

COMMERCIAL DUE DILIGENCE. OR NOT?



COUNSEL'S CORNER

Jane Tang and her company Virginia Oak Venture, LLC brought a lawsuit regarding the purchase of a McKinney Texas apartment community. Ms. Tang was of the view that the amount paid was far in excess of its value.

Tang alleged that the defendants (for my purposes, sellers, broker and agent) severely over-represented the cash flow expected to be derived, and misrepresented the extent of repairs. Tang also contends that she was defrauded by a real estate salesman, his broker, and the prior owners.

The Collin County trial court rendered partial summary judgments in favor of some of the defendants. A jury trial followed against the remaining defendants, all of which ultimately resulted in a loss to Tang.

So she appealed.

With specific reference to the salesperson O.D. Fought, Jr., Tang argued that Fought grossly misrepresented the occupancy levels of the property, its income and expenses, supplied false data to the appraiser and lender, hid from Tang the existence of accurate rent rolls, financial data and a previous purchase of the property for half the price some 10 months earlier, and more.

Tang argued that Fought represented both Seller and Tang, and as such, owed fiduciary duties to both. As evidence to support that conclusion, Tang alleged that Fought located an attorney to create Tang's LLC, agreed to be personally named as its registered agent, drove her to see 10 properties he was attempting to sell, directed her to a particular lender, and prepared all the documents involved in the deal.

Fought contended that he was merely working hard on the seller's behalf to sell the apartments, and that he was never acting as Tang's agent. Evidently the jury believed him.

The evidence furnished to the jury regarding rent rolls and income streams may have been accurate and largely correct as of the month of the sale, although it could also have been misleading. There was indeed evidence of high occupancy levels, but that circumstance changed after the expiration of “signup specials.” There was also the possibility that some evicted residents were allowed to reoccupy apartments, and thus become tenants yet once again.

More confusion followed Fought’s possible misrepresentations about the condition of the property, but it is possible that the jury deemed none of such matters material and disregarded such possible misrepresentations.

Tang then alleged that Fought and his broker committed fraud, since it was alleged that Fought only partially disclosed accurate rent rolls, financial statements and the property’s condition.

The Appellate Court’s analysis of the fraud claim against the sales agent was short-lived, since “. . . Tang made no effort to make an independent investigation to determine the physical condition of the property, the value of the apartment complex, the circumstances of occupancy levels, or other pertinent factors she should have taken into account when making the decision to purchase.”

The Appellate Court found no reason to disagree with the jury’s decisions, so the Defendants prevailed again. See *Virginia Oak Venture, LLC and Jane Tang v. O.D. Fought, Jr., et al*; No. 06-13-00076-CV; Texas Court of Appeals, 6th District; February 7, 2015.

Lessons learned:

1. In the past, my stock suggestion to brokers and agents was to encourage the buyers and tenants to conduct as much due diligence as possible within the option period, by hiring independent professionals not suggested by the agents and brokers. In this situation the buyer evidently did none of that, but still the broker and agents were able to adequately defend a claim.
2. *However*, I would like to believe that if the buyer had undertaken the normal due diligence I suggest of all buyers and tenants, she would have discovered some or all of these issues and either would not have made the decision to purchase or would have seriously negotiated the purchase price. Southward.
3. Practice Point: Make clear to all parties who you represent. Do it at the inception – ‘first contact rule’ – but then there is nothing that precludes you from reminding the parties several more times before and at closing, in writing. Keep copies too.

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