RISK REDUCTION ISSUES

INTRODUCTION

The Michigan Association of REALTORS®, both through its Public Policy Committee and its Legal Action Committee, is constantly striving to reduce sources of risk for REALTORS®. While it may not seem to be the case, the sources of risk for REALTORS® have been steadily reduced over the years. However, most specific types of risk can be avoided only if REALTORS® are proactive. As an example, the seller's disclosure act substantially reduces the risk of fraud claims against REALTORS®, but only so long as REALTORS® and their clients properly use the seller's disclosure form.

This article will review various tools available to REALTORS® to reduce the risk of claims against them. It is not possible to cover every technique for risk reduction in a single article or in a single class. Other matters of risk reduction are covered in different topics which are part of this legal update. Nonetheless in this article we will discuss a number of major risk reduction techniques.

DISCUSSION

a. The Beginning – Independent Contractor Agreements

There are two major sources of potential conflict which exist from the day an agent joins her first brokerage firm. One major source of conflict is with the government. Is the agent an independent contractor or an employee for purposes of workers compensation, withholding taxes, unemployment insurance, and claims of negligence by third parties? Are the commissions earned by associate brokers or salespersons part of the broker's "gross receipts" under the Michigan Business Tax? The other major source of conflict occurs when and if the agent decides to move to another brokerage firm (which is a fact of life). Both of these issues can be addressed in an independent contractor agreement. Specific provisions regarding departing salespersons are covered under another topic as part of this legal update. In this article, we will focus on the regulatory provisions.

A broker and an agent can effectively eliminate any controversy with the state and federal government with respect to the agent's status by simply utilizing an independent contractor agreement. In the absence of an independent contractor agreement, the government will consider numerous factors in determining whether a person is acting as an employee or an independent contractor of the brokerage firm. The tests focus generally on the amount of control the brokerage firm is exercising over the agent. The tests applied by the Internal Revenue Service and other governmental agencies are so subjective that it is almost impossible to predict in advance whether an agent would be treated as an independent contractor or employee.

Fortunately, both NAR and MAR have obtained legislation which permits brokers and agents to eliminate any uncertainty as to the status of the agent as an independent contractor.

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NAR obtained legislation that created a "safe harbor" for purposes of federal income taxation. 26 U.S.C. § 3508. MAR obtained an amendment to the Occupational Code and other state laws by which brokers and agents can conclusively establish an independent contractor relationship for various state law purposes. Under both laws, an independent contractor status exists between a broker and salesperson if: (1) a written agreement exists in which the real estate broker states that he does not consider the associate broker or salesperson as an employee for federal and state income tax purposes; AND (2) not less than 75 percent of the annual compensation paid by the real estate broker to the associate broker or salesperson is from commissions from the sale of real estate.

To eliminate any controversy over the status of salespersons as independent contractors, it is an absolute requirement that the broker and salesperson have a written independent contractor agreement in place. While brokers and salespersons are certainly free to develop their own form of independent contractor agreement, it is highly recommended that the "taxation" provisions of the MAR form of independent contractor agreement be included in any customized independent contractor agreement. The "taxation" provisions of the MAR form have been reviewed and accepted by the Internal Revenue Service.

If a brokerage firm and salesperson do not have a written independent contractor agreement in place, but nonetheless treat the salesperson as an independent contractor, then the consequences could be catastrophic. If, for example, a brokerage firm failed to pay unemployment taxes on a salesperson who was later deemed to be an employee, the Michigan Employment Security Act would require the brokerage firm to not only pay all contributions owed, but also allow the Michigan Employment Security Commission to assess penalties up to 50 percent of the amount owed and interest up to 50 percent of the amount owed. Similarly, if the Internal Revenue Service ultimately determined that the salesperson was an employee and not an independent contractor, then the brokerage firm could be required to pay significant penalties to the IRS for failing to comply with withholding requirements.

b. Indemnification Clauses in Listing Agreements

Listing agreements should contain a provision addressing liability for injuries which occur on or to the property while it is listed. There is one scenario under which REALTORS® presently have liability for potentially dangerous conditions and another area in which there is a movement to create liability.

In 1997, the Michigan Court of Appeals considered the issue of whether a REALTOR® could be liable for conditions at an open house in Michigan. *Anderson v Weingand,* 223 Mich App 549; 567 NW2d 452 (1997). In this case, a homeowner and a REALTOR® were sued by a person who slipped and fell on ice. The snow had fallen the day before the open house, and the owners had cleared the driveway and sidewalk of the snow. The owners then left to visit relatives, as their REALTOR® did not want them present during the open house.

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On the following day, a Sunday, the sun was shining in the morning and it was relatively warm. However, as the day went on the temperature dropped. Unfortunately, a residue of snow left on the sidewalk had melted in the morning but then froze again into black ice in the afternoon. A person who fell on the black ice while walking up to attend the open house sued both the sellers and the listing REALTOR®.

The Michigan Court of Appeals upheld the trial court's decision to dismiss the case against the homeowners. The Court found that a homeowner is not required to go back and re-examine a sidewalk on an hourly basis to determine if ice has formed on the sidewalk. Instead, homeowners are only required to take reasonable measures within a reasonable time after a snowfall to reduce the hazard of injury to persons like the plaintiff in this case.

Unfortunately, the Court of Appeals did not rule in favor of the REALTOR®. The Court found that the homeowners had granted temporary possession and control of the property to the REALTOR® for purposes of holding the open house. Since the REALTOR® was in possession and control of the property at the time of the fall, the Court found that the REALTOR® could be liable for any injuries suffered by the plaintiff. Further, since the plaintiff was an invitee to the property (as opposed to a licensee), the REALTOR® was required to take reasonable steps within a reasonable time to diminish the risk of injury on the ice.

Since this case was decided in 1997, Michigan case law has developed which protects property owners and REALTORS® from some of these types of claims. In more recent years, Michigan courts have generally determined that when there is a danger which would be open and obvious to a reasonable person, a property owner is not liable for damages suffered by someone who is injured by reason of the condition. Michigan courts have held that a "condition is open and obvious if it is reasonable to expect an average person of ordinary intelligence to discover the danger upon casual inspection." In general, there is no duty to warn someone of an open and obvious danger.

In *Dyer v Russell*, unpublished opinion per curiam of the Michigan Court of Appeals, issued December 18, 2007 (Docket No. 273574); 2007 WL 4415467, the Court considered a case in which the plaintiff, a licensed assistant to a REALTOR®, went to the defendant's home for the purpose of showing the house to potential buyers. The licensed assistant slipped and fell down the basement stairs. The REALTOR®'s licensed assistant sued the sellers, arguing that they were liable to her for premises liability. The trial court granted sellers' motion for summary disposition finding that the poor condition of the basement stairs was open and obvious.

The REALTOR®'s licensed assistant in this case contended that despite the fact that the condition of the basement stairs was open and obvious, the sellers should nonetheless be liable because the basement stairs did not comply with the Michigan Residential Building Code as adopted by the City of Lansing. It was contended that the basement stairs were narrow, steep, and did not have handrails or walls on either side. The Court of Appeals determined that there was no authority in Michigan to demonstrate that private owners of residential real estate can be liable for a building code violation under the circumstances of that case.

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It should be noted that under Michigan law, generally, a property owner can still be responsible for an open and obvious danger on their property if "special aspects" exist in the case. Typically, a "special aspect" is a condition that makes the open and obvious danger unavoidable to a person. In this particular case, the plaintiff contended that her status as a licensed assistant to a REALTOR® was in fact a "special aspect." She claimed that the stairs were effectively unavoidable because she had some obligation to the property owners to descend the basement stairs. The trial court and the Court of Appeals rejected this argument, finding that the Plaintiff's status as a licensed assistant for a REALTOR® did not constitute a "special aspect."

A second line of potential liability is presently being pursued against REALTORS®. This potential liability arises from damage allegedly caused to a residence by the REALTOR®, a cooperating REALTOR®, or a prospective buyer. For example, if a prospective buyer on visiting the seller's residence turns on and leaves on a gas burner which ultimately results in a fire, the insurance company of the seller may seek reimbursement from either the listing REALTOR® or the cooperating REALTOR® who was showing the residence to the prospective buyer. It should be noted that the attempted assertion of this type of liability is being resisted, and we are presently unaware of any case finding a listing or cooperating REALTOR® liable for this type of damage claim.

Both of these types of liability can be handled by including appropriate indemnification language in the listing agreement. Under this type of indemnification provision, the sellers would indemnify the listing and cooperating REALTORS® for these types of claims. Language similar to the following provision is suggested:

> INDEMNIFICATION: Seller shall indemnify and hold harmless Broker, Broker's agents and cooperating agents, from any and all liability for any reason as a result of injury to person(s) or damage or loss to property arising out of the marketing of Seller's home pursuant to this listing.

c. Contractual Reduction of the Period of Liability to a Seller or Buyer

More than one REALTOR® has been faced with the situation where he has been sued by an unhappy buyer or seller almost three (3) years after he last had any dealings with the seller or buyer. Such claims are typically based on a claim of breach of fiduciary duty and/or alleged misrepresentation. Unfortunately, agents involved in the transaction are no longer with the brokerage firm and are not to be found. Further, the witnesses that are still with the brokerage firm have a very vague recollection of the transaction or circumstances which formed the basis for the claim. These practical problems arise from the fact that most claims which can be asserted against REALTORS® are subject to a three-year statute of limitations, and other claims, such as breach of contract, are subject to a six-year statute of limitations. In other words, the seller or buyer has between three and six years to timely sue the REALTOR®.

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In 2005, the Michigan Court of Appeals considered the validity of a provision in an employment application which shortened the time frame in which an employee of DaimlerChrysler Corp. had to file a civil rights suit against his employer. *Clark v Daimler-Chrysler Corp,* 268 Mich App 138; 706 NW2d 471 (2005). The ordinary statute of limitations for a civil rights claim is three years. This case involved an employment application in which the employee agreed that he would bring any civil rights suit within six (6) months from the date of the occurrence of the facts which provided the basis for the suit. The Court of Appeals held that such a provision was enforceable.

After the *Daimler-Chrysler* decision, it was not certain whether a court would uphold the validity of a similar contractual shortening of the statute of limitations as between REALTORS® and buyers and sellers. However, a subsequent Court of Appeals decision demonstrated that such a provision would be upheld. *Dean v Haman,* unpublished opinion per curiam of the Michigan Court of Appeals, issued May 16, 2006 (Docket No. 259120); 2006 WL 1330325. In this case, a buyer sued a home inspector for allegedly missing defects in the home. The buyer sued the home inspector approximately nine months after the inspection. The contract between the buyer and the home inspector had indicated that any claims must be brought against the home inspector within six (6) months from the date of the inspection. The trial court dismissed the action against the home inspector based on the six-month contractual limitation. The Michigan Court of Appeals affirmed the decision of the trial court. The Court determined that six (6) months was a reasonable period of time for the buyers to discover any defects which may have been missed by the home inspector. Obviously, if the Court of Appeals determined that any defects missed by a home inspector could reasonably be discovered within six (6) months of the inspection, it follows that the Court would also find that any defects allegedly concealed by a REALTOR® could also be discovered within six (6) months from the date of closing.

The last revisions to MAR's Buy and Sell Agreement, Exclusive Listing Contract, and Exclusive Buyer's Agency Agreement all contain a paragraph entitled "LIMITATION," which sets forth a six-month contractual limitation for a buyer or seller, as applicable, to file claims against the REALTOR® arising out of the transaction. For example, MAR's Exclusive Listing Contract provides:

> LIMITATION: Seller and Broker agree that any and all claims or lawsuits between the parties relating to this Agreement must be filed no more than six (6) months after the date of termination of this Agreement. The parties waive any statute of limitations to the contrary.

REALTORS® wishing to incorporate a limitation provision into their various agreements may use the wording set forth in the MAR forms.

d. Agency Disclosure Forms

REALTORS® have been required to comply with Michigan's Agency Disclosure Law for over ten years. Some REALTORS® complain that it is sometimes difficult to comply with the agency disclosure requirements. All REALTORS® should be aware of the fact that the Michigan Agency Disclosure Law has provided substantial protections to all REALTORS® in at least two scenarios.

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First, many REALTORS® continue to engage in buyer representation without the benefit of a buyer's agency agreement. Claims are sometimes asserted by sellers that a cooperating REALTOR® has improperly failed to make disclosures of material facts about the buyers to the sellers or to the listing REALTOR®. Fortunately, in most instances the cooperating REALTOR® has made an appropriate agency disclosure and can demonstrate that all parties were aware that she was representing the buyers, as evidenced by the agency disclosure form.

Second, courts have found that agency disclosure by a listing REALTOR® shields the listing REALTOR® from certain types of claims asserted by buyers. In the typical scenario, a listing REALTOR® receives offers from more than one unrepresented buyer (*i.e.*, the listing REALTOR® is working with several buyers as customers). The offers are then submitted to the seller with a recommendation by the listing REALTOR® that the seller accept one of the offers for reasons specific to the seller.

When the second, losing buyer finds out that the seller accepted the other offer based upon the REALTOR®'s recommendation, the losing buyer has tried to sue the listing REALTOR®, contending that he breached a fiduciary duty owed to that buyer. In these instances, the listing REALTOR® has prevailed based on the fact that he made the appropriate agency disclosure to both buyers indicating that he was representing the seller.

e. Seller's Disclosure Form

The Michigan Seller's Disclosure Act (the "SDA") has been in effect since January 1, 1994. The correct use of the seller's disclosure form has served not only to protect sellers, but also to protect REALTORS®. The correct use requires that sellers, NOT THEIR AGENT, complete the form. Correct use requires that the sellers complete the form honestly and completely. It should be noted that at the time the SDA went into effect, many commentators thought that the seller's disclosure form would be the cause of new claims against sellers and their agents. These commentators worried that the SDA would be used as a sword against sellers and their agents, as opposed to a shield. Recent Michigan Court of Appeals decisions demonstrate that these commentators were wrong.

In *Sterrett v Theisen*, unpublished opinion per curiam of the Michigan Court of Appeals, issued September 20, 2005 (Docket No. 262226); 2005 WL 2292677, the Sterretts bought a house and some adjoining real property in rural Clinton County from the Theisens. The Theisens' home was listed by a REALTOR® firm. The Theisens had indicated on the seller's disclosure statement that they were not aware of any encroachments, easements, zoning violations or non-conforming uses, or of any settling, flooding, drainage, structural or grading problems on their property.

After closing, the Sterretts hired a contractor to build a large pond on an area in the middle of the property in front of their house. Unfortunately, during the excavation, the excavator struck a large underground drain. The drain was about 15 inches in diameter and ran through the middle of the property. According to the Sterretts, despite the expenditure of large sums of money to fix the drain and fill in the land, their property flooded each time it rains.

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The Sterretts sued the Theisens, the listing agent and the listing brokerage firm. The Sterretts claimed that all of these defendants made misrepresentations and violated the Michigan Consumer Protection Act.

It should be noted that the listing agent testified that in the Spring of 2003, he heard some concerns from another potential buyer of the Theisens' property regarding an easement through the property. A prior title search did not turn up any easements. However, the listing agent contacted a title insurer and requested that it further research the title. The title company then determined that no easement had been recorded with the register of deeds; however, "an easement for drain purposes vested in the Clinton County Drain Office" was disclosed to the title company. This information had been provided to the Sterretts prior to closing.

The Sterretts' claims against the Theisens and their REALTOR® were based in part upon the alleged misrepresentation made by the Theisens in the seller's disclosure statement that they were unaware of easements on their property. The trial court summarily dismissed this claim, and the Court of Appeals affirmed the dismissal by the trial court.

Both the trial court and the Court of Appeals determined that the Sterretts' reliance upon the representation in the seller's disclosure statement was unreasonable. First, the Court noted that the seller's disclosure statement is simply a representation to the Sterretts that the Theisens were unaware of any easements on the property. The Sterretts could provide no evidence to show that the Theisens knew this representation was false when they made it. Further, the Sterretts were provided with a revised title commitment from their title insurer which disclosed the existence of a drain easement on the property prior to closing. Thus, the Sterretts were in possession of facts that would lead a reasonable person to make further inquiries into the extent of the easement.

The result in this case conforms exactly with the intent and purpose of the SDA. In their seller's disclosure form, the Theisens disclosed exactly what they knew about the property from their having lived on the property. There was no reason for them to know, nor could the buyers demonstrate that the Theisens were aware, of a pipe buried deep beneath the soil.

In the second case, *Vettese v Zehr*, unpublished opinion per curiam of the Michigan Court of Appeals, issued December 15, 2005 (Docket No. 255919); 2005 WL 3439788, Vettese purchased a home from the Zehrs. After closing, Vettese discovered serious problems with the foundation of the home. Vettese sued the Zehrs, making multiple claims against them, including an alleged violation of the SDA.

Vettese claimed that the Zehrs violated the SDA when they provided a disclosure statement which was substantially blank. Presumably, the disclosure statement was substantially blank because the Zehrs had never lived in the house that they sold to Vettese. The trial court dismissed Vettese's claim based on the SDA, and the Court of Appeals affirmed that dismissal.

The Court of Appeals reviewed the primary purpose and requirements of the SDA. The Court of Appeals found that the SDA mandates that the seller disclose to a purchaser, via the statutorily required disclosure statement, certain information concerning the condition of the premises. The Court also further determined that liability for errors and omissions in a seller's disclosure statement is limited by the terms of the SDA. The Court found that the SDA permits a buyer to terminate a binding purchase agreement where a disclosure statement is not timely

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delivered, although this power of termination expires upon the conveyance of the property at issue. The Court of Appeals held, "By its terms, the SDA provides no other remedies." The Court went on to find that based upon the SDA's plain terms, any remedy available under the SDA was extinguished upon the closing of Vettese's purchase of the property from the Zehrs.

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 opinion per curiam of the Michigan Court of Appeals, issued August 3, 2001 (Docket No. 2221954); 2001 WL 879012, Court of Appeals 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* 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 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. *Roberts v Saffell,* 2008 WL 3876309 (Mich App). 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; 691 NW2d 770 (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.

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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.

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,* unpublished opinion per curiam of the Michigan Court of Appeals, issued February 24, 2004 (Docket No. 241507, 249015); 2004 WL 345495, 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 that 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

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> [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 "[s]tructural 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 . . . .

When MAR drafted the SDA, it was specifically designed so as not to create any new claims against sellers or their agents. Case law in the almost 15 years since the law was enacted has proven this to be true. However, in order to take advantage of the protections afforded by the SDA, REALTORS® need to make certain that a seller's disclosure form is used correctly for each residential property listed by them.

f. Merger and Integration Clauses in Purchase Agreements

In December of 2002, we advised REALTOR® that there appeared to be a revival occurring in the courts with respect to enforcement of so-called "merger" clauses in contracts. Since that time, we have strongly recommended that every purchase agreement include a merger clause.

To refresh your memory, the decision in 1992 involved a buyer who had sued a seller claiming that the seller had misrepresented the condition of the building which the buyer had purchased from the seller. *Indiana Lumbermen's Mut Ins Co v County of Luce*, unpublished opinion per curiam of the Michigan Court of Appeals, issued June 7, 2002 (Docket No. 236082); 2002 WL 1277026. The case against the seller was dismissed because the contract contained an "integration" clause (also called a "merger" clause) which indicated that all of the terms of the sale were contained within the four corners of the buy-sell agreement. The court held that because discussions between buyer and seller concerning the condition of the property were not reduced to writing in the buy-sell agreement, the buyer could not successfully sue the seller for alleged misrepresentations regarding the condition of the building which were made prior to the time the buy-sell agreement was signed. The court concluded that where a buy-sell agreement contains a "merger" or "integration" clause (these terms are used interchangeably by Michigan courts), neither the buyer nor the seller can maintain a lawsuit based on the failure of any condition, contingency or representation that is not written into the buy-sell agreement.

The Michigan Supreme Court frequently looks to Black's Law Dictionary as a reference source. Black's Law Dictionary defines an "integrated contract" as a "contract which contains within its four corners the entire agreement of the parties." In other words, an "integrated contract" is a writing adopted by the parties as the final and complete expression of their agreement. As a general rule, courts will not accept into evidence oral testimony or other

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documents that contradict the terms of an integrated contract. Under Michigan law, an integration clause conclusively establishes the completeness of a written agreement. Generally, where a contract states on its face that it embodies the entire agreement between the parties, the meaning of that contract may only be determined from the document itself. Everything outside the document, including letters, notes and testimony about what one party thought the agreement meant is "parol" evidence and is not admissible.

Obviously, REALTORS® are bound by NAR's Code of Ethics and should not make misrepresentations with respect to the condition of real estate or otherwise. We are not suggesting that merger or integration clauses should be included in all REALTORS®' purchase agreements in order to permit them to safely make misrepresentations prior to the buyer and seller entering into a buy-sell agreement. That being said, REALTORS® are also aware of the fact that disappointed buyers often bring lawsuits where they mistakenly allege that a seller or listing REALTOR® made misrepresentations, when in fact the seller or listing REALTOR® never made any such representations. The presence of a merger clause in the purchase agreement simply allows REALTORS® to dispose of these claims against them in a more summary and less expensive manner. Assuming courts continue to enforce merger and integration clauses, then presumably the presence of such clauses will actually act as a deterrent to the commencement of litigation.

g. Waiver Clauses in Purchase Agreements

Michigan courts are generally willing to enforce waiver provisions set forth in purchase agreements. For example, in *McKind v Palms Investments, LLC*, unpublished opinion per curiam of the Michigan Court of Appeals, issued May 8, 2007 (Docket No. 273138); 2007 WL 1342557, Palm Investments ("PI") had purchased an apartment building at 1001 E. Jefferson in Detroit in 2003 for $1.25 million. The deed setting forth that purchase price was recorded in February 2004. In May 2004, McKind agreed to purchase the apartment building from PI for $2.3 million. The purchase agreement provided that McKind had an opportunity to enter the property to make inspections and investigations. The following waiver provision was included in the purchase agreement:

> ***Waiver.*** *Purchaser acknowledges that Purchaser has made or has had an adequate opportunity to enter upon the property and to make all inspections and investigations of the records relating to the Property and ... of the physical condition of the Property, which Purchaser has deemed necessary. Purchaser acknowledges that Purchaser is completely satisfied with the review of all books and records relating to the Property . . . and the physical condition of the Property, and Purchaser is not relying on any information, documents, representations or warranties which may have been provided or made by the Seller or any of its shareholders, officers, directors or agents . . . .*

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In the three months following the signing of the purchase agreement, McKind made non-refundable earnest money deposits totaling $75,000. In July 2004, the property was appraised for $2.31 million. A rent roll dated July 14, 2004, which was attached to the appraisal report, indicated that 34 of 69 of the rental units were occupied. There were additional addenda and a second agreement to purchase the property for $2 million, at which time McKind made another non-refundable deposit. Ultimately, McKind made non-refundable deposits totaling $200,000.

According to McKind, he made his first "tour" of the interior of the apartment building in December of 2004 – almost eight months after the purchase agreement was signed. McKind was accompanied by a representative of PI and a representative of a lender. During the tour, McKind was told by PI's representative that some units could not be viewed because they were occupied. The lender's representative nevertheless opened the door of one such unit, and McKind observed that the unit was unoccupied. He also observed that the ceiling was caved in, exposing a hole in the ceiling through which water was leaking down from the allegedly renovated roof.

McKind sued PI for fraud. He claimed that PI had indicated that it had invested large sums of money in renovating the building. He further alleged that the rent roll PI had provided was false. McKind also asserted that even if PI had not engaged in intentional fraud, it certainly had made innocent misrepresentations entitling him to the return of his earnest money deposits.

Both the trial court and the Court of Appeals ruled against McKind. The waiver was enforced against McKind. In addition, the Court found that there was a merger clause in the purchase agreement which eliminated any claims based on innocent misrepresentations.

h. "As Is" Clauses in Purchase Agreements

There is no question that the use of "as is" clauses in purchase agreements provides certain protections to sellers and their agents. However, used alone as a risk reduction technique, the protections offered by an "as is" clause are highly overrated. An "as is" clause alone will not defeat a buyer's claim that the seller fraudulently concealed a defect or that the seller made fraudulent representations that were relied upon by the buyer in entering into a binding buy-sell agreement.

It is now well settled in Michigan that an "as is" clause will defeat a buyer's claim for a defect that should have been discovered by a reasonably competent inspector. As an example, if a seller represents that a roof is in excellent condition, and a buyer feels rain while standing in the middle of the living room, the buyer cannot later recover from the seller based upon the seller's misrepresentation regarding the roof. Obviously, the buyer was not entitled to rely upon such an obvious lie. On the other hand, the Michigan Court of Appeals has consistently held that even if an "as is" clause is included in a buy-sell agreement, a seller still has a duty to disclose any concealed conditions known to the seller. Michigan courts will not treat a condition as "concealed" if "a competent inspector should reasonably have been expected to discover evidence of the defect."

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REALTORS® representing buyers should strongly recommend that the buyers have inspections performed prior to purchasing a residence. Seller's agents should willingly provide the opportunity for an inspection. If a buyer declines to have an inspection after being offered an opportunity for an inspection, the buyer will not be able to prevail on a claim against a seller for alleged concealed defects, if evidence of those defects would have been discovered by a reasonably competent inspector.

The danger to buyers who do not undertake inspections or do not hire competent inspectors is demonstrated by an unreported Court of Appeals decision in *Miner v Teasel*, unpublished opinion per curiam of the Michigan Court of Appeals, issued April 10, 1998 (Docket No. 197225, 199165, and 199892). In this case, the buy-sell agreement contained an "as is" clause. In addition, the buyers' purchase of the property was made contingent upon an inspection. The buyers never had a complete inspection done for the property but, instead, waived the inspection contingency after a casual walk-through inspection. After closing, the buyers claimed to have discovered defects that cost more than $74,000 to correct. The buyers sued both the seller and also the buyers' agent. The trial court summarily dismissed the buyers' claims as being frivolous and awarded sanctions to the seller and the buyers' agent.

The Court of Appeals affirmed the trial court, finding that where there is an "as is" clause, the buyers could only recover for concealed defects. The Court again found that where a defect reasonably should have been discovered by a competent inspector, the defects are not concealed and the buyers cannot recover anything.

It should also be noted that in this case, the buyers claimed that the buyers' broker had breached her fiduciary duty by advising them to waive the inspection contingency. The Court of Appeals found that even if the buyers' claim was true, *i.e.*, that the buyer's agent advised them to waive the contingency, the buyers could not recover because they did not rely on her advice, and had in fact conducted an admittedly incomplete inspection. The Court attributed the buyers' damages to their own ineffective inspection and dismissed the claims against the buyer's agent. Obviously, REALTORS® representing buyers should make certain that they can document, either in their buyer agency agreement, the purchase agreement, or some other document, that they recommended that the buyers have an inspection performed on the property.

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i. Release Forms

The potential use of a release clause to limit liability was included in a risk reduction article prepared for MAR's 1998 Legal Update. MAR urged that REALTORS® consider using release forms based upon a decision rendered by the Court of Appeals in *Brook v Holmes*, 163 Mich App 143, 145; 413 NW2d 688 (1987), which at that time was still good law. That case involved the release clause contained in the Greater Lansing Board of REALTORS® form which provided:

> And, we hereby release ______________________ and ________________ Broker(s) in this transaction, their respective agents, employees, attorneys, and representatives with respect to all claims arising out of the performance of such Buy and Sell Agreement and Addendum and counteroffers thereto, all claims arising by virtue of any purported representations to us as to the condition of the property, and all claims arising from the existence of any special assessments and/or utility bills, which have been, or may in the future be, levied against such property.

The court held that this release was valid unless a buyer could demonstrate that it was obtained through duress, a misrepresentation by the REALTOR® as to the nature of the release clause, or fraudulent or overreaching conduct by the REALTOR® in securing the release.

Several years later, MAR's Legal Action Committee authorized MAR's participation in an appeal in *Hall v Small*, unpublished opinion per curiam of the Michigan Court of Appeals, issued May 12, 2005 (Docket No. 252814). In that case, the Court of Appeals issued an opinion affirming the enforcement of the release clause involved in that case. The use of the release clause had enabled both the listing and cooperating REALTORS® to have all claims dismissed against them. On December 27, 2005, the Michigan Supreme Court denied the buyers' application for leave to appeal, thereby affirming the opinion of the Court of Appeals as to the enforceability of the release clause.

Later that same year, there was yet another case involving the issue of enforceability of release clauses. *Huhtasaari v Stockemer*, unpublished opinion per curiam of the Michigan Court of Appeals, issued December 20, 2005 (Docket No. 256926); 2005 WL 3481429. In that case, the Stockemers had originally purchased their residence in July 1978. On May 6, 2002, in anticipation of the sale of their home, the Stockemers completed a seller's disclosure statement in which they specifically indicated that the home's roof was approximately three years old and that it did not leak.

Within two weeks of listing the property, the listing REALTOR® obtained prospective buyers for the Stockemers' home. The prospective buyers submitted an offer to purchase which resulted in an inspection in mid-May 2002. The home inspector terminated the inspection upon finding mold in the Stockemers' attic. The home inspector allegedly told the listing agent's son,

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who was present during the inspection, that "there was black mold in the attic." The prospective purchasers withdrew their offer, and the listing REALTOR® advised the Stockemers to take their home off the market. The Stockemers took their REALTOR®'s advice and removed it from the market on June 12, 2002.

The Stockemers' home was re-listed on July 31, 2002. The Stockemers reported to their listing REALTOR® that they had soda-blasting performed in the attic and they had been advised that the mold in the attic was harmless and not black mold. The listing REALTOR® advised the Stockemers to revise their seller's disclosure statement to indicate the prior mold problem in the attic, but the Stockemers refused to do so.

In August 2002, the Huhtasaaris then submitted an offer to purchase through their agent. The seller's disclosure statement that was provided to the Huhtasaaris was the same form that was submitted to the prospective buyers who submitted an offer in May 2002. The seller's disclosure form contained no reference to the prior mold problem in the attic.

The closing on the Huhtasaaris' purchase of the Stockemers' home was conducted in early September 2002. Shortly after closing the Huhtasaaris undertook renovations of the home, mold was discovered behind the wallpaper in the kitchen. The mold was also observed by a drywall contractor. The Huhtasaaris then had testing done on the home. Their environmental engineer issued a report indicating that "the mold growth and related structural damage" in the kitchen was "a direct result of long-term water leakage from the flashing area between the lower roof and the house wall." The Huhtasaaris then sued the Stockemers, the listing agent and the buyers' agent for fraudulent concealment, misrepresentation, and failure to disclose known defective conditions of the property, in violation of the Michigan Consumer Protection Act.

The trial court granted the listing agent summary disposition based upon the following language in the purchase agreement:

> WE FURTHER HOLD CENTURY 21 MECK AND ITS COOPERATING OFFICE AND THEIR SALESPERSONS, BROKERS, AND EMPLOYEES, RESPECTIVELY HARMLESS AND DO HEREBY INDEMNIFY THEM AGAINST ALL CLAIMS, ACTIONS, OR SUITES [SIC] FOR DAMAGE OF ANY NATURE WHATSOEVER, ARISING FROM THEIR ACTIONS LEADING TO THIS SALE AND FROM OUR DECISION NOT TO AVAIL OURSELVES OF ANY OR ALL OF THE INSPECTIONS.

The Huhtasaaris claimed that this release provision was invalid because of the fraudulent misrepresentations and disclosures of the Stockemers. The Court of Appeals rejected this argument, noting that in signing the purchase contract, the Huhtasaaris had acknowledged that "no representations, promises, guaranties, or warranties of any kind, including, but not limited to, representations as to the condition of the premises were made by the Broker, his/her salespersons, other cooperating salespersons or persons associated with Broker." The Court of Appeals found that this language in the purchase agreement barred the Huhtasaaris from asserting that their execution of the release in the purchase agreement was in reliance upon representations made by either REALTOR® with regard to the condition of the property.

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The Huhtasaaris also attempted to invalidate the release by claiming there was a lack of consideration. The Court of Appeals, as in prior decisions, rejected this claim, finding that the release was incorporated into the closing documents for the sale of the house and did not comprise a separate or distinct transaction requiring separate and distinct consideration.

Prior release cases decided by the Court of Appeals generally involved releases obtained from sellers and buyers at closing. This *Huhtasaari* case is important inasmuch as the trial court and the Court of Appeals chose to enforce a release obtained at the time of execution of the purchase agreement. REALTORS® should seriously consider incorporating release provisions both into their purchase agreements and into their closing documents.

REALTORS® should be aware of the case of *Stout v Withrow*, unpublished opinion per curiam of the Michigan Court of Appeals, issued February 14, 2008 (Docket No. 271632); 2008 WL 400675, a decision for which the REALTORS® are presently seeking leave to appeal to the Michigan Supreme Court. MAR's Legal Action Committee authorized MAR's participation in this case both before the Court of Appeals and the Supreme Court. This case provides proof of the old legal bromide that "bad facts can make for bad law."

In this case, it was alleged that the REALTOR® conspired, in essence, with the seller to conceal a completely defective septic system. The buyer was a recently divorced woman of very modest means. The defective septic system resulted in the backup of human waste into the bathroom sink and tub, which rendered the home uninhabitable.

In this case, the REALTOR®'s attorney, on at least three (3) occasions, sought to have the case dismissed based on the fact that the buyer had executed a release. The REALTOR®'s attorney contended that the release provided by the buyer was enforceable, as it was not procured by fraud, duress, or overreaching by the REALTOR®. The trial court refused to grant the dismissal. The Court of Appeals, in a published decision, affirmed the decision of the trial court. The Court of Appeals appeared incensed at the alleged conduct of the REALTOR®. The Court of Appeals found that the alleged fraud of the REALTOR® in concealing the defects in the septic system and presenting that the property was like new resulted in the buyer not obtaining an inspection. In turn, the lack of the inspection left the buyer uninformed as to the true condition of the property. Thus, the alleged fraud of the REALTOR® with respect to the condition of the property was deemed to be fraud used in obtaining the release.

The decision in *Stout v Withrow* runs counter to all previous decisions enforcing releases obtained, at least in part, by MAR. While REALTORS® should continue to use releases, their attorneys should be mindful of this case.

j. Attorney Fees Provisions

When REALTORS® are wrongly sued in a transaction, one of the first questions asked is "can we recover our attorneys fees?" Unfortunately, under the common law, winners of litigation are not entitled to reimbursement for their attorney fees and costs. The only time winners can recover their attorney fees is when there is an applicable statute that expressly authorizes reimbursement of attorney fees and costs, and those types of statutes are few and far between.

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There has always been a question as to whether a contractual agreement requiring a loser to pay the attorney fees of a winner would be enforceable in the context of a real estate transaction. In its *Boyd v Burke*, unpublished opinion per curiam of the Michigan Court of Appeals, issued May 17, 2007 (Docket No. 275313); 2007 WL 1452516, the Michigan Court of Appeals provided an answer. In this case, Paul Burke ("Burke") became interested in purchasing the house of Curtis and Eulanda Boyd (the "Boyds"). RE/MAX Gaylord acted as a dual agent for both Burke and the Boyds. It should be noted that there was no dispute that RE/MAX Gaylord acted as a dual agent by agreement of both parties and after all "relevant and legally required disclosures."

The purchase agreement called for Burke to purchase the Boyds' property in a furnished state. A dispute arose as to what was going to be included in the furnishings. Ultimately, the transaction ended with Burke refusing to close and rescinding the transaction. Burke contended that the purchase agreement was not enforceable because it did not completely set forth the items which were to be included as furnishings with the home.

The Boyds sued Burke and RE/MAX Gaylord. The Burkes contended that RE/MAX Gaylord was negligent in preparing the purchase agreement. The trial court ruled in favor of RE/MAX Gaylord. The Court of Appeals found that there was no ambiguity in the purchase agreement; thus, it would have been enforceable. The trial court awarded attorney fees to RE/MAX Gaylord. On appeal, the Boyds contended that RE/MAX Gaylord should not have been awarded attorney fees.

The Court of Appeals found that there was no dispute that the basis for the attorney fees award was a contractual provision in the purchase agreement. The purchase agreement provided:

> In any action or proceeding arising out of this agreement, the prevailing party, [sic] shall be entitled to actual and reasonable attorneys fees and costs. This shall also be applicable to any Realtor(s) who become a party to such action or proceeding which Realtors shall be considered a third party beneficiary to this contract.

REALTORS® may wish to include an "attorney fees provision" in purchase agreements, listing agreements, and buyer agency agreements. The theory is that a seller, buyer or other party may think twice before suing if they face the prospect of paying the REALTOR®'s attorney fees. Of course, it should be kept in mind that this sword has two edges. If an attorney fees provision is included, for example, in a listing agreement and a REALTOR® loses in ensuing litigation, the REALTOR® could be stuck paying the other party's attorney fees. Typically, payment of attorney fees does not fall within coverage of an errors and omissions insurance policy.

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k. Home Warranty Programs

Home warranty programs are an effective way to limit risk. Obviously, when a necessary repair is covered by a home warranty program, the parties can avoid a lawsuit. REALTORS® who provide information to sellers and buyers about a particular home warranty program should make certain that the company is reputable and has a good record for handling claims. Moreover, as with inspectors, REALTORS® are cautioned against putting themselves in a position where a party can argue that the REALTOR® should be responsible if the warranty company fails to perform as required under the contract. At a minimum, REALTORS® should make certain that a seller (or buyer) understands that the home warranty company is a separate company not affiliated with the broker. Moreover, a REALTOR® is well advised to present the seller (or buyer) with information on a number of different home warranty programs and let the seller (or buyer) choose one.

l. MCPA Defense

It is assumed that by now all REALTORS® are aware of the fact that in June of 2007, the Michigan Supreme Court rendered a decision which exempts REALTORS® from liability under the Michigan Consumer Protection Act (the "MCPA") if the claims alleged against them are based on their daily activities, *i.e.*, claims arising from a real estate transaction. It should not be assumed, however, that all attorneys are aware of the decision by the Michigan Supreme Court.

If REALTORS® are sued under the MCPA, their attorney must assert the exemption from the MCPA as an affirmative defense at the start of the case. While it is not difficult to assert this affirmative defense, it is fatal if it is not asserted by the REALTOR®'s attorney. The following is a sample affirmative defense to an MCPA claim against a REALTOR®:

> The claims set forth in the Complaint for violation of the Michigan Consumer Protection Act are barred for the reason that Defendant is exempt.

The Michigan Association of REALTORS® spent in excess of $100,000 in pursuing and obtaining an exemption for REALTORS® from liability under the MCPA. A REALTOR® should not lose the benefit of this hard-won victory simply by reason of their attorney's failure to include a two-line affirmative defense in the answer to the complaint.

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CONCLUSION

The adoption of any or all of the risk reduction techniques discussed in this article will not provide an absolute shield against litigation for at least two reasons. First, REALTORS® are human and, like all people, will on occasion make mistakes. Second, as REALTORS® are more than aware, anyone with a filing fee can bring a lawsuit against another party. However, adoption of the risk reduction techniques described in this article can deter litigation when a buyer or seller consults with a competent lawyer prior to initiating litigation, or in the event litigation is in fact filed against a REALTOR®, can assist that REALTOR®'s attorney in obtaining summary disposition of the case.

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