

# Does the “As Is” Clause and California’s Disclosure Exemption Protect an REO Sale From Non-Disclosure Liability?



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**D**espite the wonderful ring of an “as is” clause and its ability to conjure images of absolute freedom from any disclosure liability – this is not the case in California (and most jurisdictions for that matter). As discussed below, an “as is” clause does not offer the perfect escape hatch from all duties of disclosure.

Under *Civil Code* § 1102, in most residential real estate transactions, transferors of residential property must provide purchasers with a Real Estate Transfer Disclosure Statement (TDS). Things to be disclosed to buyers under §1102 include the following examples: environmental hazards; adjoining items where maintenance may be an issue with neighbors; encroachments/easements; structural modifications made without permits; fill problems; soil problems; flooding; major damage to property; zoning violations; neighborhood noise problems; CC&R’s; common area info; notices of abatement or citations against the property; and lawsuits. But, under §1102.2 a seller of a foreclosure property is not required to complete a TDS.

Despite the fact that the seller of a foreclosure property is exempt from providing disclosures on a TDS, a duty to comply

with the common law duty of disclosure still exists. This duty is independent of the statutory requirements of the TDS.

In *Lingsch v. Savage* (1963) 213 Cal.App.2d 729, the Court held that sale of real property “as is” does not waive potential claims of common-law misrepresentation. It also held that “as is” serves only to give notice of patent defects (*essentially visible defects*) and means that the buyer accepts the property in the condition in which it is reasonably observable by him or her. However, if the Purchase and Sale Agreement is augmented by language indicating that the buyer is relying on his or her own inspection of the property, it may also relieve the seller of the duty to inspect for defects or to disclose matters that the seller should know, but does not.

*Lingsch* recites the common law duty in stating: “It is now settled in California that where the seller [of real property] knows of facts materially affecting the value or desirability of the property which are known or accessible only to him and also knows that such facts are not known to, or within the reach of the diligent attention and observation of the buyer, the seller is under a duty to disclose them to the buyer.

Failure of the seller to fulfill such duty of disclosure constitutes actual fraud.”

More recently, *Karoutas v. HomeFed Bank* (1991) 232 Cal.App.3d 767, affirmed the *Lingsch* holding and applied it to a foreclosing bank. *Karoutas* involved the foreclosure sale of property that had damage to the foundation which could not have been detected by a potential buyer on a drive-by inspection of the property. Since the bank was aware of the damage and the buyer could not have known or discovered the damage, and because the damage was material, the court allowed the borrower to rescind the sale.

As explained further in *Karoutas*, the doctrine of caveat emptor (buyer beware) does not actually apply to nonjudicial foreclosure sales. “Thus, it is the general rule that courts have power to vacate a foreclosure sale where there has been fraud in the procurement of the foreclosure decree or where the sale has been improperly, unfairly, or unlawfully conducted, or is tainted by fraud, or where there has been such a mistake that to allow it to stand would be inequitable to the purchaser and parties.”

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"We cannot believe that the Legislature, in enacting §2924 et seq., intended to immunize beneficiaries from liability for deceit, or to expand the risks borne by purchasers to include the assumption of damages resulting from a beneficiary's fraud."

The first step in acquiring any liability for a failure to disclose a defect in title or the property is notice. A seller or his or her agent must have actual knowledge of the defect in order to be liable for failing to disclose a material fact. Typically, Courts have held that the defect must have a negative impact on the market value. Unfortunately, there is no check list that sets any hard and fast rules for the REO seller to follow. For example, California Courts have even held that failing to disclose a murder that occurred in a home 10 years prior to the sale negatively impacted the market value and was a breach of the duty to disclose.

Ultimately, a buyer's remedy for a breach of the duty to disclose is harsh. The remedies can include both rescission of the sale and damages. Fraud and deceit damages are available to the buyer as well. The take away lesson here is that the "as is" clause does not immunize a seller from disclosing against 1) any known defects that materially decrease the market value of a property and 2) defects not apparent or within the reach of the diligent attention of the buyer. ☺

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