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Responsibility for Undisclosed Defects in Pre-Owned Real Property

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Case Commented On: *Smiley v Salat*, 2018 ABPC 178 (CanLII)

The freely available "virtual library of Canadian legal information" that is CanLII does not allow Google or other internet search engines to index its text or case names and display them in search results (except for Supreme Court of Canada decisions). As a result, CanLII's million-plus Canadian court decisions and other documents usually do not turn up on a web search, which provides individuals with some privacy, as explained in the CanLII Privacy Policy. However, when a third party links to a CanLII decision, as I have done in this post, the text can be indexed by search engines. Some decisions should be widely available through a Google or similar search. I think this decision by Provincial Court Judge Don Higa is a good example of a decision that should be easily accessible to both lawyers and non-lawyers. It is a good summary of the law that determines when a seller is liable for defects in a just-purchased home and other properties, when those defects were not disclosed by the seller or were not noticed during an inspection. Accessible, understandable law is important to purchasers, especially first-time home owners, faced with unexpected problems and their potential financial and emotional consequences. It is also important to sellers who need to know whether or not settling is their best option.

Judge Higa conveniently divided the issue in this case of who was liable for the 2016 repairs to the sewer line into six questions. It is these six questions – adapted below to be more generic – that sellers or buyers experiencing a dispute about a defect need to consider. The facts of this particular case – the fairly common problem of a sewer backing-up due to intrusive tree roots – illustrate the type of evidence required in order to answer the six questions.

1. Are there defects affecting the property?

The law relating to defects is well settled in Alberta. In *Gibb v Sprague*, 2008 ABQB 298 at paragraph 16, Justice Manderscheid confirmed that the general legal principle applicable to the purchase and sale of real property is *caveat emptor* – "let the buyer beware." Normally, defects are the responsibility of the buyer once the sale has closed.

However, there are limited exceptions to that general principle. As noted in *Gibb v Sprague* (at para 17, quoting *Temple v Thomas*, 2007 ABQB 316 at para 39), those exceptions are: (1) fraud, (2) a mutual mistake resulting in a total failure of consideration or a deficiency in the land conveyed amounting to error in *substantialibus*, (3) a contractual condition, or (4) a warranty collateral to the contract which survives the closing. In *Smiley v Salat*, the buyers relied on the fraud exception, alleging that the sellers failed to alert them to latent defects and, as a result, were guilty of a fraudulent misrepresentation.

Because the sellers in this case argued that the tree root problem was a maintenance matter and not a defect, Judge Higa explored the nature of a "defect" and how to distinguish one from a maintenance issue (at paras 38-47). A defect is an imperfection or shortcoming, "a fault in a component of the improvements to the property" (at para 39, quoting *McKenzie v Smith*, 2016 ABQB 114). Judge Higa noted that maintenance issues can usually be identified by visual observation and inspection. However, underground sewer lines are not as easily inspected as are problems with eavestroughs or chimneys or furnaces, and potential tree root intrusions are not easily identifiable. Therefore, he found the tree root issues to be defects and not maintenance matters.

2. If defects exist, are they patent or latent defects?

The distinction between a patent and a latent defect is crucial to determining the extent of the seller's obligation to disclose. Judge Higa relied upon the law as summarized in *Gibb v Sprague.* Justice Manderscheid first described patent defects in the following terms:

> Patent defects are those that can be discovered by conducting a reasonable inspection of the property and making reasonable inquiries into its qualities. The vendor is not obliged to call patent defects to the purchaser's attention. In the case of patent defects, the purchaser must rely upon their own personal inspection. Accordingly, absent concealment of such defects by the vendor, the purchaser cannot complain of such defects and *caveat emptor* will apply (*Gibbs v Sprague,* at para 19).

Justice Manderscheid next described latent defects:

> On the other hand, a latent defect is one that could not have been identified by a purchaser upon a reasonable inspection of the property. For that reason, a latent defect known to a vendor must be disclosed to the purchaser. Should a vendor fail to disclose to a purchaser a known latent defect, caveat emptor will not bar the purchaser's claim for damages resulting from such failure to disclose (*Gibbs v Sprague,* at para 19)

The parties' purchase and sale agreement usually deals with latent defects. In this case, Judge Higa noted the sellers specifically represented:

> 6.1(h) Except as otherwise disclosed, the seller is not aware of any defects that are not visible and that may render the Property dangerous or potentially dangerous to occupants or unfit for habitation (at paras 7 and 52).

Because sewer lines are underground and root intrusions cannot be observed through unaided visual inspection, Judge Hagar found the defect in this case to be a latent one (at para 56).

3. If defects exist and they are latent defects, did the sellers have knowledge of those defects and fail to disclose their existence, or were the sellers reckless as to the existence of the defects?

Evidence is required in order to prove the sellers' awareness of the defects. In this case, after the buyers bought the property, they discovered a document entitled "House Service Video Inspection" – a form used by the City of Calgary's Water Services. It indicated that services were provided at the property in August 2015. That form motivated the buyers to contact the City and they subsequently received their home's service history, listing each time the seller's called the City about the home's sewer lines following a sewer back-up in 2001/2002, and when City crews worked on the sewer lines. Evidence of the seller's knowledge, and their failure to advise the buyers, was therefore clear in this case.

4. If latent defects exist, did they render the property dangerous or potentially dangerous, or unfit for habitation?

The wording in clause 6.1(h) is common and many cases have interpreted the meaning of "… that may render the Property dangerous or potentially dangerous to occupants or unfit for habitation." The leading authority is *Swayze v Robertson* (2002), 39 RPR (3d) 114 (Ont Sup Ct Justice), which Judge Higa quoted as follows:

> [T]he correct approach must be to consider it in the context of whether the latent defect has caused any loss of use, occupation and enjoyment of any meaningful or material portion of the premises or residence that results in the loss of enjoyment of the premises or residence as a whole… (at para 60).

It is not difficult for a sewer back-up to meet this test. In this case, 4 inches of water covered the laundry room and there was raw sewage and toilet paper in the water. Judge Higa held that sewage water and its solids were "serious and dangerous matters, rendering areas unfit for human habitation" (at paras 62).

5. Does any clause in the agreement of purchase and sale affect the buyer's claim?

Most purchase and sale agreements include a clause that states that, except as otherwise described in the agreement, "there are no other warranties, representations or collateral agreements … including any warranty, representation or collateral agreement relating to … the existence or nonexistence of any environmental condition or problem" (at para 64). The agreement in this case included an example of this type of provision in clause 6.4.

The question was whether the root intrusion into the sewer lines was "an environmental condition or problem." Judge Higa held it was not because the defect was in the sewer line, not in the tree roots. The sewer line was a man-made object added to the property as an essential component. Clause 6.4 therefore did not apply.

6. If the sellers are liable, what are the damages suffered by the buyers?

Having resolved the first five issues, Judge Higa determined that the sellers breached clause 6.1(h) and were liable to the buyers for damages. The last question was: how much?

The buyers had sued for $32,000, made up of $27,000 for analysis and repair of the sewer line, and $5,000 for loss of use and enjoyment of their home. The $5,000 claim was denied because no evidence or argument was presented to support it (at para 69).

As for analysis and repair of the lines, the only evidence of the buyers' out-of-pocket expenses was three bills, one for just over $6,000, a second for just under $1,000, and a third, for an estimate, for around $150. The $6,000 bill was for replacing the sewer line, rather than simply patching it. No evidence was presented as to why replacing the entire line was necessary. Another company had provided an estimate of just over $4,000 to patch the sewer line. Judge Higa set damages for repairing the line at $4,000 (at para 72). The $1,000 bill was for landscaping, backfill and cleanup, which Judge Higa accepted as necessary (at para 73). The cost of the estimate for remedial work was also allowed.

Lastly, although the buyers spoke of the time and effort expended by them to clear the area, including removal of the deck, there was no evidence of the actual time spent or monetary value for the work and no evidence of the necessity for the work. Judge Vega therefore did not make a monetary award for this claim (at para 76).

Judge Higa's findings on the amount of damages indicated the need for more evidence, such as oral testimony from those who did the repair work and from those who provided estimates for the necessity of repairs. Many claims for damages falter for lack of evidence; often the evidence simply does not exist or the people whose testimony is needed are unable or unwilling to attend court.

Costs

In the end, the buyers recovered just over $5,000, plus interest from the May 2016 date of the sewer back-up, and their $200 small claims court filing fee. They won, but their damages were considerably less than the $32,000 they claimed – only about 15 percent. As a result, Judge Higa ordered each party to bear their own costs (at para 79).

This aspect of the case is a common cautionary tale: do not claim more than you can prove with relevant and admissible evidence. That, of course, is easier to say than do because the available evidence is not always known when the claim is issued.

Each party was represented by a lawyer at trial, and legal fees would be the primary costs each part would bear as a result of this part of Judge Higa's order. In addition, in May 2017 the buyers had made an application for summary judgment in this case, claiming that the sellers had no defence to their claim. The result of that application was a written judgment by Judge Laura Burt: *Smiley v Salat*, 2017 ABPC 140. Summary judgment – judgment without a trial – is only granted when there is no genuine issue requiring a trial. Here the problem once again was the evidence; crucial portions of it were hearsay evidence in the buyer's affidavits. Judge Burt therefore denied summary judgment and reserved costs to the trial judge. Judge Higa's order that each party bear their own costs would therefore include the costs of the summary judgment application.

Conclusion

It is likely that both the sellers and the buyers were out-of-pocket as a result of this small claims action, and that only the lawyers involved came out ahead – another common cautionary tale.

The greatest value of Judge Higa's decision is likely its usefulness as a precedent and guide to future buyers and sellers faced with the question of whether the sellers are liable for undisclosed defects. This decision is a good illustration of one reason (and not the only or even the most important reason) why taxpayers pay for judges and courthouses. Courts do not merely resolve the disputes that come before them. They also set precedents that help us predict the likely outcome of similar disputes, and thus play a significant role in access to justice. Precedents need to be easily available to play that role and CanLII, funded by Canadian law societies, has achieved its goal of making Canadian law accessible on the internet. However, people do have to know that the CanLII database must be searched separately, and that does limit it accessibility, especially as a tool for pointing people in the right direction initially.

> *This modest post was inspired by the daily conversations my son and I had in mid-March 2015 to discuss whether the water seeping into the basement of his just-purchased, first home was a latent or patent defect, whether he had or could get the evidence he needed to prove it was a latent defect, and whether it was worthwhile for him to sue.*

This post may be cited as: Jonnette Watson Hamilton, "Responsibility for Undisclosed Defects in Pre-Owned Real Property" (October 2, 2018), online: ABlawg, http://ablawg.ca/wp-content/uploads/2018/10/Blog_JWH_Simley_v_Salat_Sept2018.pdf