

# Real Estate Agent or Real Estate Investor?

[On behalf of Dornish Law Offices, PC](#) | Jun 21, 2014 | [All, Real Estate Practice](#)

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The old adage “If it walks like a duck and it quacks like a duck, it’s a duck” might as well be the title of this article, since most of what I am about to tell you is aptly covered by that adage. Real estate investors are often told by experts and gurus that they can engage in activities, or build whole businesses around conduct which, at least in Pennsylvania, is within the description of the practice of real estate, and requires a real estate agent’s license and affiliation of the agent with a real estate broker.

National speakers do not know this law, and do not recognize that its violation in Pennsylvania is criminal, subject not only to substantial fines for each and every errant transaction, but even to prison time for violations of the law, regardless of whether the expert told you what to do or you did it on your own, without criminal intent, in blissful ignorance. I could make more money as a lawyer if I let you proceed in blissful ignorance, violating the law and incurring the risk of big fines and penalties for your actions, and then tried to defend you later, negotiating with the Attorney General’s office to reduce the large fines and avoid the jail time. But I make a good living as an investor, and have a busy law firm already, without more of these cases.

I do have cases for several investors right now, fighting against investigations and actions brought by the Real Estate Commission and the Attorney General’s Office alleging the unlicensed practice of real estate and illegal contracts with consumers, causing the Consumer Protection Bureau to seek money back from the investors for those consumers. I want to give you the information to keep you from becoming another one of those investigations, so you can make money, and I can make money drafting contracts, doing closings, fighting to lower real estate taxes and forming entities instead of defending suits against you.

Now that I have your attention, the burning question is “what activities can bring these investigations and actions down on me, and what can I do to avoid these problems?” First, if you have been told to consult with buyers or sellers of real estate to bring them together, and to collect a consulting fee on the HUD-1 for the sale, or even off the HUD-1, don’t do that ever. I

recently reviewed a form of consulting agreement given to its franchisees by a national real estate investing franchisor, which puts up billboards all over Pennsylvania, looking for cheap houses to buy. The form document used in hundreds of transactions for over a decade absolutely positively violates the Pennsylvania Real Estate Licensing and Registration Act, which I will hereafter refer to as RELRA. The franchisee can't sue in PA courts to collect fees under that agreement, and faces fines and jail time for each time they used the contract if investigated and prosecuted.

Consulting with real estate buyers and sellers to find buyers for properties, or properties for sellers, and negotiating the terms of the agreements between them is either the practice of real estate, requiring a real estate license, requiring all fees to be collected through a licensed real estate broker, 63 P.S. Section 455.201, or it is the practice of law, requiring a law degree and passing the bar exam.

Even licensed real estate agents can't just charge a direct consulting fee payable to themselves personally for services bringing buyers and sellers together, without running the transaction and fees through their broker's company, and sharing the fees with the broker. You would think this is obvious, but I now see one of these transactions every few months and have to tell the buyers and agents involved that the agents can lose their licenses and even face criminal charges for that conduct. 63 P.S. Sections 455.301 and 303.

What about tying up a group of different properties by signing agreements of sale or options to buy them? If an investor does that as part of a plan to buy a significant number of the properties under contract or option, actually buys many of the properties on which agreements or options were obtained, and then has left over properties the investor can't use him or herself, that activity to dispose of the leftover properties is very defensible as part of an investing business.

However, if the actual business is to market all of the properties under agreement as available for sale to third parties, and the investor intends not to buy the properties, but to assign the contracts or options to others and collect a fee or commission on the sale of the properties to the end buyer, the business walks and quacks like a real estate brokerage, not a real estate investment business. The investor is really practicing real estate without a license, and is liable to being prosecuted for that activity.

Finally, keep in mind that the practice of real estate in Pennsylvania includes not only activity assisting others in buying and selling properties,

but activity in helping landlords to manage and rent, and tenants to find and rent real estate as well. Many national real estate investing gurus have come to Western PA and marketed turnkey programs to their out of state buyers to buy properties here. They have indicated that they can find, negotiate for purchase, help to close, plan for and complete renovations, and then rent and manage the properties for the out of town investors. Not only are the finding and negotiating agreements on those properties the practice of real estate, as indicated above, but the management and rental activities also violate the PA RELRA. 63 P.S. Section 455.201(3).

Now that you know what you cannot do as a Pennsylvania real estate investor without violating RELRA, I'm sure many of you are wondering what you can do as a real estate investor in Pennsylvania without a real estate license. First, you can always buy property and resell it. However, remember that PA has a wet funds rule for closing, which means you can't do an "A to B to C" transaction with you in the middle as B, if you don't have the money or credit available to buy from A before you get the money from C.

Unless the seller of the property you are buying has restrictions on time or amounts for resale in their deed, as Fannie Mae does, or in their contract, as many REO companies do, you can even do both closings one right after another. Even the title company for which I am an agent allows me to close these transactions back to back, as long as both closings are separately covered by title insurance. No matter how many times you buy and resell properties, you are not acting as a real estate agent, since agents never do that. You don't have to tell the seller of the property you are buying that you plan to resell the property for a profit, but if you are trying to sell a property you have an option or a contract to buy, you have to tell the buyer that you control but don't yet own the property you are selling. To do otherwise is a blatant misrepresentation of what you have and what you can sell. The right forms can really help you to do this.

It is not yet illegal in Pennsylvania to assign a contract or an option which is assignable, or to take a fee based on the value of the assignment in an incidental transaction. However, if you try to make a business out of doing this over and over again, the original options or contracts misrepresent your intent to the sellers, and if the sellers are consumers, the Attorney General's Consumer Protection Bureau will be interested in that misrepresentation. The Real Estate Commission will also be interested in your business. The PA Department of Revenue is also interested in the

assignment, since the assignment is considered a separate transaction in real estate, subject to a second set of transfer taxes.

If you are not making a lot of money on the transaction, so you don't want to pay for a second title insurance policy and closing, deed and recording, you can still differentiate your transaction from a real estate agent earning a commission from a seller for bringing a buyer, by charging a release fee instead of a fee for assignment. Suppose you are buying a property for \$20,000 and selling for \$25,000.00. Doing a whole closing in an "A to B to C" transaction would cause you to put money into the property and pay costs eating into your profit.

However, you can go to the willing seller and tell them you will let them sell to your buyer for \$25,000.00, and will release the seller from selling to you for a \$4,000.00 release fee. The seller can make an extra \$1,000.00 or so, you, provided they agree to sell to your buyer and pay you the fee. I make the release of the seller from the agreement of sale to you conditional on their selling to your buyer, so the buyer and seller are less likely to go around you. I send it to the closing agent for the transaction, so they are aware of the condition on the release, which then creates a cloud on the title only if that closing agent closes without paying you from closing.

If you are still focused on charging other investors consulting fees, you must have a written consulting agreement which clearly describes the activities on which you are consulting, and none of those services can be services which require a real estate license, a license to practice law, or any other professional licensure, registration, or certification, such as an appraisal, certain contractors' bids, or home inspection. Finding the right terms for a consulting agreement to dance between the various requirements of all such licensing and registration acts is a real minefield, and can easily lead to problems for the investor who does this. Just the term consulting fee on a HUD will invite investigation of the details of the agreement.

On the management side of real estate, you simply cannot manage property you don't own in Pennsylvania without being a REAL officer/employee of the owner. (Only five officers are exempt from being real estate agents). For many years, I have used the limited partnership/limited liability company general partner structure for my own rental properties, and advised it to my clients. You can use the same structure having your LLC own at least a 1% general partnership interest in each limited partnership which your LLC manages. Managing as an owner does not

violate RELRA, because owners are always allowed to manage their own properties.

Sometimes, if you are making money doing things which you later learn are against certain laws, and nobody has started an investigation or prosecution, you hesitate to quickly change your business practices and business model. You ask, how will anyone find me and my business, and start an investigation or prosecution? The simple answer is that real estate agents who have taken classes, passed tests, paid for continuing education, insurance and shared their commissions with their brokers resent you for taking away customers with whom they have spent time showing homes or making listing presentations. With good cause, they will turn you in for violating the laws which they know and follow.

Dissatisfied consumers who learn from your buyers or their former neighbors that you received more for selling their house than they did, buyers who learn they paid you more than you paid the seller, or family members who see the consulting fee to you on a HUD are also good candidates to make claims against you with the Bureau of Consumer Protection. The Real Estate Commission is actively looking for violators of RELRA to protect Pennsylvania owners from unlicensed, uninsured real estate consultants.

Finally, real estate investors who don't get paid and try to sue to enforce illegal contracts learn that they can't sue in court when they try, 63 P.S. Section 302. Worse, they bring investigations and prosecutions on themselves by trying to collect.

My advice to all real estate investors is to learn the laws applicable to your business, and follow them. It is far better to make less money on your real estate investing in a legal business, than to make more money on an illegal business and lose that money and more to fines, penalties, attorneys' fees, and even risk jail time!

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