**Arizona Association of REALTORS®**

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**Disclosure & Due Diligence**

**Risk Management Certification Core Course**

**Instructor Manual**

**Instructor Manual**

**Zoom activities in blue**

For the Instructor: Course Layout

**Format**

The black text appears in both manuals, while red text denotes answers to questions or other information contained only in the instructor version.

**Timing**

The course is timed out in segments. This should allow you to adjust the timing as needed; for instance, if you need to spend more time on one section than what is allotted, you may adjust by spending slightly less time on a subsequent section. The timing is designed to allow for answering student questions.

**Start with** asking the students to take a moment at the beginning of the course to briefly answer the following questions:

1. What is the most important thing you hope to learn in this course?
2. What risk-related areas or topics most concern you?

If you have time at the end of the course, allow the students to refer back to their answers to the above questions and verify that their concerns were addressed in the course material

If you have time at the end of the course, allow the students to refer back to their answers to the above questions and verify that their concerns were addressed in the course material.

The following key factors should be a part of your delivery:

1. The material presented should have immediate usefulness to the learners.

2. The material presented should be relevant to the learners’ practice. Adult learners need to be able to see the relevancy of what they are learning

3. The environment should be where learners have an opportunity to share their experiences. Adult learners accumulate knowledge most effectively when they are active participants in their own learning process. Design activities or assignments that encourage them to explore a subject matter on their own and learn from personal experience. Pose a question or problem and then ask them to arrive at a solution on their own, or place them in groups and have them collaborate in order to discuss the issue at length and benefit from one another's experience and skill sets. DO NOT TOWN ALL THE ACTIITIES IN THIS OUTLINE.

4. The presentation should be engaging.

**Utilizing the learning activities allow the students to both assess their own experience and learn from the experiences of others making the learning more meaningful than when it is based simply on lecture delivery**

**Live Streaming classes – ADRE requires a minimum of 5 engagement opportunities outside of town-halls**

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**Arizona Association of REALTORS®**

# Course Introduction and Learning Objectives

**Introduction**

This course addresses risk management topics and issues related to disclosures and due diligence. The Disclosures Unit will identify risks associated with brokers’ failure to make the required disclosures to clients and customers, seller disclosure requirements under common law and Arizona statutes and buyer disclosures. The Due Diligence Unit will explain the use of the *Buyer Advisory* in assisting buyers in the due diligence process and identify the risks associated with failing to complete the appropriate inspections and investigations. Portions of the text in this course were taken from *Arizona Real Estate: A Professional’s Guide to Law and Practice Vol 3,* by K. Michelle Lind, Esq., General Counsel for the Arizona Association of REALTORS®. This course covers material from chapters 14 and 16.

**Learning Objectives**

*Upon completion of this course, students will be able to:*

* Avoid the risks associated with failing to make the required disclosures to clients and nonclients.
* Identify required seller disclosures as required by common law and Arizona statute.
* Identify items required to be disclosed by buyers in a transaction.
* Explain the use of the *Buyer Advisory* in assisting buyers with due diligence inspections and investigations.
* Avoid risks associated with buyers failing to complete the appropriate inspections and investigations.

**Unit 1: Disclosure**

**What you don’t know *can* hurt you…**

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# Unit 1, Segment 1: Broker Disclosures

***Timing: 90 minutes total for this segment, approximately 10-15 minutes for each case***

**Learning objective of this segment:**

* To identify the risks associated with failing to make the required disclosures to clients and non-clients

**Poll #1 Intro question**

How many years have you been in real estate?

* less than 1 year
* 1-5 years
* 6-10 years
* 11-20 years
* over 20 years

Are you a

* Associate broker
* Designated broker
* Managing broker
* Agent

**What risks are associated with failing to make the required disclosures to clients and nonclients?** ZOOM if you don’t do the poll: this could be a great breakout exercise – break into groups and have groups make a list – then report back in townhall fashion)

* ***Civil penalties***
* ***Misrepresentation***
* ***Liability related to undisclosed property defects***
* ***Others:***

**Introduction**

Brokers owe fiduciary duties to their principals in a transaction. However, brokers and salespersons have certain duties to disclose to clients and nonclients under common law. The following cases highlight the required disclosures.

***[Note: For the following cases, the students have only the case facts and space to make notes on the decisions.]***

## *Jennings v. Lee*, 105 Ariz. 167, 461 P.2d 161 (1969)

***CASE RECORDING***

**Case Facts:**

* The buyer traded a parcel of land for an operating restaurant.
* The broker acted as a dual agent in the transaction, representing both parties.
* The seller was aware the restaurant was not generating enough income to be sustainable.
* The broker saw copies of at least two different income statements for the restaurant, provided by the seller.
* The income statement the broker showed to the buyer reflected inflated figures almost five times the actual profit.
* When the buyer voiced her concern that she should have her attorney review the transaction, the broker discouraged her from doing so.
* Two months after the transaction was completed, the buyer realized the discrepancy in income and filed suit against the broker and seller, seeking rescission of the contract.

**Decision Key Points:**

* ***An appellate court ultimately granted the buyer’s request for rescission and found that the elements necessary to establish fraud on the part of the seller were present.***
* ***In regard to the actions of the broker, the court found he had breached his fiduciary duty by showing the buyer the false operating statement and failing to disclose his knowledge of the correct statement, which he had in his possession.***
* ***The court’s decision highlighted the broker’s duty to disclose to his client information in his possession pertaining to the transaction.***

***Part of fiduciary duty is to make a complete and full disclosure of all known material facts that might affect the client’s decision to sell or buy a property.***

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## *Morley v. J. Pagel Realty & Insurance*, 27 Ariz. App. 62, 550 P.2d 1104 (1976)

***CASE RECORDING***

**Case Facts:**

* The seller accepted an offer presented by the listing broker that provided for carryback financing but no deed of trust.
* After COE, the buyers deeded the property to a third party for cash.
* The buyers subsequently defaulted on the note and filed for bankruptcy.
* The sellers sued their broker for failing to inform them they should have required the buyer to execute a deed of trust, which could have been recorded to secure the buyers’ performance.

**Decision Key Points:**

* ***The broker had a duty to affect a sale for the client on the best terms possible.***
* ***The broker had a duty to disclose to the client all information the broker possessed pertaining to the transaction.***
* ***The broker was obligated to inform the sellers they should require security for carryback.***
* ***A broker should make all explanations commensurate with the education and understanding of the client and, if the broker can’t give competent advice, should allow the client the opportunity to obtain advice elsewhere.***
* ***You can’t use ignorance of the law as a defense for not following or knowing about the law***

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## *Mason v. Bulleri*, 25 Ariz. App. 357, 543 P.2d 478 (1975)

***CASE RECORDING***

**Case Facts:**

* The sellers entered into a contract for the sale of their home calling for an initial deposit and down payment from the buyers, with the remainder to be paid as a lump sum within the next two years. The court contended that the “language of the contract contemplated the retention by the sellers of a security interest in the property.”
* The buyers told the listing broker the balance would have to be unsecured, as they would have to mortgage the home to come up with the down payment.
* The broker did not disclose this information to the sellers, instead advising them that a deposit was in place and the buyers had sufficient cash to make the down payment.
* The broker had the buyers fill out two different offers for different amounts, both lower than the asking price. He presented the lower offer to the sellers without advising them of the existence of the higher offer.
* At some point, the sellers refused to proceed with the sale. The broker proceeded to file suit against the sellers to force the payment of claimed commission.

**Decision Key Points:**

* ***An appellate court denied the broker’s claim for any commission.***
* ***The court held that it is the broker’s duty to deal with his principal in good faith and disclose any information he has concerning the buyer’s ability to complete the purchase***
* ***To the above-stated issue, the court found that the broker had seriously breached his fiduciary duty by failing to disclose that, although the contract provided for the sellers to retain a security interest in the property, the buyers had represented they would be unable to complete the purchase if the sellers retained that security interest.***
* ***The court also stated that the broker additionally breached his fiduciary duty to his client by presenting the lower offer and failing to disclose that the buyers were willing to pay a higher price.***

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## *Kimmel v. Clark*, 21 Ariz. App. 455, 520 P.2d 851 (1974)

***CASE RECORDING***

**Case Facts:**

* The seller entered into a listing agreement with a broker to sell her home.
* The listing broker produced a buyer with whom a satisfactory purchase agreement could not be reached.
* The broker then produced another buyer who agreed to purchase the property for the listed price and produced a $1,000 check as a deposit.
* It turned out that the buyers were ‘straw men’ and were actually the son and daughter-in-law of the broker, a fact she did not disclose to the seller.
* The broker sued the seller for claimed commission, arguing she had produced a ready, willing and able buyer under the terms of the listing agreement.

**Decision Key Points:**

* ***The trial court found in favor of the seller and that decision was upheld on appeal.***
* ***The court held that “a broker employed to sell property may not, without the principal’s full knowledge and consent, become the purchaser.”***
* ***The court found a fiduciary relationship existed between the broker and the seller and had clearly been breached by the broker for failing to disclose her relationship with the buyers.***

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## *Lombardo v. Albu*, 199 Ariz. 97, 14 P.3d 288 (2000)

***CASE RECORDING***

**Case Facts:**

* The sellers, in default on their loan, entered into a loan agreement with their lender to list and sell their home to pay the loan. They proceeded to list the property.
* Another broker, representing the buyer, presented an offer to the listing broker, which was accepted.
* Prior to presenting the offer, the buyer’s broker was told by the buyer that her husband had serious financial problems and had filed for bankruptcy. The wife hoped to avoid discovery of this fact by making an offer in her name only.
* The buyer’s broker did not disclose to the sellers that the wife was not an “able” buyer or might be unable to perform.
* Had the sellers been aware of the situation, they would have sought other conditions in the contract, such as the right to keep the property on the market.
* After several delays in closing, the buyer was unable to close on the property.
* The sellers ultimately lost their equity in the home when it was sold at a trustee’s sale.
* The sellers filed suit against the other parties involved, claiming negligent misrepresentation on the part of the buyer’s broker.

**Decision Key Points:**

* ***After the trial and appellate courts held that the buyer’s financial information was confidential and the buyer’s broker had no duty to disclose it to the seller, the case was eventually heard by the Arizona Supreme Court, who reversed the decision.***
* ***The court stated that a covenant of good faith and fair dealing exists as a legal duty between buyers and sellers, which requires them to disclose facts material to the transaction.***
* ***The court cited the Restatement (Second) of Agency §348(e), which states:***

***Although the making of a contract by the agent does not constitute a representation by him that his principal is known by him to be solvent or honorable, if the agent knows that the principal does not intend to perform the contract because of hopeless insolvency or other reason, the making of a contract for him under such conditions subjects the agent to liability. [Citation omitted.]***

* ***The court further stated that “the performance of an agent’s fiduciary duty to its principal is compatible with the agent’s duty to deal fairly with all parties to the transaction.”***
* ***To the argument of confidentiality, the court stated that even if the information was confidential, the Restatement (Second) of Agency §395 allows an agent to disclose confidential information if doing so is necessary to protect themselves or a third party.***

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## *Aranki v. RKP Investments, Inc.*, 194 Ariz. 206, 979 P.2d 534 (App. 1999)

***CASE RECORDING***

**Case Facts:**

* The sellers listed their home with a broker. They did not disclose any material defects in the property to the listing broker.
* The buyers, represented by their broker, purchased the property.
* After closing, the buyers discovered defects in the property that were not disclosed to them prior to the sale.
* The buyers proceeded to file suit against the sellers, and also against the listing broker (by way of warranty and fraud claims), and the buyers’ broker (by way of negligent misrepresentation claims).

**Decision Key Points:**

* ***After a trial court found in favor of the defendants, the plaintiffs appealed the decision.***
* ***The appellate court reversed the judgment in favor of the plaintiffs (appellants) regarding the buyers’ brokers and the sellers.***
* ***As to the listing broker, the appellate court affirmed the trial court’s judgment that the facts did not support the claim of negligent misrepresentation.***

**Regarding the Listing Broker:**

* ***The court stated that while the listing broker owed a fiduciary duty to his clients, the sellers, his only duty to the buyers was to deal fairly with them.***
* ***Supporting the duty of fair dealing, the court found the listing broker had no knowledge of the property defects and no duty to perform any investigations to discover defects not readily apparent.***
* ***The court further stated the listing broker was not liable to the buyers for passing along information obtained from the seller without proof the listing broker knew or should have known the information might be false.***

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**Matching case with action exercise (use chat and put exercise in handout)**

**Write the letter next to the case name that relates to the DISCLOSURE action that resulted from the case:**

\_\_\_ Jennings v Lee

\_\_\_ Morley v J. Pagel Realty & Insurance

\_\_\_ Mason v Bulleri

\_\_\_ Kimmel v Clark

\_\_\_ Lombardo v Albu

\_\_\_ Aranki v RVP Investments

A. Full disclosure of all known material facts (Jennings)

B. Disclose best terms which includes discussions regarding information the broker possess about the transaction (Morley)

C. Disclose any information that the buyer is or maybe unable to perform (Mason)

D. Disclose relationships with buyer (Kimmel)

E. Ability to perform is not confidential information (Lombardo)

F. Listing broker may pass along information obtained from seller (Aranki)

## Segment Conclusion

**What is the main difference between the different disclosures required for clients vs. nonclients?**

***While you must make full and complete disclosure to your principal, you only owe the duty of good faith and fair dealing to nonclients.***

**In what type of situation might you incur risk for passing along information to a buyer obtained from your seller?**

***If you have reason to believe the information is false or you have witnessed evidence indicating the information is false.***

**What should you do if your client requests information regarding a transaction beyond the scope of your expertise?**

***Recommend they obtain advice from a qualified professional.***

# Unit 1, Segment 1: Broker Disclosure List

**Poll #2 (two questions in this poll) after page 6**

1) Have you ever been involved in a legal dispute or complaint pertaining to disclosure/non-disclosure?

* Yes
* No

2) If you have been involved in a disclosure/non-disclosure, which of the following did it pertain to:

* dual agency
* reasonable care
* procuring cause
* other

Disclosure obligations imposed by common law are reflected by the ADRE Commissioner’s Rules.

**Disclosures to Seller Clients:**

* All offers (R4-28-802(B))
* Any known information that the buyer is or may be unable to perform (R4-28-1101(B))
* If the broker, broker’s family or a business entity in which the broker has an interest is the buyer (R4-28-1101(E))
* If the broker is receiving any compensation, rebate or profit for the transaction (and obtain written consent)(R4-28-1101(G))
* The name of each employing broker receiving compensation from the transaction (R4-28-701)

**Disclosures to Buyer Clients:**

* All known defects existing in the property (R4-28-1101(B)(3))
* Any known information that the seller is or may be unable to perform (R4-28-1101(B)(1))
* The possible existence of a known lien or encumbrance on the property (R4-28-1101(B)(4))
* If the broker, broker’s family or a business entity in which the broker has an interest is the seller (R4-28-1101(E))
* If the broker is receiving any compensation, rebate or profit for the transaction (and obtain written consent)(R4-28-1101(G))
* The name of each employing broker receiving compensation from the transaction (R4-28-701)

# Unit 1, Segment 2: Seller Disclosures

***Timing: 60 minutes total for this segment, approximately 15-20 minutes for each case***

**Learning objective of this segment:**

* To identify required seller disclosures as required by common law

**What risks are associated with sellers failing to make the required disclosures?**

* ***Civil penalties associated with fraud and misrepresentation***
* ***Rescission***
* ***Others:***

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**Introduction**

Sellers have certain common law duties to disclose material facts about a property. In some cases, they have a duty to disclose property conditions regardless of whether or not they consider them material. The following cases highlight some important disclosures required under common law.

*Note:* Specific disclosures required by Arizona statute will be covered in Segment 4.

## *Hill v. Jones*, 151 Ariz. 81, 725 P.2d 1115 (App. 1986)

***CASE RECORDING***

**Case Facts:**

* The buyers and sellers entered into a contract for a home with a wood floor.
* The sellers disclosed no past termite damage and the termite report indicated no visible evidence of infestation or previous treatment.
* After close of escrow, the buyers learned from a neighbor that the house had past termite infestation. The buyers also discovered part of the wood floor was crumbling.
* The termite inspector had not seen the treatment holes in the patio because of stacked boxes and did not find the termite damage inside because a large plant covered the area.
* When the buyers filed suit against the sellers, they discovered the sellers had received two termite guarantees from the previous owner, had treated the house twice for termites and that the existing termite damage had not been repaired.

**Decision:**

* ***The court found the seller had duty to disclose known facts to the buyer.***
* ***The court delineated a seller’s duty to disclose known facts materially affecting the value of a property that are not readily observable and are not known to buyers.***
* ***The court further stated that under certain circumstances, nondisclosure of a known fact may be equivalent to the assertion the fact does not exist and, therefore, may be given the same legal effect as fraud and misrepresentation.***
* ***Not telling is the same as lying***

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## *Universal Inv. Co. v. Sahara Motor Inn, Inc.*, 127 Ariz. 213, 215, 619 P.2d 485, 487 (1980)

***CASE RECORDING***

**Case Facts:**

* The buyer purchased a motel from the seller “as is.”
* Prior to the sale, the buyer inspected and approved the premises.
* After closing, the buyer learned from the City of Tucson that the motel’s electrical system was in violation of city code and stopped making payments on the note.
* The seller sued for the amount of the note on the property.

**Decision Key Points:**

* ***What can be interpreted from the decision is that, if the buyer asks the seller about an aspect of the property, the seller has a duty to disclose the information, whether or not the seller considers the information material.***
* ***In this case, the court stated that an inquiry about the condition of the electrical system would have required the seller to disclose all they knew; however, no such inquiry was made. Therefore, the seller was not held liable for the electrical problems.***

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## *S. Development Corp. v. Pima Capital Management Co.*, 201 Ariz. 10, 31 P.3d 123 (App. 2002)

***CASE RECORDING***

**Case Facts:**

* The buyer purchased two apartment complexes from the sellers.
* The sellers made no warranties and the properties were purchased “as is.”
* The buyer had two engineering firms inspect the property, which revealed no substantial problems with the plumbing.
* Two years after the sale closed, the buyer discovered the property had defective plumbing due to the polybutylene pipe used in both buildings.
* The buyer sued the sellers for fraud and nondisclosure for failing to disclose the defective plumbing.

**Decision Key Points:**

* ***The trial court ruled in favor of the buyer (plaintiff) and the decision was upheld by the appellate court.***
* ***The court held that known latent defects in a property must be disclosed, regardless of whether the property is being sold “as is.”***

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**Matching case with action exercise (use chat and put exercise in handout)**

**Write the letter next to the case name that relates to the DISCLOSURE action that resulted from the case:**

\_\_\_ Hill v Jones

\_\_\_ Universal Inv. Co. v Sahara Motor Inn, Inc.

\_\_\_ S. Development Corp v Pima Capital Management Co.

A. If the buyer asks the seller about an aspect of the property, the seller has a duty to disclose the information (S. Development Corp v Pima Capital Management Co.)

B. Known latent defects in a property must be disclosed (S. Development Corp. v. Pima Capital Management Co)

C. Disclose known facts to the buyer (Hill v Jones)

**Seller Property Disclosure Statement (SPDS)**

You have a seller that doesn’t want to fill out the SPDS, how do you explain to them the value in completing the form?

Does not filling out he SPDS relieve the seller of any obligation to disclose material facts?

Do you review the SPDS after the seller has filled it out?

Do you review the SPDS when it is sent to your buyer, as a buyer agent?

What is your obligation, if any, to disclose a red flag item if the seller refuses to and tells you not to disclose it?

If seller hasn’t seen the property, what part of the SPDS CAN they fill out?

What if it is an estate sale?

What do you do if you don’t receive a SPDS?

What do “flippers” need to disclose? Licensed contractors

**Disclosure – Multiple Offers/Back-Up Offers**

When can you disclose you are in a multiple offer situation?

ZOOM: Using chat: What form is used for sellers to give you written instruction on accepting only written offers and/or to take back up offers. Possible answers: ER, EA, written email instructions or text – emphasize it just must be in written format

# Unit 1, Segment 3: Buyer Disclosures

***Timing: 15 minutes total for this segment***

**Learning Objective of this segment:**

* To identify items required to be disclosed by buyers in a transaction.

**What risks are associated with buyers failing to make the required disclosures?**

* ***Failure to fulfill contractual obligations***
* ***Civil penalties***
* ***Others:***

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**Buyer Disclosures**

Because the major consideration flowing from the buyer to the seller is price, the buyer’s legally and contractually required disclosures generally center around their ability to perform on the contract. Buyer disclosures include:

* All known facts materially affecting the transaction
* All facts materially affecting the buyer’s ability to pay the purchase price
* All facts critical to their ability to perform, such as if the buyer:
* ***Must sell their existing home or other property to qualify for financing***
* ***Must lease a property to qualify for financing***
* ***Must complete a sale before the funds for the down payment will be available***
* ***Has filed bankruptcy***

What needs, if anything, needs to be disclosed for site unseen offers?

Does buyer have to disclose they are making more than offer?

# Unit 1, Segment 4: Statutory Disclosures

***Timing: 60 minutes total for this segment***

**Learning objective of this segment:**

* To identify the specific disclosures required by Arizona statutes in accordance with federal regulations

**What risks are associated with statutory disclosures?**

* ***Regulatory sanctions***
* ***Civil liability***
* ***Others:***

**Specific Disclosures**

Several specific disclosures are required by statute. They are:

**Lead-based Paint Disclosure**

* Required in transactions involving properties constructed prior to 1978.
* Before the buyer is obligated under any contract to purchase the property, the seller must:
* Provide the lead hazard pamphlet.
* Disclose any information concerning known hazards.
* Provide any available records or reports concerning lead-based paint.
* Permit the buyers with an opportunity to conduct a lead-based paint risk assessment or inspection.
* Contracts on homes constructed before 1978 must contain certain language and disclosures to satisfy the statutory requirements. The AAR Disclosure of Information on Lead-based Paint Hazards form may be used for this purpose.

**What specific risks are addressed by the LBP Disclosure?**

* ***Regulatory sanctions***
* ***Possible criminal sanctions***

**Can the LBP Disclosure be completed after contract acceptance?**

***Yes, although it is always best to provide the buyer with the disclosure before a contract is executed, if at all possible. This issue is addressed by HUD and the EPA in Part III of the Interpretive Guidance for the Real Estate Community on the Requirements for Disclosure of Information Concerning Lead-based Paint in Housing. The Interpretive Guidance confirms the disclosure information can be provided to the buyer after contract acceptance if the buyer has the unilateral right to cancel the contract after receipt of the disclosures.***

**Is the use of MLS electronic lead-based paint disclosures acceptable?**

***Yes, the EPA has indicated this is acceptable as long as:***

* ***The buyer receives and signs the completed lead-based paint disclosure form “before the point of obligation”; and***
* ***The buyer’s agent obtains a copy of the original disclosure form signed by the seller from the listing broker and attaches it to the form signed by the buyer. The two forms must “add up” to a single completed form for the file. In other words, it is permissible to get it signed in this manner but the brokers must still have a complete disclosure in the file signed by both parties.***

**What are the penalties for violation?**

***There are procedures to determine the appropriate enforcement response outlined in the Guidelines for Assessments of Civil Penalties for Violations of the Disclosure Rule. No warnings will be given; immediate civil penalties will be issued for violations. In addition, a person who knowingly or willfully violates this law can be subject to criminal sanctions, including imprisonment for up to one year and criminal fines of $25,000 for each day of violation.***

**Zoom: Breakout: What are the effects of lead-based paint poisoning**

### Lead poisoning symptoms in adults

Signs and symptoms in adults might include:

* High blood pressure
* Joint and muscle pain
* Difficulties with memory or concentration
* Headache
* Abdominal pain
* Mood disorders
* Reduced sperm count and abnormal sperm
* Miscarriage, stillbirth or premature birth in pregnant women

Signs and symptoms of lead poisoning in children include:

* Developmental delay
* Learning difficulties
* Irritability
* Loss of appetite
* Weight loss
* Sluggishness and fatigue
* Abdominal pain
* Vomiting
* Constipation
* Hearing loss
* Seizures
* Eating things, such as paint chips, that aren't food (pica)

**What properties are exempt from the LBP disclosure requirements?**

* Property constructed in 1978 or later
* Housing for elderly (retirement communities composed of persons over the age of 62) or disabled housing unless a child under the age of six will reside therein
* Foreclosure transactions
* Short-term leases (100 days or less where no renewal or extension can occur)
* Lease renewals where the disclosures were previously made and no new information since the initial disclosure was provided
* Purchase, sale or servicing of mortgages
* Sale or lease of zero-bedroom dwellings

**Swimming Pool Barrier Disclosure**

A.R.S. §36-1681(E) states that “A person on entering into an agreement to build a swimming pool or contained body of water or sell, rent or lease a dwelling with a swimming pool or contained body of water shall give the buyer, lessee or renter a notice explaining safety education and responsibilities of pool ownership as approved by the department of health services.”

**Planned Community/Condominium Disclosure Information**

Certain specific disclosures are required when the transaction involves a sale in planned communities/condominiums. When the development has fewer than 50 units, the seller is required to make the required disclosures, providing the buyer with a number of items including:

* ***A copy of bylaws and rules of the association***
* ***A copy of the declaration CC&Rs***
* ***Information related to fees and dues***
* ***Contact information for the association, including phone number, address, contact person, etc.***
* ***A copy of the association’s operating budget***
* ***Others***

When the development has 50 or more units, these disclosures must be made by the association.

These disclosures must be made within 10 days of written receipt of the pending sale. (For sellers, this would mean within 10 days after contract acceptance.)

**Notice of Soil Remediation**

If the seller has actual knowledge that the property has been subject to soil remediation, it must be disclosed in accordance with A.R.S. §33.434.01 and 49-701.02. This means the seller knows “…the property has been used for the disposal of excavated soils which do not meet predetermined residential soil remediation levels or remediation standards for residential exposure assumptions…” A.R.S. §49-701.02(B).

**Affidavit of Disclosure**

An Affidavit of Disclosure is required for sellers of five or fewer parcels of land, other than subdivided land, in an unincorporated area not located in a subdivision.

**What specific risks are addressed by the Affidavit of Disclosure?**

* ***Seller failure to disclose***
* ***Rescission claims***
* ***Broker liability for failure to advise seller of laws***

**What are the time requirements?**

***The seller is required to furnish the affidavit to the buyer at least seven days before the transfer of the property.***

**Does this apply only to vacant land?**

***The affidavit applies to all land sold in five or fewer parcels in an unincorporated area, whether improved, unimproved, vacant, residential or commercial.***

**What kind of information must be disclosed?**

***The affidavit must address issues such as legal access, physical access, road maintenance, floods and floodplains, utilities and services, water, wells, septic systems, percolation tests, and zoning deficiencies.***

**What if the seller does not know some of the required disclosure information?**

***Some of the items do not allow for an “unknown” response. If the seller does not know or have access to the requested information, they should indicate that on the form and provide any necessary explanation on the explanation lines.***

**Is the seller required to make any other disclosures?**

***Yes, a seller is still required to disclose all known material defects in addition to the statutory disclosures addressed in the affidavit. In addition, if the information in the affidavit changes, a new affidavit must be recorded.***

**What action must a buyer take to rescind a transaction after receiving the affidavit of disclosure?**

***The buyer can rescind the transaction within five days of receipt of the affidavit of disclosure. Written notice of rescission from the buyer to the seller within the time period should be sufficient.***

**Meth Lab (and other Dangerous Drug Lab) Disclosure**

SB 1256, Arizona’s drug lab remediation program has been transferred from BTR to the Arizona Department of Environmental Quality. This same legislation repealed the law that: (1) mandated remediation of properties used as drug labs; and (2) required disclosure of the fact that the property had served as an illegal drug lab and remains unremediated.

Note: Although AZ law no longer statutorily requires disclosure of drug labs, this type of information is material in a transaction.  Accordingly, the SPDS at lines 205-206 asks the seller if they are “aware if any portion of the Property has ever been used as a ‘Clandestine drug laboratory’.

ZOOM: YES/NO: Is this a required disclosure: Yes/No

**Subdivision Disclosures/Public Reports**

Sellers of new homes in subdivisions are required to provide the buyer with the Public Report and a chance to review it prior to signing a contract.

**What risks are addressed by subdivision disclosures and Public Reports?**

* ***Failure to disclose critical information regarding physical and environmental characteristics of the property***
* ***Transactions involving illegal subdividing of property***

**What items are addressed in a Public Report?**

The Public Report contains vital information about the subdivision, including:

* ***Identity of developer***
* ***Physical characteristics***
* ***Environmental characteristics***
* ***Conditions limiting use or occupancy***
* ***Road maintenance***
* ***HOA info***
* ***Flooding and drainage issues***
* ***Adjacent land use***
* ***Location of gas pipelines***
* ***Vicinity to airports***
* ***Documentation of subdivision’s planned completion***
* ***Availability of utilities***
* ***Availability of schools, shopping facilities, public transportation and emergency services***

(Older public reports are available on line if you are looking for information on a resale property:

<http://services.azre.gov/publicdatabase/SearchDevelopments.aspx>)

**Illegal Subdivisions Acting in Concert**

In addition, you should be aware of “red flags” which may indicate illegal subdividing of property. These may include:

* ***“Too good to be true” financing offers***
* ***Monies paid out of escrow***
* ***Lot release provisions***
* ***Others***

**Other Statutory Disclosures**

The following disclosures are also required by statute:

* Military airport disclosure (A.R.S. §28-8484): requires sellers of residential property to disclose if the property is located “in the vicinity of a military airport or ancillary military facility.”
* Public airport information (A.R.S. §28-8486): if a residential property is located in the vicinity of a public airport, this must be disclosed to buyers. For this purpose, a recorded map is available at the county recorder’s office. (Sometimes referred to as a noise contour map)

**Unit 2: Due Diligence**

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# Unit 2, Segment 1: Due Diligence and the *Buyer Advisory*

***Timing: 15 minutes for this segment***

**Learning objective of this segment:**

* To explain the use of the *Buyer Advisory* in assisting buyers with due diligence inspections and investigations.

ZOOM: POLL: Which of the following is not covered in the Buyer Advisory?

* Crime Statistics
* Fair Housing
* Market Conditions
* 1031 Exchanges

**In general, what risks are associated with the due diligence period?**

* ***Failure to allow enough time for inspections***
* ***Failure to use qualified inspectors***
* ***Failure to review and understand important documents related to the transaction***
* ***Disputes regarding property conditions***
* ***Failure to account for surrounding area conditions***

**What is the significance of the *Buyer Advisory*?**

* ***Just as the seller has a duty to disclose, the buyer has a duty to satisfy themselves as to the condition of a property. The Buyer Advisory was created, in part, to combat efforts to expand broker duties and liabilities related to inspection and discovery.***
* ***Buyers must share some responsibility for evaluating the condition of a property prior to purchase – this cuts down on disputes between buyers and sellers regarding the condition of a property, buyer claims of negligent misrepresentation, etc.***
* ***REALTORS® are not licensed inspectors; the Buyer Advisory aids buyers in seeking out qualified professionals to perform needed inspections and investigations. It also contains important resources for buyers to identify areas of concern and access important information such as tax records, insurance claims history, zoning information and much more.***
* ***When deciding disputes between buyers and sellers regarding property defects, courts often place great weight on whether or not the buyers inspected the property. By making a thorough inspection of documents, physical conditions, and conditions affecting the surrounding area prior to closing, buyers can protect themselves in the event of a dispute after the sale.***

# Unit 2, Segment 2: Document Review

***Timing: 30 minutes total for this segment***

**Learning objective of this segment:**

* To identify the risks associated with buyers’ failure to review important documents related to the transaction

**Risk Identification**

The *Buyer Advisory* contains valuable information for buyers concerning documents that should be reviewed during the due diligence period. Better-educated buyers reduce your risk and theirs by equipping themselves with the information necessary to thoroughly and effectively investigate a property. Identify the potential risks associated with reviewing the following documents:

**B/O Room: General nature: identify 3-5 potential risks with buyer not completely reviewing these documents**

**Purchase Contract:**

* ***Buyer’s assertion their broker didn’t tell them what the contract said***
* ***Failure to understand their contractual obligations***
* ***Failure to understand their legal rights***
* ***Others…***

**Best Practice:\_\_\_\_\_\_\_\_\_\_\_\_\_\_\_\_\_\_\_\_\_\_\_\_\_\_\_\_\_\_\_\_\_\_\_\_\_\_\_\_\_\_\_\_\_\_\_\_\_\_**

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**MLS Printout:**

* ***Failure to verify MLS info***
* ***Failure to realize MLS info is not part of purchase contract***
* ***Use as exhibit in summons and complaint or other pleadings in a civil case***
* ***Others…***

**Best Practice:\_\_\_\_\_\_\_\_\_\_\_\_\_\_\_\_\_\_\_\_\_\_\_\_\_\_\_\_\_\_\_\_\_\_\_\_\_\_\_\_\_\_\_\_\_\_\_\_\_\_**

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**Subdivision Public Report:**

* ***Transactions involving illegal subdividing***
* ***Failure to verify info in the Public Report***
* ***Failure to understand limitations of use or occupancy***
* ***Failure to understand physical and environmental characteristics***
* ***Others…***

**Best Practice:\_\_\_\_\_\_\_\_\_\_\_\_\_\_\_\_\_\_\_\_\_\_\_\_\_\_\_\_\_\_\_\_\_\_\_\_\_\_\_\_\_\_\_\_\_\_\_\_\_\_**

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**Title Report or Title Commitment:**

* ***Failure to understand Schedule B Exceptions***
* ***Failure to recognize the impact of Schedule B Exceptions on future property use***
* ***Failure to obtain needed professional advice***
* ***Others…***

**Best Practice:\_\_\_\_\_\_\_\_\_\_\_\_\_\_\_\_\_\_\_\_\_\_\_\_\_\_\_\_\_\_\_\_\_\_\_\_\_\_\_\_\_\_\_\_\_\_\_\_\_\_**

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**Loan Documents:**

* ***Insufficient time to secure financing***
* ***Failure to understand financing obligations***
* ***Failure to submit proper documentation***
* ***Failure to identify predatory lending practices***
* ***Others…***

**Best Practice:\_\_\_\_\_\_\_\_\_\_\_\_\_\_\_\_\_\_\_\_\_\_\_\_\_\_\_\_\_\_\_\_\_\_\_\_\_\_\_\_\_\_\_\_\_\_\_\_\_\_**

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**HOA Disclosures:**

* ***Failure to understand HOA dues and fees***
* ***Liability for current or unpaid dues***
* ***Alterations or improvements in violation of covenants***
* ***Others…***

**Best Practice:\_\_\_\_\_\_\_\_\_\_\_\_\_\_\_\_\_\_\_\_\_\_\_\_\_\_\_\_\_\_\_\_\_\_\_\_\_\_\_\_\_\_\_\_\_\_\_\_\_\_**

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**Affidavit of Disclosure:**

* ***Failure to investigate critical issues contained in the affidavit***
* ***Failure to understand rescission rights***
* ***Others…***

**Best Practice:\_\_\_\_\_\_\_\_\_\_\_\_\_\_\_\_\_\_\_\_\_\_\_\_\_\_\_\_\_\_\_\_\_\_\_\_\_\_\_\_\_\_\_\_\_\_\_\_\_\_**

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**NOTE: The following are town-hall style discussion (these topics are not included in the above breakout room activity**

**Seller’s Property Disclosure Statement (“SPDS”):**

* ***Failure to verify items within the SPDS***
* ***Failure to investigate disclosed repairs***
* ***Others…***

**Best Practice:\_\_\_\_\_\_\_\_\_\_\_\_\_\_\_\_\_\_\_\_\_\_\_\_\_\_\_\_\_\_\_\_\_\_\_\_\_\_\_\_\_\_\_\_\_\_\_\_\_\_**

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**Covenants, Conditions and Restrictions (“CC&Rs”):**

* ***Failure to understand restrictions***
* ***Liability associated with CC&R enforcement***
* ***Others…***

**Best Practice:\_\_\_\_\_\_\_\_\_\_\_\_\_\_\_\_\_\_\_\_\_\_\_\_\_\_\_\_\_\_\_\_\_\_\_\_\_\_\_\_\_\_\_\_\_\_\_\_\_\_**

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**Homeowner’s Association (“HOA”) Governing Documents:**

* ***Failure to understand related fees***
* ***Failure to understand association rights and remedies***
* ***Others…***

**Best Practice:\_\_\_\_\_\_\_\_\_\_\_\_\_\_\_\_\_\_\_\_\_\_\_\_\_\_\_\_\_\_\_\_\_\_\_\_\_\_\_\_\_\_\_\_\_\_\_\_\_\_**

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**Economic Items** **(i.e. financial statements, rent rolls, deposits, leases, service contracts):**

* ***Discrepancies in statements related to income-producing properties***
* ***Others…***

**Best Practice:\_\_\_\_\_\_\_\_\_\_\_\_\_\_\_\_\_\_\_\_\_\_\_\_\_\_\_\_\_\_\_\_\_\_\_\_\_\_\_\_\_\_\_\_\_\_\_\_\_\_**

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**Home Warranty Policy:**

* ***Failure to understand coverage and limitation***
* ***Others…***

**Best Practice:\_\_\_\_\_\_\_\_\_\_\_\_\_\_\_\_\_\_\_\_\_\_\_\_\_\_\_\_\_\_\_\_\_\_\_\_\_\_\_\_\_\_\_\_\_\_\_\_\_\_**

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**LBP Disclosure Form:**

* ***Failure to understand legal rights associated with LBP disclosures***
* ***Others…***

**Best Practice:\_\_\_\_\_\_\_\_\_\_\_\_\_\_\_\_\_\_\_\_\_\_\_\_\_\_\_\_\_\_\_\_\_\_\_\_\_\_\_\_\_\_\_\_\_\_\_\_\_\_**

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**County Assessors/Tax Records:**

* ***Failure to verify critical information such as assessed value, tax liability, square footage, date built, etc.***
* ***Others…***

**Best Practice:\_\_\_\_\_\_\_\_\_\_\_\_\_\_\_\_\_\_\_\_\_\_\_\_\_\_\_\_\_\_\_\_\_\_\_\_\_\_\_\_\_\_\_\_\_\_\_\_\_\_**

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**Professional Home Inspection Report**

* ***Failure to use a qualified inspector***
* ***Failure to discover costly defects in a property***
* ***Failure to identify areas excluded from an inspection***
* ***Others…***

**NOTE:** Home inspectors should have E & O Insurance

**Best Practice:\_\_\_\_\_\_\_\_\_\_\_\_\_\_\_\_\_\_\_\_\_\_\_\_\_\_\_\_\_\_\_\_\_\_\_\_\_\_\_\_\_\_\_\_\_\_\_\_\_\_**

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**Termites and Other Wood Destroying Insects and Organisms**

* ***Failure to properly evaluate the condition of a property***
* ***Failure to discover past treatments, infestation or existing damage***
* ***Others…***

**Best Practice:\_\_\_\_\_\_\_\_\_\_\_\_\_\_\_\_\_\_\_\_\_\_\_\_\_\_\_\_\_\_\_\_\_\_\_\_\_\_\_\_\_\_\_\_\_\_\_\_\_\_**

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# Unit 2, Segment 3: Physical Inspections

***Timing: 60 minutes total for this segment***

**Learning objective for this segment:**

* To identify the risks associated with buyers’ failure to complete appropriate inspections and investigations

**Home or Property Inspections**

**What risks are associated with failing to perform a home inspection?**

* ***Failure to discover property defects***
* ***Misinterpreting the condition of a property***
* ***Failure to discover red flags***

**Why should buyers perform a home inspection?**

***A qualified inspector can detect many existing or potential problems that could be costly to repair. The majority of disputes between buyers and sellers are related to material defects in a property; buyers should take every precaution to uncover any existing problems during the inspection period. A qualified home inspector may also be able to recommend needed evaluation by other professionals.***

**How can a buyer be sure an inspector is qualified?**

***The Buyer Advisory contains links to websites of the Arizona Board of Technical Registration, which provides a list of certified home inspectors, and the American Society of Home Inspectors, which provides additional information on home inspections.***

**Repairs and New Construction**

**What risks are associated with failing to investigate repairs or new construction (additions)?**

* ***Work not properly permitted***
* ***Work not expertly performed***

**How does the *Buyer Advisory* aid buyers in investigating repairs and new construction?**

The *Buyer Advisory* contains a link to a guide on hiring a licensed contractor to perform an inspection. Also, it directs buyers to where they can find information regarding permitting.

**Roof**

**What risks are associated with failing to inspect the roof of a property?**

* ***This can be a costly repair!!***
* ***Failure to notice past leaks and/or water damage***

The *Buyer Advisory* contains information on hiring a licensed roofer as well as a link to the Arizona Roofing Contractors Association.

**Wood-destroying Insects and Other Wood-destroying Organisms**

**What risks are associated with failing to complete this inspection?**

* ***Failure to discover past or present infestation or damage***

**Swimming Pools and Spas**

**What risks are associated with failing to inspect swimming pools and/or spas?**

* ***Cleaning systems and pumps can be costly to repair***
* ***Failure to comply with city and county ordinances***

**How does the *Buyer Advisory* aid buyers in swimming pool/spa inspection?**

The *Buyer Advisory* contains directions and web links for buyers to access pool barrier contact information for cities and counties, the Arizona Department of Health Services Private Pool Safety notice and the state law on swimming pools.

**Square Footage**

**What risks are associated with failing to verify square footage?**

* ***May be material to the transaction***
* ***Use and/or resale concerns***

Links to websites containing lists of appraisers and architects may be accessed in the *Buyer Advisory*.

**Sewer, Septic, and Other On-site Wastewater Treatment Facilities**

**What risks are associated with failing to verify sewer connection?**

* ***Falsely identifying a property as being connected to sewer***

**What risks are associated with failing to inspect an on-site wastewater treatment facility or septic system?**

* ***Failure to comply with ADEQ rules regarding inspection and transfer of ownership***

The *Buyer Advisory* contains a link to the ADEQ website for information on requirements.

* ***Failure to identify whether the facility or septic system has any issue – cracks proper size, etc.***

**Water/Well Issues**

**What risks are associated with failing to investigate water/well issues?**

* ***Disputes regarding the availability and quality of the water to the property***
* ***Failure to understand General Stream Adjudications that may affect the property***

**Soil Conditions**

**What risks are associated with failing to investigate soil conditions?**

* ***Structural problems associated with soil movement***
* ***Failure to identify possible problems with suitability for building/improvements***

**How does the *Buyer Advisory* aid in investigating soil issues?**

The *Buyer Advisory* contains links to sites detailing where soil conditions may be an issue, as well as a link to a list of certified engineers who can perform any needed inspections.

**Previous Fire/Flood**

**What risks are associated with failing to investigate previous fires/floods?**

* ***Failure to identify possible future problems or needed repairs***
* ***Disputes regarding existing damage and/or mold problems***
* ***Adequacy of repair/remediation***
* ***Deficiencies on permits/inspections after repairs***

**Pests**

**What risks are associated with failing to complete a pest inspection?**

* ***Failure to identify pest infestation which may be material to the buyer***

The *Buyer Advisory* contains links to information on scorpions, roof rats, termites and bark beetles.

**Endangered and Threatened Species**

**What risks are related to investigating issues related to endangered and threatened species?**

* ***Failure to understand impact on land uses and/or suitability***

The *Buyer Advisory* contains a link to the U.S. Fish and Wildlife website to provide information for buyers if this is a concern.

**Deaths and Felonies on the Property**

Because sellers and listing brokers are not liable for failing to disclose this type of information, it is up to the buyer (if it is material to them) to investigate by contacting the local law enforcement agency.

**Indoor Environmental Concerns:**

**What risks are related to failing to investigate the possible presence of mold?**

* ***Failure to understand health hazards***
* ***Failure to recognize signs indicating the presence of mold***

The *Buyer Advisory* contains several links where buyers can find information and resources related to the presence of mold.

**Radon Gas and Carbon Monoxide**

The presence of radon gas and/or carbon monoxide should be investigated by a home inspector. This can usually be done for an additional fee. A link to information on state radon levels can be found in the *Buyer Advisory*.

**Clandestine Drug Labs**

Residual contamination arising from the illicit manufacture of methamphetamine and other drugs carried out in clandestine drug laboratories presents a serious risk of harm to human and environmental health.

**Property Boundaries**

**What risks are associated with failing to verify property boundaries?**

* ***Disputes regarding encroachments and/or use of property by others***

The *Buyer Advisory* contains a link to a list of surveyors.

**Flood Plain Status**

**What risks are associated with failing to investigate whether the property is located in a flood plain?**

* ***Increased insurance premiums***
* ***Failure to comply with lender requirements to obtain flood hazard insurance***
* ***Failure to understand the effect on future improvements/encumbrances***

The *Buyer Advisory* contains links to county and state websites where buyers can access information and location of flood plains.

**Insurance (Claims History)**

**What risks are associated with failing to investigate issues related to the insurability of a property?**

* ***Inability to secure homeowner’s insurance***
* ***Inability to secure financing***
* ***Failure to understand the effect of past insurance claims***
* ***Insurance cancellation***

The *Buyer Advisory* contains links to resources where buyers can obtain information on homeowner’s insurance and order a claims history, as well as information on filing a complaint against an insurance company.

**Other Property Conditions**

What risks are associated with failing to investigate the functionality of plumbing, cooling/heating systems and electrical systems?

* ***Possible presence of polybutylene pipes***
* ***Failure to identify needed repairs***

# Unit 2, Segment 4: Surrounding Area Conditions

***Timing: 20 minutes for this segment***

**Learning objective of this segment:**

* To identify risks associated with sellers failing to complete the appropriate investigations of conditions affecting the surrounding area

**Environmental Concerns**

**What risks are associated with failing to investigate environmental concerns?**

* ***Failure to consider the proximity of landfills or environmental hazards***

The *Buyer Advisory* contains links to resources where buyers can obtain information regarding the location of landfills, wildfire information, air and water quality and more.

**Electromagnetic Fields**

The *Buyer Advisory* contains links to information on electromagnetic fields and potential associated health risks.

**Superfund Sites**

**What risks are associated with failing to investigate superfund sites?**

* ***Failure to identify a property as being in an area designated by the ADEQ as requiring cleanup***

The *Buyer Advisory* contains links to the ADEQ and EPA websites where buyers can view maps and obtain further information.

**Freeway Construction and Traffic Conditions**

**What risks are associated with failing to investigate the proximity of existing and planned freeways?**

* ***Failure to consider undesirable noise***
* ***Failure to discover planned roadway construction affecting the property***
* ***Failure to account for traffic conditions***

The *Buyer Advisory* contains a link to the Arizona Department of Transportation where buyers can access information on roadway construction and planning, as well as a link to investigate traffic conditions in the surrounding area.

**Crime Statistics**

Many buyers consider crime statistics in the surrounding area material to their decision to purchase property. The Buyer Advisory provides links to city crime statistics as well as contact information for local law enforcement agencies.

**Sex Offenders**

Sellers are not required to disclose the presence of sex offenders in the surrounding area. Buyers, especially those with children, may wish to access the state sex offender registry to investigate the possible presence of sex offenders in the vicinity. A link to the registry is contained in the *Buyer Advisory*.

**Military and Public Airports**

**What risks are associated with failing to investigate the proximity to military and/or public airports?**

* ***Failure to consider air traffic noise and disturbances***
* ***Failure to build on***

The *Buyer Advisory* contains links where buyers can access maps of military and public airports to determine proximity.

**ZOOM POLL QUESTION: ???**

**Forested Areas**

Buyers purchasing property in a forested area may wish to obtain information on wildfires. The *Buyer Advisory* contains links to resources where buyers can obtain information on protecting their property.

**Zoning/Planning/Neighborhood Services**

**What risks are associated with failing to investigate zoning and planning issues?**

* ***Inability to subdivide or split property***
* ***Suitability for intended use***
* ***Suitability for septic or on-site wastewater treatment facility***

The *Buyer Advisory* contains links to various city and town planning departments.

**Schools**

**What risks are associated with failing to investigate area schools?**

* ***Failure to consider enrollment caps, school ratings and state standards***

For buyers with school-aged children, the condition and availability of area schools may be a significant consideration. Links are available in the *Buyer Advisory* to investigate area schools. Buyers are also recommended to make an on-site visit to the school.

**City Profile Report**

Obtaining a city profile report may be important to buyers, especially those relocating from another area. These reports contain information such as demographics and finances from a number of sources. The *Buyer Advisory* contains a link where buyers can access city profiles.

**Due Diligence Conclusion**

***Timing: 10 minutes***

The *Buyer Advisory* was created to allow buyers to take a more active role in completing desired inspections and investigations on a property. The *Buyer Advisory* also encourages buyers to familiarize themselves with a property by talking to neighbors and driving around the neighborhood. Additional links are provided to assist buyers in obtaining further information on government agencies and fair housing issues.

**Instructor: How do you explain the buyer advisory to your buyer to get the buyer to do their due diligence**

**How can you use the *Buyer Advisory* to assist buyers in completing due diligence inspections and investigations?**

* ***Identify important issues***
* ***Explain why certain issues may be important***
* ***Direct them to sources of additional information***

NOTE: What is the due diligence of the agent (keep buyers on task)