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This month we report on a disturbing case that expands a seller's duty to disclose prior litigation.

Prior Litigation is a Material Fact Within the Seller's Duty to Disclose

Brokers and agents should take special note of the February 2009 decision of the California Court of Appeal in *Calemine v. Samuelson*. The Los Angeles County trial court ruled that Walter Samuelson, the seller of a condominium purchased by Calemine, met his burden of disclosure of facts regarding the existence of previous water intrusion. The Court of Appeal disagreed and held that the seller was obligated to disclose the existence of two lawsuits relating to that water intrusion 20 years prior, even though the repairs had been undertaken.

The facts seller knew —

In 1983, Samuelson and his wife bought a newly constructed 3-story condominium unit ("condo") in a multi-building condominium development. The lower level of the condo was a garage and bonus room. Samuelson was aware of construction defects and water intrusion in the complex and in his unit.

During the time Samuelson lived in the condo:

- He observed intermittent incidents of water intrusion and flooding in the lower level of the condo.
- He was a plaintiff along with the HOA and other unit owners in a 1986 construction defect lawsuit filed against the developer (first lawsuit).
- He knew that the repairs made after settlement of the first lawsuit were not effective throughout the development.
- He served on the HOA board as president from March 1993 to June 1994, and as treasurer from June 1994 to April 2001.
- He received the 1997 reports estimating the waterproofing repair costs at over \$1m.
- He knew that the HOA received \$410,000 from the early 1998 settlement of the second lawsuit
- He knew that the HOA accepted the lowest bid (by CHI for \$119,800) to do repairs to the complex common area and individual units after settlement of the second lawsuit.
- He knew that the CHI's proposal cautioned that "this is only one phase only of our due diligence in attempting to mitigate the water intrusion problem being encountered at this time. This proposal will only solve a portion of the problem. The remaining work is necessary to mitigate fully."
- He knew that after CHI's repair work was completed in November 1998, CHI wrote to him in care of the HOA that the "next proposed phase of work will apparently involve clean up,

patching, painting and 'band-aid' covering up of existing subterranean garage and storage room walls."

- o He knew that CHI confirmed discussions with HOA board members that "we can take no responsibility nor give any guarantees whatsoever, that the water penetration issues, through the retaining walls, will be controlled or corrected, due to the existing hydrostatic pressures..., or any other issues relating to dampness, as we are not addressing these issues in the garage/storage contract."
- o He knew that after the second repairs were completed, occasionally damp spots would appear on the garage floor during periods of heavy rain.

The disclosures seller made --

In the fall of 2001, Samuelson and Calamine negotiated for the sale of the condo and Samuelson signed a real estate transfer disclosure statement (TDS) in which he stated he was aware of "[f]looding, drainage or grading problems" and added the notation "[h]eavy rains below ground walls & slab." He explained that water came up through the cracks in the garage slab approximately five to six times during the almost twenty years he lived in the condo. Samuelson did not disclose the litigation in the TDS, and he never mentioned the lawsuits during the two or three conversations he had with Calamine during the transaction, because he believed he was obligated only to disclose pending actions. The listing agent completed the agent section of the TDS by stating: "Water damage noted in garage. Buyer is urged to get a physical inspection from a licensed contractor."

In May 2002, Calamine obtained an inspection report that revealed evidence of below grade leakage in the garage south and west walls, moisture bubbling & efflorescence at below grade foundation walls and staining along hairline floor cracks in garage, and moisture staining at base boards in the bonus room. The report said: "Status of leakage cannot be visually ascertained." The report recommended further investigation and contact with the seller for status/information to determine if repairs had been or would be made, which would typically be an H.O.A. repair.

In June 2002, Calamine obtained a termite report which also noted that the garage area had excessive moisture-damaged drywall and plaster, the source of which appears to be from soil abutting a retaining wall. The termite report noted that other contractors had installed additional concrete and drainage in the past, and that there was no moisture evident at the time of inspection.

Calamine contacted Samuelson for an explanation. According to Calamine, Samuelson stated: "We've had some water intrusion near the bottom of this wall and up through the slab and the homeowners association came in. They dug out around the patio areas, waterproofed the wall, put in French drains. Then inside the garage—on the outside they dug down the wall, exposed the wall, waterproofed the wall put French drains in. Put the dirt back in. Rebuilt the patios. On the inside of the unit they waterproofed the walls and put these drywall—you know, drywall in those areas. Haven't had a problem since. Problem solved." According to Samuelson, he stated that there had been some water damage "and we weren't having it anymore, it had been fixed."

On the basis of Samuelson's explanation, Calamine believed the water intrusion problem was a minor issue. Escrow closed in July 2002 and the Calamines moved into the condo.

The floods that came –

In January 2005, the condo garage flooded and it flooded again in March 2005 and in January and April 2006. After the first flood, Calemine learned that there had been two lawsuits, that the HOA had received a recovery from the developer in the first lawsuit and made repairs, that the repairs were ineffective, that a second lawsuit was settled with the contractor, and additional repairs were made.

The lawsuit buyer filed –

The Calemines filed a lawsuit against Samuelson in August 2005, alleging that:

- o he breached his duty to make full and complete disclosures of past actions,
- o he failed to disclose he was a member of the HOA board at the time of the second lawsuit, and
- o he failed to describe the repairs made after the second lawsuit.

Samuelson asked the court to throw the case out, because the undisputed evidence showed that:

- o Calemines were aware of all material facts relating to the water intrusion;
- o he did not make any representations that were knowingly false;
- o the TDS imposed no duty on him to disclose the specific facts that Calemines claimed were omitted or concealed, including the scope of prior repairs, the decision to implement limited repairs, the existence of nonpending lawsuits and the settlement of a lawsuit.

The Calemines argued that the court should decide whether the information Samuelson provided to them in the TDS was incomplete, misleading or inaccurate. The trial court agreed with Samuelson finding “that there was sufficient disclosure of defects by moving defendant Walter Samuelson.”

The duty to disclose –

A seller of real property has a common law and a statutory duty of disclosure. The courts have established the common law duty that where the seller knows of facts materially affecting the value or desirability of the property and also knows that such facts are not known to or within the reach of the diligent attention and observation of the buyer, the seller is under a duty to disclose them to the buyer. Undisclosed facts are material if they would have a significant and measurable effect on market value. Once the essential facts are disclosed, a seller is not under a duty to provide details that would merely serve to elaborate on the disclosed facts. Failure to disclose a material fact, may subject the seller to liability because his conduct in the transaction amounts to a representation of the nonexistence of the facts he failed to disclose. Whether the undisclosed fact is of sufficient materiality to have affected the value or desirability of the property is a “question of fact” for the court or jury to decide.

The California Civil Code establishes a residential seller’s statutory duty to disclose. The statutory duty does not alter a seller’s common law duty of disclosure, but makes the required disclosures specific and clear. Civil Code section 1102.6 mandates the precise disclosure form which must be used which requires a seller to answer whether he or she is “aware of any significant defects/malfunctions” in the slabs and sidewalks, and whether he or she is aware of “[f]looding, drainage or grading problems” and “[a]ny lawsuits by or against the Seller threatening to or affecting this real property, including lawsuits alleging a defect or deficiency in this real property or ‘common areas’ (facilities such as pools, tennis courts, walkways, or other areas, co-owned in undivided interest with others).” Furthermore, Civil Code

section 1102.7 requires Seller to make each disclosure in “good faith,” defined as “honesty in fact in the conduct of the transaction.”

The appellate court decisions –

The appellate court found that the Samuelson’s disclosures, on the TDS and orally, concerning the *existence of water intrusion* were adequate and made in good faith, and that there was no evidence that Samuelson had any reason to doubt the accuracy of his representation that the repairs had resolved the problem in the condo garage, i.e., there had been no water intrusion for several years prior to the sale to Calemine. Further information concerning the type and scope of repairs made is within the category of “elaboration” that the courts have determined is not part of a seller’s duty of disclosure.

However, the appellate court found that Samuelson’s disclosures concerning the *existence of the lawsuits* was within his duty to disclose information materially affecting the value or the desirability of the property. The court said, “case law holds that while disclosure of the details of a lawsuit alleging defects in the property need not be disclosed, a seller’s duty of disclosure encompasses disclosure of the existence of such a lawsuit.” The court cited a decision in another case and explained that once the seller has satisfied its duty of disclosure by informing the buyer of the existence of the litigation and its settlement, “the details of the suit were certainly within the diligent attention of the buyer, who could have examined the file in its entirety to learn all the details of the suit and its settlement.”

Samuelson failed to disclose to Calemine the existence of either the first or second lawsuit, which disclosure would have enabled Calemine to examine the details of those actions and evaluate their purchase in light of information including that the water intrusion had existed since the condominium was built, repairs throughout the complex were twice ineffective, and the CHI repairs were made on a budget governed by the amount of the second lawsuit settlement. Without Samuelson’s disclosure of the existence of the lawsuits, these matters were not within appellants’ diligent attention. The existence of the two lawsuits was material, because Calemine stated that they would not have purchased the condo had they known about the prior lawsuits.

The case was sent back to the trial court for determination whether Samuelson was obligated to disclose the existence of the lawsuits as a material fact affecting the desirability and value of the condo.

What this case means for brokers

This case is important to real estate brokers when selling a home where there was a lawsuit about alleged damage to the property. Simply disclosing the damage is not sufficient. The broker must also disclose the existence of the lawsuit, even if it was 20 years ago and the defects have been repaired without further problems! Failure to do so may result in another lawsuit – one against the broker!

Reminders!

Employer’s Duty to Train Supervisors

2009 is an AB 1825 training year. If your company has 50 or more employees, you must provide all supervisors with harassment prevention training. A seminar that meets the state law requirements is

available. Contact Sylvia J. Simmons at The Giardinelli Law Group, APC at the email address or phone number below for information.

Do Not Use the Loan Modification Listing Agreement Form

Real estate licensees who have the CAR Loan Modification Listing Agreement (LMLA) form are being advised by CAR not to use it until further notification due to a regulatory interpretation taken by the Department of Real Estate. For that reason, the LMLA was rescinded by CAR and was omitted from our April newsletter report on new forms.

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