

# New Jersey Law Journal

VOL. CLXXXVII—NO.4—INDEX 262

JANUARY 22, 2007

ESTABLISHED 1878

## Professional Malpractice

### Reducing Brokers' Exposure

To avoid malpractice liability, brokers must know their duties

By Marc C. Singer

In an uncertain real estate market, where housing prices begin to decline and expectations based upon prior market conditions become unrealistic, real estate professionals often become targets for malpractice claims. That is not to say that all claims against real estate professionals are meritless, but in some instances claims are fueled more by frustration with the marketplace than the conduct of the real estate professional. Knowing potential sources of liability and addressing them upfront can help minimize exposure to such claims and limit potential liability.

There is no way to anticipate all of the circumstances which may give rise to a malpractice claim. In an effort to minimize exposure to such claims, understanding the various duties owed by real estate professionals to buyers and sellers enables counsel to develop strategies for real estate brokerage clients that can be implemented in their professional practice. This article does not provide an exhaustive explanation

---

*Singer is a member of Saiber, Schlesinger, Satz & Goldstein of Newark. He handles various litigation issues affecting the real estate industry.*

of all of the potential claims real estate professionals can face. Rather, it seeks to provide a framework of legal issues and relationships to be familiar with, sensitize counsel to some of the concerns faced by the residential brokerage industry and propose some practical strategies to consider when representing brokers or agents in the residential brokerage industry.

Making sure the real estate professional understands his relationship with the client (i.e. buyer or seller) and the concomitant duties and responsibilities is the first step toward avoiding malpractice. A fiduciary duty exists between a real estate broker and his client. "The broker is looked upon as a fiduciary and is required to exercise fidelity, good faith and primary devotion to the interests of his principal." *Mango v. Pierce-Coombs*, 370 N.J. Super 239, 256 (App. Div. 2004) (quoting *Ellsworth Dobbs, Inc. v. Johnson*, 50 N.J. 528, 553 (1967)).

In recent years, many states have taken steps to address some of the confusion and conflict concerning fiduciary duties that can arise when agents work with both buyers and sellers in the purchase and sale of a property. New Jersey requires all real estate agents to provide a buyer and seller with a Consumer Information Statement, identifying and explaining four types of agency relationships the real estate agent is permitted to engage in. They are: seller's

agent; buyer's agent; disclosed dual agent; and transaction broker. The first three are the most common in New Jersey.

A "seller's agent" works exclusively for the seller, owing fiduciary duties to the seller that include reasonable care, undivided loyalty, confidentiality and full disclosure. Similarly, a "buyer's agent" works exclusively for the buyer, owing these same fiduciary duties to the buyer.

Both a buyer's agent and seller's agent must act honestly and fairly with all parties by not making misrepresentations and by disclosing any known material defects that could reasonably affect the physical condition of the property. As a "disclosed dual agent," however, the agent is acting for both the buyer and seller. Such a situation often arises when the agent represents the seller in marketing the property and also the buyer who is purchasing the property. Such an agency relationship can only be entered into in New Jersey by obtaining the informed written consent of both sides. In such situations, not only must the agent act honestly and fairly with all parties, the duty to maintain confidential information provided by one side may conflict with the duty to disclose such information to the other. Accordingly, the disclosed dual agent must caution the parties up front of this situation.

A "transaction broker" is really not an agent but rather a facilitator of the transaction. In that situation, the broker puts the parties together, manages the transaction and works with both sides in

communicating terms and conditions that the parties mutually agree upon without advising either side on strategies to gain an advantage in the transaction.

Regardless of which agency relationship is established, the real estate professional must disclose to a prospective buyer known material defects or conditions affecting the value of the property. Over the years, the courts and state legislature have imposed greater and greater affirmative duties on real estate professionals to disclose conditions that could adversely affect the value of a property or impact a reasonable buyer's decision to purchase a property. It has long been the rule that any known material defects in a property must be disclosed by the broker to prospective purchasers. So, for example, if the broker is aware that a property has a water problem or is infested with termites, such information must be disclosed. See *Weintraub v. Krobatsch*, 64 N.J. 445 (1974). Real estate professionals will find themselves subject to liability if they fail to disclose a known material defect to a prospective buyer if the condition affecting the property is not readily observable to the buyer. See *Mango*, 370 N.J. Super. at 254. Similarly, from the standpoint of the seller, the real estate agent must disclose material information concerning the buyer which relates to the transaction. Take, for example, a buyer who the agent knows lacks sufficient funds to perform. Such information should be disclosed. See *Restatement (Second) of Torts* §551 (1977 & Supp. 1997).

While the law is clearer concerning the duty to disclose material issues affecting the property or transaction, less clear is how far this duty to disclose extends to off-site conditions. Recent case law and legislation in New Jersey has imposed upon real estate brokers and agents the duty to disclose material off-site conditions not evident to the buyer that could impact the value of a property. For example, knowledge of the existence of a superfund site within close proximity to a property is something that should be disclosed. See *Strawn v. Canuso*, 140

N.J. 43 (1995).

The New Residential Real Estate Off-Site Conditions Disclosure Act, N.J.S.A. 46:3C-1 to 12, passed shortly after and superseded by the New Jersey Supreme Court's decision in *Strawn*, imposes a statutory requirement that brokers representing developers in the sale of new residential construction advise prospective purchasers of the existence of off-site conditions that are harmful or could materially impact the value of the property. Municipalities and other government agencies are required to maintain lists of material off-site conditions. The existence of these lists, which are available to the public for inspection, are to be disclosed to prospective buyers. These lists include, among others, environmental sites on the National Priorities List or those sites that involve hazardous discharge, landfills, high voltage electrical utility lines and transformers, wastewater treatment plants and airport safety zones. Similarly, New Jersey's Megan's Law requires brokers to provide buyers with municipal contact information to ascertain the existence of registered sex offenders in the area.

Understanding and following these disclosure requirements is critical. Real estate brokers and agents are not only subject to general common law claims such as fraud and negligence, but also are subject to liability under the New Jersey Consumer Fraud Act, N.J.S.A., 56:8-2, et seq. (CFA). The CFA protects consumers (i.e., buyers and sellers) from affirmative acts involving deception, fraud or misrepresentation, as well as acts of omission where material facts are concealed, omitted or suppressed. Intent is not required. Any misrepresentation, whether by commission or omission, that is "material to the transaction" may be actionable under the CFA. See *Vagias v. Woodmont Properties, L.L.C.*, 284 N.J. Super. 129, 134-135 (App. Div. 2006). The *Vagias* case illustrates the importance of verifying critical information. There, the real estate agent sold a property to the buyers, knowing that the buyers wanted to purchase a property located in a particular section of Montville

Township because the schools were better and the area was more prestigious. The agent mistakenly (but unintentionally) represented that the property was located in that section without verifying that fact. Because the buyers' decision to purchase was based primarily on this misrepresentation, the agent was held liable under the CFA. Simply put, when a real estate professional is confronted with making representations concerning facts critical to a transaction, he or she must verify that information.

Whether something is "material" is fact sensitive and dependant on the attendant circumstances. The courts generally will look to whether the defect, condition or representation is critical to the value of the property or the decision to enter into the transaction. For example, representing that a property is zoned for multifamily use when it is zoned only for single-family use is material when the buyer is purchasing based upon this representation. See *Ji v. Palmer*, 333 N.J. Super 451 (App. Div. 2000). Conversely, a broker does not have a duty to disclose everything that may be a nuisance. For example, there is no duty to investigate and disclose offensive or abusive neighbors where that is not a condition or issue in the sale. See *Levine v. The Kramer Group*, 354 N.J. Super. 397, 405 (App. Div. 2002).

Real estate professionals often do not live in the properties they sell and, therefore, they are less likely to know about material defects with the property. To grapple with the issue of disclosure, New Jersey has adopted a Seller's Disclosure requirement form, upon which the seller identifies any known defects concerning the property. A real estate agent should not fill this form out for the seller. It should be completed based solely upon the seller's personal knowledge. This reduces the exposure to potential negligence and fraud claims by placing the primary burden of disclosure on the seller. If the real estate professional complies with this regulation and properly obtains and provides a Seller's Disclosure, the broker and agent will be exempt from certain provisions of the

CFA, thereby precluding an award of attorneys' fees or punitive damages. N.J.A.C. 13:45A-29.

The agent must, however, affirmatively make reasonable efforts to ascertain that the information in the disclosures is not false and disclose any information he discovers concerning a material defect in the property that is otherwise not disclosed; especially if that information contradicts a statement in the Seller's Disclosure.

When counseling real estate brokerage firms and professionals to minimize exposure to potential litigation, it is prudent to suggest the brokerage company and its brokers and agents implement the following types of practices and policies in their business activities:

*Do not give legal advice* — although a buyer or seller may look to a real estate professional for advice or counsel, believing that he or she may understand the legal ramifications involved based upon their experience, it is a best practice for all real estate professionals to always recommend the party seek advice from qualified counsel.

*Put it in writing* — avoid the "he said, she said" or "had I only known" scenarios by recommending that brokers and agents confirm their conversations with principals contemporaneously through a letter or e-mail. Also, keep-

ing copious internal notes of those conversations helps avoid questions as to what was said at the time.

*Do not speculate* — while it is important to disclose material conditions, the real estate professional should be counseled to avoid speculating as to when or how a particular condition or issue arose. Not much different than counseling a prospective witness for deposition, it is important that a real estate professional not guess.

*Never discourage further investigation* — Real estate professionals are often concerned that insignificant items can be blown out of proportion if investigated. In most instances, if the issue is insignificant, it will have little impact on the transaction and if the issue is significant, the real estate professional may have avoided liability for negligence or, worse, fraud.

*Be careful making referrals* — buyers and sellers often ask for referrals of home inspectors, attorneys and the like. To avoid issues of conflict that may later arise from a referral gone bad, remind clients they are free to choose whomever they wish and recommend they interview several professionals before choosing.

*Provide sources of information* — too many professionals make representations that are not based on personal knowledge or a competent source. If the

source of the information is other than personal knowledge, a professional should say so. Such conduct builds trust and avoids later questions regarding whether the agent made a misrepresentation.

*Verify material facts* — because the CFA imposes liability even for unintentional misrepresentations, checking the accuracy of the information or, at a minimum, qualifying that the information is questionable is a best practice.

*Avoid modifying or opinion words* — words often have varying connotations and their use can sometimes (either intentionally or unintentionally) mislead a party into believing an issue is more or less important than it really is. Words such as "normal," "minor," "cosmetic," "noticeable," "simple," "large" or "small" should be avoided.

*Be honest* — while perhaps the easiest recommendation to follow, simply being upfront and honest will go a long way in building relationships which can not only prevent litigation, but may actually facilitate more business.

There is no way to prevent all malpractice claims. However, by counseling real estate professionals on their duties, the various affirmative disclosures they must make and implementing clear policies and procedures to follow, their exposure to liability can be substantially reduced. ■