

RealEstateNews

INFORMATION TO HELP YOU WHEN BUYING OR SELLING | July 2024 |

Vested Interest Identifying conflicts of interest

By Peter O'Malley, author of *Inside Real Estate*

In this
Issue:



page 1

Vested Interest
Identifying Conflicts
of Interest

page 2

How's the Market
Upward Trend Continues

page 3

Vested Interest
continued

page 4

What Do You Want From
Your Real Estate Agent?
Sales Career Opportunity



In any financial transaction where substantial sums of money change hands, there is always a high probability some of the parties involved are afflicted by a 'conflict of interest'.

In the real estate industry, conflict of interest is apparent in nearly every transaction that takes place, whether it's a rental apartment, the sale of a house or a strata manager sourcing the best insurance option on a block of apartments.

Just because a potential conflict of interest exists, it does not mean the relevant parties will be compromised. But they could be - and that's the reason it pays to identify any areas of conflict of interest.

Below are some common examples where conflict of interest exists and how they can easily impact on the counterparties.

The buyer has another property to sell, locally

An agent's fiduciary duty lies with the person paying them, the vendor.

However, a potential buyer may say to the agent something to the effect, 'if you can help us get this one, you can have ours to sell'. Suddenly there is a potential conflict of interest at play. If the agent can get that buyer across the line, they make two sales rather than one.

Continued page 3

How's the Market

Upward trend continues

By Peter O'Malley, author of *Inside Real Estate*



The property market faced some negative data during May but prices continued to trend up.

Unemployment and inflation both rose, with the RBA now pondering whether another rate hike is required.

Given the RBA meet every 6 weeks now as opposed to the first Tuesday of the month, they have to make the crucial call at their June 17-18 meeting or wait until early August.

Economists believe they will sit on the fence in June and reassess in August, by which time everyone is hoping the inflation trend has broken to the downside.

If inflation is indeed trending upwards in a sustainable fashion, waiting until August could be damaging. It's worth noting two points about the RBA Cash Rate of 4.35%.

It is one of the lowest in the developed economies and Australia now has one of the highest rates of inflation in the world over the past 6 months.

Most other developed economies are experiencing disinflation.

The Federal Budget in May had some inflationary measures and personal income tax cuts will add further inflationary pressure to the economy.

None of the above seems to be bothering determined house hunters though. Inspection numbers remain healthy, bids per property is sufficient for competitive bidding in many campaigns and prices are improving, albeit modestly across the board.

Given stock levels tend to decrease during winter, the trend of modest price growth will continue.

A possible rate hike in August combined with a surge in stock levels for the spring market could easily see the equation change quite quickly for vendors.

The premium/prestige end of the housing market is still the best performer whilst apartments with strata title building issues are under pressure.

Low rise, older established apartments with modest strata levies are most appealing to first home buyers, whilst downsizers are supporting demand for quality lifestyle apartments at the upper end.

Those entering the market as buyers will quickly learn the pricing of properties during marketing campaigns is all over the place.

To highlight the confusion, if you consider two \$2.5 million properties that go to market with different firms.

One firm will quote the obligatory 10% below the reserve price, meaning their Guide is \$2.25 million or thereabouts.

The second firm then prices their \$2.5 million property with an auction Guide of \$2 million.

The same buyers inspect both properties and tell the first agent their price guide is too high, based on the competitor's guide for a similar property.

Auction clearance rates were hovering around 50% over the past month.

The clearest example of properties being underquoted in contravention of the Underquoting Guidelines for agents, is when an auction passes in by more than 10% above the agent's auction guide.

To increase integrity in agent's pricing, the Dept. of Fair Trade should be investigating any failed auction campaign where the property passes in by more than 10% above the agent's price guide.



The existence of this subtle inducement to the agent and how they handle it may never be known to the vendor. Make no mistake though, a version of this occurs every week in the property market.

The developer promises the agent the resale

To get access to the best opportunities, developers and flippers will tell agents, 'if you can find us something to renovate or develop, we will give the resale back to you'.

Suburbs that have undergone rezoning in recent times are prime candidates where this type of arrangement takes place.

Agents hunting sites on behalf of developers, but being paid by the vendor, is beyond conflict of interest, it's essentially a form of insider trading. If an agent approaches you with the offer of an off market buyer for your development site, tell the agent the commission payable by you to them, is \$0.

Then, go and get independent professional advice. When it comes to selling development sites, understanding rezoning and planning changes, the seller cannot afford to pay an agent that is working with the buyer.

Strata managers

The conflict of interest that exists in the strata space has made National news in recent times. A strata firm is under investigation for potentially using their wholly owned insurance subsidiary to insure strata title schemes, without disclosing the fact.

A reasonable person who concedes a company systematically awarding business to itself through an undisclosed, wholly owned subsidiary company is the epitome of 'conflict of interest'.

Furthermore, it is alleged the strata firm took commissions 3 times the industry average, for sourcing the insurance company in question, even though it was a wholly owned subsidiary they awarded the policies to.

In the words of the investigative journalist who broke the story, the insurance arm charged 'eye watering brokerage fees, without disclosing the fact to the owners in the strata's financial returns'.

The strata manager also allegedly took kickbacks from tradespeople for providing them with work orders.

The problem with this is the strata manager is already employed and paid by the owners of the respective strata plans, to find the best contractors and tradespeople.

If this accusation is proven, the strata manager is highly conflicted given they are taking two payments (one underhanded) for doing their job.

In fairness, it should be pointed out these are accusations at this stage and they are being investigated by an independent auditor. The example highlights the risks in the sector though.

Strata managers and property managers may not have the high profile status that high performing sales agents have. But strata and property managers do distribute

an immense amount of work to tradespeople, insurance companies, handymen and service providers such as electrical appliances and contractors.

Wherever there is a continual flow of work being distributed, there is a possible conflict of interest at play.

Property managers (PM's)

PM's constantly have to work through conflicts of interest. One of the most common is the multi property landlord whom does not wish to fulfil their obligations and/or maintain their properties.

The tenant may be quite rightly complaining to the property manager, but the property manager is concerned about holding their client to account, lest they lose the client's portfolio.

Another contentious area is rental references.

The agent may have a tenant that is constantly late with the rent and does not look after the property as they should. One day, the property manager gets a call from another agency stating the tenant in question has made an application for an apartment.

The agent chasing the reference wants to know - 'are they a good, reliable tenant?'

If the tenant leaves, the original agent can find a more reliable tenant. If they tell the truth about the tenant's non-performance in certain areas, they may not get the subject property and decide to stay put.

The agent suddenly has a conflict of interest they didn't have before that phone call came in.

Building inspectors

It is now customary for vendors to provide the due diligence reports upfront. On the whole, this has been a good initiative because it has saved multiple buyers collectively spending thousands of dollars on reports for the same property.

These reports are usually ordered and coordinated by the selling agent. Therefore, the agent becomes the consistent conduit between the building inspection firm and the marketplace.

Without meaning to, the building inspector faces a moment of truth if and when they find issues at the property.

If they go overboard in the written report, the agent may not continue providing them work. Conversely, if this is not highlighted, the report lacks credibility and could come back to haunt the building inspector.

The above list is by no means an exhaustive list of where conflict of interest exists in the property market. It merely demonstrates the need for consumers to remain vigilant at all times.

Being oblivious to a potential conflict of interest means you are unintentionally one step closer to being exploited. By staying aware and alert, you can follow the respective transaction through to a successful conclusion.





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