

To Disclose or Not to Disclose, That is the Question for Michigan Residential Sellers

Introduction

In general, sellers of residential property are required to make certain disclosures about the physical condition of the property involved in the transaction. For example, residential sellers must disclose whether the home has a history of termite infestation or has been subject to major damage from fire, wind, floods, or landslides. The National Association of Realtors defines stigmatized property as property that “has been psychologically impacted by an event, which occurred or was suspected to have occurred on the property, such event being one that has no physical impact of any kind.”¹ Included in this definition are murder scenes and sites of suicides, deaths, and AIDS-related illnesses.

Some states have enacted laws, known as stigma disclosure statutes, regarding the disclosure of psychological facts, but Michigan has not. In those states that have enacted stigma disclosure statutes, there are no hard and fast rules about disclosing property stigmas, and disclosure laws vary from state to state. In Michigan, the Seller Disclosure Act² provides the mandatory guidelines for disclosures. But the language in the form required under Michigan’s Seller Disclosure Act suggests that residential sellers are not required to disclose information about the property beyond its physical condition. In spite of this, many buyers *feel* that residential sellers should disclose any and all information concerning the property, including stigmas. Without a clear and definite law addressing this matter, the question remains whether Michigan residential sellers have a duty to disclose stigmas associated with the real property.

This author suggests that in Michigan, on the basis of recent court decisions and Michigan statutes, residential sellers and their agents have no duty to disclose stigmas associated with the real property involved in the transaction.



By Evelyn Williams

STIGMATIZED

Historical Development of the Duty to Disclose

The Doctrine of *Caveat Emptor*

Historically, advising a homeowner when to disclose certain conditions associated with the real property to the prospective buyer was quite simple. Why? The doctrine of *caveat emptor* (let the buyer beware) prevailed in all land transactions. The doctrine holds that

because title, possession, and control of real property is relinquished during a sales transaction, the seller could shift all responsibility for the condition of the land to the purchaser. This doctrine presumed that the buyer would make all necessary inspections and inquiries before entering into the agreement; thus, upon entering into the contract, the buyer is assumed to accept the property “as is.” Under the doctrine, unless the seller intention-

ally misrepresented the facts, the seller owed no duty to the buyer regarding the condition of the land.

Despite providing both the buyer and the seller with a bright-line answer regarding whether a duty to disclose conditions associated with the property was owed by the seller, the doctrine often produced harsh results. As a result, courts began to adopt a number of exceptions to the doctrine. In addition,



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several states enacted seller disclosure requirement statutes designed to mandate disclosures in specific instances.

Case Law

In the late 1980s, case law began to appear that specifically addressed the issue of stigmatized property and whether a seller had a duty to disclose a stigmatizing event associated with the real property. Rulings in two well-known cases, *Reed v King*³ and *Stambovsky v*

Ackley,⁴ led to some states adopting laws specifically addressing stigmatizing events and the seller's duty to disclose such events.

In *Reed*, the buyer purchased a home from the seller, who failed to disclose that a woman and her four children were murdered in the house 10 years earlier. The plaintiff learned of the incident after the sale of the home and sought rescission of the contract. The court of appeals stated that the murders were mate-

rial facts that the seller had a duty to disclose. The court reasoned that the buyer could not be charged with the duty to inquire into and discover the 10-year-old murders because "[t]he murder of innocents [was] highly unusual"; thus, the buyer could not have been reasonably expected to anticipate the possibility of a murder occurring on the property.⁵

In *Stambovsky*, a buyer sought rescission of a contract to purchase a home in New York

upon learning that the house he had contracted to buy had a reputation for being haunted. At the time of the case, New York had held that the doctrine of *caveat emptor* prevailed. However, the court held that the seller was estopped from denying that the house had a reputation for being haunted and granted relief to the buyer. The court reasoned that the purchaser was estopped from denying the haunting because the seller had advertised the property as being haunted and, even upon a reasonable inspection by the most prudent buyer, such information would not be readily discoverable.

In both *Reed* and *Stambovsky*, the courts addressed psychological defects associated with real property and the seller's duty to disclose stigmatizing events. However, the set of facts used to determine when the duty to disclose was owed differed. In fact, today it appears that no two courts have used the same set of facts to determine whether a seller owed a duty to disclose stigmatizing events. As a result, there is no consistency in this area of the law.

Michigan Seller Disclosure Act

In 1993, the Michigan Legislature enacted the Seller Disclosure Act (the Act). The Act specifically mandates that a seller in residential real estate transactions involving between one and four residential dwelling units must disclose specific physical details about the conditions of the property held for sale. Each disclosure under the Act must be made in good faith. For the purposes of the Act, "good

faith" means "honesty in fact in the conduct of the transaction."⁶ Under the Act, an aggrieved buyer may bring a cause of action for failing to disclose certain physical conditions of the property under various theories of fraud or negligence.

Although the Act requires a seller of residential real estate to disclose certain physical conditions associated with the real property involved in the transaction, it does not require the seller to disclose non-physical defects.

Analysis

Does Michigan Law Require Disclosures Beyond the Physical Characteristics of the Property?

According to common law and the Act, a seller of residential real property involved in a real estate transaction has no duty to disclose non-physical defects associated with property for the following reasons. First, a cause of action may not be sustained. Under common law, a claim of fraud may be established when the seller, by word or actions, intentionally suppressed material facts to create a false impression when there was a legal or equitable duty to disclose. It is not enough that the seller had knowledge of the defect and failed to disclose it; "rather, the seller must make some type of misrepresentation."⁷ In stigmatized property litigation, the seller generally does not make any form of representation about the stigmatizing event. Thus, neither a claim of fraud nor a claim of innocent misrepresentation can be sustained.

Silent fraud is the suppression of material fact that a party is in good faith duty-bound to disclose. In order to establish a claim of silent fraud, a plaintiff must show that some type of representation was made that was false or misleading and that there was a legal or equitable duty to disclose.⁸ Again, in cases involving stigmatized property, the seller generally does not assert a statement of any kind regarding the stigma; instead, the seller simply omits the fact. Thus, a buyer's cause of action based on silent fraud could not be maintained.

Furthermore, in order to maintain a silent fraud cause of action, the buyer must not only establish that the seller had a legal or equitable duty to disclose a fact, but also must establish that the seller suppressed a "material fact" that the seller had a duty to disclose in good faith.

In the context of the Michigan Consumer Protection Act, Michigan courts have defined a "material fact" as a fact that is "important to the transaction or affects the consumer's decision to enter into the transaction."⁹ The standard for determining if the fact was material is an objective standard. However, stigmas relate to personal values, preferences, and perceptions. In other words, stigmas are subjective in nature.

Whether the occurrence of a stigmatizing event associated with the real property is a fact that is important to the transaction or affects the consumer's decision to enter into the transaction is a crucial question in determining if a duty to disclose was owed by the seller. Initially, the court in *Reed* held that the stigmatizing event was a fact material to the transaction that the seller had a duty to disclose. However, the California Legislature later passed a stigmatized property statute that provided sellers with immunity from liability based on a failure to disclose psychological defects, which included murder. Such legislation indicates that California no longer holds the view that a stigmatizing event is a material fact that would affect the transaction or the consumer's decision to enter into the transaction.

Although the court in *Stambovsky* held that the seller was required to disclose the haunting of the house, the court based its reasoning on equitable considerations and

Fast Facts

Included in the definition of stigmatized property are murder scenes and sites of suicides, deaths, and AIDS-related illnesses.

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not necessarily on the conclusion that the stigma was a material fact that would affect the transaction or the buyer's decision to enter into the transaction.

Does the Michigan Seller Disclosure Act Impose a Duty on a Residential Seller to Disclose Stigmas Associated with the Real Property?

Under the Act, a seller is required to disclose specific information regarding the condition and information concerning the property known to the seller in good faith. As noted earlier, for the purposes of the Act, "good faith" means "honest in fact in the conduct of the transaction." Although the Act requires that disclosure should be made in good faith, a determination that a fact is material does not necessarily impose a duty to disclose all conditions that may be considered unpleasant. Applying the doctrine of *ejusdem generis* to cases involving stigmas and the Act, the existence of murders, suicides, or AIDS-related illnesses would not rise to the same level of offensiveness as generated by farms, landfills, airports, and shooting ranges, all of which present problems with odor and noise pollution.

In summary, the occurrence of a stigmatizing event on the property may be considered an unpleasant characteristic of the home; however, it does not rise to the offense level generated by farms, landfills, airports and shooting ranges, which a seller has a duty to disclose under the Act.

Should the Michigan Legislature Adopt a Law That Provides Sellers Immunity from Liability Based on a Failure to Disclose Stigmatizing Events?

There are numerous reasons why the Michigan Legislature should adopt a law providing sellers with immunity from liability based on a failure to disclose a stigmatizing event.

As stated previously, there is no duty for the seller to disclose the stigmatizing event, and, without the representation, the buyer is unable to establish the necessary elements for a *prima facie* case of fraud.¹⁰ Thus, adopting this new law would merely be implementing the position the courts have already taken regarding this particular area of the law.

Furthermore, to maintain a cause of action, a plaintiff must establish that the defendant's act or failure to act was the cause of the plaintiff's alleged injury. "[A]ny interruption in the causal connection between the defendant's conduct and the plaintiff's injury will [also] relieve the defendant of liability."¹¹ In stigma claims, the plaintiff's alleged injury stems from a general public fear resulting in a decrease in property value. "This intervention caused by the irrational fears of third-parties destroys the necessary proximate causation."¹² A seller has no control over what the general public might fear. As a result, the buyer will not be able to establish that the seller's failure to disclose the stigmatizing event associated with the real property was the proximate cause of the alleged injury.

In addition, to maintain a cause of action, the plaintiff must establish damages with reasonable certainty. "Because certain properties are less likely to suffer from stigma, and stigma associated with property dissipates over time, it [would be] difficult [for courts] to determine the extent of stigma damages with any degree of certainty."¹³ Determining the effect of stigmas is different from determining actual physical damage. With physical damage, there is concrete evidence of the alleged injury; however, with psychological defects, the alleged injury is speculative.

Furthermore, imposing a duty to disclose stigmas may lead to a "windfall for the buyer." If the buyer never re-sells the property or remains in the home, an award of damages based on general public fear creates the risk that the buyer will be awarded damages for injury that he or she may never incur. "[P]ublic fear of stigma does not continue indefinitely."¹⁴ In fact, studies have shown that "decreases in property value are short-lived."¹⁵ "Plaintiffs who sell their property at the peak of the public's heightened concern may experience damages from stigma; however, those who do not sell their property may gain benefits in the long run without actually incurring any injury."¹⁶

For instance, the home in which Gianni Versace was murdered was sold three years after his death for \$20 million. The listing agent for the Pacific Palisades home in which "Thelma Todd—a popular film actress of the 1920s and '30s who appeared in a couple of

Marx Brothers films—was suspiciously found dead," reported that he received "75 calls after six hours of posting the 'For Sale' sign."¹⁷ The listing agent believed that "the history of the [home] . . . actually helped increase the interest."¹⁸ Additionally, when the bank foreclosed on O. J. Simpson's Brentwood estate, it was auctioned to a bank for \$2.6 million (a \$500,000 discount); however, it was later resold for almost \$4 million. Most notably, the home in *Stambovsky* was later resold for \$900,000, which the realtor reported was "a reasonable market value."¹⁹

Last, but not least, adoption of the new law would also benefit the judicial system. It would provide the courts with a bright-line rule. With a bright-line rule, the number of cases appearing before the courts would be smaller. ♦

Evelyn Williams earned her J.D. degree cum laude from Thomas M. Cooley Law School, where she was editor-in-chief of the Thomas M. Cooley Law Review. At Cooley, she was on the Dean's List and received the Distinguished Student Award and a Certificate of Meritorious Award for Advanced Writing. Ms. Williams served as the American Bar Association's class representative and completed a clerkship with the United States District Court for the Southern District of Florida.

Footnotes

1. Judon Fambrough, *Disclosing Stigma*, *Tierra Grande, Journal of the Real Estate Center at Texas A & M Univ.* Vol. 8, No. 2 (Apr. 2001), at <http://recenter.tamu.edu/TGrande/vol8-2/1458a.html> (last visited Jan 22, 2006).
2. MCL 565.951 et seq.
3. *Reed v King*, 145 Cal App 3d 261; 193 Cal Rptr 130 (1983).
4. *Stambovsky v Ackley*, 169 AD2d 254; 572 NYS2d 672 (1991).
5. *Reed*, supra, 193 Cal Rptr at 133.
6. MCL 565.960.
7. *M&D, Inc v McConkey*, 231 Mich App 22, 25; 585 NW2d 33 (1998).
8. *Id.* at 28–29.
9. *Zine v Chrysler Corp*, 236 Mich App 261, 283; 600 NW2d 384 (1999).
10. *M&D*, supra at 25.
11. Eric S. Schlichter, *Stigma Damages in Environmental Contamination Cases: A Possible Windfall for Plaintiffs?*, 34 Hous L R 1125, 1147 (1994).
12. *Id.*
13. *Id.* at 1149.
14. *Id.* at 1153.
15. *Id.*
16. *Id.*
17. Betsy Schiffman, *Skeletons in the Closet*, available at <http://www.forbes.com/2002/08/16/0816home.html> (last visited Jan. 23, 2006).
18. *Id.*
19. *Id.*