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Homebuyers' Frivolous Claims Against Seller's Listing Agent Warranted Terminating and Monetary Sanctions

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Homebuyer’s frivolous claims against seller’s listing agent warranted terminating and monetary sanctions.

Peake v Underwood (2014) 227 CA4th 428

In Buyer’s action for failure to disclose defective subfloors, one of the defendants (Agent) served a CCP §128.7 sanctions motion (for filing a legally or factually frivolous pleading) against Buyer and her attorney. Buyer declined to dismiss during the statutory safe harbor period, which allows a party to withdraw a questionable pleading without penalty, and instead added common law claims based on the same facts to her statutory claims against Agent. The trial court found that the claims were without legal or evidentiary support and that continued maintenance of the action constituted objective bad faith warranting §128.7 sanctions of dismissal and attorney fees. Buyer and her attorney appealed.

The court of appeal affirmed, holding that the trial court acted within its discretion in awarding §128.7 sanctions. The record showed that no reasonable attorney would have concluded that the statutory and common law claims against Agent were factually and legally supported.

As to the statutory claims, under CC §§2079 and 1102, a seller’s agent has a duty to disclose in good faith only what a reasonably competent and diligent visual inspection would reveal; the agent is not required to inspect areas that are normally inaccessible. It was undisputed that the defective subfloors were not visible and would not have been apparent during a reasonable property inspection. Thus, as a matter of law, Agent did not breach his statutory duties and the trial court acted within its discretion in concluding that Buyer’s statutory claims were objectively unreasonable.

As to Buyer’s common law intentional and negligent concealment claims, a seller’s agent has no affirmative duty to disclose latent defects unless the agent also knows that such facts are not known to, or within the reach of the diligent attention of, the buyer. The undisputed evidence established that, before the close of escrow, Agent provided Buyer with reports and photographs disclosing the essential facts about the home’s condition. Consequently, the common law claims were without any arguable merit.
Agent did not owe Buyer any additional statutory or common law duties, and he communicated nothing that would have misled a reasonable buyer.

Nonetheless, sanctions should not be routinely awarded; attorneys and litigants must be given substantial breathing room to develop and assert factual and legal arguments. Sanctions should be imposed with restraint and are not mandatory even if a claim is frivolous. In determining whether sanctions should be imposed, an objective test of reasonableness should be applied, including whether any reasonable attorney would agree that the claim is completely without merit. This was an appropriate case for sanctions because:

- Under well-settled law, Buyer’s substantive claims were clearly without merit.
- Buyer did not present any colorable legal or factual argument supporting an extension of existing law to establish liability.
- Before and during the safe harbor period, Agent’s counsel provided specific factual and legal grounds showing that Buyer’s claims were without merit.
- Buyer’s conduct demonstrated that she did not reasonably believe the claims had any merit. Although it is unnecessary to show improper motive or subjective bad faith, the fact that a party does not actually believe in the merits of its claim is relevant to whether sanctions are warranted.

THE EDITOR’S TAKE: More decisions like this could cause a marked decrease in litigation. A run-of-the-mill action for nondisclosure of residential defects was held to be nonmeritorious and also led to the imposition of significant attorney fee liability on the buyer and her attorney.

With regard to the sellers, those parties were allowed to recover their attorney fees because their sales contract contained a fee clause and they were held to be the prevailing parties because the buyer had dismissed her action against them because they were insolvent. (In the unpublished portion of the opinion, the appellate court upheld the sellers’ attorney fee award after their successful motion to compel arbitration.) So, counsel should warn a prospective plaintiff whose documentation includes a broad attorney fee clause that if her theory includes tort claims, a later voluntary dismissal by her can be costly, even if meaningful recovery is unlikely because of nonmerit-related considerations.

With regard to the listing broker, who recovered his attorney fees (and a dismissal) as sanctions against the buyer under CCP §128.7, counsel for other buyers should be aware of the possibility that if judges think that their clients’ claims are truly meritless, they can be held liable (along with the clients) for attorney fees, even if there is no applicable clause in the sale documents saying so. (If only one of them—client or attorney—pays, the odds may be better in favor of upholding the clients’ demand for indemnity from their attorney than vice versa. Indeed, the clients may have a colorable claim to be indemnified for attorney fees that only they were ordered to pay the sellers if they can show that their bad strategy arose from bad advice from their counsel.)

Finally, with regard to the showing broker (who was originally named in the action but appears to have been dropped...
somewhere along the way), as a fiduciary of the plaintiff buyer, he undoubtedly faced significant exposure for not advising his principal to pick up on the red flags, which seemed to abound in this transaction. I wish I knew what that said about his attorney fee exposure.—Roger Bernhardt