

The Effects of an Informational Disclosure Form on the Real Estate Agency Representational Model

Gary S. Moore*
Gerald E. Smolen*
Lawrence V. Conway*

Abstract. A study of Ohio real estate brokers and home buyers finds that a mandatory disclosure requirement had limited success in altering both buyer's perceptions of the role of cooperating real estate salespersons and broker's perceptions of the role they play in the purchase and sales negotiation process between home buyers and sellers.

Introduction

This study investigates the role of cooperating brokers in the real estate sales transaction in the light of recently mandated state disclosure requirements. These legislative requirements direct the real estate agent to disclose that he is an agent of the seller. The question of the potential effectiveness of these programs has been raised by previous researchers, including Ball and Nourse [1], [2]. We have investigated the effects of a mandatory disclosure program in Ohio. Our results support the contention of Ball and Nourse [1] that these measures will not immediately change buyers' perceptions of the role of the cooperating salesperson.

Background

In approximately 70% of all sales made through multiple listing services (MLS), the broker responsible for locating the buyer is not the same broker that is listing the property [17]. The broker representing the buyer is called the cooperating broker. The respective roles played by the two brokers create a difficult question. Does the broker who locates the buyer represent the interests of the seller or the buyer? The question has created considerable debate. It arises in numerous real estate studies [1], [2], [3], [4], [5], [9], [11], [12], [13], [14], [16], [18].

According to William D. North, General Counsel of the National Association of Realtors, "... classic legal labels—fiduciary, agent, middleman—do not fit the realities of the real estate business" [12]. A serious dilemma may arise under a multitude of

*Department of Finance, The University of Toledo, College of Business Administration, Stranahan Hall, 4th Floor, Toledo, Ohio 43606-3390.
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different circumstances. For example, what is the sales agent's role when a buyer gives him confidential price information, or a seller discloses a potential economic obsolescence factor which may affect the property? If the agent promotes the sense of acting on behalf of both parties, can he represent both parties without violating confidential relationships? According to some researchers, a common result of a broker's failure to act solely as the seller's agent when generally adhering to the exclusive agency model is the "inadvertent" creation of an undisclosed dual capacity [1], [7], [10], [15]. However, a general rule of agency law states a person cannot act as agent for both parties to a transaction unless both parties know of the dual capacity, and agree to it.

In any state (except California), a real estate agent desiring access to the MLS is required to work as a "sub-agent" of the seller's realtor. Unless specific documents are signed indicating otherwise, under the law, a listing or selling real estate agent is an agent of the seller. Agency is defined as a relationship based upon an expressed or implied agreement by which one person, the agent, is authorized to act under the control of and for another, the principal, in negotiating and making contracts with third persons (*Restatement, Agency, 2d, Sec. 1*). When an agency relationship exists, the agent owes certain duties to the principal. These duties include a duty of loyalty to the principal, to obey all lawful instructions, to exercise reasonable care, to account for all monies, and to inform the principal of all relevant facts (*Restatement, Agency, 2d, Sec 381; Spritz v. Brockton Savings Bank, 305 Mass. 170, 25 N.E.2d 155*). In other words, the real estate agent is required by law to represent the interests of the seller [11], [13]. The current law is interpreted by some authors to mean that both the listing broker *and* the cooperating broker for home-sale transactions are mandated to behave aggressively in a manner to assure the seller obtains the highest possible price [1], [10], within the legal framework.

Previous studies indicate that although the cooperating broker legally represents the seller, a substantial majority of buyers believe the cooperating broker represents them. A 1983 Federal Trade Commission study claimed 75% of all buyers believed the broker assisting them actually represented the buyer [4]. A more recent FTC survey found some improvements and indicated 71% of all buyers still held this perception [5], [17].

It is appalling that approximately three of four buyers surveyed were confused regarding the agent's legal obligation to the seller. This misperception can have severe economic consequences. Lesley [10] contends that, in millions of deals, year after year, home buyers routinely divulge confidential financial information to the cooperating broker—even disclosing their highest bidding price—not realizing the broker is obligated by law to relay that information, and assist the seller in obtaining the highest price possible.

However, the existence of widespread confusion is understandable. First, the relationship between the listing and cooperating broker has a very murky history. In 1976, when the National Association of Realtors (NAR) defined the MLS as "a means of disseminating information," the California Supreme Court in *Marin County Board of Realtors v. Palson* ruled the NAR could not restrict access to the Multiple Listing Service (MLS) to members of the association. NAR reacted by changing the definition of MLS to "a blanket unilateral offer of sub-agency" [10]. Since the MLS is responsible for about 80% of all residential sales, this action effectively moved the role of the cooperating broker from a tenuous, quasi-brokage relationship with the buyer to an explicit representative of the seller [10].

Second, evidence shows that in the past most real estate agents held beliefs inconsistent with conventional "sub-agency" concepts. This belief is supported by direct observation research of real estate agents during the 1970s [8]. Ball and Nourse [1], in a survey of real estate agents, found most real estate cooperating agents held beliefs consistent with a dual agency role rather than the conventional representational model. Ball and Nourse stated:

Popular wisdom is premised on the paradigm that in a conventional residential real estate brokerage, all practitioners are exclusive agents of all sellers and must therefore act in the best interest of the sellers and not the buyers Since licensees are taught this model in their coursework, it is presumed that they understand the model and practice accordingly. Since consumers were known to be unaware of this model, the popular solution is *simply to mandate disclosure of the representations to all parties in a transaction.* (emphasis added)

Instead of accepting the notion that the residential real estate marketplace is comprised of many ignorant consumers and duplicitous agents, an alternative conclusion can be drawn from studies of real estate buyers and sellers—seller agency is simplistic in modeling the role of real estate agent in residential sales. The present study supports this alternative.

Consequently, the Ball and Nourse study concluded that the public was accurately perceiving the real estate agents' viewpoint concerning the role of the cooperating broker, and the agents' behavior in accordance with their views. Thus, the results of the FTC survey should not be totally unexpected.

State Real Estate Commissions are aware of the public's misperception. In recent years, forty-three states adopted rules aimed at making buyers aware of the agents' and the brokers' true clients [6]. States such as New York require an oral disclosure be given to the broker's client. Other states, including Ohio, recently adopted a mandatory written disclosure. Ohio law requires a disclosure form be given to the buyer. This form discloses only a single fact: the real estate agent interacting with the buyer in search of a property, in reality, represents the seller, not the buyer [17]. The primary purpose of the disclosure document is to inform the buyer. The authors believe Ohio represents an excellent case to study the effectiveness of disclosing the agency relationship.

If Ball and Nourse are correct, mandatory disclosures should have a minimal effect in changing the perception of buyers concerning the role of the cooperating agent. With the mandatory disclosure process in operation, this study endeavors to investigate the extent to which false perceptions concerning the role of the real estate sales agent (cooperating broker and sales agent) still prevail. Also, we investigate whether the educational disclosure law overcomes the long standing falsely held perception by buyers found by the FTC. Additionally, we are testing the Ball and Nourse hypothesis that mandatory disclosure will not rapidly alter buyers' beliefs regarding the cooperating broker because the perception is based upon true prevailing behavioral norms.

Methodology

The data for the analysis was collected from two different mail surveys sent to Ohio real estate brokers and home buyers. The surveys were blind mail surveys to guarantee

anonymity and to obtain truthful answers to sensitive items. A cover letter, designed to create receptiveness among the respondents and hand signed, accompanied each questionnaire. Each envelope was hand addressed and sent to each respondent with a postage-paid return envelope enclosed.

The findings of the home buyers survey were compiled from 110 responses to 488 questionnaires mailed to Dayton, Columbus, Cleveland, Dublin, and Cincinnati, the major metropolitan areas in Ohio. Home sale transactions were obtained from data published by Ameristate. The home buyers survey focused on their experiences arising from purchasing a home. The respondents had particular commonalities, e.g., they were well educated (80% had at least a baccalaureate degree) and had above state average household incomes. Median household income was \$60,000. Ninety-nine percent of the buyers purchased the home for owner-occupancy and 32% were first-time home buyers. Seventeen percent of the homes purchased were new.

The average price of homes purchased was \$138,800. The average respondent spent \$8,900 more than originally planned. When asked whether they thought the price paid accurately reflected its true worth, given later knowledge, 15% said the price should have been higher—they got a bargain (by an average of \$19,800), and 19% said it was too high (by an average of \$12,800). The remaining 66% thought the price was “about right”. Seventy-six percent of the buyers and 79% of the sellers relied on real estate agents. In 11% of the sales, buyers and sellers were represented by the same agent.

Dr. Almon Smith, former Executive Vice-President of the Ohio Association of Realtors, assisted in the second survey which was directed to brokers. The broker survey identified 500 randomly selected firms throughout the state, and provided 54 respondents who had closed a sale since May 1, 1990. The Ohio real estate brokers represented a diverse group from across the state in terms of office sales volume. Each broker was asked to report information concerning a recent specific sale. Generally, the price ranges of homes included in the brokers survey were coincident with the price range of real estate sales in Ohio. Listing prices of residential real estate reported by brokers averaged \$84,000, and sales prices, \$79,000.

On both surveys the respondents were encouraged to provide additional written comments.

Results

The findings indicated substantial compliance with Ohio's mandatory disclosure requirements, i.e., proper forms were provided to buyers by their agents. Exhibit 1 provides the buyers' responses to the questionnaire concerning their recollection of the mandatory disclosure form. Eighty-four percent of the buyers remembered receiving the mandatory disclosure report from their agent at some point in time. Forty-eight percent of the buyers indicated that they received the mandatory disclosure form sometime before the purchase offer was made.

According to buyers, present disclosure practices can be improved. The key element is this: 52% of the respondents who remembered receiving a disclosure form did *not* receive it until the day the offer was made, or later. More cynical buyers might regard failure to receive this disclosure early as a lack of forthrightness by the real estate sales agent. Situations such as these could give rise to problems in the future because a person's

Exhibit 1

Timing of Receipt of Mandatory Disclosure Forms

Of the buyers who remembered receiving the disclosure form the timing of receipt of the mandatory disclosure was as follows:

Before making an offer	48%
On the day the offer was made	44%
Within 5 days after the offer was made	6%
More than 5 days after making an offer	2%

Exhibit 2

Usefulness of the Mandatory Disclosure Form (Percent of Buyer Respondents, 1990)

	Received Before Offer	Received After Offer
Very Useful	7%	6%
Somewhat Useful	51%	32%
Not too Useful	33%	45%
Not at all Useful	9%	17%

perceptions, whether in concurrence with the facts or not, are often the genesis of subsequent legal actions. Receipt of the disclosure form prior to the offer would tend to reduce the litigation risk to the sales agent. The gravity of the difficulty moved one buyer to comment, "a real estate agent should tell the client in the *beginning* that he/she works for the seller." The respondent underlined the word "beginning" three times to make his point!

Noting mandatory disclosure is a relatively new requirement, the authors are assured standard operating practices are still evolving in the real estate profession. However, as a liability control measure, the industry should establish more specific guidelines indicating the proper time for the agent to disclose the agent-seller relationship to the buyer, i.e., very early in the relationship.

According to buyer survey respondents, 76% reported reading the mandatory disclosure closely. However, the usefulness of the report remains an important question to the buyers. In Exhibit 2, buyer data shows considerable doubt surrounding the usefulness of the information provided by the disclosure form. To the question, "In general, how useful did you find this REQUIRED report to be?," only 7% found the disclosure message "Very Useful," and 44% found it "Somewhat Useful".

Not surprisingly, the perceived usefulness of the mandatory disclosure form depended upon when it was received. As shown in Exhibit 2, the percentage of buyers who found the mandatory disclosure form "Somewhat Useful" varied depending upon when the disclosure form was received. Those who received the disclosure form prior to making

Exhibit 3

Buyer's Perception of the Role of Cooperating/Sales Agent

In home sales where two agents participated, the buyer considered the sales agent to be:

	Received Report Before Offer	Received Report After Offer
Working for the seller	42%	35%
Working for the buyer	58%	62%
Working for his/her own benefit		3%

an offer felt it was either "Very Useful" or "Somewhat Useful" 58% of the time. Those who received the form on the day the offer was made or later thought it was "Useful" only 38% of the time.

Buyer response to the mandatory disclosure form was not overwhelmingly enthusiastic. However, 51% responded positively to the form, indicating support for continuing its use.

An investigation to determine whether the mandatory disclosure form effectively countered the perceptions concerning the cooperating broker and sales agent roles revealed that for the most part, buyers still consider the sales agents to be working for them. Exhibit 3 shows the percentage of buyers who considered the sales agent to be representing the buyer. Despite receiving a mandatory disclosure form, a significant majority of these buyers still believe the agent was working on behalf of the buyer. A small but insignificant difference was found based upon when the mandatory disclosure form was received. Fifty-eight percent of the buyers who received the mandatory disclosure form prior to making an offer on a home believed that the cooperating broker was working on their behalf. For those who received the mandatory disclosure form later, 62% believed that the cooperating broker was working for them. Although an improvement from the 71% in the FTC study, it is not the significant gain expected [5], [17].

Given the findings, an important question arises regarding mandatory disclosure: Why were buyers still under the impression the cooperating brokers were representing them? Ball and Nourse [1] offer a partial explanation in their earlier study, suggesting the reason buyers believe cooperating brokers represented them was that the brokers themselves, to some extent, believed they were acting on behalf of the buyers. The results seem more consistent with Ball and Nourse's [1] contention that the buyer is employing the true behavioral norm as the basis of belief, not the legal model.

We used the results from a second survey of queried brokers to measure the effect of the mandatory disclosure on broker perceptions regarding the role of cooperating brokers. Presumably, the broker-client relationship is often governed by a condition of asymmetric information regarding their mutual comprehension of respective roles. Because brokers are required to routinely deliver the mandatory disclosure in every one of their transactions, they should be more knowledgeable than buyers concerning their legal status. Nevertheless, the effectiveness of the mandatory disclosure in changing

Exhibit 4

Who the Broker Believes He Represented

In this scale, broker represented:

Seller	70%
Buyer	11%
Buyer and Seller	19%

the perceptions of the brokers is open to question. Despite an enormous number of residential real estate sales taking the form of a standard "listing agent/selling agent" arrangement, the results indicate many brokers may have not yet accepted their roles as representatives of the seller. Exhibit 4 summarizes brokers' responses to the question, "Who did you represent in this sale?". In many cases, the brokers indicated they represented someone other than the seller. With the small number of buyer agents in Ohio transactions, the respondents indicated some sales agents continue to see themselves as either representing the buyer and the seller, or only the buyer. On the other hand, the majority of brokers see themselves as representing the seller.

The responses seem to demonstrate mandatory disclosure is having a positive effect in educating real estate market participants. The decline in percentage from the FTC survey results, to the results in Exhibit 3, may be partially explained by the use of the disclosure form.

The broker survey also examined to what extent brokers' misperceptions of a selling agent's role might extend into contract negotiations. The survey question was expected to measure the tenacity of listing brokers' beliefs in the role played by cooperating brokers in a sale transaction. Attitudinal characteristics with regard to the role of a cooperating sales agent was solicited by examining broker responses to five statements representing five different representational models.

The models were: seller's agent, buyer's agent, middleman, mediator, and dual agent. Model 1 was represented by the statement, *The selling agent should use every effort to persuade the buyer to make as many concessions as possible*. This exemplifies an attitude toward the agency relationship that is closest to the legal definition of an exclusive seller agency model.

Model 2, which we call the buyer's representational model, was represented by the statement, *The selling agent should help the buyer get good terms*. This represents a relationship where the broker is supportive of the buyer. Model 3, which we call the middleman model, was represented by the statement, *The selling agent should avoid advising on price*. As a middleman, the representative's major role is to introduce the parties. With regard to the actual negotiations, the middleman's role is passive.

An active role as a mediator is given by model 4, which is exemplified by the statement; *The selling agent should work on the buyer to increase his/her offer and the seller to reduce his/her price*. And, finally, model five, which we call the dual agency model, is represented by the statement: *The selling agent should promote a "fair deal"*. In this model the agent is an arbiter and attempts to get an equitable result.

The results indicate brokers' perceptions are currently not in strict conformity with their legal status as sellers' agents. Legally speaking, as an agent for the seller, the agent should be acting primarily in the seller's interest. As shown in Exhibit 5, some significant disparities exist between the legal status of agents and perceptions of their role in the transaction. Taking the conventional representational model view, the legal status of the selling agent acting as the seller's agent implies a mandate to use every legal means to persuade the buyer to offer as many concessions as possible. If any of the alternative models such as models 2, 3, 4, or 5 describe how practitioners view their role in negotiations, then most of the rules and understanding of courts are untrue.

We first tested the models using a conservative *chi*-square goodness-of-fit test using only the observations in the "Disagree" and "Strongly Disagree" cells. Only one model was rejected, model 1, which is associated with the conventional representational model. The resulting *chi*-square value was 9.6, rejecting the model. The other models were not rejected using this conservative test. We tested another possible behavioral distribution. Assuming half the population would "Strongly Agree" and half would "Agree" if any particular model was true, all models were rejected at the 10% level of significance, except model 5, the dual agency model. The *chi*-square values for each model respectively, under these distributional assumptions, were 33.4, 13.5, 8.46, 27.46, and 0.69. Thus, model 5, the dual agency model, is strongly supported under these assumptions. The majority of the brokers clearly upheld the perception that the cooperating agent is obligated to promote a fair deal. Our results are consistent with the findings of Ball and Nourse [1, p. 128] who surveyed agent attitudes prior to the enactment of mandatory disclosure laws and found, "The model most preferred is that of dual agency."

Exhibit 5

Broker's Perceptions of the Role of the Sales Agent/Cooperating Broker

Based on your experience as a selling agent, express your opinion on the role of the selling agent:

	Strongly Agree	Agree	Neutral	Disagree	Strongly Disagree
Selling agent should use every effort to persuade the buyer to make as many concessions as possible	4%	11%	28%	39%	17%
The selling agent should help the buyer get good terms	11%	41%	24%	17%	7%
The selling agent should avoid advising on price	35%	24%	22%	13%	7%
The selling agent should work on the buyer to increase his/her offer and the seller to reduce his/her price	10%	19%	42%	19%	10%
The selling agent should promote a 'fair deal'	53%	40%	6%	0%	0%

The results of the analysis indicate a substantial variance between the legal status of seller's agent and the broker's perception of the sales agent's role. Clearly, the mandatory information disclosure form has yet to solve the ambiguity of the role of the sales agent in a real estate transaction in Ohio.

Some Additional Observations

The chronic confusion surrounding the role of the cooperating broker is perplexing. It portends dire consequences since the law typically holds any sale made by a subagent is rescindable if the subagent leaves any impression in the buyer's mind that his interests were not properly being represented [10]. Buyers wishing to terminate a real estate transaction may have grounds for a rescission based on a misrepresentation of the cooperating broker's role. Presumably statutes requiring a mandatory disclosure of the cooperating broker should have eliminated this possibility. A strong legal argument exists wherein the buyer should not expect the cooperating broker to act on his behalf. Nevertheless, the results here raise the prospect of this defense in spite of the mandatory disclosure. Of particular importance are questions surrounding the actual presentation of the disclosure form by the agent, e.g., *Is the disclosure completed in the calm setting of an environment conducive to reflective, careful study?* Or is it pushed into the hands of the buyer while driving between properties, while he is hastily attempting to choose a property? Or is the cooperating broker simply saying, "Sign this form, it is only part of the paperwork." The latter scenarios, combined with other confusion and noise, unmistakably promotes justifiable dependence on the agent. Some presentation settings may overcome the natural presumption of knowledge of the agent's status established by signing the mandatory disclosure form. For example, presenting the disclosure form to the buyer on, or after the day of the sale (as the survey indicates is occurring in practice) effectively negates the usefulness of the disclosure form. The buyer, having already formulated a purchase decision, would rely on his natural bias of the perception of the agent's role rather than the information contained in the disclosure form. This conclusion is consistent with Ball and Nourse's [1] contention that the cooperating broker behaves as a dual agent.

Conclusion

The role of the broker and selling agent in the typical real estate transactions remains unclear. Considerable misunderstanding remains among real estate agents concerning the proper role of the selling agent. Clearly, mandatory information disclosure has yet to solve the problem of the role of the sales agent in a real estate transaction in Ohio. Buyers want to be told as soon as possible when they begin working with an agent that agents generally represent sellers rather than buyers. The degree of perceived usefulness of the mandatory disclosure was a function of when the form was received. However, despite the mandatory disclosure, the buyers tended to perceive that a cooperating sales agent was working on their behalf. Furthermore, despite the mandatory disclosure, brokers appear to be most comfortable with a model where they are seen to be

promoting a "fair deal." This was the same model previous researchers found that real estate agents preferred prior to the enactment of mandatory disclosure laws.

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