DIVISION ONE
FILED: 02/25/2010
PHILIP G. URRY, CLERK
BY: GH

IN THE COURT OF APPEALS
STATE OF ARIZONA
DIVISION ONE

LORI DELUCA; JO-ELLEN DOORN; CHERYL KAMINSKI, Plaintiffs/Appellants, v. GREGORY MCMAHON and SUSAN MCMAHON, husband and wife, Defendants/Appellees.	1 CA-CV 09-0140 DEPARTMENT D **MEMORANDUM DECISION** (Not for Publication – Rule 28, Arizona Rules of Civil Appellate Procedure)

Appeal from the Superior Court in Yavapai County

Cause No. P-1300-CV-0020060152

The Honorable David L. Mackey, Judge

AFFIRMED IN PART; REVERSED IN PART; REMANDED

Eckley & Associates, PC — Phoenix
By J. Robert Eckley
Kevin B. Sweeney
Attorneys for Plaintiffs/Appellants

Shorall McGoldrick Brinkmann — Phoenix
By Thomas J. Shorall, Jr.
Asa W. Markel
Attorneys for Defendants/Appellees

J O H N S E N, Judge

¶1 Lori DeLuca, Jo-Ellen Doorn and Cheryl Kaminski ("Buyers") appeal from entry of summary judgment in favor of Gregory and Susan McMahon ("Sellers") on Buyers' complaint. We affirm in part, reverse in part and remand for further proceedings.

FACTUAL AND PROCEDURAL HISTORY

¶2 Sellers owned a duplex in Sedona but lived in Michigan and rented out the duplex. They engaged a property manager and visited approximately once per year. In March 2005, Sellers listed the property for sale. The following month, Buyers saw an advertisement for the duplex. They called the listing agent, Harry Christie, to make an appointment to see the duplex and spent approximately 20 minutes there. During their visit, Doorn, noticing a musty odor, asked Christie "if the house had ever taken on water." Christie replied that the property had not taken on water and that the odor was caused by the prior tenant, who was a smoker and had large dogs.

¶3 Later in the day, Buyers made an offer on the property. They also executed a document entitled "Consent to Limited Representation," by which they agreed that Christie would represent them as well as the Sellers. The parties executed a purchase contract a few days later. The contract included the following advisory: "Buyer is advised by Broker to

obtain inspections and investigations of the Premises." The contract also included the following warranties: "(a) Buyer warrants to Seller that Buyer has conducted all desired independent investigations and accepts the Premises and (b) Buyer acknowledges that there will be no Seller warranty of any kind, except as stated in Lines 280-286." Lines 280 to 286 stated in part: "Seller warrants that Seller has disclosed to Buyer and Broker(s) all material latent defects and any information concerning the Premises known to Seller, excluding opinions of value, which materially and adversely affect the consideration to be paid by Buyer."

¶4 Sellers completed a Seller's Property Disclosure Statement ("Disclosure"). In response to a question in the Disclosure about problems related to drainage, Sellers wrote, "Side yard to front drainage -- pipe installed." In the Disclosure Sellers denied knowledge of "any water damage or water leaks of any kind" or "any past or present mold growth." The Disclosure included a seller's certification that the information it contained was "true and complete to the best of Seller's knowledge." It further included the following acknowledgement:

> Buyer acknowledges that the information contained herein is based only on the Seller's actual knowledge and is not a warranty of any kind. Buyer acknowledges Buyer's obligation to investigate any

> material (important) facts in regard to the Property. Buyer is encouraged to obtain Property inspections by professional independent third parties and to consider obtaining a home warranty protection plan.

¶5 Buyers obtained an inspection of the property. With respect to grading, the inspection stated, "Drainage of site/slope of soil at foundation is proper based upon visual observation," "[s]ome visible signs of soil erosion were noted around the site," and "[s]igns of poor drainage/erosion." With respect to the roof, the report stated the roof appears "serviceable/within useful life" and appeared to be "typical for age of home," but showed "evidence of prior patching/repairs." The inspection report cautioned: "The inspection does not report on the possible presence of mold. If you have concerns for the presence of mold, we recommend hiring an independent [sic] specializing in mold testing and abatement." The parties closed escrow on the house on or about June 15, 2005. In September 2005, Buyers received a report based on an investigation conducted in August that "water intrusion has taken place in both the back wall cavities, resulting in microbial growth."

¶6 Buyers filed suit against Sellers and others, including Christie and his employer. The first amended complaint alleged Sellers breached a duty to disclose all known defects, including mold, waste and termite events. They

asserted the duplex suffered a long history of water, mold and pest damage, which Sellers failed to disclose, and that Buyers had incurred repair costs. Buyers alleged breach of contract, negligent misrepresentation, mutual mistake and consumer fraud pursuant to Arizona Revised Statutes ("A.R.S.") sections 44-1521 *et seq.* (2003 & Supp. 2009).

¶7 After the close of discovery, Sellers moved for summary judgment. Over Buyers' objection, the court granted Sellers' motion, reasoning that Christie's knowledge of issues with the duplex was imputed to Buyers as well as to Sellers. It concluded:

> Pursuant to Arizona law, "[t]he knowledge of a dual agent is normally imputed to both principals." *Manley v. Ticor Title Insurance Company of California,* 168 Ariz. 568, 573, 816 P.2d 225, 230 (1991) citing *Arizona Title Ins. & Trust Co. v. Smith*, 21 Ariz. App 37[1], 376, 519 P.2d 860, 865 (1974).
>
> There is no material factual dispute that [Sellers] had no knowledge of the problems complained of by [Buyers]. . . . [Sellers] can only be imputed with the knowledge of their agent Harry Christie. Since [Buyers] may be imputed with the same knowledge, they have no cause of action against [Sellers] for breach of contract, negligent misrepresentation or consumer fraud.
>
> The Court also has considered [Buyers'] claim against [Sellers] for rescission based upon mutual mistake. The Court finds that the theory of "conscious ignorance" discussed in *Nelson v. Rice*, 198 Ariz. 563,

> 566, 12 P.3d 238, 241 (App. 2000) precludes [Buyers'] claim of rescission based upon mutual mistake. The facts are undisputed that [Buyers] were put on notice that they should investigate the condition of the property as it related to water intrusion, drainage and mold; however, they chose to proceed with the sale even in the face of their limited knowledge. The Court finds as a matter of law, [Buyers] are not entitled to rescission based upon mutual mistake under the facts of this case.

¶8 Buyers moved for reconsideration. They argued that, under Arizona law, Christie's knowledge could not be imputed to them. The court denied the motion for reconsideration, concluding:

> Even if the Court were to accept the arguments of [Buyers], the Court's Ruling granting summary judgment for [Sellers] would still stand. In addition to the Court's Ruling regarding dual agency and imputed knowledge questioned by the [Buyers], the Court ruled that the theory of "conscious ignorance" precludes [Buyers'] claim of rescission. A review of the file reflects that [Buyers] have elected to pursue rescission and not damages. Therefore, the Court's Ruling, even if modified pursuant to [Buyers'] arguments, still disposes of [Buyers'] claims against [Sellers].

¶9 The court entered judgment in favor of Sellers, awarding them attorney's fees of $40,000 and costs. Buyers filed a timely notice of appeal. We have jurisdiction pursuant to A.R.S. § 12-2101(B) (2003).

DISCUSSION

A. Standard of Review.

¶10 Summary judgment may be granted when "there is no genuine issue as to any material fact and . . . the moving party is entitled to judgment as a matter of law." Ariz. R. Civ. P. 56(c). Summary judgment should be granted "if the facts produced in support of the claim or defense have so little probative value, given the quantum of evidence required, that reasonable people could not agree with the conclusion advanced by the proponent of the claim or defense." *Orme School v. Reeves*, 166 Ariz. 301, 309, 802 P.2d 1000, 1008 (1990). In reviewing a motion for summary judgment, we determine *de novo* whether any genuine issues of material fact exist and whether the superior court properly applied the law. *Eller Media Co. v. City of Tucson*, 198 Ariz. 127, 130, ¶ 4, 7 P.3d 136, 139 (App. 2000). We view the facts and the inferences to be drawn from those facts in the light most favorable to the party against whom judgment was entered. *Prince v. City of Apache Junction*, 185 Ariz. 43, 45, 912 P.2d 47, 49 (App. 1996).

B. Mutual Mistake.

¶11 A party may be entitled to rescission based on mutual mistake concerning a "basic assumption" of the parties to the contract. *Renner v. Kehl*, 150 Ariz. 94, 97, 722 P.2d 262, 265 (1986) (quoting Restatement (Second) of Contracts

("Restatement") § 152 cmt. b (1981)). The mistake, however, may not be one on which the party seeking rescission bore the risk. *Nelson v. Rice*, 198 Ariz. 563, 566, ¶ 7, 12 P.3d 238, 241 (App. 2000).

¶12 The superior court concluded Buyers' claim for mutual mistake was barred by their "conscious ignorance" of the facts about which Buyers asserted the parties were mutually mistaken. Under the Restatement, "A party bears the risk of mistake when . . . he is aware, at the time the contract is made, that he has only limited knowledge with respect to the facts to which the mistake relates but treats his limited knowledge as sufficient." Restatement § 154(b). A comment to the Restatement further explains:

> *c. Conscious ignorance*. Even though the mistaken party did not agree to bear the risk, he may have been aware when he made the contract that his knowledge with respect to the facts to which the mistake relates was limited. If he was not only so aware that his knowledge was limited but undertook to perform in the face of that awareness, he bears the risk of the mistake. It is sometimes said in such a situation that, in a sense, there was not mistake but "conscious ignorance."

Restatement § 154 cmt. c.

¶13 Viewing the facts in the light most favorable to Buyers, we accept that Christie told them that the house had not "taken on water" and that Sellers did not disclose problems with

drainage or roof leaks. Buyers acknowledged at the time of purchase their obligation to investigate the property, however, and the inspector they hired reported water and drainage issues. The inspection report disclosed evidence that the roof had been patched and that there were signs of poor drainage and erosion. The inspector also warned Buyers that the inspection did not address the possible presence of mold and recommended an independent inspection if mold was a concern. Doorn testified Buyers were provided a list of inspectors that included roofers and mold inspectors, and that despite knowing that they could have a mold inspection, they chose to purchase the property without one.

¶14 Buyers argue the principle of "conscious ignorance" does not apply because Sellers were obligated to disclose defects in the property, including drainage issues and roof leaks. But in their claim for rescission based on mutual mistake, Buyers assert that they and the Sellers were mutually mistaken about "substantial adverse conditions" of the property. That allegation is inconsistent as a matter of law with Buyers' argument that Sellers knew of the adverse conditions and should have disclosed them. On this record, we find no error in the superior court's conclusion that Buyers' conscious ignorance of the adverse conditions precluded their claim for rescission based on mutual mistake.

C. Other Claims for Relief.

1. The effect of "conscious ignorance" on the other claims.

¶15 Rescission is a remedy, not a cause of action, and may be sought based on various theories, including fraud and breach of contract. *See Jennings v. Lee*, 105 Ariz. 167, 461 P.2d 161 (1969) (action for rescission based on fraud); *Earven v. Smith*, 127 Ariz. 354, 621 P.2d 41 (App. 1980) (breach of contract). As the superior court noted, Buyers elected to seek rescission on each of their claims. Sellers argue the court correctly dismissed each of Buyers' claims because Buyers' conscious ignorance precludes rescission on any theory of relief. Sellers contend that by attributing "conscious ignorance" to the Buyers, the court effectively found Buyers had unclean hands, which would bar their entitlement to rescission under any of their claims for relief.

¶16 The court, however, made no finding that Buyers were guilty of unclean hands, and Sellers offer no authority for the proposition that by itself, "conscious ignorance" constitutes a defense to rescission based on breach of contract, negligent misrepresentation or consumer fraud. Accordingly, we conclude the finding of conscious ignorance does not preclude Buyers' claim for rescission based on theories other than mutual mistake.

2. Imputation of Christie's knowledge.

¶17 The superior court also held Buyers could not prevail on their claims for breach of contract, negligent misrepresentation and consumer fraud because as a matter of law, Christie's knowledge was imputed to them.

¶18 As a general matter, the knowledge of an agent is imputed to the principal, and when an agent serves two principals, the agent's knowledge may be imputed to both. *Manley v. Ticor Title Ins. Co.*, 168 Ariz. 568, 572-73, 816 P.2d 225, 229-30 (1991). An exception to this general rule applies, however, in the case of misrepresentations by an agent who represents both the buyer and seller in a real estate transaction. *See Miller v. Boeger*, 1 Ariz. App. 554, 558-59, 405 P.2d 573, 577-78 (1965) (fact that agent was acting for both parties "is no defense" to action by one of them to hold the other liable for agent's misrepresentations) (quotation omitted). In *Jennings v. Lee*, one party sought to rescind a real estate transaction after discovering that the agent who had represented both parties provided her with false financial information about the property. 105 Ariz. at 168-70, 461 P.2d at 162-64. The other party argued the agent was acting as the plaintiff's agent when he gave her the false information. Adopting the principle applied in *Boeger*, the *Jennings* court concluded that the dual agency did not preclude rescission of

the contract. *Id*. at 171, 461 P.2d at 165. *See also Miller v. Wood*, 188 Cal. App. 2d 711, 714 (1961) ("Where an agent common to two parties betrays one in favor of the other the second . . . cannot charge the first with the agent's knowledge.") (quotation and citation omitted).

¶19 In this case, Sellers and Buyers both engaged Christie, who Buyers assert misrepresented the condition of the property to the benefit of Sellers and the detriment of Buyers. Sellers contend Christie's knowledge is chargeable to Buyers so as to preclude their rescission claim. Under *Boeger, Jennings* and *Wood*, however, Sellers may not rely on the dual agency to defeat Buyers' claims.

¶20 Sellers argue *Jennings* and *Wood* do not apply because in those cases the agent was guilty of actual fraud. The cases, however, do not make the distinction Sellers urge. The rule the cases articulate applies broadly to misrepresentations by agents who represent both sides to a real estate transaction; the decisions do not purport to limit the rule to occasions in which the agent acts with some greater degree of culpability.

¶21 Sellers also argue that *Jennings* is undermined by *Manley*, which was decided 22 years after *Jennings* and applied the general rule that knowledge of a dual agent is imputed to both principals without recognizing the exception stated in *Jennings*. The facts in *Manley*, however, are unlike those in

Boeger, Jennings and *Wood*. *Manley* involved a seller's claim against an escrow company. An employee of the escrow company observed circumstances suggesting fraud in a real estate transaction. 168 Ariz. at 570, 816 P.2d at 227. The employee informed the sellers' real estate agent but did not inform the sellers directly. *Id*. The court noted the general rule that knowledge acquired by an agent is imputed to the principal unless the agent is acting adverse to the principal. *Id*. at 572, 816 P.2d at 229. The sellers argued the knowledge of their agent should not be imputed to them because the agent also was the buyers' agent, but the court found that fact alone did not establish that the agent was acting adversely to the sellers. *Id*. at 572-73, 816 P.2d at 229-230. The court ultimately concluded that a question of fact remained as to whether the escrow company employee knew the agent had interests adverse to the sellers such that the agent was unlikely to convey the information to the sellers. *Id*. at 573, 816 P.2d at 230.

¶22 We do not understand *Manley* to alter the conclusion reached in *Boeger*, *Jennings* and *Wood* that the knowledge of a dual agent in a real estate transaction does not necessarily bar claims by one party to the transaction against the other. Accordingly, based on *Boeger*, *Jennings* and *Wood*, we hold that Buyers' rescission claims based on breach of contract, negligent

misrepresentation and consumer fraud are not barred as a matter of law by Christie's knowledge.

D. Motion to Quash.

¶23 Buyers also argue the superior court abused its discretion in denying their motion to quash a subpoena for the deposition of one of their experts, whom they had withdrawn, and in allowing Sellers to use the expert. We decline to address this contention because the subpoena was issued at the request of the Christie Defendants, who are not parties to this appeal. In addition, the ruling on the motion to quash is not encompassed by the judgment from which the Buyers appeal. *See* A.R.S. § 12-2102(A) (2003).

E. Attorney's Fees.

¶24 Buyers and Sellers both seek their attorney's fees on appeal. Because neither side has yet prevailed, we deny both requests, but the superior court may grant attorney's fees incurred in this appeal in its determination of fees at the conclusion of the litigation.

CONCLUSION

¶25 We affirm the superior court's ruling that Buyers' conscious ignorance precludes their claim for rescission based on mutual mistake. We reverse its decision, however, that conscious ignorance of the Buyers also precludes their right to seek rescission on their other claims for relief. We further

hold that Christie's dual agency does not as a matter of law preclude Buyers' claims for breach of contract, negligent misrepresentation and consumer fraud. Accordingly, we vacate the judgment, including the award of attorney's fees and costs, and remand to the superior court for further proceedings consistent with this decision. Buyers are awarded their costs of appeal, contingent on their compliance with ARCAP 21.

/s/_____
DIANE M. JOHNSEN, Judge

CONCURRING:

/s/_____
PATRICIA A. OROZCO, Presiding Judge

/s/_____
JON W. THOMPSON, Judge