

ANY DUTY TO DISCLOSE?

More than one listing Realtor[®] has found himself in a situation where he believes there is a defect in a property he has listed, but his seller either is in denial about the existence of the defect or simply does not want it disclosed to the buyer. The question then becomes, under Michigan law does the Realtor[®] have a duty to disclose the defect to a prospective buyer potentially in violation of his or her duty of confidentiality and loyalty to the seller. Further, if the Realtor[®] does not disclose the defect to the prospective buyer, can the Realtor[®] be liable to the buyer when the defect is discovered after closing?

The answer to these questions is most easily understood in the context of a hypothetical. Assume Partnership A owns a small shopping center in a small city. Partnership A has used Realtor[®] B for leasing and other real estate related services for the shopping center for a number of years. Partnership A decides to sell the shopping center and lists it with Realtor[®] B.

Assume further that Realtor[®] B does not receive any offers for the shopping center from local buyers. This is likely due at least in part to the fact that the shopping center was built on topography which in effect places it at the bottom of a clay bowl. As the land around the shopping center was developed, the shopping center began to flood regularly each spring. Partnership A and Realtor[®] B have been to the county drain commissioner's office on at least two occasions over the years seeking a solution to the flooding problem, but have been advised that the problem cannot be fixed. Presumably potential local buyers would have some knowledge of the flooding problem at the shopping center.

Buyer C is from out of town. Partnership A does not provide a seller's disclosure statement both because the shopping center is commercial property not requiring a seller's disclosure statement and because Partnership A has never occupied the property. Buyer C

purchases the property from Partnership A in its “as-is” condition with no representations or warranties implied as to the condition of the shopping center. The purchase of the shopping center by Buyer C closes in January. Two months later the shopping center floods after a heavy rainfall. Buyer C then discovers that flooding problems have existed at the shopping center for many years. Buyer C sues the seller, Partnership A and the listing broker, Realtor[®] B, based on various legal theories.

First, Buyer C sues Partnership A and Realtor[®] B under a fraud theory. In order to prove fraud against Partnership A and/or Realtor[®] B, Buyer C must prove the following:

- 1) Partnership A and/or Realtor[®] B made a material representation;
- 2) The representation was false;
- 3) When Partnership A and/or Realtor[®] B made the representation, they knew it was false, or, alternatively, they made the representation recklessly without knowledge of its truth as a positive assertion;
- 4) Partnership A and/or Realtor[®] B made the representation with the intention that Buyer C act upon it;
- 5) Buyer C acted in reliance upon the false representation made by Partnership A and/or Realtor[®] B; and
- 6) Buyer C suffered damage.

In our hypothetical, neither Partnership A nor Realtor[®] B made any representations to Buyer C about the condition of the shopping center. They said nothing. To date, there is no Michigan case holding a listing Realtor[®] liable for simply failing to disclose a defect to a buyer. Michigan courts have found that the imposition of a duty on the listing Realtor[®] to disclose defects to the buyer, would conflict with the fiduciary duties owed by that listing Realtor[®] to the seller. Michigan courts have characterized the relationship between a listing Realtor[®] and a buyer as a “commercially antagonistic.”

Second, Buyer C sues Partnership A and Realtor[®] B under a theory of innocent misrepresentation. An innocent misrepresentation claim differs from a fraud claim in that Buyer C would not have to prove that Partnership A and/or Realtor[®] B made a misrepresentation with fraudulent intent or for a fraudulent purpose. In other words, Buyer C would only need to show that Partnership A and/or Realtor[®] B made a representation they believed to be the truth but that turned out not to be true.

Based upon the facts in our hypothetical, Buyer C's claim for innocent representation would fail against Partnership A and Realtor[®] B. It would fail against Partnership A because Partnership A made no representations with respect to the condition of the shopping center. It would fail against Realtor[®] B for two reasons. Realtor[®] B made no representations with respect to the shopping center (innocent or otherwise) and Realtor[®] B was not in privity of contract with Buyer C. An innocent representation claim can only be made in connection with the making of a contract. Buyer C had no contract with Realtor[®] B.

Third, Buyer C sues Partnership A and Realtor[®] B under a silent fraud theory. This type of claim is also known as fraud by non-disclosure or fraudulent concealment. Buyer C would claim that Partnership A and Realtor[®] B engaged in silent fraud because they both knew about the history of the severe flooding problem at the shopping center and failed to volunteer that information to Buyer C prior to closing. Buyer C would maintain that a silent fraud claim is viable where a buyer is able to prove that a seller knew about a defective condition and did not disclose it to the purchaser.

In our hypothetical, Buyer C would lose on a claim of silent fraud or fraudulent concealment against Partnership A and Realtor[®] B. In order to make a claim for silent fraud against Partnership A or Realtor[®] B, Buyer C would have to prove that Partnership A and/or

Realtor[®] B were not completely silent with respect to the condition of the property. For example, assume in our hypothetical that Buyer C noticed that the shopping center was built in a bowl and discussed the potential for flooding with Partnership A and/or Realtor[®] B. Assume further that in those discussions Partnership A and/or Realtor[®] B indicated to Buyer C that there had been “some dampness” over the years, but nothing substantial. Under those facts, Partnership A and Realtor[®] B could be liable for silent fraud. In situations where a buyer expresses some particularized concern or makes a direct inquiry, silent fraud will be proven if the seller or the listing Realtor[®] fails to disclose material facts within their knowledge.

As another example, assume in our hypothetical that prior to putting the shopping center on the market, Partnership A and Realtor[®] B made a third trip to the county drain commissioner and were advised that drainage improvements had been made on adjacent property that will eliminate the flooding problem at the shopping center. After the property was listed, in discussions with Buyer A, it is indicated by Realtor[®] B that there was a flooding problem but that it has been fixed. Thereafter, prior to closing, Partnership A and/or Realtor[®] B are advised by the county drain commissioner that his prior information was incorrect, *i.e.*, the improvements on the adjacent property will not solve the flooding problem at the shopping center. Again, under these facts, the partnership and Realtor[®] B could be liable for silent fraud. Under Michigan law, a seller and/or a listing Realtor[®] have a duty to disclose information if necessary to correct previous representations which, when made, were believed to be true, but which are now known to be false or misleading. A seller or listing Realtor[®] who fails to do so may be liable for silent fraud.

To make certain that there is no misunderstanding, the analysis above with respect to when a listing Realtor[®] must make a disclosure to a buyer has absolutely no application when

dealing with a listing Realtor[®]'s duty to disclose to the seller, or a buyer's agent's duty to disclose to the buyer. If there is an agency relationship, the agent has a duty of complete disclosure to his or her principal unless the duty has been modified by contract. For example, if in our hypothetical Buyer C had retained the services of local Realtor[®] D and local Realtor[®] D knew that the shopping center suffered severe flooding for many years, Realtor[®] D would have a fiduciary duty to make that disclosure to Buyer C.

Finally, no discussion of the duty to disclose would be complete without a short discussion of dual agency. If, in our hypothetical, Realtor[®] B had represented both Partnership A and Buyer C, he would have been put in an impossible position. He would have had a duty of confidentiality and loyalty to Partnership A, as the seller and a duty of disclosure to Buyer C. These duties cannot be reconciled unless Partnership A and Buyer C knowingly consented to dual agency and, preferably, signed a dual agency agreement acknowledging that Realtor[®] B would not disclose to one party information learned in the agency relationship with the other party.

In sum, a listing Realtor[®] has no duty under Michigan law to disclose defects to a buyer. If a listing Realtor[®] makes misrepresentations to a buyer, then he or she could be liable for fraud. If, in response to questions or inquiries from a buyer, a listing Realtor[®] fails to fully disclose what he or she knows, then he or she could be liable for silent fraud. Further, if a listing Realtor[®] makes a representation to a buyer and later finds out that the representation is untrue, the Realtor[®] may be liable for silent fraud if he or she does not correct his or her prior statement.