

Calif. Ruling Shows Disfavor For Real Estate Fiduciary Fraud

By **Jon Weininger** (May 12, 2020)

In a real estate fraud case against a realtor, the California Court of Appeal's First Appellate District recently upheld a jury verdict awarding the aggrieved buyer both out-of-pocket and benefit-of-the-bargain damages. This case solidifies the majority position in California that aggrieved buyers who have been misled by faithless fiduciaries can recover expansive remedies to compensate for their loss.



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In *Moore v. Teed*, the First District weighed in on whether benefit-of-the-bargain damages may be recovered in fraud cases involving real estate transactions. California courts of appeal are split, with several allowing such a recovery while others do not.

Moore is the latest decision out of the First District, which along with the Second District have allowed plaintiffs to recover all damages to fully compensate them for the detriment caused by a faithless fiduciary's fraud, including benefit-of-the-bargain damages under California Civil Code Sections 1709 and 3333.

The facts in *Moore* were straightforward. The plaintiff alleged he was fraudulently induced by his realtor to purchase and renovate a residence, based on the defendant-realtor's representations that he and his construction team could complete the renovations for \$900,000. As it turned out, the defendant was not a licensed contractor, and the foundation that his team constructed was defective and had to be replaced. Further, the true cost of the promised renovations far exceeded what the defendant had represented to the plaintiff.

After a jury trial, the plaintiff prevailed on a fraud claim and was awarded both the out-of-pocket expenses he incurred to replace the defective foundation plus benefit-of-the-bargain damages, reflecting the difference between the renovation's promised costs and the actual costs to do the same work.

The defendant's appeal raised the question of whether benefit-of-the-bargain damages is a proper measure of damages in fraud actions involving real estate transactions. *Moore* holds that in cases involving fraud claims against fiduciaries, the answer across much of California is yes.

Under California law, there are two measures of damages for fraud: out-of-pocket and benefit-of-the-bargain. The out-of-pocket measure restores the plaintiff to the "financial position enjoyed by him prior to the fraudulent transaction, and thus awards the difference in actual value at the time of the transaction between what the plaintiff gave and what he received."^[1]

The benefit-of-the-bargain measure satisfies "the expectancy interest of the defrauded plaintiff by putting him in the position he would have enjoyed if the false representation relied upon had been true; it awards the difference in value between what the plaintiff actually received and what he was fraudulently led to believe he would receive."

Ordinarily,^[2] defrauded parties are limited to recovering their out-of-pocket losses. By statute, this rule applies to transactions involving the "purchase, sale or exchange of property." Civil Code Section 3343(a) states:

One defrauded in the purchase, sale or exchange of property is entitled to recover the difference between the actual value of that with which the defrauded person parted and the actual value of that which he received, together with any additional damage arising from the particular transaction.

In support of his appeal, the defendant relied on Civil Code Section 3343(a) and holdings out of the Fifth District Court of Appeal, which have limited damages for fraud claims against fiduciaries in real estate transactions to out-of-pocket damages.[3]

Moore rejected the defendant's argument and sided with prior decisions of the First District and a Second District Court of Appeal case, *Fragale v. Faulkner*, in concluding that "benefit-of-the-bargain damages are recoverable in fraud actions where a fiduciary induces an individual to purchase, sell, or exchange real property to their detriment."

Although recognizing the limitation in Civil Code Section 3343(a), Moore noted that the California Supreme Court's decision in *Alliance Mortgage* had clarified that this section "does not apply ... when the victim is defrauded by its fiduciaries." Instead, in fiduciary cases, the broader measure of tort damages under Civil Code Sections 1709 and 3333 are available.

Civil Code Section 1709 provides that:

One who willfully deceives another with intent to induce him to alter his position to his injury or risk, is liable for any damage which he thereby suffers." And Civil Code §3333 provides the general tort measure of damages by permitting recovery of "the amount which will compensate for all the detriment proximately caused thereby, whether it could have been anticipated or not.

What emerges from Moore is a growing majority trend in California that will hold faithless fiduciaries fully accountable to their principals for all damages caused by their duplicity.[4]

What Real Estate Lawyers Should Take Away From Moore

Real estate practitioners should take at least three things away from Moore.

First, its holding should apply to both commercial and residential real estate transactions.

Second, the expansive damages applicable to fraudulent fiduciary real estate cases is not limited to just purchase and sale transactions, or only to realtors, but includes exchange transactions and any fiduciaries who may be involved in them. This would appear to cover like-kind exchanges under Section 1031 of the Internal Revenue Code.

Third, Moore did not alter existing damages law that continues to govern claims for negligent misrepresentation by a fiduciary. In those cases, where intentional fiduciary fraud is not present or has not been proven, "plaintiff is only entitled to its actual or 'out-of-pocket losses suffered." [5]

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[1] Moore, quoting Alliance Mortgage Co. v. Rothwell.

[2] See Alliance Mortgage Co.

[3] See Hensley v. McSweeney and Overgaard v. Johnson.

[4] In addition to Moore, see Salahutdin v. Valley of California, Inc. (where benefit-of-the-bargain damages was the appropriate remedy under Civil Code sections 1709 and 333 based on "determination that the faithless fiduciary shall make good the full amount of the loss of which his breach of faith is a cause."); and Fragale v. Faulkner (where measure of damages for fiduciary's intentional misrepresentation is not confined to actual or out-of-pocket losses; affirming jury's award that effectively afforded a benefit-of-the-bargain recovery to plaintiffs).

[5] See Fragale.