

**Real Estate Agent Referred Home Inspectors:
Buyer Protection or Buyer Deception?**

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PROPOSAL

TITLE

Real Estate Agent Referred Home Inspectors: Buyer Protection or Buyer Deception?

STATEMENT OF HYPOTHESIS

Establishing a state law prohibiting parties with a vested interest in the sale of real estate from referring home inspectors to potential buyers would add a layer of investment protection for the buyer and the lien holder.

INTRODUCTION

Home inspections are becoming ever increasing in popularity for buyers of real estate. real estate agents will normally recommend a inspection to their clients not only for the client's protection but also to pass the liability from the agent to the home inspector if a problem were to be uncovered after the buyer moved in. Some lending institutions and insurance companies are also requiring that a home inspection be completed prior to closing, especially for first time homebuyers. Media attention with mold, asbestos, radon, and unprofessional contractor work has also heightened the awareness of the necessity of having a home inspector look over the property prior to purchase.

Regardless of the reason, a home inspection is a wise decision as the inspection results can be used to negotiate a lower purchase price, used to render the purchase contract

void if structural or safety problems are identified, or used in budgeting for future repair, replacement, and maintenance of structural and mechanical components. The inspection results can also be used to validate the home as a sound investment for both the buyer and the lien holder. For these reasons alone, it is imperative for the buyer to choose an inspector who is licensed, insured, qualified, and independent so that they can get a thorough, detailed report on the condition of the structural and mechanical components of the home.

Licensed, insured, and qualified makes sense for hiring any type of contractor, but a buyer may question the relevance and importance of choosing an inspector operating under the realm of independence. That is specifically where the problem lies and when a buyer chooses a home inspector referred by a person who has a vested interest in the sale of the home, they may not be getting the inspection they desire or need to ensure they are making an educated decision on their chosen property. An independent inspector believes that it is unethical for a real estate agent or any party with a vested interest in the sale of the home to refer a particular home inspector, an independent inspector upholds the duty to his or her client only, and an independent inspector will strive at all times to further the general public's awareness of this huge but intentionally kept hidden problem.

STATEMENT OF THE PROBLEM

Various home inspection statistical reports indicate that approximately 70% of home inspectors are hired as a result of a referral from a real estate agent. Real estate

agents are in business to make money and except for areas where buyer's agency exist, agents have a contractual liability to the seller even though many buyers believe the agent is working for them. For this reason, agents will attempt to protect the sale of the home, ultimately protecting their commission. There are relatively few contingencies placed on the offer to purchase contract except for financing and a home inspection. Traditionally financing is pre-approved therefore, the home inspection, in most cases, would be the only contingency preventing the contractual obligations in the offer to purchase. In order to protect the deal, the agent will recommend an inspector who is known not to be thorough and qualified or an inspector in collusion with the agent who will ensure the deal will go through. With this type of inspection, the buyers may find themselves purchasing a home with many defects, defects that could have repaired by the seller, allowed a lower price to be negotiated with the seller, or a means for the buyers to rescind the offer to purchase.

PROPOSED SOLUTION

Heightened awareness of the problem with real estate agent home inspection referrals among buyers in the market to purchase a home or those considering purchasing a home is a key component in reducing the problems associated with a poor or collusive inspector. While awareness is critical, it is not the only solution. Enacting a law that prevents parties with a vested interest in the sale of the home, such as real estate agents, from referring a particular home inspector will provide an additional layer of protection for the homebuyer.

SCOPE

In this paper, the author will specifically identify the problems associated with real estate agent home inspector referrals, identify the reasons why an agent and home inspector would intentionally deceive a home buyer, identify why this problem is intentionally kept hidden, and identify possible solutions to rectify the problem and protect buyers from making a costly mistake.

While there may be other parties with a vested interest in the sale of a particular home, the author's intent in this paper is to focus solely on the problem presented with real estate agent home inspector referrals.

METHODS

In order to demonstrate the significance of the problem, data and information will be gathered and included from recent court decisions involving inspectors found to be in collusion with agents and involving buyers who have found themselves living a nightmare in the midst of a "money pit". In addition, information will be gathered from newspapers, periodicals, and various Internet sites to add credence to the problem as well as aiding in development of a possible solution and/or solutions. Only one state in the United States has a law prohibiting inspector referrals from real estate agents and this law will be used as a basis for a possible solution.

QUALIFICATIONS

As a Wisconsin State Licensed Home Inspector and owner of Salm Inspections, LLC d/b/a National Property Inspections, the author has observed the inherent problems with real estate agent inspector referrals. The author is also passionate in performing inspections for his clients in a manner that would epitomize the standards in the home inspection profession. Due to his passion and his belief that a serious problem exists within the inspection profession, he is a member of the Independent Home Inspectors of North America, an elite group of approximately 100 home inspectors who believe that real estate agent referred home inspectors is unethical and present a conflict of interest. Members of this association pledge not to solicit real estate agents for referrals and to educate consumers on the problem.

CONCLUSION

When this project is completed, the author intends to send it to the State Representatives for Wisconsin in hopes to draw some attention to the problem as well as a basis for implementing the proposed solution. In addition, the author will use the document on his website as a marketing and educational tool for prospective clients.

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OUTLINE

Thesis-As the owner of an independent inspection company it is my intent to demonstrate this conflict of interest and to demonstrate the need of establishing a state law in Wisconsin prohibiting parties (specifically real estate agents) with a vested interest in the sale of real estate from referring home inspectors to potential buyers to add a layer of needed investment protection for the buyer and the lien holder.

- I. Introduction-Background information on the Real Estate Market and Home Inspections
 - A. Housing affordability/record home sales for 2003
 - B. Reasons for a buyer to have an inspection
 - C. Buyer and lien holder protection
- II. Real Estate Agent referred Home Inspectors present an inherent conflict of interest.
 - A. Percentage of home inspection gained by agent referrals
 - B. Nature of referrals in any business or occupation
 - C. "Good" inspector vs. "Bad" inspector

III. The reasons why a real estate agent would refer a poor inspector to their buyer.

- A. Agent's vested interest in the sale of the home because of their commission
- B. Examples of different scenarios affecting the agent's commission
- C. Liability-indemnification of the referral by the inspector's insurance

IV. The reasons why an inspector would deceive their client or collude with the real estate agent.

- A. Market saturation with home inspectors
- B. Deal killers/catch 22 for the home inspector
- C. Too difficult to turn back/inspectors don't realize they are doing wrong

V. The reason why the general public has no knowledge of the growing problem.

- A. General public has no knowledge because of media cover up
- B. Vermont court case
- C. HouseMaster court case
- D. Home inspector exculpatory clauses

VI. Conclusion-Items that can be done to protect the buyer and the lien holder from falling victim to this often hidden problem of agent referred home inspectors.

A. Increased public awareness

B. State law prohibiting home inspector referrals from a real estate agent

C. Personalized awareness by my business

VII. Further Research

A. Independent Home Inspectors of North America

B. Home Owner's Against Deficient Dwellings.

ABSTRACT

According to the National Association of Realtors, the United States is on pace to have another record setting year in home sales and new construction. With a strong housing affordability index throughout the year, most families earning the median income could potentially afford a home with a price tag between \$177,000 and \$241,800. For most families their home purchase is the single largest investment of their lives and for some, it is their only investment. As with any investment, buyers of real estate look for some investment protection or a validation that they are making a wise decision. More often than not this is accomplished with the buyers hiring a home inspector. A home inspection can mean the difference between a sound investment and a "money pit" for the buyers.

While a home inspection is an excellent tool for the buyer to validate their investment decision and to learn about their chosen property, the process by which a buyer selects a home inspector can actually negate the effectiveness and purpose of a home inspection. In fact, many buyers are not even aware of the injustice served to them until well after they have moved into their dream home when deficiencies in the condition of the structure and the mechanicals are discovered and costly problems begin to surface. Unknowingly the buyers hired a home inspector who was not serving their best interests because they hired an inspector recommended by the real estate agent, the same agent who has a vested interest in the sale of the home.

This document discusses the inherent conflict of interest that exists when a real estate agent recommends a particular inspector to the buyer. The primary goal of this document is to convince you, the reader, that in order to provide a needed layer of investment protection for the buyer, a state law must be enacted that prohibits people with a vested interest in the sale of the home, specifically a real estate agent, from recommending a particular inspector to their client (the buyer). To convince you of this growing problem, the ensuing document uncovers the problems that exist with agent referred home inspectors by identifying the reasons why an agent would refer a poor and unqualified inspector to their clients (the buyers) and by identifying the reasons why an inspector would knowingly deceive their client and collude with the real estate agent. This document also identifies some recent court cases in which the problems with agent home inspector referrals are brought to the public's eye adding credence to the growing but often hidden problem.

Real Estate Agent Referred Home Inspectors: Buyer Protection or Buyer Deception?

Background on the Real Estate Market and Home Inspections

According to David Lereah, chief economist for the National Association of Realtors, in the first half of 2003 the housing affordability index experienced the highest levels in thirty years with a slight drop for the third quarter (U.S. National-Reuters). The housing affordability index measures the ability of a family earning a median income to buy a home at the median price, with an index of 100 meaning that a family of median income has the amount needed to purchase a home at the median. Indices over the 100 mark mean that a family has more than enough money to purchase a median priced single family home. The index for the first half of 2003 was 143.8, falling to 136.6 in the third quarter. The median income for a family in the third quarter was \$53,641 and the median priced starter home was \$177,000. With an affordability index of 136.6, the median income family had more than enough money to afford a home over the median price. In fact, according to the National Association of Realtors, "A family earning the median income could afford a home costing \$241,800" (U.S. National-Reuters).

While the index has slightly fallen for the third quarter of 2003, Lereah states, "The index is about the same as it was for all of last year, which was a record year for sales" (U.S. National-Reuters). What does this mean? Our nation is on track to have another year of record home sales and buyers are purchasing homes costing well above the median priced home. If buyers are purchasing a home within the parameters of the housing affordability index, in all likelihood, they will purchase a home with a price tag between \$177,000 and \$241,800. For most buyers, an investment of a quarter of million dollars could tag the purchase as the single largest investment of their lives, an investment so large that some people may argue it goes against the financial planning principle of diversification because for many it is their only investment.

With such a large investment, it is recommended that each buyer hire a home inspector to inspect the home prior to closing the deal. Many real estate agents will recommend that their clients have an inspection not only for the client's protection, but also to pass the liability from the agent to the home inspector if a problem were to be uncovered after the buyer moved in. Some lending institutions and insurance companies are also requiring that a home inspection be completed prior to closing, especially for first time homebuyers. Regardless of the reason, a home inspection is a wise decision because in most cases it is the only investment protection the buyer has, as the inspection can mean the difference between a sound investment and a "money pit" for the buyer. The inspection can also be used as a tool for the buyer to negotiate a lower purchase price,

used to render the offer to purchase contract void if structural or safety problems are identified, or used in the budgeting for future repair, replacement, and maintenance of structural and mechanical components.

Unfortunately, most buyers are not aware of the significance or importance of a home inspection, and they often view the inspection as just one more necessary step in the buying process when, in reality, it is the single most important event in the buying process. It is the only event in which the buyer (and lien holder) receives critical information regarding the soundness of their investment; information that can validate the buyer's decision to purchase their chosen home or to continue in their search to find a more structurally and mechanically sound home. With the need for this critical information, it is imperative for the buyer to choose an inspector who is licensed, insured, qualified, and independent so that the buyer can get a thorough, detailed report on the condition of the structural and mechanical components of the home.

Ensuring that a contractor or a provider of professional services is licensed, insured, and qualified may be fundamental to any person seeking help on a project or even a buyer searching for an inspector, but a buyer may question the relevance of hiring an inspector that operates under the realm of independence. Unfortunately for the buyer there are not many inspectors who claim independence and because of this, a significant problem exists in the real estate market because buyers (and lien holders)

may not be getting the investment protection they thought they were getting or the protection they need in a society where each is for their own. This is specifically where the problem lies because a majority of the home inspectors chosen by the buyer are as a result of a referral from the real estate agent, a person in the contract who has a vested interest in the sale of the home. An independent inspector believes that it is unethical and presents a conflict of interest for a real estate agent or any party with a vested interest in the sale of the home to refer a particular home inspector. As the owner of an independent inspection company it is my intent to demonstrate this conflict of interest and to demonstrate the need of establishing a state law in Wisconsin that would prohibit parties (specifically real estate agents) with a vested interest in the sale of real estate from referring home inspectors to potential buyers to add a layer of needed investment protection for the buyer and the lien holder.

The Problem With Real Estate Agent Referrals

The American Society of Home Inspectors is one of the nation's oldest and most recognized home inspector associations. According to Rob Paterkiewicz, Executive Director for ASHI, "65 to 75 percent of their 7,000 home inspectors' business comes from recommendations and referrals from the real estate community" (Evans). These are staggering numbers and Paterkiewicz even admits that it is of concern to him and his association because, "...it is imperative that the referral carries no obligation with it" (Evans). Paterkiewicz's comments infer that there might be a problem and cause for

concern within the inspection profession because of the heavy reliance on referrals from the real estate community. Why the concern? A referral is a referral, right? Wrong, not when it comes from someone who has a vested interest in the sale of the product or service.

Many people rely on family and friends for referrals or recommendations on products and services. It is a natural reaction to ask people if they have tried this or that or to ask people what they think about a particular service offering. If a person has ever been to a doctor, they may have been referred to another doctor or specialist for additional treatment or therapy. Organizations around the world such as Business Network International (BNI) thrive on referrals. Passing over 2 million referrals in 2002, BNI generated hundreds of millions of dollars worth of business for its members (Business Network International). Similar networking organizations exist throughout the country, both at a national and a local level, playing an important role in the growth of small and large businesses. Even from an individual standpoint, people as consumers look to others to help them make decisions on products and services or to validate their purchase decision. Everyone wants a referral or recommendation in hopes that they will make a good decision or choose a good product or service provider. Referrals have become a part of our life, compounding the problem of real estate agent referrals, as you will see.

When a buyer signs the offer to purchase contract, he or she is often faced with a number of contingency clauses such as financing and the inspection. For most buyers, financing is already pre-approved through their lending institution so the financing clause is essentially a moot point unless something were to happen with the buyers income from the time the offer to purchase is signed up until closing. This leaves the inspection contingency, which in many cases the buyer has not considered or thought about until they are at the point in which the offer is written. It is at this juncture in the purchase process that the buyer typically turns to the real estate agent to see if they know any inspectors. Most buyers do not personally know a home inspector and because of our referral-based society and our reliance on networking, the buyer assumes that the real estate agent is giving them the name or names of good inspectors.

Unfortunately, this is the first fatal mistake made by many buyers. Due to the reliance on referrals and recommendations in our society, the buyer automatically assumes the real estate agent is looking out for the best interests of the buyers. Unknowingly to most buyers, the real estate agent is under contractual liability to the sellers, and is in fact working for the sellers unless a buyer's agency exists. Through personal sales techniques and tactics of the real estate agent, the buyer is often made to feel as though the agent is working for them and has a genuine concern for their welfare. While there is nothing inherently wrong with making people feel good and treating

them with respect, issues can be raised when these tactics are used only to fog the minds of the buyer and to downplay an important contractual obligation.

The second fatal mistake made by many buyers is that they do not recognize the looseness of the term "good". What may be good in accordance with one person's standards may not be for another person. The term "good" by a real estate agent may often mean an inspector who is not very qualified, does not do a very thorough job, or is in collusion with the agent because the inspector is not likely or even willing to uncover the structural and mechanical problems that may exist with the home. So in essence, what is "good" in the eyes of the real estate agent is in fact "bad" for the buyer. If the real estate agent said to the buyer, "I know a good inspector who is not qualified, who is not very thorough, and who will probably overlook a lot of the issues", the buyer would certainly choose to look elsewhere for their inspection needs. In reality, the buyers are not going beyond the recommendation of the agent because they honestly believe the agent is looking out for them and if the agent says he or she knows a good inspector, the inspector has to be the most qualified and thorough in the area.

Why Would a Real Estate Agent Refer a Poor Inspector to their Buyer?

The bottom line to the question of why a real estate agent would refer a poor inspector to their buyer is that the agent has a vested interest in the sale of the home. Real estate agents make their income from the commissions they receive on home sales. Most commissions range from 3 to 7 percent of the sale price of the home, with split commissions taking place when the listing agent and the selling agent are two different people. In most areas, the market is saturated with real estate agents, making it increasingly difficult and competitive for agents to get listings and to find buyers. In essence, the livelihood of any real estate agent depends on getting listings and most importantly, closing deals.

The problem for most real estate agents is that there is someone in the buying process that can tinker with their commission, either by reducing it or ultimately voiding the commission through a cancelled offer to purchase contract. This person is the inspector and while the inspector is not really the person that would void the contract or reduce the sale price affecting the commission, the inspector is giving the buyer the information that would be needed to do so. Consider the following scenario. A real estate agent is both the listing and selling agent for a \$150,000 home. A 7 percent commission would net this agent \$10,500 upon closing the deal. The agent advises the buyers to look in the telephone book and/or internet to find an inspector and the

inspector finds some major structural issues with the home. The buyers are not satisfied with the findings and elect to void the contract and continue to look at other homes. The agent has just lost \$10,500. In the same scenario, the buyers decide to negotiate a lower purchase price as a result of the inspection. The new sales price is \$135,000. The commission to the agent has now been reduced from \$10,500 to \$9,450 and the seller is unhappy with the agent because an inspector was hired by the buyers that found all of these problems. The agent will probably not get any listing referrals by this seller from friends and families.

Consider the next scenario. The same agent is the listing and selling agent of a \$150,000 home. With a 7 percent commission, upon closing, the real estate agent would net \$10,500. Having a family of his or her own, a mortgage, bills, and after just losing out on a previous deal due to an inspection, the real estate agent decides he or she is going to recommend an inspector to the buyers, an inspector that is either not qualified, not very thorough, or in collusion with the real estate agency in order to ensure that the deal will go through. The real estate agent asks some probing questions of other agents in his or her office, receiving the names of some "good" inspectors. The agent even offers to call the inspector and set up the inspection appointment for the buyers. The inspection goes well, no issues with the home, and the agent gets full commission. Having just rebounded from the blown deal with the last inspector, the agent finds that it made his or her life much simpler by having the

buyers use the agency's preferred inspector or their so called "good" inspector. More importantly to the agent, his or her commission was not affected.

People may argue that behavior of this nature by the real estate agent could make them susceptible to a liability suit if some material defects were uncovered after the buyers moved in. This is a valid point however it is interesting to note that many providers of Errors and Omissions Insurance for home inspectors, such as The Foundation for Real Estate Appraisers, provide indemnification for the real estate agent in a referral situation (FREA). The indemnification limits the liability of the real estate agent by placing any liability that stems from the inspection on the policy of the home inspector. This is one reason that many real estate agents and agencies prefer to recommend inspectors with Errors and Omissions policies versus those that do not. Unfortunately, the cause for the favoritism towards an inspector with Errors and Omissions insurance is not for the buyer's protection but for the real estate agents protection.

As previously mentioned, there are some areas of the country in which buyer's agency exists where there is a buyer's agent with a buyer's representation contract. In this contractual arrangement, the agent representing the buyer is someone other than the selling or listing agent. In these types of contracts there is some hope that the agent, if referring a home inspector, is recommending the most qualified, most thorough

inspector in the area. Dennis Robitaille, Executive Director for the Independent Home Inspectors of North America, sheds a shadow of doubt on this as he states, "They (buyer's agents) are not recommending the best guys, because they don't get paid if the deal doesn't go through" (Evans). In other word, even under contractual obligation to the buyer in a buyer's agency, the buyer may not be getting the investment protection they need.

Why Would an Inspector Deceive the Client (Buyer)?

Taking a look at the home inspector listings in the yellow pages of the telephone book or any home inspection site on the Internet would show observers that many markets are saturated with home inspectors. Currently 27 states have licensing laws for home inspectors, which tends to eliminate those inspectors that may have been providing inspection services on a part time basis. Licensing tends to reduce the number of practicing home inspectors but it does not produce an elite group of professionals as each state has its own credentialing requirements that run the gamut in regards to difficulty and the knowledge needed for an inspector to become licensed. For the states with no licensing requirements, markets can be saturated with all kinds of service providers posing as home inspectors with no control by a regulatory agency.

Regardless of the licensing requirements, every market is full of inspectors. With or without licensing, there are issues with buyers being restricted of access to the best inspectors with the dominance of referrals by real estate agents.

Due to market saturation there is significant competition among inspection companies. With close to 70 percent of inspection business coming from real estate agent referrals, most inspection companies direct their marketing campaigns towards the real estate agents and their agencies. For anyone that is or has been in sales or marketing, directing marketing efforts towards the real estate agents appears to be the most logical way to gain business from a cost and productivity standpoint. The real estate agents have direct contact with the potential customers of the inspectors, the buyers. This is a very low cost and easy marketing approach for the inspector because it only takes a little time and perseverance on the part of the inspector to get his or her name out there in front of the real estate agents and agencies. Unfortunately most home inspection businesses get their business in this manner and the problem with this marketing approach is that there is a catch.

The catch with marketing directly to real estate agents is that it can cause the inspector to lose sight of his or her customer. A "deal killer" is a term used in the real estate market to tag an inspector as a person who is nit picky or thorough in their inspection techniques. As mentioned earlier, real estate agents make their money by having deals go through. As Dennis Robitaille, Executive Director of the Independent Home Inspectors of North America, states, "there's only so many agents out there who are going to put up with losing deals" (Lewis). If an inspector kills a deal or causes the

purchase price to be renegotiated, thereby eliminating or decreasing the agent's commission, the agent in all likelihood will discontinue referring that particular inspector and potentially let other agents know that the inspector is a poor inspector.

Unfortunately, the inspector is coined a poor inspector, not because of his or her capabilities and expertise, but because the inspector was too thorough and killed the deal.

When an inspector is labeled as a "deal killer" it can potentially spread throughout the local market especially among the real estate agents, greatly affecting the inspectors business. If an inspector has built his or her business on agent referrals, he or she will find that business will take a serious turn for the worse, as the phone will stop ringing because the agent referrals stop. With this in mind, the inspector quickly loses sight of his or her customer because it becomes a battle of pleasing their customer (the buyer) and also pleasing the agent. Unknowingly to the buyer, the inspector will attempt to gloss over items of concern during the inspection or blatantly look over items so as to not rock the boat with the agent. Unfortunately, it is not until the buyer moves into the home that they realize they did not receive a good home inspection.

As the owner of a home inspection business, I can honestly say that deciding who to work for, the agent or the buyer, is a decision most home inspectors are faced with early on in their business. When I first started my business, I solicited agents for

referrals. As mentioned previously, agent referrals make the most sense from a marketing standpoint and most inspectors get their business this way. Fortunately for my business and my customers, I was able to see the true light when it came to agent referrals. On many occasions I was asked to provide a favorable report and I had my clients distracted during the inspection by the agent so they could not talk with me. I also found myself worried about putting on a good performance for the agent because I was concerned about getting the next inspection referral from that real estate agent. I quickly learned that I was not giving 100% to my customers by trying to also focus on what the agent thought of my business and the inspection. From an ethical standpoint, I found this to be incredibly off target, as my undivided attention and focus should be with my customers, the ones who are paying me. By quickly realizing this, I was able to reverse the direction of my business and direct the loyalty of my business to my customers by declaring my independence of agent referrals and directing my marketing efforts in an ethical manner.

It is also important to note that most states that have some form of licensing or credentialing for home inspectors have adopted a code of ethics and/or standards of practice for its licensees. For those states that do not have licensing requirements, inspectors often join inspector associations to separate themselves from the general inspection community. These associations such as the American Society of Home Inspectors (ASHI), the National Association of Home Inspectors (NAHI), and the

National Association of Certified Home Inspectors (NACHI) also adopt standards of practice and a code of ethics for its members. In fact many states have adopted the ASHI code of ethics and standards of practice into their own licensing laws. In most code of ethics declarations by the associations and regulatory agencies, one of the most important declarations is that the member act in good faith towards the client (American Society of Home Inspectors). For an inspector to accept agent referrals and steer the direction of the inspection so as to not rock the boat with the agent or as some might say "to step on the commission hose of the agent" would be in direct violation of the code of ethics of many of these associations.

Unfortunately, many inspection businesses and their inspectors will deny any claims of collusion with an agent or that they attempt to sugar coat problems with the home. The problem stems from the fact that they have become so intertwined in this problem that they do not realize they are doing it. If they do realize they are doing it, they are too afraid to change because if they did, the bottom line of their business would change so drastically, they may find themselves bankrupt or out of business. It would be difficult for anyone earning a six-figure revenue to lose over half of this in period of a couple of months. This is what home inspectors enjoying a good lifestyle and an easy job are faced with when they become comfortable soliciting agent referrals. It is too difficult to turn away, they lose sight of who their true customer is, and the buyer is sucked into purchasing a home with many problems.

Are Agent Referrals Really That Significant of a Problem?

Many people will often comment that if real estate agent referrals were such a huge problem then the media would have certainly brought the issues to light. It is a huge problem but a person only has to open the newspaper to see all of the real estate agent home listings. Real estate accounts for a large amount of the advertising revenues for many publications. They are not going to expose a problem in the real estate market when it could jeopardize their income. Real estate associations, such as the Wisconsin Realtors Association, also pump large amounts of money into the state government with their lobbying efforts. As a matter of fact, the attorney for the Wisconsin Realtors Association is a member of the state licensing board for home inspectors (WI Department of Regulation and Licensing). This presents another ethical problem in my opinion, but that argument should be saved for another project.

In reality, there have been a few recent court cases that have exposed some of the problems with real estate agent referrals and the collusion that often results when an inspector establishes a relationship with an agent. In Montpelier, Vermont a couple received some relief from the Vermont Supreme Court in March of this year, allowing them to get the names of former clients of the defendant, their inspector who they have charged with breach of contract. The case began in 1997, when the homebuyers,

Sylvia Covington and Paul Schmitt, were shown a home for sale by a real estate agent, Ann Swanson in East Corinth, Vermont (Allen). Upon the signing of the offer to purchase, the agent recommended that they contact Richard Lalancette to complete the inspection. In their suit, Covington and Schmitt said, "Lalancette's inspection failed to identify serious structural flaws in the house" and "they also claimed Lalancette had colluded with Swanson" (Allen). The plaintiffs argue that Lalancette was "motivated not to issue unfavorable reports that would prevent real estate closings" (Allen). They also claim that the inspector was "motivated by a desire to continue receiving referrals" from the real estate agent (Allen).

Another recent court case was decided on March 11, 2002 in the Appellate Division of the New Jersey Supreme Court. The plaintiffs, Steven and Gina Herner, instituted a suit in May 1996 against HouseMaster alleging negligence and consumer fraud against them in an inspection report issued to them in May 1995 (Plaintiffs vs. HouseMaster). The Herner's received \$37,000 in compensatory damages in November 1997, but sought a settlement under the Consumer Fraud Act in addition to the money initially awarded to them to repair the items the inspector for HouseMaster had overlooked. The focal point of this particular suit is not the expertise or qualifications of the inspector but the manner in which the inspector gained business and how the inspector provided a report on the condition of the property.

HouseMaster is one of the nation's largest home inspection franchises in North America. In this particular case, the franchisor of HouseMaster, Kenneth Austin, was required to testify and the marketing materials of the franchise were subpoenaed. It was found that HouseMaster franchisees rely on real estate agents for approximately 80% of their business and they are trained to provide a "balanced" report. Undisclosed to the consumer,

HouseMaster's marketing and training strategy emphasizes rendering a "balanced" report which stresses the positive aspects of a house, as well as the negative in such a way as to water down negative findings such that a consumer will have as little basis as possible to call the sale off or have solid evidence upon which to renegotiate the price. (Plaintiffs vs. HouseMaster)

In fact, the case also discovered that HouseMaster trains their inspectors to hide their relationship with the Realtor and act as if they do not know the agent. In this case it was determined that "HouseMaster's system of home inspection resulted in a report to the HERNERS which was so balanced as to render it pabulum and worthless" (Plaintiffs vs. HouseMaster).

A person could argue these are only a few cases and thousands of inspections are completed every day in the United States by inspectors referred by real estate agents. This is true, but many cases do not come to fruition because of exculpatory clauses

inspectors write into their reports. One such clause that is common in inspector reports is:

Notwithstanding the provisions of any applicable statute, the sole and exclusive remedy available to the Client is damages in an amount not to exceed the fees actually paid by the Client for services, and all other remedies, statutory or otherwise, are hereby expressly waived by Client. (Kass)

As Benny Kass writes, "our legal system permits parties to enter into such contracts, subject to certain limitations." The buyer hires a home inspector and has the inspection completed, only to find the exculpatory clause at the end of the report. Not only does the clause limit the liability of the inspector by placing limits on the damages the buyer can seek from the inspector but it also convinces the buyer that is all they can get back if the inspection goes awry. While this is not legal in Wisconsin, I personally know many inspectors throughout the country who have exculpatory clauses and freely give back the inspection fee if there are questions on the integrity of the inspection. Upon return of the fee the inspector will also have the buyer sign a waiver of responsibility for future claims.

There's a Problem. What Can Be Done?

Most importantly, the consumers (the buyers) have to be educated on this growing problem with real estate agent referrals. As a member of the Independent Home

Inspectors of North America, I believe that it is unethical for a real estate agent or any party with a vested interest in the sale of the home to refer a particular home inspector and I will strive at all times to further the general public's awareness of this huge but intentionally kept hidden problem (Robitaille). I believe it is my duty not only to educate my customers of this problem but to also let everyone I come into contact with, home buyer or not, know and understand this problem as well. Unfortunately, the severity of the problem tends to land on deaf ears unless it is a victim of this costly problem.

The best means to combat the growing problem is to establish state laws that prohibit parties with a vested interest in the sale of the home from referring home inspectors.

There is only one state that has such a law and that is Massachusetts. Under this law,

Real estate brokers and salesmen may not directly recommend a specific home inspection company or home inspector unless representing the buyer as a buyer's broker. Brokers, however, may provide assistance to buyers in accessing information on licensed home inspectors. (Board of Registration)

In other words, real estate agents can only provide a list of all of the licensed home inspectors to their clients. In this situation, the process of finding a qualified home inspector is put into the hands of the buyer, enabling them to make the decision of who they would like to have complete their home inspection by making some calls and interviewing home inspection companies. Ken Bates, a Massachusetts' home inspector comments about the law saying, "it's taking away business from the favorites of the

broker” and “his phones have been ringing more since the law was enacted because it’s harder for agents to blackball him” (Lewis).

Conclusion

As a member of the Independent Home Inspectors of North America not only is it important for my business to uphold the ideals of the association but it is important for my business to further consumer awareness of the problem and push for the enactment of a similar law like the one in Massachusetts. Considering that a state law could conceivably be a difficult battle and not likely to happen overnight, it has been most important for me to let those in my circle of influence know the nature of the problem and educate them on how they can avoid falling victim to the fallout that is common with an agent referred home inspector. For me personally, my criticism of agent referred home inspectors is not necessarily a ploy for buyers to use my business for inspection needs as I always encourage people to talk to family and friends to find the best inspector. I also always recommend they do their homework and do some research on the local inspection companies. Find out where they get their business from, if they have insurance, what kinds of tools they use, are they staying abreast with technology, what associations do they belong to, and do they back up their findings and reports? These are the things anyone would ask of any contractor or tradesman. Why should it be any different with a home inspector? Why would anyone rely on an inspector that a real estate agent says is, “good”.

For further information on the Independent Home Inspectors of North America I encourage you to visit their website: www.independentinspectors.org. Information regarding problems with inspection companies and builders can be obtained at the Home Owners' Against Deficient Dwellings website: www.hadd.com.

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