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Real Estate Broker Disclosure Duties: The Buyers' Broker

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It is common knowledge that California real estate brokers must, when representing a seller of residential property, disclose to the buyer all known or reasonably ascertainable material facts relating to the condition of the property.

Here, we examine the obligations a real estate broker has when representing a buyer, as discussed in the recently decided case of Michel v. Palos Verdes Network Group, Inc., 2007 WL 3208735 (Cal.App. 2 Dist.).

In Palos Verdes Network Group, Buyer's broker Larry Moore employed at least two sales agents, Mike Kirkpatrick and Nicola Lagudis. During about January 2000, Kirkpatrick attempted to obtain a listing for the subject property and, in the process of so doing, conducted a pre-listing visual inspection of the property which Kirkpatrick documented in his notes. Kirkpatrick's pre-listing visual inspection revealed possible water leaks, cracked interior walls, and damage to the pool.

The sellers ultimately listed the property with a broker other than Kirkpatrick's broker.

During the listing period, Kirkpatrick showed the property to sales agent Lagudis's clients Carl and Sydne Michel. The Michels tendered an offer to purchase the property, which was accepted.

Lagudis then visually inspected the property, prepared a transfer disclosure statement (TDS), and gave the TDS to the Michels. Kirkpatrick reviewed Lagudis' TDS and observed that the TDS did not contain material information which Kirkpatrick had documented in his pre-listing visual inspection notes. Kirkpatrick did not, however, supplement the TDS with the additional information, nor did he otherwise provide the additional information to the Michels.

The rainy season started after escrow closed. New cracks appeared in the interior walls, which the Michels repeatedly patched. In addition to fixing the cracks, the Michels also sought building permits for a remodeling project, which, in turn, necessitated a soil inspection.

The engineer who conducted the soil inspection discovered that poor top soil and fill had caused ground movement which had tilted the foundation of the house about 3.5 inches from level, which in the engineer's opinion was causing the repeated cracks in the interior walls of the house.

Upset with the engineer's report, the Michels met with Kirkpatrick during January 2001. The Michels told Kirkpatrick about the engineer's report and said it would cost about \$500,000 to remedy the damage and its cause. Kirkpatrick, for the first time, told the Michels that Kirkpatrick had noticed interior wall cracks during his pre-listing visual inspection of the property and provided the Michels with a copy of the his pre-listing inspection notes.

The Michels filed suit against the sellers of the property, for breach of contract; against the sellers' real estate broker Palos Verde Network Group, for violation of Civil Code § 2079 inspection and disclosure requirements; and against Larry Moore, the real estate broker who represented the Michels with respect to the purchase of the subject property and who employed sales agents Kirkpatrick and Lagudis, for violation of Civil Code § 2079, for fraudulent concealment of property defects, and for negligent non-disclosure of property defects.

The claims against the sellers and the sellers' real estate broker were resolved prior to trial, and the sellers filed for bankruptcy protection.

At trial, Larry Moore, the Michels' real estate broker, moved for a judgment of nonsuit¹ on the Michels' cause of action for negligent non-disclosure. The motion was granted.

Following conclusion of the trial, the jury returned a verdict in favor of Moore (and against the Michels) on the remaining two causes of action: violation of Civil Code § 2079 inspection and disclosure requirements and fraudulent concealment of property defects. Rejecting the section 2079 claim, the jury found Moore (through sales agent Lagudis) had not failed to conduct a reasonably competent and diligent inspection of the property, nor had Moore failed to disclose to the Michels any material fact about the property that such an inspection would reveal. The jury also rejected the Michels' claim for fraudulent concealment, finding that Moore had not intentionally suppressed or concealed from the Michels any material fact. The Michels' appealed.

The appellate court said that, "[s]tated in a nutshell, [the Michels] claim [that broker Moore] is liable for not telling them before they bought their home about Kirkpatrick's walk-through and notes."

The appellate court first addressed the jury's rejection of the Michels' section 2079 claim, noting that, by its terms, "section 2079 imposed a duty only from the *listing* broker who is *selling* the property to the buyer; it does not impose a duty on the buyer's own broker . . . [and that there was] nothing in the [court] record [regarding] a written agreement or evidence of [the selling broker and Moore] acting in cooperation to find a buyer." (Italics in original). Thus, even though the jury found that Moore had satisfied the inspection and disclosure requirements of section 2079, as a matter of law, Moore could not have violated section 2079 because he had no legal obligation to comply with its requirements.

The appellate court also noted that the jury's verdict reflects the facts that "Lagudis may very well have been *competent* in her visual inspection of the property [and] in preparing her TDS for [the Michels] AND Kirkpatrick may very well have had *no fraudulent* intent in not telling [the Michels] about his [pre-listing] inspection and notes . . . – circumstances justifying the jury's verdict . . . – but that does not mean [broker

Moore] did not injure [the Michels] by not telling them before they bought the house about Kirkpatrick's notes."

"A [real estate] broker has a fiduciary duty to its client. . . . The fiduciary duty is greater than the negligence standard of due care under section 2079. . . . Thus, a [real estate] broker can be professionally competent under section 2079 without satisfying the greater duty of a trusted fiduciary."

"A fiduciary must tell its principal of all information it possess that is material to the principal's interests. . . . A fiduciary's failure to [do so] is constructive fraud. . . . Constructive fraud is a unique species of fraud applicable only to a fiduciary or confidential relationship. . . . [C]onstructive fraud comprises any act, omission or concealment involving a breach of legal or equitable duty, trust or confidence which results in damage to another even though the conduct is not otherwise fraudulent."

Construing the Michels' cause of action for negligent non-disclosure as one for constructive fraud/breach of fiduciary duty, the appellate court in Palos Verdes Network Group held that broker Moore's compliance with section 2079 did not prove Moore satisfied his higher – fiduciary – duty to the Michels. The appellate court also held that Moore's lack of liability for intentional fraud does not, by itself, prove an absence of liability for constructive fraud/breach of fiduciary duty, as such claims do not, unlike claims for intentional fraud, include a requirement to prove "intent".

The appellate court remanded the case to the trial court for further proceedings on the Michels' negligent non-disclosure claim.

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Mr. Earle is licensed to practice law in all California state trial and appellate courts, the United States Supreme Court, the United States Court of Appeals for the Ninth Circuit, and federal trial courts in the Northern District of California. He is also a licensed Real Estate Broker.

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¹ A motion for non-suit concedes, for purpose of the motion, the truth of plaintiff's allegations and challenges whether those facts are sufficient as a matter of law to prove a prima facie case.