under an MLS arrangement, sub-agents) of sellers. The idea of buyer agency, even though it existed, was perceived to be the exception rather than the norm and, thus, was largely ignored. Given the recent growth of buyer agency relationship, attention must be paid it in the legislative framework. Thus, for example, consideration may be given to:

- specifying the minimum requirements for written agency agreements and not just listing or exclusive listing agreements as is currently the position in all provinces but Nova Scotia and Saskatchewan, and perhaps establishing, as a default setting, the need for all agency agreements to be in writing except where the brokers can establish that the absence of a written agreement is not attributable to their fault (as is currently the case in Nova Scotia);
- requiring that in all transactions brokers disclose, in writing, to seller and buyer the representative capacity in which they are acting;
- prescribing (by regulation) standard form agency agreements (or their minimum terms);
- extending brokers' statutory duty of disclosure on purchasing property, to situations in which they are selling property owned by them (as has been done in Manitoba, New Brunswick, Nova Scotia and Saskatchewan);
- prescribing (by regulation) standard form disclosure statements (or their minimum terms);
- extending the (admittedly limited) statutory right of brokers (in some jurisdiction, e.g. Newfoundland, Ontario, Prince Edward Island) to sue for their commission under expired written listing agreements to embrace all expired written agency agreements.

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143 *Dirksen* v. *Au*, [1996] B.C.J. No. 2738 (Prov. Ct.)

144 *Rooney* v. *Neumann*, [1997] A.J. No. 470 (Prov. Ct.); *Johnstone* v. *Dame*, [1995] B.C.J. No. 2637 (S.C.).

145 *Johnstone* v. *Dame*, [1995] B.C.J. No. 2637 (S.C.); *Mateazzi* v. *Mateazzi*, [1997] B.C.J. No. 2137 (Prov. Ct.); *Pavenham Development Corp.* v. *Sladen*, [1997] B.C.J. No. 2103 (S.C.).

In essence the object of these reforms would be to ensure that the legislative framework places all agency relationships, whether the client is a seller or buyer, on the same footing and require the disclosure of critical facts relevant to clients and customers thereby minimizing the risk of misunderstanding (and litigation).

More generally, however, if the aim of the Task Force is to seek uniformity in the legislative frameworks governing the industry, then thought should also be given to what matters should be dealt with by statute, by regulations and by the by-laws and rules of the industry's governing bodies.

Industry Self-Regulatory Frameworks

The provincial industry governing bodies are conferred broad regulatory powers over their members including the power to establish rules and codes of conduct for, and to take disciplinary action against, members.

It should be noted that in the absence of express statutory language to the contrary, the powers of provincial governing bodies do not extend to affecting changes to the laws of agency or of vendor and purchaser. That is, the rules and by-laws adopted by such bodies cannot confer rights, or impose obligations, on industry members that directly or indirectly conflict with the common law or statutory rights of clients, customers and third parties with whom industry members have dealings. However, persons seeking to challenge a rule of conduct must establish that it in fact infringes on their rights.[146]

In brief, the governing bodies must take care not to "trespass" inadvertently on matters beyond their jurisdiction. However, there is nothing to preclude industry governing bodies from enhancing, if they so wish, the protection afforded by the law to clients and customers.

Similarly, any rules or codes of conduct should be consistent with the common law and statutory rights of brokers,[147] although it would appear possible for a governing body to establish rules, breach of which would subject a broker to disciplinary action but not confer any rights on clients or customers *vis-a-vis* brokers.

However, one thing would seem reasonably certain, namely, the move to self-regulation in the industry will give rise to "litigation" by:

- dissatisfied clients and customers seeking to have industry members, with whom they have had dealings, disciplined; and
- industry members who, having been disciplined, seek to challenge the decision of the disciplinary body.

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146 *Toronto Dominion Bank* v. *Real Estate Council of Alberta*, [2002] A.J. No. 75 (Q.B.).

147 *Struthman* v. *Routly*, [1994] O.J. No. 1535 (Gen. Div.).

ANNEX A

DUTIES OF BROKER AND CLIENT

BROKERS'S DUTIES	CLIENT'S DUTIES
A. *Duties from Agreement*	**A. *Duties from Agreement***
1. Perform mandate	1. Remunerate broker
2. Obey instructions	2. Indemnify broker
3. Act in person	3. Perform specific obligations in agency agreement
4. Exercise care and skill	
5. Disclose information	
6. Indemnify principal	
B. *Fiduciary Duties*	**B. *Fiduciary Duties***
7. Loyalty	NIL
8. Avoid all conflicts of interest:	
i. Not act for both parties	
ii. Not make secret profit	
iii. Not buy client's property	
iv. Not sell own property to client	
v. Not misuse confidential information	
9. Disclose all conflicts of interest	
C. *Statutory Duties*	**C. *Statutory Duties***
10. Deliver listing agreements	NIL
11. Account*****	
12. Deliver offers, acceptances, etc*****	
13. Deliver statements on sale of business*****	
14. Not induce breach of contract*****	
15. Make certain promises in writing*****	
***** These duties owed to both client and customer.	

DUTIES OF BROKER AND CUSTOMER

BROKER'S DUTIES	CUSTOMER'S DUTIES
1. Honesty	NIL
2. Exercise care and skill in ensuring accuracy of information conveyed	
3. Exercise care and skill in Performing specific undertakings	
4. Not to misrepresent their authority	
5. Statutory obligations (see above 11-15)	