Sellers Disclosure Revisited

By the Demco Law Firm, P.S.

Oregon, Washington and Idaho have enacted statutes that generally require sellers to complete Disclosure Forms when selling residential property. In all three states, the duty of disclosure is limited to the seller's "actual" or "personal" knowledge. Because these statutes were enacted recently, we are only now beginning to see how judges and juries treat the disclosures. The early returns from these decisions suggest that the real estate profession may need to rethink its approach to seller disclosure.

Consider the results from these recent Washington trials.

"It Was fixed." The seller of a home had experienced flooding from a blocked culvert on a neighboring property three years earlier. Each time the culvert became blocked, the county cleared it, and the flooding stopped. A year before the sale, the culvert became blocked again, but the flooding did not reach the seller's property. The sale took place more than a year after the last time the culvert was blocked. When the seller completed the Disclosure Statement, he answered "yes" to the question: "Is there any settling, soil, standing water, or drainage problems on the property?" The seller changed his answer to "no" after his agent assured him that he had no obligation to disclose a past problem that had been fixed. Although the seller instructed the listing agent to disclose the past flooding, she did not. After the purchasers moved into the house, the culvert again became blocked, causing minor flooding on the property. The buyer sued the seller and listing agent and recovered $38,000. On appeal, the Court of Appeals held that the evidence was sufficient to find that the listing agent had "actual knowledge" of an existing drainage problem and affirmed the jury's verdict because there were lingering questions whether the problem had been completely repaired.

"Don't Know" A seller and agent were aware that the floor in the daylight basement of a house sloped, but did not know whether the floor had settled or was poured that way. The seller initially answered "No" to the question about settlement or slippage, but changed the answer to "Don't Know" after speaking with the listing agent. The buyers noticed the sloped floor at their inspection, but were assured by their inspector that it was "normal." After moving into the house, the buyers became concerned about the sloped floor and hired another inspector who believed that the floor had settled. The buyers sued the seller and listing agent for providing a false disclosure. Although there was no evidence that the seller or listing agent had actual knowledge of settlement, the buyers recovered over $190,000 for damages, including the cost of repair, emotional distress and attorney fees.

"One False Disclosure" The seller had extensively remodeled the house, but had not obtained permits or inspections, except for a small entry addition. The Disclosure Statement stated that no permits or inspections were obtained with a notation "obtained permit for addition." Although the seller's father (a licensed contractor) had replaced the septic system without a permit, the Disclosure Statement indicated that the system had not been repaired on modified. The seller made this false disclosure out of concern that her father

could lose his contractor's license and because she had experienced no problems with the septic system. After moving in, the buyer realized the consequences of the un-permitted remodeling and sued the seller for fraud regarding the permits, the septic system and other minor defects. Although the seller had expressly disclosed the un-permitted remodeling, the jury awarded the buyer over $100,000 of damages, ten times the cost of a new septic system.

These cases and other like them suggest that juries are unlikely to consider disclosure statements from a seller's perspective. Instead, juries uniformly seem to take the buyer's perspective and often treat the disclosures as a warranty from the seller. The seller is in the best position to know of and disclose problems with a property and has an economic interest in concealing or minimizing any defects. If a problem does exist, the seller's assertion that he did not know or thought the problem had been fixed will likely be disbelieved. In other words, no seller can count on "actual" or "personal" knowledge as a defense to a fraudulent concealment claim.

An Exercise. In most cases, the disclosure statement is either filled out by the seller with no more instructions or guidance than to fill it out to the seller's actual knowledge. As a result, most sellers do not appreciate the degree to which buyers will rely on their disclosures, and they usually take no more than twenty minutes to describe the history of the house. To appreciate how inadequate this approach is, take a disclosure form and complete it for your own house using your actual knowledge. After you have finished, carefully walk through the entire property looking for anything that is incorrect or incomplete. Unless you or your house is perfect, you will notice many conditions that should have been disclosed but weren't. If you were a typical seller (with an economic interest in having a bad memory), you would probably forget or overlook even more conditions as a result of having lived with them for years. A condition that is "normal" to the seller may be perceived as a defect by the buyer.

A seller is entitled to sell the property for its actual value in its actual condition. The only way to do that is by making full disclosure. Any time that you market a house with undisclosed defects, both you and your seller risk being sued. Even worse, your professional reputation is at risk. Protecting your livelihood requires affirmative steps to ensure that you are accurately representing your listings.

- Emphasize the importance of the disclosure statement to your sellers. Sellers already do not want to complete the disclosure statement and will gladly accept any suggestion from you that it is not important. Tell your sellers to take their time and walk through the property while they answer the questions. Encourage your sellers to use extra paper for a thorough description of the property.

- Explain the benefits of disclosure. Once a seller has disclosed a condition, the buyer has a duty to investigate. If the seller is not sure whether a problem exists or was fully repaired, disclosing what the seller does know will shift the risk of that condition to the buyer.

- Never advise less disclosure. If your seller wants to disclose a past defect or a potential problem, do not discourage them. If you advise a seller not to disclose a possible defect, you are asking to be sued. Too much disclosure does not produce lawsuits.

- Know your own duties. A listing agent has no duty to independently inspect the property for the buyer, but is obligated to disclose latent material defects that are known to the licensee. After the seller has completed the disclosure form, you should review it carefully to ensure that it is consistent with your own observations, and you should not market the property until you and the seller have agreed to the disclosures.

- Feel free to provide your sellers with a copy of this bulletin. Reading true horror stories from other sellers may be more meaningful than general advice about full disclosure.

Ultimately, avoiding lawsuits requires you to cultivate a culture of complete disclosure. Sellers look to you for guidance in making disclosures. Take that opportunity to emphasize the importance of full and complete disclosure. If a problem has been fixed, disclosing that it occurred will only inform the buyer that the seller was diligent in maintaining the property. Any failure to disclose a past or potential problem, however, has the appearance of fraudulent concealment.

You should always assume that the buyer is going to learn everything about the property after moving in. Many corrected problems leave physical traces such as water stains or noticeable patching. Neighbors are inexplicably compelled to ensure that buyers know the entire history of their new homes. How the buyer reacts to this information depends entirely upon the disclosures that the seller made.

A buyer who first learns of past flooding from a neighbor will feel cheated, even if the problem has been fixed. As often as not, even problems that have been repaired have a way of recurring. A seller who did not disclose the past defect because of a good faith belief that it had been fully repaired has legal defense, but will probably still lose. If you and the seller discussed whether to disclose the past flooding and agreed not to, a jury is especially unlikely to accept the explanation that you honestly believed the problem had been repaired. If it was not a problem, what harm was there in disclosing it?

On the other hand, if the buyer already knows the history of the property, the neighbor can only confirm what he already knows. Even if the problem does reoccur, the buyer has no legal claim if the seller disclosed all available information.

If your sellers sense that you are encouraging full and complete disclosure, they will be more likely to pay careful attention to the disclosure form. On the other hand, if you minimize the importance of the disclosure form or discourage full disclosure, sooner or later you will be sued for fraud. Even if you win the lawsuit, licensees who have been parties to such claims will tell you that the damage is done when the accusation is made.