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HIGHLIGHTS

ARTICLE: ARE YOU MY BROKER? THE EVOLVING LEGAL STATUS OF THE REAL ESTATE SALESPERSON

By Karl E. Geier

CEQA

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MILLER STARR REGALIA

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ARTICLE:
ARE YOU MY BROKER? THE EVOLVING LEGAL STATUS OF THE REAL ESTATE SALESPERSON

By Karl E. Geier[*]

1. Introduction

Under the Real Estate Law that governs the regulation of brokers and salespersons by the Bureau of Real Estate, a salesperson is theoretically subject to supervision and control at all times by the broker that employs the salesperson, which broker is also responsible for the salesperson's actions and omissions.[1] However, the status or role of a "salesperson" in relation to real estate brokerage can often be ambiguous and confusing. Under the Worker's Compensation and Unemployment Laws, the salesperson is generally treated as a nonemployee "independent contractor" or "commission agent," whereas under the tax laws the salesperson is generally an employee.[2] The Real Estate Law expressly states that whether the parties couch their relationship in terms of "independent contractor" or "employer and employee," the obligations of brokers and salespersons under the licensing laws and to members of the public apply without regard to the terms used by them in their contractual relationships.[3] The law further makes brokers directly responsible to supervise the salespersons in their employ, and liable for their torts under the doctrine of respondeat superior.[4]

Recently, the application of standard concepts of respondeat superior and broker supervision has come under challenge in the context of disclosure obligations, where the real estate industry contends the salesperson's knowledge or failures to disclose should not be imputed to the brokerage as a whole, and in the context of commission-sharing arrangements, where the courts are evidently willing to allow separate deal making between salespersons, even when not employed by the same broker, so long as their compensation is funneled "through" the brokers.

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Recent changes by the legislature also seem to give the salesperson greater autonomy and visibility while allowing the shift of managerial authority to salespersons as well.

This article summarizes the existing regulatory treatment of salespersons in relation to their employing brokers under the Real Estate Law, and then discusses the recent changes alluded to above, including (1) the decision in *Horiike v. Coldwell Banker Residential Brokerage Company*,[5] now under review by the California Supreme Court, which found the knowledge of one salesperson to be imputed to the broker and to other salesperson employees of the same broker for purposes of fraud and nondisclosure liabilities, and (2) the decision in *Sanowicz v. Bacal*,[6] which sanctioned the separate agreement of two mere salespersons to share commissions from their "shared listings," seemingly placing the interests of the agents ahead of those of the public as required by the regulatory statutes. The article concludes with an analysis of the recent legislative revisions that further erode the distinction between "broker" and "salesperson" and reduce the broker's supervisorial responsibilities, as well as the ramifications of these changes for the real estate industry and the public generally.

The issues discussed in this article arise under several distinct statutory schemes that render general conclusions or predictions about the evolving status of salespersons hazardous. However, the article poses the question whether interests of the public would be better served by a more consistent treatment of salespersons as subordinates of their employing brokers rather than as independent actors in most circumstances.

2. The Regulatory Background

Under the Real Estate Law, a salesperson must be employed by a licensed real estate broker.[7] The salesperson must physically lodge his or her license with the broker, and must inform the Bureau of Real Estate when he or she leaves the employ of a broker or accepts employment by another.[8] The salesperson cannot engage in any real estate related activity that requires a

license except in the service of a licensed real estate broker; a salesperson cannot independently solicit listings or otherwise render services for compensation, nor may the salesperson accept compensation from any person other than the broker who employs him or her.[9]

These attributes of the broker-salesperson relationship have at their root a basic premise, which is that the broker, not the salesperson, is the person liable for the activities of the brokerage business and is responsible for supervising all employees and agents under the employ of the broker.[10] The greater autonomy and responsibility accorded to brokers is reflected by the licensing laws, which require a broker to have several years of experience in the real estate business *before* becoming a broker, and which also impose greater educational prerequisites and additional licensure examinations for brokers than for salespersons.[11]

The Real Estate Law does not require the relationship between broker and salesperson to be that of an employer and employee; to the contrary, the statute expressly allows the parties to define their relationship as either "independent contractor" or "employer-employee."[12] However, the obligations of all such persons to the public under the Real Estate Law and the regulations of the Real Estate Commissioner apply regardless of how the two parties define their relationship to each other.[13] The Real Estate Law makes "protection of the public . . . the highest priority for the [Bureau] of Real Estate in exercising its licensing, regulatory, and disciplinary functions" and makes the protection of the public "paramount" to all other interests sought to be prosecuted by the Bureau.[14] A broker is required to exercise reasonable supervision over all of his or her salespersons, as detailed in the Real Estate Commissioner's regulations.[15]

Given the purpose of the licensing laws for the protection of the public, it is no surprise that for purposes of general tort liability, the broker-salesperson relationship is one of respondeat superior, a concept that signifies the level of control implicit in an employer-employee relationship rather than a mere principal-agent relationship.[16] A salesperson can only operate under the

supervision and control of a particular licensed broker under whom he or she is licensed.[17] A salesperson can only be licensed under the employing broker; the salesperson cannot accept compensation from anyone other than his or her employing broker and a broker cannot pay a commission to any person other than another licensed broker or a salesperson licensed under the same broker that is paying the compensation.[18] A salesperson also is prohibited by the regulatory law from paying compensation to any other person.[19] The purpose of these restrictions is to prevent the holder of the license—a salesperson's rather than a broker's license—from holding himself or herself out to clients as their direct representative and to assure that all of the salesperson's activities occur under the presumptively watchful eye of a supervisory broker.[20] A broker whose salesperson's wrongful acts cause damage to the principal is liable to the principal even if the broker was unaware and did not participate in those acts.[21]

3. Recent Court of Appeal Decisions

(a) The Disclosure Duties of a Broker with Multiple Salespersons: *Horiike v. Coldwell Banker*. Despite the clear intent of the Real Estate Law to treat salespersons as subordinate persons employed by a broker who owes fiduciary duties to the principal, the real estate industry persists in its view that "practical realities" and their business model override the evident legislative purpose. This is highlighted by the industry's response to the *Horiike* decision,[22] currently on review before the California Supreme Court. *Horiike* poses the specific question of whether a corporate broker is a unitary entity that owes disclosure duties to its principals irrespective of whether separate individual licensees (brokers or salespersons) are "representing" separate parties to the deal. The basic facts of *Horiike* were that the listing broker, Coldwell Banker, had knowledge of certain facts through its sales associate, a salesperson licensee, and that the listing broker, Coldwell Banker, failed to disclose those facts to the buyer, whom it also represented through another salesperson licensee. The court of appeal noted that in this situation the broker was a "dual agent" with fiduciary obligations to both the buyer and the seller, and as such had breached its duty of disclosure to the

buyer. In the words of the court of appeal: "When a broker is the dual agent of both the buyer and the seller in a real property transaction, *the salespersons acting under the broker have the same fiduciary duty to the buyer and the seller as the broker*."[23] Reversing a directed verdict in favor of Coldwell Banker, the court of appeal held that the trial court's instructions incorrectly instructed the jury that the "listing salesperson" had no fiduciary duty to the buyer, and therefore the broker also did not have such a duty.

The court of appeal's *Horiike* decision was met with immediate protests by some members of the real estate industry, who claimed it failed to recognize the need for large brokerages to operate through salespersons without having knowledge of one salesperson attributed to the brokerage or to other salespersons. The California Supreme Court granted review based on a petition for review that framed the question presented as whether, "[w]hen the buyer and the seller in a residential real estate transaction are each independently represented by a different salesperson for the same brokerage," a particular Civil Code section, Civ. Code, § 2079.13, subd. (b) (pertaining to dual agency disclosures) "makes each salesperson the fiduciary to both the buyer and the seller with the duty to provide undivided loyalty, confidentiality and counseling to both."[24] The question posed by the appellant, Coldwell Banker, specifically *presumes* that each of the two salespersons "independently" represented the buyer and seller, respectively, even though they are in the same brokerage firm. This manner of framing the issues would seem to beg the question of whether it is the *broker*, acting through its salespersons, who owes the duty in question, or whether the broker is somehow a neutral party who lacks ultimate authority or responsibility for the actions of its salespersons. The California Association of Realtors has filed a brief as amicus curiae in support of Coldwell Banker in this appeal.

Whether the Supreme Court ultimately analyzes the *Horiike* question in the manner presented by the petition remains to be seen. This article is not intended to provide an analysis of the parties' respective arguments or to predict or recommend a particular outcome. However, the decision rendered will affect the

responsibilities of salespersons to "their" clients as well as the responsibilities of brokers' organizations for the actions of salespersons as "their" agents, even if the issue is merely one of statutory construction under the "dual agency" statute. If the decision affirms the argument that two salespersons employed by the same broker are independent of each other and that their fiduciary duties are several and not imputed to the broker, then a basic precept of the broker-salesperson hierarchy will have been eroded, if not eliminated, in a manner that directly affects the public and is not merely an issue "between licensees."

(b) Rights of Salespersons to "Share Listings"; the *Sanowicz* Decision. The same appellate panel that decided *Horiike* (Division 5 of the Second District Court of Appeal), has already reached a conclusion that undercuts the limitations of the Real Estate Law on treatment of salespersons as independent actors. In *Sanowicz v. Bacal*,[25] the court of appeal held that two sales agents employed by the same broker were permitted to share commissions earned under a "shared listing agreement" entered into between themselves while in the broker's employ, and their agreement could be enforced even if one of them had left the original broker's employment and was employed by a third party broker when the actual sale occurred. Reviewing the trial court's grant of a demurrer, the court of appeal held, as an issue of first impression, that the agreement between two agents to share commissions was "not illegal" under the Bus. & Prof. Code, § 10137, because that statute does not prohibit agreements between licensees to share commissions, it only prescribes the "manner of payment" of commissions by requiring the commission to go through the broker. The court of appeal rejected arguments referencing the purpose of the statute or the policy underlying the statute, finding the issue solely to be one of construing the "unambiguous" language of § 10237. The court relied upon the "plain meaning" of the portion of § 10237 that merely provides "it is unlawful for any licensed real estate salesperson to pay any compensation for performing any of the acts within the scope of this chapter to any real estate licensee except *through the broker* under whom he is at time licensed." By this reading, the fact that

one salesperson agreed to split commissions even after he or she left the employee of the particular broker, did not affect the propriety of such an agreement.

The *Sanowicz* court did not explain whether the interest of the public generally, which is the principal benefactor of the Real Estate Law,[26] received "maximum protection" from such a narrow and parsimonious reading of the limited language of the statute. The court also did not consider the question of whether an agent who brings his or her "own" listing to a new broker when the salesperson leaves the prior broker can implicitly commit the new broker to pay consideration earned under that listing to a second salesperson who remains employed by the original broker, or vice versa, or whether such arrangements are in the interest of the brokers and their customers, i.e., the public generally. Although the court acknowledged that the regulatory structure existed, it considered the issue solely one of contractual relationships *between* agents and not as implicating the policy of the Real Estate Law or the fiduciary obligations owed by a broker to its clients or customers. This decision occurred despite the apparent purpose and intent of the Real Estate Law, including § 10237, to limit the activity of salespersons to acting solely for the employing broker and to require all licensed activity to be supervised by a licensed broker with whom the salesperson *exclusively* lodges his or her license.[27]

It is submitted that *Sanowicz* is out of step with the overall structure and purpose of the Real Estate Law and should not be considered the final word in this area. Encouraging sales agents to enter into "joint ventures" to share commissions independent of their brokerage relationship, and allowing them merely to funnel the compensation received through the broker without recognizing the supervisory nature of the relationship and the fact that the broker, not the salesperson, ultimately owes fiduciary obligations to the principals, is not consistent with the statutory structure and should not be encouraged by rulings of this nature.

4. Legislative Developments

Despite the thesis of this article, that licensed salespersons are

not independent entrepreneurs with legally independent relationships to the public separate from their employing brokerages, the Legislature also has been undermining this regulatory policy in recent legislation.

Prior to the recent amendments, the Real Estate Law plainly provided that a real estate *broker* is one who sells or buys or offers to sell or buy or solicits listing or negotiates the sale of real property,[28] and a real estate *salesperson* is a person who is *employed by a licensed real estate broker* to do one or more of these actions.[29] Only bookkeepers, stenographers, or other clerical personnel employed by the broker are exempt from the requirement that any such person be licensed (see Bus. & Prof. Code, § 10133.2), and only the licensed broker employing the salesperson can compensate a salesperson for doing any of these acts.[30] Associated with these restrictions on activities of a salesperson is the general duty of the *broker* to supervise; Bus. & Prof. Code, § 10177, subd. (h), provides that it is grounds for the suspension or revocation of the broker's license whenever a broker:

> "*As a broker licensee*, failed to exercise reasonable supervision over the activities of *his or her salespersons*, or, as the officer designated by a corporate broker licensee, failed to exercise reasonable supervision and control of the activities of the corporation for which a real estate license is required."[31]

The otherwise nondelegable nature of this supervisorial responsibility is further supported by the provisions of Bus. Prof. Code, § 10137.1, which requires all partners of a partnership that performs the acts of a broker to have a *broker's* license; a salesperson cannot be a partner in a real estate brokerage but can only be employed by a broker (either as an employee or independent contractor) who is responsible for the supervision of that salesperson.[32]

The Legislature recently has made inroads on these general supervisorial schemes in the following respects:

(1) A new statute, Bus. & Prof. Code, §§ 10159.6 to 10159.7, enacted in 2014 as SB 2018, authorized the marketing and

other activities of "sales teams" that bear the names of two or more licensees, who may be merely salesperson licensees and not brokers, so long as the responsible broker's identity also appears "as prominently and conspicuously as the team name" in all advertising, and the advertising "does not imply the existence of a real estate entity independent of the responsible broker."[33] This statute incongruously then goes on to provide that "the supervision of a salesperson *required by this part* is limited to regulatory compliance and consumer protection."[34] This little-noticed change is buried in § 10159.7, subd. (a)(4)'s definition of "responsible broker" but refers to "the supervision of a salesperson required by this part," which appears to reference Part 1 of Division 4 of the Business & Professions Code, i.e., all of the Real Estate Law, §§ 10000-10562.5.[35] It thus would appear to have *restricted* the long-standing principle of supervision of all activities of the salesperson by the responsible broker, and effectively restricted the scope of a broker's oversight and scrutiny of salespersons and their activities in general, and is not by its terms limited to the use of "team names." As a result, the Legislature has seemingly narrowed the meaning of "supervise" as used in other portions of the Real Estate Law, including the grounds for discipline in failing to properly supervise under § 10177(h).

(2) More recently, the Legislature in 2015 adopted SB 146, which "clarifies" some of the provisions of SB 2018. It continues the language of Bus. & Prof. Code, § 10159.5, subd. (b)(2), which as enacted provided that "this section" does not "change a real estate broker's duties under this division to supervise a salesperson." However, SB 146 has amended the above-quoted language of § 10159.7, which now provides even more emphatically than before, that "the supervision of a salesperson required by *this part or any other law* is limited to regulatory compliance and consumer protection."[36] The Bureau of Real Estate issued an advisory effective July 16, 2015, to the effect that SB 146 "does not change, reduce or limit a real estate broker's

statutory obligation to supervise salespersons operating under his or her license." However, the statutory language of § 10159.7(a)(4), as amended by SB 146, would seem to have the opposite effect.

(3) Perhaps of lesser concern, the Legislature in 2011 enacted SB 510, adding Bus. & Prof. Code, § 10164, subd. (a), which allows for the appointment of a salesperson licensee to act as the manager of a branch office of a licensed broker, responsible for the "day to day" activities of that office, but also stating clearly that the employing broker remains fully responsible to supervise the licensee in that office under § 10177(h).[37] In AB 607, amending § 10164, however, the Legislature in 2015 further expanded the scope of a salesperson's authority by allowing a salesperson under the employ of a broker to withdraw funds from the broker's trust account under certain circumstances, although still under the supervision of the broker. This provision is narrowly drafted (unlike the preceding provisions regarding "teams," "team names," and "the supervision of a salesperson required by this part") but is yet another instance of an expanded level of authority and autonomy for salespersons, and inherently dilutes the policy of requiring *broker licensees* directly to control brokers' trust accounts.

5. Conclusion

This article is not intended to impugn the integrity of the real estate salesperson, nor to undercut the valuable services rendered by salespersons marketing as "teams" and coordinating the efforts of others as branch managers and the like. The real estate brokerage industry has consolidated in many regions of the country, and the larger organizations that employ salesperson licensees and broker licensees operating as salespersons employed by other brokers necessarily will feature their salesperson employees in marketing and in the handling of their clients' business. Many real estate professionals serve the public and their employing brokers extremely well, and pose little risk to themselves, their employing brokers, or their clients and customers. However, the

tendency of the industry, the courts, and the Legislature to blur the line between broker and salesperson has the potential to dilute the responsibility of brokers for their employed salespersons' conduct and performance. The continued legislative and judicial tinkering in this area should proceed with caution.

ENDNOTES:

[1]*California Real Estate Loans, Inc. v. Wallace*, 18 Cal. App. 4th 1575, 1581, 23 Cal. Rptr. 2d 462 (1st Dist. 1993).

[2]See 2 *Miller & Starr, California Real Estate 4th*, Agency and Broker Liability, § 3:72 (2015).

[3]Bus. & Prof. Code, § 10032, subd. (a).

[4]*Gipson v. Davis Realty Co.*, 215 Cal. App. 2d 190, 209, 30 Cal. Rptr. 253 (1st Dist. 1963); *In re King Street Investments, Inc.*, 219 B.R. 848, 48 Fed. R. Evid. Serv. 1437 (B.A.P. 9th Cir. 1998).

[5]*Horiike v. Coldwell Banker Residential Brokerage Company*, 169 Cal. Rptr. 3d 891 (Cal. App. 2d Dist. 2014), review granted and opinion superseded, 174 Cal. Rptr. 3d 294, 328 P.3d 1035 (Cal. 2014), *review granted, opinion superseded, may not be cited.*

[6]*Sanowicz v. Bacal*, 234 Cal. App. 4th 1027, 184 Cal. Rptr. 3d 517 (2d Dist. 2015).

[7]Bus. & Prof. Code, § 10132.

[8]Bus. & Prof. Code, §§ 10160, 10161.8.

[9]Bus. & Prof. Code, §§ 10032, 10132, 10137.

[10]See Bus. & Prof. Code, § 10177, subd. (h). See also Cal. Code Regs., tit. 10, §§ 2725.

[11]See Bus. & Prof. Code, §§ 10150.6, 10151. See *2 Miller & Starr, California Real Estate 4th*, Regulation and Licensing of Real Estate Professionals and Appraisers, § 4:14 (2015) for further discussion.

[12]Bus. & Prof. Code, § 10032, subd. (b)

[13]Bus. & Prof. Code, § 10032, subd. (a).

[14]Bus. & Prof. Code, § 10050.1.

[15]See Cal. Code Regs., tit. 10, §§ 2725, 2725.5.

[16]*California Real Estate Loans, Inc. v. Wallace*, 18 Cal. App. 4th 1575, 1581, 1581 n.2, 23 Cal. Rptr. 2d 462 (1st Dist. 1993); *Gipson v. Davis Realty Co.*, 215 Cal. App. 2d 190, 203, 207-208, 30 Cal. Rptr. 253 (1st Dist. 1963).

[17]Bus. & Prof. Code, § 10132.

[18]Bus. & Prof. Code, § 10137.

[19]Bus & Prof. Code, § 10137.

[20]*California Real Estate Loans, Inc. v. Wallace*, 18 Cal. App. 4th 1575, 1583, 23 Cal. Rptr. 2d 462 (1st Dist. 1993).

[21]*California Real Estate Loans, Inc. v. Wallace*, 18 Cal. App. 4th 1575, 1581, 1581 n.2, 23 Cal. Rptr. 2d 462 (1st Dist. 1993); *Gipson v. Davis Realty Co.*, 215 Cal. App. 2d 190, 203, 207-208, 30 Cal. Rptr. 253 (1st Dist. 1963).

[22]*Horiike v. Coldwell Banker Residential Brokerage Company*, 169 Cal. Rptr. 3d 891 (Cal. App. 2d Dist. 2014), review granted and opinion superseded, 174 Cal. Rptr. 3d 294, 328 P.3d 1035 (Cal. 2014), hearing granted, *opinion superseded and may not be cited*.

[23]*Horiike v. Coldwell Banker Residential Brokerage Company*, 169 Cal. Rptr. 3d 891 (Cal. App. 2d Dist. 2014), review granted and opinion superseded, 174 Cal. Rptr. 3d 294, 328 P.3d 1035 (Cal. 2014), hearing granted, *opinion superseded and may not be cited*.

[24]See the California Supreme Court's posted "Issues Pending . . . Civil Cases" memorandum, updated as of November 25, 2015, http://www.courts.ca.gov/documents/NOV2515civpend.pdf, which references Civ. Code, § 2079.13, subd.(b).

[25]*Sanowicz v. Bacal*, 234 Cal. App. 4th 1027, 184 Cal. Rptr. 3d 517 (2d Dist. 2015).

[26]See § 10050, subd. (b)

[27]See Bus. & Prof. Code, § 10160. See also discussion in text accompanying notes 5 to 21, *supra*.

[28]Bus. & Prof. Code, § 10131, subd. (a).

[29]Bus. & Prof. Code, § 10132.

[30]Bus. & Prof. Code, § 10138.

[31]Bus. & Prof. Code, § 10177, subd. (h) (emph. added.).

[32]Bus. & Prof. Code, § 10132.

[33]Bus. & Prof. Code, § 10159.6.

[34]Bus & Prof. Code, § 10159.7, subd. (a)(4).

[35]See Bus. & Prof. Code, § 10159.7, subd. (a)(4).

[36]Bus. & Prof. Code, § 10159.7, subd. (a)(4), as amended by SB 146, effective as urgency legislation July 16, 2015.

[37]Bus. & Prof. Code, § 10164, subd. (b).

