

## **SELLER DISCLOSURE ACT – AN UPDATE**

### **I. INTRODUCTION**

The Seller Disclosure Act ("SDA") is now over 10 years old. When it was passed in 1994, many people were quite concerned about the potential impact of the legislation. Some critics feared that the legislation would result in increased liability for sellers and REALTORS®. These critics felt that the SDA had radically changed the common law, and that for the first time, sellers would be required to make certain warranties about the condition of their homes. Other critics had just the opposite concern – *i.e.*, that the SDA would be deemed to have wholly eliminated a home seller's liability for fraudulent statements. Fortunately, as has been made clear by case law that has developed over the last 10+ years, the passage of the SDA has had neither such result. This article will look at the SDA cases that have come out over the last 13 years and discuss the impact of the SDA on existing law.

### **II. DISCUSSION**

#### **A. No Separate Cause of Action Under the SDA**

Under the SDA, if the seller fails to provide the buyer with an accurate, complete seller's disclosure statement, the buyer has the right to terminate the purchase agreement at any time up until the actual closing. MCL 565.954(3). Once the sale has closed, however, the sale may not be rescinded on the basis that there were untruthful statements contained in the seller's disclosure statement. It has been consistently held that after closing, there is no separate cause of action under the SDA, rather, a buyer must look

to traditional common law theories of recovery. (See, for example, the unpublished decisions of the Michigan Court of Appeals in *Pena v Ellis* (2006), *Vettese v Zehr* (2005), and *Timmons v DeVoll* (2004).)

**B. SDA Did Not Eliminate a Seller's Liability for Fraud and Misrepresentation – Common Law Causes of Action Still Exist.**

**1. Traditional Common Law Principles.**

Before discussing the impact of the SDA, we want to briefly summarize Michigan law as it relates to the responsibility of home sellers.

It has traditionally been the law in Michigan that home sellers are liable for false statements that they knew were false. One crucial element of a fraud claim is that the buyer must have relied on the false statement and that the buyer's reliance must have been reasonable.

It has also traditionally been the law in Michigan that a seller can be held liable for even an innocent misrepresentation. Again, however, the buyer's reliance on the false statement must have been reasonable.

Where the buyer has purchased the home "as is," a seller cannot be held liable for an innocent misrepresentation, but can still be held liable for a knowingly false statement.

Finally, traditionally sellers have no general obligation to volunteer information about their home. Sellers can be liable for "silent fraud" ONLY if the buyer made a specific inquiry and the sellers failed to fully respond to that inquiry by disclosing all information they knew about the specific problem.

## 2. How Has The SDA Changed The Common Law?

First and foremost, under the SDA, sellers are now required to volunteer certain information about the property – *i.e.*, sellers are required to answer the specific questions set forth in the seller's disclosure statement. It has been suggested that the SDA imposes not only a duty to simply answer the specific questions in the seller's disclosure statement, but also to volunteer any other relevant information. In *Fritz v Tapke*, an unpublished 2001 decision of the Court of Appeals, the Court suggested that the SDA imposes a legal duty to report "known conditions affecting the property," even if not prompted by a specific question on the disclosure form. Specifically, the Court said:

... The statutory form reads: "Instructions to Seller: (1) Answer ALL questions. (2) Report known conditions affecting the property." If a seller is only required to report conditions listed in the questions, the second instruction would be mere surplusage. Therefore, the instructions require more from the seller than simply answering the questions. The "good faith" required by the statute extends not just to answering specific questions asked by the form, but in honestly reporting the condition of the property. ...

An examination of the specific facts of the *Fritz v Tapke* decision, however, reveals that in that case, the trial court had found that the sellers had made knowingly false statements in the seller's disclosure statement. For example, the sellers had told the buyers that the septic system was "ok" when in fact the sellers had needed to pump the system continuously so it would function. The trial court had also made a determination that the seller's statements in the disclosure statement that the roof did not leak were false. (The sellers had argued that the leaks were actually coming from the water around the windows

near the roof – so that their statement that the roof did not leak was technically accurate.) Thus, while there is language in the *Fritz* decision that suggests the Court was expanding the disclosure duties of sellers under the SDA, the actual holding in the case simply held the seller liable for a knowingly false statement in their seller's disclosure statement.

A second change to the common law as a result of the SDA has to do with a seller's liability for innocent misrepresentations. It has been held that with respect to false statements in a seller's disclosure statement, a seller can only be liable if it is shown that the seller knew that the statements were false – *i.e.*, that a seller cannot be liable for an innocent misrepresentation in a seller's disclosure statement. This rule is best perhaps illustrated by a 1994 case involving a significant leaking problem in the roof of a glass-paned sunroom. *Bergen v Baker*, 264 Mich App 376 (2004). While the buyer admitted that the seller's disclosure statement had indicated that there were roof leaks, the buyer argued that the sellers should be liable because they failed to disclose the extent of the problem. The trial court had dismissed the case in favor of the sellers and the buyers appealed. In discussing the seller's potential liability for fraudulent statements in the seller's disclosure statement, the Court of Appeals held:

Reviewing collectively the language of the relevant statutes that comprise the SDA, it is evident that the Legislature intended to allow for seller liability in a civil action alleging fraud or violation of the act brought by a purchaser on the basis of misrepresentations or omissions in a disclosure statement, but with some limitations. Liability is precluded for errors, inaccuracies, or omissions in a seller disclosure statement that existed when the statement was delivered, where the seller lacked personal knowledge and would not have had personal knowledge by the exercise of ordinary care . . . and thus

proceeds in good faith to deliver the disclosure statement to the buyer.

In its interpretation of the SDA, the Court in *Bergen* noted that the statute specifically provides that the seller is not liable if he does not know of the problem and could only have discovered the problem through the inspection of inaccessible portions of the home and/or an inspection by a person with expertise in a science or trade beyond the knowledge of the seller. The sellers in this case had answered affirmatively to the question as to whether the "roof leaks," but had added: "complete tear-off & replacement June 1998." Noting that reasonable minds could conclude that this response indicated that there had been a past problem but that it had been corrected, the Court of Appeals sent the case back to the trial court to determine whether the statement was in fact false and whether the seller knew it was false when it was made.

**C. Reasonable Reliance Requirement is Not a Change to the Common Law.**

Several unreported decisions discussing the SDA have dismissed a fraud claim on the basis of the court's finding that the buyers had not reasonably relied upon the seller's allegedly false statements in the disclosure statement. In *Timmons v DeVoll* (2004), for example, the buyers allegedly found numerous defects in the home after they moved in, including alleged defects with the electrical, plumbing and HVAC systems. The Court of Appeals noted that the buyers had had the home inspected, that the buyers had relied upon that inspection, and, moreover, that the defects had not been concealed and would have been discovered by a reasonably competent inspector. The Court noted that there was a long-established rule of law in Michigan (dating long before the SDA was enacted) holding

that, "there can be no fraud where a person has the means to determine that a representation is not true." In *Timmons*, the court concluded, the buyers could not have reasonably relied on the alleged misrepresentation in the seller's disclosure statement:

. . . because before closing on the property [the buyers] opted to have the closing contingent upon an adequate inspection of the home "in order to determine if there were faults" in the home; and pursuant to [the buyers'] inspection, [the buyers] requested certain repairs and corrections be made before proceeding to closing; [the buyers] had constructive knowledge that certain building permits were not pulled for the "structural modifications, alterations or repairs made" on the home; and all of the evidence demonstrates that the alleged misrepresentations could have easily been identified by a competent home inspector. Therefore . . . [the buyers] had "the means" to determine whether the [seller's disclosure statement] contained true statements. . . .

#### **D. Completing the Form**

REALTORS® should be aware of issues that have arisen concerning several specific questions on the seller's disclosure statement.

Previous disputes often arose over the "Appliance" section of the seller's disclosure statement. A typical example was where a seller had excluded the refrigerator from the listing, but had nonetheless completed the seller's disclosure statement indicating that the refrigerator is working. The buyer often claimed that he had relied on the seller's disclosure statement and assumed that the refrigerator was included. In order to clarify this issue, MAR obtained an amendment to this section which now provides:

**Appliances/Systems/Services:** The items below are in working order. (The items below are included in the sale of the property only if the purchase agreement so provides):

A current problem arises under Question 8 under "other items," which provides:

Farm or farm operation in the vicinity; or proximity to a landfill, airport, shooting range, etc.?

unknown \_\_\_\_\_ yes \_\_\_\_\_ no \_\_\_\_\_

There is no definition of either "the vicinity" or "proximity," so we have no idea whether it means within 100 feet or within 10 miles. In one recent unpublished case, the sellers claimed that a shooting range located 6/10 of a mile away from their home was not "in the proximity." *Pena v Ellis* (2006). The trial court dismissed the case in favor of the seller and the buyer appealed. The Court of Appeals reversed the decision, holding that because reasonable minds could differ on the question of whether 6/10 of a mile is in the "proximity" of the sellers' home, this is a question of fact (and thus to be decided by the jury). Based upon this decision, sellers should simply be told that there is no definitive answer to this question. A seller should answer "yes" if a condition exists nearby which impacts his property, e.g., a nearby landfill causes a stink on the seller's property. Also, a careful seller would simply state, for example, "city airport approximately one mile away."

Finally, while there are several questions on the form which ask about the current condition of the property (e.g. "Roof: Leaks?"); other questions are not so limited (e.g., "Has there been evidence of water?"). As to the second type of question, we are often asked whether there is any limitation on the time period of the inquiry. Based also upon the decision in *Pena v Ellis* (2006), the answer to that question appears to be "no." (Court held that SDA required sellers to disclose the fact that basement had flooded 26 years ago.)

**E. Duty to Amend Disclosure Form**

It has been consistently recognized that it is not a violation of the SDA if something occurs after the seller's disclosure statement is completed but before the closing that renders the statement inaccurate. MCL 565.956. However, if such inaccuracy relates to "structural/mechanical/appliance systems," then the seller has a duty to update the seller's disclosure statement. Of course, once the disclosure form is amended, the purchase agreement once again becomes subject to revocation by the buyer. A failure to amend, where required, will give rise to a cause of action for a silent fraud. *Pena v Ellis* (2006). Interestingly, however, the Court of Appeals has indicated that the duty to amend does not apply to all questions in the seller's disclosure statement, but only "structural/mechanical/appliance system" changes. In the unpublished decision in *Huhtasaari v Stockemer* (2005), for example, the Court found that there was no evidence that an attic mold condition, which had been remediated by the sellers, resulted in a "structural/mechanical/appliance system" change necessitating an amended disclosure statement.

We often get calls from buyers' agents who have demanded an amended seller's disclosure statement so their buyer can rescind the transaction. It is unlikely that the buyer's right to rescind will depend on whether the seller can be "tricked" into providing a new form. A court would likely find that if an amendment is required, the buyer has a right to rescind, even if the seller refuses to actually amend the form. The buyer's right to rescind will more likely turn on whether the seller actually had an obligation to amend the form.

Logically, it would seem that the seller's obligation to amend the form will depend on the type of occurrence. For example, Question 1 under "property conditions" states, "Has there been any evidence of water?" Once there is a leak, the answer to that question is "yes," even if the seller has the basement repaired. On the other hand, the question about the furnace, asks simply if the furnace "is in working order." If the furnace breaks down after the disclosure form is provided to the buyer, but is subsequently repaired by the seller, the answer to this question is still "yes," so presumably a seller would not need to amend the form in this instance. If the buyer has the home inspected and discovers various defects which the buyer disclosed to the seller, does the seller need to amend the seller's disclosure statement? Logically, it would NOT seem necessary to amend the form for the buyer that had the inspection performed. The seller's disclosure statement is intended to tell the buyer what the seller knows about the property, it is not a representation as to the condition of the property. Thus, presumably, the seller would have no obligation to amend the form to tell a buyer what *that* buyer's inspector discovered about the property.

What if the buyer that performed the inspection backs out of the deal – for example, because the buyer's inspector found evidence of prior termite infestation? Does the seller have to amend the seller's disclosure statement before providing it to future potential buyers? We believe the answer to this question is in most cases "yes." The seller now has knowledge that there may be termites and cannot in good faith answer that question the same way. A seller who takes issue with an inspector's findings can either

investigate further or qualify his answer – *i.e.*, “one inspector believes that there may have been a termite problem in the past, seller has no actual knowledge of any problem.”

### **III. CONCLUSION**

The SDA has not radically changed the law to the benefit of either buyers or sellers. While not a perfect statute by any means, it does require sellers to answer certain questions about the condition of their home and provide a written record as to what the buyers were told. Sellers should be advised to complete the seller’s disclosure statement carefully and completely; buyers should be advised to review the form carefully and follow up on any issues raised.

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