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Blocked Views, Flooding Blues, and Parking for Pews

Summarizing some of the more interesting cases affecting REALTORS® in 2011

ALLEGED VERBAL PROMISES NOT IN THE CONTRACT CANNOT BE BASIS FOR FRAUD CLAIM

In one of the more important cases from the last year, the Georgia Supreme Court ruled that buyers could not rely on alleged verbal representations regarding the views they would have from their condominium units. The eight buyers who brought the lawsuit each purchased residential condominium units at Atlantic Station in late 2005 or early 2006. The buyers alleged that the developer advertised "spectacular city views" and the real estate brokers verbally advised buyers that any future development would be low to mid-rise buildings. However, each buyer signed an agreement containing a provision stating that "[t]he views from and natural light available to the Unit may change over time due to, among other circumstances, additional development and the removal or addition of landscaping". There was also a disclaimer at the top of the first page of the purchase and sale agreement as required by the Georgia Condominium Act stating that "ORAL REPRESENTATIONS CANNOT BE RELIED UPON AS CORRECTLY STATING THE REPRESENTATIONS OF SELLER". Finally, there was an express disclaimer in the purchase and sale agreement in which the buyer affirmed that they did not rely upon any representations or statements of Brokers; and a comprehensive merger clause. A merger or entire agreement clause provides that the purchase and sale agreement is the entire agreement of the parties and that no representations outside of those contained in the contract are being relied upon by any party. In this case, the entire agreement clause provided as follows:

> 24. ENTIRE AGREEMENT. This agreement contains the entire agreement between the parties hereto. No agent, representative, salesman or officer of the parties hereto has authority to make, or has made, any statements, agreements, or representations, either oral or in writing, in connection herewith, modifying, adding to, or changing the terms and conditions hereof and neither party has relied upon any representations or warranty not set forth in this Agreement. No dealings between the parties or customs shall be permitted to contradict, vary, add to, or modify the terms hereof.

Purchasers filed this lawsuit on December 31, 2008, raising, among other things, allegations of fraud in the inducement, negligent misrepresentation, negligent supervision, as well as negligence claims against the individual defendants. As one of the buyers' remedies, the complaint sought the rescission of the contracts which had it been successful would have forced the seller to repurchase all of the units.

On the same date the lawsuit was filed, counsel for purchasers sent a certified letter to Developers' counsel demanding rescission on behalf of all eight purchasers. The letter stated that purchasers "desire a rescission and hereby tender same." Though the letter purported to give developers thirty days to respond to the demand for

rescission, the letter also stated that purchasers already "filed the enclosed civil action against all the named defendants."

The legal requirements for the rescission of a contract where the buyer tries to undo the transaction and give back the property to the seller is often the subject of confusion on the part of both REALTORS® and their attorneys.

In general, a party alleging fraudulent inducement to enter a contract has two options: (1) affirm the contract and sue for damages from the breach of contract; or (2) promptly rescind the contract and sue in tort for fraud. Where a party elects to rescind the contract, he or she must do so prior to filing the lawsuit.

In this case, the buyers failed to tender rescission prior to filing their lawsuit. As the Court explained, it is well settled law in Georgia that one who seeks the rescission of a contract on the ground of fraud must offer to give back what he or she bought *as a condition precedent* to bringing the action. The rationale for this requirement is that the party charged with perpetrating a fraud should be given the opportunity to redress the wrong before being served with a suit for rescission.

In this case, the buyers sent a certified letter to Developers' counsel purporting to rescind their agreements on the same day they filed their lawsuit. However, the letter clearly stated that the lawsuit had already been filed. Given that the Developers should have been given the opportunity to correct any wrong before being served with a lawsuit, Purchasers' demand for rescission, served contemporaneously with the filing of their lawsuit, could not be held to satisfy this requirement.

While the Supreme Court did not address the timeliness of the offer to rescind, Georgia law also requires the party seeking rescission to offer to give back the property as soon as he or she learns of the fraud and not do any improvements to the property subsequent to the tender of the property. For example, a buyer is seeking to rescind his or her purchase of a single-family home due to some alleged fraud of the seller would never want to paint a bedroom a different color, add wallpaper, plant additional shrubs or trees or make other modifications or improvements to the property. This is because such actions would reflect an intention on the part of the buyer to keep the property and can be a basis to deny the claim for rescission.

The Supreme Court then turned its attention to the conflict between the alleged verbal representations and the representations set forth in the purchase and sale agreement. The Court explained that it is well-settled law in Georgia that a party who has the capacity and opportunity to read a written contract cannot afterwards sue for fraud based on oral representations that differ from the terms of the contract. In fact, the Supreme Court ruled that the only type of fraud that can relieve a party of his obligation to read a written contract and be bound by its terms is a fraud that prevents the party from reading the contract.

The crux of Purchasers' argument was that they are not bound by the terms of their agreements because the brokers promised "spectacular city views" at the same time that the developer was moving forward with plans to erect a 46–story condominium across the street that would ultimately block Purchasers' views. Nevertheless, the Purchasers all signed agreements that expressly state that the views may change over

time, oral representations of the sellers could not be relied upon, Purchasers did not in fact rely upon any oral representations or statements of Brokers, and the entire agreement clause bars a claim to the contrary.

The Supreme Court also explained that in any case alleging fraud the buyers' must prove, among other things, that their reliance on allegedly fraudulent representations (*i.e.*, that the spectacular views from the units would not change) is justified or reasonable. The Court then held that if the contact contained a valid merger or entire agreement clause, it precluded the buyers as a matter of law from arguing that their reliance was reasonable.

This case is an important decision for REALTORS® because had the case been decided in favor of the buyers, it would have opened the door to endless claims against REALTORS® from buyers and sellers alleging that they relied on verbal representations contrary to the written terms of the contract. Fortunately, the Supreme Court reaffirmed its long standing position on disputes of this type.

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THE CASE OF THE UNDISCLOSED FLOODED HOUSE

When a buyer purchases a house that later floods, you can pretty well rest assured that the buyer, if he or she wasn't told about previous flooding, will sue the seller and the listing broker (or at least think about it).

This is what happened in the recent case of *Shaw v. Robertson*. Shaw purchased a home that flooded when the North Fork of Peachtree Creek overflowed during Hurricane Ivan. Shaw sued the seller and the listing broker contending that they committed fraud by failing to disclose that the property had flooded previously and was located in a flood zone. However, prior to purchasing, Shaw did little to learn about the potential for flooding on the property. She spent around 15 minutes at the property before authorizing her real estate agent to make an offer on the house. She did not notice the storm drains in front of the house. She did not recall having reviewed flood maps of the property on the FEMA website. She signed a contract to buy the house "as is," and closed without having the house inspected or having the boundaries surveyed. She never noticed that a creek was nearby.

Shaw saw on her settlement statement at the closing that a company had performed a flood survey on the property, for which she was charged $25, but she never saw the survey itself and her lender did not require her to purchase flood hazard insurance. The survey indicated that the property was "partially within a Special Flood Hazard Area." The existing structure, however, was not affected and was not in the floodplain. Shaw's settlement statement at closing also included $350 for a property appraisal fee, but she did not see the appraisal itself. The appraisal indicated that the property was located in FEMA Zone X and referenced a FEMA map date and number.

Shaw did not know until after she moved in that the house even had a crawlspace. After the flood, Shaw's neighbor told her that part of the property was in a flood plain and the FEMA had purchased the property across the street because it was

also in a flood plain. Shaw left the property and never returned, and her lender foreclosed on it.

Even though Shaw did nothing to protect herself, she nevertheless argued that a genuine issue existed on whether the sellers committed fraud by not disclosing that the property had previously flooded. The Court of Appeals disagreed. The Court first explained that caveat emptor or buyer beware is the law in Georgia. There is an exception to the law allowing buyers to sue sellers for passively concealing defects. However, the exception only applies to defects that the buyer could not have discovered through the exercise of due diligence.

Shaw argued that an inspection could not have revealed the previous water damage because it had been completely repaired. She also argued that a property inspection would not have disclosed that the property was located in a flood zone, and that even if she had looked at the public flood maps, they were "confusing and inconsistent and the property boundaries indiscernible." She also argued that the maps did not show whether the property had sustained previous flooding or water damage. Finally, she contended that she properly relied on the Seller's Disclosure Statement which did not reveal any flooding issues.

In considering these arguments, the Court viewed the key question in the case as whether Shaw could have discovered that the property was in a flood zone by exercising due diligence rather than whether the sellers failed to disclose the previous flooding. In answering this question, the court found that a review of reasonably accessible public documents would have revealed that the property was located in a flood zone. In fact, in her amended complaint, Shaw included as exhibits copies of a FEMA Flood Map Report showing that he property is located in Flood Zones "AE, 0.2% ANNUAL CHANCE, X," and a Flood Insurance Rate Map for the area showing both the location of the nearby North Fork of Peachtree Creek in relation to the property and the areas designated Flood Zones AE and X, which cover about a third of the street on which the property is located. Finally, a FEMA "Letter of Map Amendment Determination Document" states that portions of the property were located in a Special Flood Hazard Area, although the structure on the property was outside of the area.

While the FEMA maps do not document whether this particular property had been flooded before, the Court observed that they do establish whether the property might flood at some time in the future. The Court noted that the buyer's complaint was not that the property was damaged from previous flooding, but rather that previous flooding would have given Shaw notice of the possibility of future flooding. As the Court saw it, the possibility of future flooding is what the FEMA maps show, and the maps are not only public record but were reviewed upon her lender's direction by a flood certification company and an appraiser before Shaw closed the sale. Because a review of reasonably accessible public documents would have revealed that the property was located in a flood zone, the Court ruled that the sellers were under no burden to disclose that fact to Shaw.

Shaw also argued that the Brokerage Relationships in Real Estate Transactions Act (BRRETA), requires that agents and brokers not convey false information during a real estate transaction. BRRETA requires that a broker disclose to all parties any adverse material facts pertaining to the physical condition of the property "actually

known by the broker that could not be discovered by a reasonably diligent inspection of the property by the buyer." It also requires a broker to disclose

> [a]ll material facts pertaining to existing adverse physical conditions in the immediate neighborhood within one mile of the property which are actually known to the broker and which could not be discovered by the buyer upon a diligent inspection of the neighborhood or through the review of reasonably available governmental regulations, documents, records, maps and statistics.

Regardless of whether the broker in this case knew any adverse facts about the property or immediate neighborhood, the Court again found that since Shaw failed to act diligently, she was unable to recover from the agents or broker based upon any alleged failure on their part to disclose information.

This case is one of the more important decisions on flooding ever handed down by our Georgia Court of Appeals. The Court is saying that if a buyer could have discovered that a property is in a special flood hazard zone by reviewing FEMA maps, that is sufficient to put the buyer on notice of the potential for flooding and relieves the seller from making such a disclosure. The lesson of the case is that buyers need to determine if a property is in a flood hazard zone and, if it is, to carefully investigate the realistic potential for the property and the improvements thereon to flood.

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DUE DILIGENCE REQUIRED TO MAINTAIN A CLAIM OF FRAUD

Church #2 bought property from Church #1 and later sued alleging that Church #1 misrepresented the property that was included in the sale. Church #2 was allegedly told by Church #1 that the property included an adjacent parking lot, when in fact, this was not a part of the property that was conveyed.

The parties entered into a purchase and sale agreement and attached a survey of the property. The survey showed the church property plus the adjacent parking lot. However, the survey also included a "deed" line separating the church property from the parking lot. While the survey of the church property included distances and directions from which a legal description could be prepared, the adjacent parking lot did not have distances and directions.

During the due diligence period set forth in the purchase and sale agreement, Church #2 asked Church #1 to prepare another survey of the property and Church #1 agreed to do this. The second survey also showed both properties and like the first survey included directions and distances around the church property. The second survey stated specifically that it was a boundary survey of the church property and contained a written legal description setting forth a metes and bounds description of the surveyed property following the directions and distances of the lines encompassing only the property owned by Church #1. Moreover, the second survey specifically described the adjacent land as being an area 70 feet over the surveyed property line.

During the due diligence period, Church #2 obtained a commitment for title insurance on the property to be purchased from Church #1. The title insurance

commitment contained the same metes and bounds description of the property that was shown on the second survey (and that excluded the adjacent land).

Prior to closing, the pastor of Church #2 learned from a previous tenant of the property that Church #1 did not own the adjacent parking lot. The pastor of Church #2 then called the pastor of Church #1 who allegedly assured him that Church #1 owned the entire parking lot. The pastor of Church #2 relied on this assurance and closed on the property without further inquiry. After the closing, Church #2 eventually learned that it had not purchased the adjacent parking lot and sued Church #1 for fraud and misrepresentation.

On appeal to the Georgia Court of Appeals, the Court first explained that in a fraudulent misrepresentation claim, justifiable reliance on the false information was an essential element of the claim. Reliance cannot be justified if the buyer could have protected itself against the fraud through the exercise of due diligence. The Court of Appeals then ruled that unless a purchaser of real property is fraudulently prevented from examining the property or an examination would not have disclosed the falsity of a misrepresentation, it cannot be permitted to claim that it has been deceived by false representations about which it could have learned.

In this case, an examination of documents in the possession of Church #2 before the closing would have revealed that the adjacent land was not included within the boundaries of the purchased property. Accordingly, the Court of Appeals held that the evidence was plain and indisputable that Church #2 failed as a matter of law to exercise due diligence to discover the true boundaries of the purchased property.

There are many lessons in this case. The most obvious is that while we should trust in God in spiritual matters, it still pays to do your homework in real estate transactions and carefully review the information you have been provided by the seller.

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FORMER HUSBAND NOT ENTITLED TO NOTICE OF FORECLOSURE

A wife bought a property and assumed the existing mortgage on the property. The wife eventually defaulted on the mortgage and the banks foreclosed on the property. Prior to the foreclosure, the wife's former husband wrote the bank and said he now owned the property as a result of a divorce decree. In foreclosing on the property, the bank sent notice to the wife but not to the husband (who was not on the title at the time the mortgage was assumed). The ex-husband sued arguing that the bank wrongfully foreclosed and that he should have received notice of the foreclosure. The Georgia Court of Appeals disagreed and ruled that under Georgia law, only the debtor has to receive notice of the initiation of foreclosure proceedings. The lesson of the case is that transferring property from one person to another will not slow down the foreclosure nor impose any new notice obligations on the mortgage lender.

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