

**REAL ESTATE AGENTS' TRUST ACCOUNT COMPLIANCE:**

**CONSUMER PROTECTION**

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**ABSTRACT**

*Licensing of property agents in Australia varies within each individual state and territory. The introduction of legislation aimed to regulate the property industry and to enhance consumer protection. An individual working in the property industry buying, selling, leasing and negotiating in property transactions must be either licensed or hold a certificate of registration under the relevant legislation. In New South Wales there has been a steady increase in fraud with agency's trust accounts. The aim of this research was to identify any trends contributing to trust accounting fraud in property agents' trust accounts. The purpose of the research was to undertake a 20 year data set document analysis of public records such as court cases and enforcement notices relating to the misappropriation of trust account funds. The findings identified a total of 140 instances of fraud, involving 171 individuals, with 84.80% of these individuals licenced, and 13.45%, holding a certificate of registration. A very small percentage, 1.75%, did not hold either a licence or certificate of registration. The various reasons for the misappropriation of trust funds included gambling, funds to operate the property agency business, personal debts, loan scheme scam, pre-drawing of sales commission, and funding legal expenses.*

Keywords: Consumer Protection, Fraud, Landlord, Property Agency, Real Estate Agent, Regulation, Trust Accounting, White Collar Crime

**INTRODCUTION**

The property profession in Australia encompasses property agents, and this includes real estate agents, business agents, rural agents, property and livestock auctioneers, and strata managing agents. Licensing of property agents in Australia is regulated under the auspices of individual state and territory Offices of Fair Trading. An individual working in the property industry buying, selling, leasing and negotiating in property transactions must be either licensed or hold a certificate of registration under the relevant legislation. Therefore, to enhance consumer protection, the legislation is accompanied with mandatory requirements for the keeping of trust accounts.

**Trust Accounting**

Trust Accounting has been identified as the recording, classification, reporting and analysis of all trust money received by a property agency on behalf of their client. Examples of trust money include deposits on sales, rent from tenants, bonds, prepaid advertising, prepaid auction fees, and strata levies. In addition to mathematical dimensions, trust accounting is also concerned with regulatory compliance. Hence, an agency's books and records must meet the provisions of the relevant legislation (Author, 2016). The legislative obligations placed on real estate agents can be enormous and time consuming. Ultimately, the licensee of the property agency is considered accountable for all trust money held on behalf of the property owner, tenants, purchasers and other stakeholders with a vested interest (Author, 2016).

However, with the documented increases in trust accounting fraud there is a clear need to enhance consumer protection in the property industry (Office of Fair Trading, 2008b). Government appears to indicate

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acknowledgement of the large sums of money involved in real estate transactions, particularly in regards to the sale and purchase of property. The licensed property agent will hold a percentage of the property purchase price in their trust account. In other words, this money is held “in trust” on behalf of the vendor and purchaser. Therefore, the safe keeping of these monies held in trust and the level of competence by the people who supervise this money requires an ethical code of conduct to preserve and enhance consumer protection. As consumers engage in property transactions relatively infrequently they have limited knowledge of the property industry sector. A risk management objective of the legislation in NSW has highlighted the need for the correct handling of trust money, and the licensing regulation is regarded as an important way of protecting consumers (Office of Fair Trading, 2008b). In summary, all property agents throughout Australia, are required to hold clients’ money in a trust fund for the exclusive benefit of their client

### Property Services Compensation Fund in NSW

In order to strengthen consumer protection, under the Property, Stock and Business Agents Act 2002 (PSBA Act 2002), in NSW, the Property Services Compensation Fund (PSCF) was established to provide financial compensation to people whose money had been misappropriated by a licensed property agent. For instance, for the purpose of reimbursing landlords, tenants, vendors or purchasers who have suffered financial loss due to a licensee failing to correctly account for funds held in the trust account of the property agency. Prior to this legislation, compensation was maintained by the Real Estate Services Council.

Whilst the government acknowledges this important aspect, and the compensation fund provides a mechanism for financial compensation, this is not to be considered a replacement for integrity, ethics and accountability for the property agent professional. Research undertaken over a decade ago also identified risk relating to trust accounting could be associated with a “lack of knowledge of trust accounting”, “failure to have proper financial systems in place to monitor and review trust accounts regularly”, “failure to monitor the actions of staff” or to “comply with audit requirements and fraudulent conduct” (Office of Fair Trading NSW, 2008b:56 The Report).

Each year the Office of Fair Trading, NSW, receives consumer complaints associated with the property services industry. During the last two decades, the complaints from consumers include issues relating to fraud occurrences, duty of care, negligence, and mismanagement of their clients’ financial requirements. However, this research paper is primarily focused on trust accounting fraud in New South Wales. In NSW, for the financial year ended 30<sup>th</sup> June 2003 there were 35 claims totalling \$362,400 against the compensation fund. However, this dramatically increased for the financial year ended 30<sup>th</sup> June 2007 to 264 claims totalling \$918,906 against the compensation fund. In the financial year ended 30<sup>th</sup> June 2016, there were 255 claims totalling \$2,400,000. The table below sets out the increases in monetary value of fraud claims from 2003 to 2007 inclusive, and for the 30<sup>th</sup> June 2016 financial year. The years in between those dates were not reported in the annual reports for Fair Trading, and similarly between 2017 to 2020. A limitation of the data in Table 1 is related to the data collection process. In this regard, the Office of Fair Trading NSW does not report the value of *each* individual transaction involved in trust accounting fraud. Therefore, the *total amount paid* column in the table below, is the accumulated compensation for each financial year. The *number of claims* represented for this accumulated figure, is identified in the last column.

**Table 1: Statutory Compensation Fund Claims in NSW**

At 30 <sup>th</sup> June	Total Amount Paid \$	Number of Claims
2003	362,400	35
2004	763,524	276
2005	751,196	146
2006	1,024,096	82
2007	918,906	264
2008 to 2015	Data unavailable	
2016	2,400,000	255
2017 to 2019	Data unavailable	

Source: Author: Compiled from *The Report - Statutory review of the Property, Stock and Business Agents Act 2002*, Chapter 12 (Office of Fair Trading, NSW, (2008b) and *Individual Annual Report 2016*

The Report, referenced above in Table 1 also estimated that approximately \$1,089 billion trust moneys were held by property agencies for the financial year ended 30<sup>th</sup> June 2007. Over the years, the Office of Fair Trading NSW has undertaken a number of reviews with regards to the PSBA Act 2002. In 2008 a statutory review of the PSBA Act 2002 identified as one of the main objectives underpinning this legislation was "...to limit consumer risks in the property transaction process..." and "...to provide a licensing-based framework and business conduct requirements to limit these risks..." (Office of Fair Trading, NSW, 2008b:2).

## **Occupational Licensing**

As mentioned previously, with the documented increases in trust accounting fraud, and the subsequent criminal convictions of property agents, the question arises whether there is a need to change property agency regulation to improve consumer protection. Linked to property agency regulation is the need for occupational licensing requirements which is widely used in Australia and also overseas. Additionally, occupational licensing requirements are mandated throughout the world for many other professions and in particular the property sector in NSW has been regulated for over 120 years. The mishandling of trust money is a criminal offence and this is usually accompanied by a jail sentence.

For the property professional, inadequate accounting, poor financial control and security will increase the risk of financial fraud. Therefore, two fields of research are drawn together. Firstly, theories and concepts of governance within occupational licensing and secondly, white-collar crime occurrences impacting with occupational licensing.

The question therefore arises whether or not white-collar crime in a property agency can be prevented. Existing research identifies white-collar crime in a variety of industries, however, there has been no extensive research undertaken for trust accounting fraud within the property industry in Australia. If the research is able to identify the reasons for trust accounting fraud, or a trend, then preventative measures can be implemented to deter and minimise the occurrence of fraudulent behaviour. This outcome will be of benefit to both government and the consumer, and the concept can be adapted for the conveyancers' and legal professions' trust accounts.

The aim of this research is to identify trends contributing to trust accounting fraud in property agents' trust accounts. The main purpose and objective of the research will be to undertake a document analysis of public records such as court cases and enforcement notices relating to the misappropriation of trust account funds. Due to the complexity of each jurisdiction mandating varying compliance for trust accounting records and procedures, the research focuses on the legislative requirements and data for the state of New South Wales only. However, comparisons within Australia and overseas, are provided where this is relevant.

The first part of the research discusses the literature relating to white collar crime and occupational licensing. The paper continues with the analysis and discussion of the main themes emerging. The conclusion summaries the findings.

## **LITERATURE REVIEW**

This section contains a review of the literature for white-collar crime and its association with occupational licensing. Agency theory relationship is based on trust, and involves the consumer engaging a person to act on their behalf. One party is designated as the agent, and acts for and on behalf, or is a representative for the other party, designated the principal (Ross 1973). For the property agency industry, this is akin to the licensed real estate agent representing the role of the agent, with the vendor or landlord classified as the principal. The transactions usually also include various amounts of money held on behalf of the landlord and or vendor. The regulatory impact for property agents is to ensure correct accountability in the handling of trust money – which has been identified as "...one of the greatest areas of risk property owners face in transactions with real estate agents..." (OFT 2008a:56).

### **White Collar Crime v. Blue Collar Crime**

Edwin Sutherland, a sociologist, is considered the "grandfather" of white-collar crime as he is associated with first identifying the term *white-collar crime* and the relationship with an individuals' occupation. His writings and research contributed to the fundamental theories of white-collar crime. In summary, his speech delivered

in 1939, and his research undertaken in subsequent years, identified two fields of study, namely crime and high society.

He attempted to prove a correlation between money and social status, based on the premise of the likelihood of the offender being sentenced to jail and concluded that the majority of individuals sentenced to jail for white-collar crime, could also be considered blue-collar crimes. Therefore, is there a difference between the white-collar crime and the blue-collar crime? Does fraud include both white-collar crime and blue-collar crime? Due to the changing nature of the work force and society in general, to some extent these questions would have different answers during the last 80 years.

Sutherland had identified white-collar crime as “those illegal activities that occur in connection with a person’s job or work” and further concluded, “a crime committed by person of respectability and high social status in the course of his occupation” (cited by Braithwaite 1985:3). However, in today’s context, white-collar crime can also broadly include false or misleading advertising, evading corporate taxes, computer crime, corporate crime, and the misappropriation of trust money held in a property agents’ trust account.

Subsequently to Sutherland, there have been a number of definitions relating to white-collar crime, such as Clinard (1952:127) who defined white-collar crime as “a violation of the law committed primarily by groups such as businessmen, professional men, and politicians in connection with their occupations” (cited in Federal Probation 1958:33). This definition deviated slightly with Hartung (1953:31) who proposed white-collar crime as “a violation of law regarding business which is committed for a firm by a firm or its agents in the conduct of its business” (cited in Federal Probation 1958:33). Therefore, is the misappropriation of trust money considered white-collar crime? There is a possibility that the answer is yes, according to these various definitions. Trust money evolves from the furtherance of running a property agency business, the agent is required by law to be the holder of an occupational license, and the fraud is the stealing of the trust funds. Therefore, to further define the “white-collar crime” concept it is important to recognise that the crime which has been committed is identified as *job-specific*. (Clinard 1952, Hartung 1953, Van Onna 2020, Gottschalk 2022).

Currently in the 21st Century there is no definition in law, for white-collar crime. However, generally this term is considered as a non-violent crime for financial gain, such as insider trading, money laundering, tax evasion, embezzlement, identity theft, mail and communications fraud and other types of fraud (Investopedia 2019, Eckard 2019, Roberts 2019). Consequently, the opposite approach is used for blue-collar crimes which contain characteristics of a violent crime such as assault and battery, drug crimes, sex crimes, theft such as shoplifting and burglary (Roberts 2019, Eckard 2019).

Subsequently, over the decades, models for financial fraud were developed which focused primarily on the elements necessary to create the fraud rather than categorising the individuals’ social status or wealth.

## **Models of Financial Fraud Theory**

Models of financial fraud theory were developed from the 1950’s using characteristic elements associated with fraud. For instance, target, access, capability, motivation, opportunity, and rationalisation. Cressey (1953) developed the Fraud Triangle solely from empirical research and variants subsequently emerged. For instance, the corruption equation (Boyd 1995) and the fraud diamond (Wolfe and Hermanson 2004) evolved. These later models incorporated elements due to the changing nature of the workforce, human behaviour and technological changes. Lou and Wang (2009:75) describe the triangle as the “...core of all fraud auditing standards...” and according to Gill (2011:28) it is the “...early fraud warning instrument...”.

Literature over the last few decades is divided on the mandatory existence of the elements within these models developed. However, researchers concluded the fraud triangle could be a combination of the fraud triangle elements and their subcategories (Wheeler 1992; Coleman 2001, Schuchter and Levi 2013). In contrast, researchers (Croall 2001; Ones and Viswesvaran 2001; Wolfe and Hermanson, 2004) considered the Fraud Diamond an improved version of the Fraud Triangle

## **Occupational Licensing**

Occupational licensing for real estate agency was first introduced into NSW during the 1800’s and formalised progressively during the next two hundred years. Similarly, with overseas countries, legislation was also gradually introduced. It was noted by Kleiner (2000), that a substantial amount of research was undertaken

by economists, in America, until the late 1990s. Subsequently this research area did not gain very much attention during the next 30 years. However, occupational licensing has since expanded to a number of other professions to include for instance, doctors, lawyers, and dentists

During the last few decades, America has undertaken a number of studies to examine the impact of occupational licensing on industry earnings, employment, and quality service and compliance. Their findings however, could not indicate clearly the effects of licensing regulation and quality of service and compliance delivered to the consumer. With real estate brokers this included the broad areas of general complaints about rights and responsibilities, mishandling of a sale, and specific issues such as lack of accounting procedures for trust money, unethical activity, failure to account for monies, misrepresentations in advertising or statements of claim and refunds.

Therefore, it is within the one area of “compliance” issues i.e. the mishandling of trust money, which will inform the research in this study.

### **Consumer complaints and quality of service**

Since the early 1930’s the real estate brokerage industry throughout the United States has been stringently regulated. However, with a great deal of variance in the licensing requirements within each state. In Texas, for example, the licensing regulation for real estate agency, was initially incorporated in 1939, whereas, in comparison to NSW licensing was regulated in the very early 1800s for the agricultural industry and business brokerage, and real estate agency regulation in 1941. However, an article in 1971 by Amdur highlighted the need for a more stringent real estate agents’ regulation approach, for the state of Texas, USA. This was aimed to provide better outcomes for the public when dealing with real estate agents. Furthermore, the research cited increases in the population and the volume of land exchanged through agents as a contributing factor.

Minimising consumer complaints and providing consumer protection has been the underpinning aim when occupational licensing was gradually introduced by many countries, including Australia. However, over the last few decades, researchers have undertaken a variety of studies to determine why consumer complaints exist and if there is a further mechanism to diminish the complaint cycle. For this purpose, Maurizi (1980) measured the quality of contractors by the number of consumer complaints in California (USA) and hypothesized that consumer complaints were correlated in proportion to the increase of licences issued. He also commented on the relationship between an increase in contractor licence examination schools and the quality of contractors, and noted that the written exam over the last decade had changed only slightly in its content.

For instance, the contractors were able to use the contents of the past exams to assist passing the course, which was not necessarily a reflection of the quality of their knowledge and skills. Under these circumstances he questioned whether in fact, consumers were receiving any benefits or quality of service with the current mandated occupational licensing requirements and the existing exam environment.

Interestingly Johnson and Loucks (1986) found the quality of service to increase as a result of fewer licensees per capita. A 10% reduction in licensees yielded a 5.7% decrease in complaints per transaction. A further empirical study in America concluded that “the level of complaints against real estate agents is smaller if the licensing board is comprised of a greater number of industry members”. (Shilling & Sirmans 1988:6). Additionally, the result of their enquiry into the relationship between complaints against real estate agents and pass rates of the exams conducted by the licensing board, suggested that a decrease in the pass rate decreased the total number of complaints. Interestingly, Carroll & Gaston (1981:973) commented that most states in the USA, comprise of over 80 occupations being licensed. And their empirical evidence indicated “that restrictive licensing may lower received service quality”, however, this is in contrast to the conclusions reached by Johnson & Loucks (1986).

Another study by Carroll & Gaston (1983) considered the interconnection of occupational licensing with the quality of service provided to the consumer. Their conclusions resulted with two broad categories that could be named as the major effects for licensing requirements being *price effect* and the *quality effect*. Subsequently researchers in the economics concluded that occupational licensing increased prices, for instance commission charged, the income of the licenced individual also increased. However, in the area of quality and service it was difficult to draw any definite conclusions (Barker 2008).

Therefore, trends relating to licences per capita weighted against the number of complaints, and examination pass rates, have varied with these different studies undertaken. There appears to be no apparent trend dominating the research findings.

## Control Mechanisms from the Regulator

Research undertaken by Jamison and Berg (2008:9), concluded that governments establish regulation of utilities to “improve sector performance” and debated whether this implied to control market power and /or to facilitate competition, or to protect operation and customers from politically-driven decisions. However, Stigler (1971:1) took a more cynical viewpoint and concluded that regulation for occupational licensing was either for the “protection and benefit of the public” or a second view being the “political process” of politicians. Similarly, earlier research undertaken by Clark (1952) identified occupational licensing as a possible revenue collecting purpose. In contrast Rottenberg (1962) suggested that licenses should be a prerequisite for the practice of a trade and for the use of a specified occupational title.

Researchers (Bryson & Kleiner 2010) consider that the government is best positioned to determine the depth and level of skills required for various occupations; which will also include taking into account their interface with the consumer. The regulation of occupations through the offering of specialised skills and monitoring the good character of the individuals is considered an important approach. Similarly, the changing technological advancements make it necessary for individuals to be upskilled constantly. Therefore, education is acknowledged as a benefit for the consumer and provides better standards of service and expertise (Rudolph 1998). There is also evidence internationally which endorses compulsory education associated with technical knowledge, such as relevant laws (Oladokum & Olatoye 2011). Similarly, in New Zealand, where it is considered that there is a “...more sophisticated, better-educated profile of vendors and purchasers...”, the market demands advanced agents’ qualifications (Crews 2004:1).

In summary the literature identified white-collar crime as a descriptor for individuals who were educated, intelligent and affluent and had committed a crime against society and the crime was generally related to “job-specific”. Researchers also developed theoretical elements and variants for the *fraud triangle*, *corruption equation* and the *fraud diamond*. The need for regulatory theory was linked to the concept of occupational licensing, aimed to provide consumer protection. The research methodology is discussed in the next section.

## RESEARCH METHODOLOGY

The methodology included the exploration of the relevant issues emerging due to the gap in the literature for this research topic (Lincoln and Guba, 1985). As the research method provided various insights into the research problem this method was considered exploratory and inductive (Williams 2007). Therefore, the research was undertaken using a mixed method approach, with the qualitative research method dominant. This commenced with the incorporation of archival research and document analysis. The final stage of the research was limited to the application of basic trend data analysis. The quantitative data analysis sought to present reality through numeric statistical value.

The research scope was focused on the misappropriation of trust funds in New South Wales property agencies. The archival research for the pilot study consisted of sources considered secondary data. This included court cases, Fair Trading Annual Reports tabled at NSW Parliament; minutes arising from the sitting of the NSW Parliamentary Assembly where there is mention of fraudulent activity for property agents; transcripts from the Court of Appeals on trust accounting fraud convictions; Fair Trading enforcement notices published quarterly; media releases by Fair Trading and newspapers;

The data from the annual reports was sought as a check method against the courts reports and media releases; and where relevant to provide further insight regarding the trust account misappropriation, and other necessary data.

The time frame of the documented cases and notices ranged over 20-years commencing approximately in mid-1997 and ending in mid-2017. A pilot study was initiated to collect qualitative data and develop the coding system for the larger 20 year data set analysis. The coding system was refined where appropriate which led to the development of themes, patterns and trends. A key characteristic of exploratory methods was the identification of the patterns and trends, which then became the foundational building blocks for emerging themes. Therefore, coded data is considered the “building blocks for data analysis” (Hennink et al. 2011:227). During the analysis of the textual context, the codes were refined and sub divided (Boyatzis 1998).

In summary, coding has been described as “... an exploratory problem-solving technique without specific formulas or algorithms to follow. Coding is only the initial step toward an even more rigorous and evocative analysis and interpretation for a report. Coding is not just labelling, it is *linking*”. (Saldana 2013:8) and ...“a

method that enables you to organize and group similarly coded data into categories or “families” because they share some characteristic – the beginning of a pattern...” (Saldana 2013:9). Therefore, it was possible to add codes throughout the project, or maybe to divide issues into two or three codes or even to merge codes where appropriate. The code development continued until there was no further need to add codes i.e. “the point of saturation” (Glaser and Strauss 1967, Hennink et al. 2011:217).

The licensing data from NSW Fair Trading was correlated to identify trends with increases of white-collar crime against the number of licences/certificates held or issued during each relevant year. Triangulating the data aimed to provide reinforcement towards the creditability of the outcomes identified in the archival research process (Patton, 1990; Eisner, 1991; Bowen, 2009).

The next section discusses the analysis of the 20 year data set.

## ANALYSIS AND FINDINGS

The 20-year data set analysis commenced from the 1<sup>st</sup> July 1997 and ending on the 30<sup>th</sup> June 2017. Only data associated with the misappropriation of trust funds was considered. The code book developed during the pilot study phase formed the basis to commence coding the entire documents in the data set.

The research findings identified 140 *instances* of fraud reported. The term *instances* refers to the fraud incident occurring and is counted as one occurrence and includes the corporation licence and any associated parties such as directors, proprietors or employees. Of the 140 *instances*, 81.43% instances involved only one person undertaking the fraud, 15.00% instances were two people involved and 3.57% instances involved three people. There were no instances recorded where there were more than 3 people involved. Therefore, the total *instances* of 140 occurrences represented 171 individuals, which is summarised below in Table 2.

**Table 2:** Analysis of Fraud Instances

INSTANCES	Instances	% of Instances	Total Individuals Involved
Instances of 1 person involved	114	81.43%	114
Instances of 2 people involved	21	15.00%	42
Instances of 3 people involved	5	3.57%	15
	<b>140</b>		<b>171</b>

Source: Author

Licensing status for these 171 individuals, showed that 84.80% were licenced, and 13.45% only held a certificate of registration, with 1.75% being unlicensed and/or unregistered as a certificate holder. This licensing analysis is presented below in Table 3.

**Table 3:** Licensing Analysis Relating to Fraud

Category	Total Individuals	%
Licensed individuals	145	84.80%
Certificate of Registration	23	13.45%
No Licence or Certificate	3	1.75%
<b>Total Individuals</b>	<b>171</b>	<b>100.00%</b>

Within the 171 individuals involved in the 140 *instances*, there were eleven (11) *instances* which related to employees and this represented eleven (11) individuals. In other words the employees carried out the fraud and owners, directors or licensees of the business were not involved.

### Reasons for fraudulent activities

There was a further analysis investigating the reason for misappropriation of trust funds. For instance, were the trust funds for personal use, genuine errors or maybe other exceptional circumstances required to be taken into consideration. The results were varied with the 140 *instances*. Reasons provided for the fraud occurrence, include funds to operate the business, personal debt, Nigerian loan scheme scam, funding legal expenses, and

gambling. However, with many of the *instances* recorded, reasons were not included with the reports available for analysis.

Therefore assumptions were adopted. There were seven (7) *instances* (5.00%), where it appeared that trust fund discrepancies leaned towards negligence and careless management skills with overseeing the trust account, rather than genuine accounting errors. This conclusion was deduced because of the prosecution outcome, in comparison to the remaining cases where there were criminal actions, imprisonment and licensing disqualification imposed. For instance, with the 5.00% *instances* assumed were related to negligence, the prosecution outcomes were a reprimand with conditions imposed. Examples include:

- trust book records were in a mess
- reprimand and prohibition from signing trust account cheques
- disqualification from dealing with trust funds
- varying conditions including CPD points and monitoring for two (2) years
- penalty and reprimand plus implementation of correct trust accounting practices; temporary disqualification and/or ability to handle or hold trust funds.

Furthermore, there were no *instances* of reported genuine accounting errors.

There were 129 *instances* where the fraud involved either the owners, directors or licensees in charge of the business i.e. all these categories were associated with the business and were not employees with an arms-length approach. Therefore, this would have provided the fraudster easy access to the trust funds on an ongoing basis. And, there were eleven (11) *instances* where this fraud involved employees. However, again, the employees were in a position of accessing the trust funds.

However, there are also other possibilities which are not evident from the 20 year study. With the 7.86% *instances* involving employees, it could be assumed that these are the *instances* where Fair Trading and/or internal and external auditing controls detected the fraud and then prosecution proceedings commenced. Therefore, the question arises whether or not there were additional fraud situations involving staff, where the event was not detected through external investigations, but detected internally and quickly rectified by the owners of the business, before the matter became evident. It would be unlikely for an owner to turn themselves into Fair Trading and admit the staff fraud, as they themselves would be exposed to the risk of prosecution also, if proven that their supervision methods and processes were inadequate. This approach is also assuming that the misappropriated funds were fully reconstituted and therefore no loss occurred.

### **Trust fund composition**

Whilst the analysis was not able to identify the composition of the trust funds misappropriated, a few cases involving strata trust funds leaned towards this being an obvious target as these funds, particularly the strata sinking fund, are retained for the long term useage of the owners, rather than accessed on a regular basis. In attempting to identify whether one type of trust fund was more at risk it appeared that employees would aim for the property management whereas owners, directors and licensees were not particular as to which trust accounts they misappropriated. The limitation of the research data here is linked to the absence of the reports identifying the number of trust accounts and type of trust accounts operating in each of these scenarios. However, a generalisation is that up until the 22<sup>nd</sup> March 2020, there was no provision in the PSBA Act 2002 for separate property management trust funds and sales trust funds. Therefore, there is the notion that the owners, directors, licensees would be randomly withdrawing funds from the trust accounts as their need arose. Whereas the majority of the employees committed the fraud by retaining rent money and/or bond money, and did not issue a trust receipt to the tenant. Therefore, the funds were not banked into the trust bank account and without a receipt there was no paper trail for auditing purposes.

### **Licensing Activity**

The final stage of the research was a mixed-method approach, with the aim to compare quantitative data from different perspectives, using basic trend data.

The licensing activities in NSW were analysed from the available data commencing from 1997 to 2015 inclusive, which was the last year this type of data was publicly provided in the annual reports issued by Fair Trading NSW. The new licences issued each year were analysed to compare the percentage increase from the previous year, and similarly for the total licences held i.e. including continuing current licences plus new licences. This analysis is shown in columns A to D inclusive, below in Table 4. Similarly, the certificates of



registration were analysed, and column G provides the percentage increase of total certificates of registration held for each year.

**Table 4:** New South Wales – Licensing Activity

Year	New Licences	Total Current Licences	New Licence % increase on previous year	Total Current Licence % increase on previous year	New Certificates of Registration	Total Current C.O.R.	Total C.O.R. % increase on previous year
	A	B	C	D	E	F	G
1996 - 1997	1,206						
1997 - 1998	1,240	23,260	2.82%				
1998 - 1999	1,384	23,657	11.61%	1.71%			
1999 - 2000	1,602	23,927	15.75%	1.14%	3,881		
2000 - 2001	1,457	23,986	-9.05%	0.25%	3,765	10,339	-2.99%
2001 - 2002	1,519	24,593	4.26%	2.53%	4,257	11,509	13.07%
2002 - 2003	1,911	25,393	25.81%	3.25%	5,090	13,671	19.57%
2003 - 2004	2,523	26,533	32.03%	4.49%	8,020	15,378	57.56%
2004 - 2005	2,593	26,980	2.77%	1.68%	4,906	15,482	-38.83%
2005 - 2006	2,480	26,441	-4.36%	-2.00%	4,867	15,711	-0.79%
2006 - 2007	2,820	26,653	13.71%	0.80%	5,076	16,456	4.29%
2007 - 2008	2,768	26,898	-1.84%	0.92%	5,379	17,495	5.97%
2008 - 2009	2,705	27,367	-2.28%	1.74%	4,637	17,223	-13.79%
2009 - 2010	3,323	28,577	22.85%	4.42%	5,718	18,360	23.31%
2010 - 2011	3,391	29,611	2.05%	3.62%	5,992	19,477	4.79%
2011 - 2012	3,230	30,049	-4.75%	1.48%	4,916	17,179	-17.96%
2012 - 2013	2,586	29,489	-19.94%	-1.86%	5,160	17,478	4.96%
2013 - 2014	3,549	31,094	37.24%	5.44%	6,616	19,463	28.22%
2014 - 2015	3,579	32,445	0.85%	4.34%	7,723	21,988	16.73%

Source: Author, Compiled from Fair Trading annual reports

The two financial years ending 30<sup>th</sup> June 2003 to 30<sup>th</sup> June 2004, indicate a high increase of new licenses, 25.81% and 32.03% respectively. However, total licence growth for each of those years did not increase with the same proportion. At 3.25% and 4.49% respectively, these increases are well below the new licence rate of growth increase. Therefore, these figures indicate that many licences were not renewed during those financial years. A possible explanation could relate to the introduction of CPD as a mandated requirement for licence renewal. If individuals were no longer practising in the industry this added financial burden could be unattractive. Additionally, the year 2003 was when educational requirements eased, and industry experience was abolished. These changes could also be attributed as reasons for the overwhelming response of new licence applications from 2003, which is evidenced in the table above. Once the industry experience was removed, and educational requirements softened there were very few barriers to quality control the growth in this sector.

The global financial crises appeared to impact in later financial years following the increased surge, and in particular the financial years ended 2012 and 2013 experienced a downturn of 4.75% and 19.94% respectively, for new licences. The following financial year, 2014, indicated a recovery and catch up at 37.24%, with the financial year 2015 having very little movement. There is no data for the financial years 2016 and 2017. However, data for the financial year 2018 is discussed in conjunction with the certificate of registration analysis later in this section. In summary, new licences issued were 2.97 times (nearly triple) the quantity in

the financial year end 2015 by comparison to the financial year end 1997. And total licences held were 1.4 times the quantity in the financial year end 2015 by comparison to the financial year end 1997. Many of the non-renewed licenses could also relate to the natural attrition of individuals no longer working in the industry, entering into retirement age, or deceased. It is also interesting to note that whilst new licences increased in specific years, the total of all licences held for each financial year did not increase in the same proportion, as shown in column D in the above table 4. The conclusion is that renewals were obviously falling behind at approximately half the rate in comparison to new licenses being issued, although this data is not available explicitly. The certificate of registration holders are analysed to compare if there are similar trends.

New certificates issued for the two financial years ending 30<sup>th</sup> June 2003 to 30<sup>th</sup> June 2004, indicate a high increase of new certificates, 19.57% and 57.56% respectively. This is a similar pattern to new licences, however, the financial year end 2005 indicates a 38.83% reduction for new certificates. A possible explanation could be that Fair Trading NSW changed the method of data collection, or data from financial year 2004 belongs in part to financial year 2005. However, similarly with new licences there are irregular pattern growths and this is also identified with certificates. The financial year end 2014 for both licences and certificates yielded a steady growth and this could be related back to the passing of the global financial crises and the economic recovery underway. In summary, new certificates issued were 1.99 times (nearly double) the quantity in the financial year end 2015 by comparison to the financial year end 2000 (first financial year of available data). And total certificates held were 2.13 times the quantity in the financial year end 2015 by comparison to the financial year end 2000 (first financial year of available data). These figures indicate nearly every non-renewal was replaced with a new application, which is in contrast to the licensing activity data which indicated only half this rate. However, obtaining a certificate of registration is a simple task with specific educational modules which are usually completed in approximately one week, in comparison to a more involved course for licensing purposes.

As data for licence and certificate activity was not available for each of the financial years 2016 and 2017, the data for the financial year end 2018 was utilised instead. As indicated above in table 4, for the financial year ending 2015, the total new licences issued were 3,579 and certificates 7,723. This equates to a total of 11,302 new licence/certificates issued, and a total of 54,433 current licences/certificates. In comparison with data available for 2018, the total new licences and certificates of registration were 12,796 and the total current licences/certificates were 58,541. This indicates that in 2016 and 2017, less licences and certificates of registration were renewed. As mentioned previously though, the limitation is that we do not have the data to classify if the licence and certificates for either non-renewals or renewals, relate to prior the 2003 regime or afterwards.

Therefore with the *instances* of fraud discussed earlier it was noted that some offences commenced with the licence suspension, the issuing of a penalty notice and then a progression to a court hearing. A comparison of data was undertaken to determine a relationship between licence/certificate individuals with complaints and penalty notices issued. Below in Table 5 is an overview of this summarised data.

**Table 5: Comparison Licence activity v. Complaints and Penalties**

		Total Current Licences	Total Current Certificates	Net Real Estate Complaints	Penalties - Offences
		A		B	C
1	1996 - 1997	-	-	814	-
2	1997 - 1998	23,260	-	735	-
3	1998 - 1999	23,657	-	650	-
4	1999 - 2000	23,927	-	750	13
5	2000 - 2001	23,986	10,339	900	42
6	2001 - 2002	24,593	11,509	2,100	243
7	2002 - 2003	25,393	13,671	808	121
8	2003 - 2004	26,533	15,378	1,436	52
9	2004 - 2005	26,980	15,482	1,756	484
10	2005 - 2006	26,441	15,711	2,181	51
11	2006 - 2007	26,653	16,456	2,650	164

12	2007 - 2008	26,898	17,495	2,612	92
13	2008 - 2009	27,367	17,223	2,440	38
14	2009 - 2010	28,577	18,360	2,564	99
15	2010 - 2011	29,611	19,477	2,358	71
16	2011 - 2012	30,049	17,179	2,341	46
17	2012 - 2013	29,489	17,478	1,444	56
18	2013 - 2014	31,094	19,463	2,232	108
19	2014 - 2015	32,445	21,988	2,410	209
20	2015 - 2016	Not reported	Not reported	2,757	Not reported
21	2016 - 2017	Not reported	Not reported	1,470	Not reported

**Source: Author**

The financial year end 2003 and onwards shows a steady increase with total individuals holding either a licence or certificate of registration. Whilst complaints were very low at 808 instances for financial year ended 2003, offences were higher than in earlier years, except for year end 2002 which was discussed previously. Financial year end 2004 through to 2008 inclusive resulted in more complaints lodged every year, coinciding with continuing increases of total licences and certificates. However, not very comparable with penalty notices as these continued to fluctuate higher and lower for various years. The data indicates an obvious trend of increase with consumer related problems and complaints from the years 2003 and onwards. The peak though occurred for financial year ending 2016 where complaints peaked at 2,757. Further analysis undertaking a correlation approach between fraud instances, licensing activity and consumer complaints was not possible due to some financial years omitting data in the Annual Reports.

## CONCLUSIONS

The final results from the 20-year data set analysis have provided insights into the occurrence of trust fund misappropriation. All *instances* were a deliberate misuse of trust funds. Reasons provided for the misappropriation of trust funds include gambling, funds to operate the property agency business, personal debts, Nigerian loan scheme scam, pre-drawing of sales commission, and funding legal expenses. It is proposed to continue with the data collection for NSW to enable further analysis and comparisons with other jurisdictions in Australia.

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