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ALAN M. WEINBERGER*

The cruellest lies are often told in silence.[1]
—Robert Louis Stevenson

INTRODUCTION

Returning home from grocery shopping one evening last spring, a forty-two-year-old architect was killed in the presence of his wife and children on the street outside his St. Louis townhouse by a gunshot to the neck during an attempted carjacking.[2] By the next morning, police had arrested and obtained a confession from a recently released parolee wearing an electronic ankle bracelet.[3] Several homes in the neighborhood, previously considered to be generally free of serious crime, were listed for sale at the time of this incident. Human experience teaches that other homes are likely to be offered for sale in the aftermath of this incident. Private morality and conscience will inform each seller's decision whether to volunteer information about this notorious crime to potential purchasers from outside the community, or to respond expansively if asked about security. Some of these sellers may also seek the advice of counsel.

Advising real property vendors whether to disclose unfavorable information to potential purchasers was easy for our ancestors in the profession.[4] Under Anglo-Saxon common law imported into the United States, sellers of real property were indeed the chosen people.

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1. ROBERT L. STEVENSON, VIRGINIBUS PUERISQUE AND OTHER PAPERS 72 (New York, Charles Scribner & Sons 1907) (1881).

2. Michael D. Sorkin, *Horror Greets Family After Quiet Night Out*, ST. LOUIS POST-DISPATCH, Mar. 25, 1995, at 1.

3. *Id.*

4. *See, e.g.*, Carol M. Rose, *Crystals and Mud in Property Law*, 40 STAN. L. REV. 577, 577 (1988) ("Sell that house with the leak in the basement? Lucky you, you can unload the place without having to tell the buyer about such things at all."); Alan M. Weinberger, *Expanding the Fiduciary Relationship Bestiary: Does Concurrent Ownership Satisfy the Family Resemblance Test?*, 24 SETON HALL L. REV. 1767, 1793 (1994) ("Silence may not be golden, but at least it did not constitute actionable fraud.").

The doctrine of caveat emptor[5] effectively protected vendors against any continuing liability after closing. After delivering the deed of conveyance and relinquishing possession, sellers could sleep well at night, secure in the knowledge that they could not be exposed to legal liability, even by reason of express representations in the contract of sale.[6] Such was the state of real property law well into the 1960s.

Erosion of the doctrine of caveat emptor has changed everything. Not only has the legal table been turned on sellers of real property in recent years, even their own agents are now turning against them as judicial decisions within the past decade have imposed a duty on real estate agents to disclose information to purchasers.[7] Confronted with expanded exposure to legal liability, the real estate brokerage industry has opted for self-protection. Nationwide, brokers are sponsoring legislation to shift the burden of information disclosure to their principals,[8] and their lobbying efforts thus far have succeeded in enacting disclosure statutes in approximately half of the states.[9] As a result, what was once a routine legal matter has become a client-counseling minefield. While blanket disclosure of faults and defects may avoid subsequent litigation (including the possibility of punitive damages),[10] unnecessary disclosure of negative information may place the seller at a competitive disadvantage, perhaps to the point of jeopardizing the transaction.[11] Conscientious practitioners can provide no better test for what requires disclosure than the Golden Rule: Would the

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5. The Latin maxim provided in its entirety: "*Caveat emptor, qui ignorare non debuit quod jus alienum emit.*" ("Let a purchaser, who ought not be ignorant of the amount and nature of the interest which he is about to buy, exercise proper caution."). HERBERT BROOME, A SELECTION OF LEGAL MAXIMS 528 (10th ed. 1939), *cited in* Dawn K. McGee, Note, *Potential Liability for Misrepresentations in Residential Real Estate Transactions: Let the Broker Beware*, 16 FORDHAM URB. L.J. 127, 129 n.8 (1988).

6. Indeed, most sellers would not have considered legal representation necessary in residential transactions involving real estate brokers strictly bound by fiduciary duty to act in their best interest. Real property sellers had but one concern—collecting a check at closing for the difference between the contract price and the earnest money down payment delivered by purchaser at the time of contract formation.

7. *See infra* notes 211-214 and accompanying text.

8. *See infra* notes 187-220 and accompanying text.

9. *See infra* note 187. Additionally, even the federal government has found it necessary to regulate the field. Beginning October 28, 1995, no contract for the sale of a home built before 1978 is enforceable unless the seller provides purchaser a copy of a lead hazard information pamphlet prepared by the Environmental Protection Agency, and a form disclosing any known presence of lead-based paint. Residential Lead-Based Paint Hazard Reduction Act of 1992 §§ 1002–1061, 42 U.S.C. §§ 4851–4856 (1995).

10. *See generally* M. David LeBrun, Annotation, *Recovery of Punitive Damages in Action by Purchasers of Real Property Charging Fraud or Misrepresentation*, 19 A.L.R.4TH 801 (1983).

11. Steven W. Koslovsky, *To Disclose or Not to Disclose: An Overview of Fraudulent Nondisclosure*, 50 J. MO. B. 161, 161 (1994).

seller want the information if he were a potential purchaser of the property?[12] Unfortunately, the quality of the advice clients are likely to receive from an attorney will recall to mind the familiar (if not particularly instructive) childhood nursery rhyme:

> Engine, engine Number 9
> Going down Chicago line.
> If the train goes off the track,
> Will I get my money back?
> Yes . . . , no . . . , maybe so,
> All the way to Mexico.[13]

This Article explores one of the most extraordinary legal reforms of the past generation:[14] the nationwide erosion of the common-law doctrine of caveat emptor in transactions in real property.[15] Caveat emptor is a time-honored principle of both Anglo-Saxon and Roman legal traditions,[16] and is firmly entrenched in the common-law history of this country.[17] Its continued vitality is largely limited to commercial real estate transactions,[18] although deterioration has occurred in that field.[19] Part I of this Article explores the origins and causes of the decline of the doctrine of caveat emptor, and provides a brief comparative analysis of its status in other legal systems. Part II analyzes the contemporary common-law doctrine imposing a duty on vendors to

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12. Alan Silverstein, *Mandatory Seller Disclosure Finally Introduced to Ontario*, TORONTO STAR, Mar. 19, 1994, at F26.

13. The author is indebted to Professor Kent Syverud of the University of Michigan Law School for reciting this rhyme in another context during a presentation delivered at the annual meeting of the Association of American Law Schools in January 1995.

14. An influential commentator has identified the erosion of caveat emptor as illustrating a pattern of judicial substitution of fuzzy ambiguity for well-defined rules of decision to the point that litigants no longer have a clear sense of their legal rights and obligations. Rose, *supra* note 4, at 580-82.

15. With respect to transactions in personal property, the doctrine of caveat emptor began to unravel by the early part of this century. Today every state except Louisiana has replaced the doctrine of caveat emptor in personal property transactions with the Uniform Commercial Code's provisions covering implied warranty, good faith, and fair dealing. U.C.C. §§ 1-203, 2-314, 2-315 (1995).

16. *See infra* notes 29-30 and accompanying text.

17. "No principle of the common law has been better established, or more often affirmed, both in this country and in England, than . . . the maxim of caveat emptor . . . ." Barnard v. Kellogg, 77 U.S. (10 Wall.) 383, 388 (1870).

18. In addition to the application of the doctrine to commercial real estate sales, caveat emptor appears to survive in some residential transactions. *See, e.g.*, Bultemeier v. Ridgway, 834 S.W.2d 896, 897 (Mo. Ct. App. 1992) (holding that caveat emptor applied to sheriffs' execution sale). *But compare* Hill v. Thompson, 564 So. 2d 1, 11 (Miss. 1989) (holding that caveat emptor applied to foreclosure sale) *with* Gibb v. Citicorp Mortgage, Inc., 518 N.W.2d 910, 918 (Neb. 1994) (holding that "as is" clause in foreclosure sale is relevant but not controlling).

19. *See infra* note 181 and accompanying text.

disclose latent defects that adversely affect the value of real property offered for sale in the marketplace. Finally, in Part III, the Article considers the paradoxical impact of state mandatory disclosure statutes on the doctrine, arguing that their enactment has arrested the erosion process. As the unintended beneficiaries and economic inefficiencies of disclosure statutes become apparent, the flight from caveat emptor may be reversed.

I. ORIGINS OF CAVEAT EMPTOR AND CAUSES OF ITS DECLINE

"Caveat emptor" is shorthand for a rubric of affirmative legal defenses formerly available to sellers of real property to effectively thwart claims by disappointed purchasers. Among these defenses were the statute of frauds,[20] the parol evidence rule,[21] and the doctrine of merger by deed.[22] In its essence, the doctrine of caveat emptor provided that sellers of real property, dealing at arm's length with prospective purchasers, owed no duty to disclose unfavorable information about the property. Vendors, therefore, incurred no legal liability by withholding their knowledge of defective conditions.[23] The law required buyers to fend for themselves by exercising a healthy modicum of skepticism as to a property's value and quality.[24] In a very real sense, purchasers were expected to govern themselves by the philosophy that every acquisition of real property represented a gamble.[25]

Caveat emptor reflected two underlying assumptions. First, sellers and purchasers occupied equal bargaining positions and shared an equal opportunity to inspect the quality of property and discover defective conditions before the transfer of title.[26] Second, manufac-

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20. The statute of frauds requires that a contract for the sale of an interest in land be in writing. RESTATEMENT (SECOND) OF CONTRACTS § 110 (1981).

21. The parol evidence rule makes oral statements inadmissible to contradict the terms of a written contract. U.C.C. § 2-202 (1995).

22. The doctrine of merger by deed states that any assurances, representations, or warranties by a seller do not survive the contract phase unless specifically listed in the deed. ROGER A. CUNNINGHAM ET AL., THE LAW OF PROPERTY § 11.13, at 862 (2d ed. 1993).

23. *See, e.g.*, Peek v. Gurney, 6 L.R.-E. & I. App. 377, 403 (H.L. 1873) ("Mere nondisclosure of material facts, however morally censurable . . . would in my opinion form no ground for an action in the nature of an action for misrepresentation.").

24. As one commentator explained: "The purchaser was deemed perfectly capable of inspecting the property and deciding for himself whether he wanted it, and if anyone were foolish enough to buy a pig in a poke, he deserved what he got. Short of outright fraud that would mislead the buyer, the seller had no duties to disclose anything at all." Rose, *supra* note 4, at 580-81.

25. Walter H. Hamilton, *The Ancient Maxim Caveat Emptor*, 40 YALE L.J. 1133, 1187 (1931).

26. *See* WARREN G. MAGNUSON & JEAN CARPER, THE DARK SIDE OF THE MARKETPLACE at x (1968).

turers and sellers of tangible property were not in the business of supplying information, and any information furnished to purchasers was merely incidental to the actual product. The omission or falsity of this information, as the argument went, ought not form the basis for legal liability.[27] Although these assumptions may once have been quite realistic, each has now been rejected as inconsistent with modern notions of justice, fair dealing, and sound public policy.

A. Origins of the Doctrine of Caveat Emptor

Protection of purchasers against shoddy or defective goods was not part of the tradition of the legal systems that would later influence our own.[28] Although its source is often traced to sixteenth century English decisions involving the sale of chattels,[29] the doctrine of caveat emptor originated much earlier in primitive Roman law.[30]

As originally applied to the transfer of real property, the doctrine of caveat emptor evolved in agrarian societies where unimproved land

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27. *See supra* notes 4-6 and accompanying text.

28. The principle of caveat emptor in the sale of real property is also found in early Jewish law. Transactions in land were excluded from the legal prohibition against overreaching. MENACHEM ELON, THE PRINCIPLES OF JEWISH LAW 216 (1975) ("[T]he scholars called land something that is always worth the money paid for it."). Caveat emptor is not found in Islamic law. SUSAN E. RAYNER, THE THEORY OF CONTRACTS IN ISLAMIC LAW 144 (1994). Under that system, a buyer of land who discovers defects upon transfer of possession may choose to annul the contract. *Id.* at 327-29.

29. *See, e.g.*, Hamilton, *supra* note 25, at 1156-64. The phrase itself first appeared in a text containing advice on horse trading published in 1534. *Id.* at 1164; KEVIN M. TEEVEN, A HISTORY OF THE ANGLO-AMERICAN COMMON LAW OF CONTRACT 136 (1990) ("[I]f he be tame and have been rydden upon, then *caveat emptor*." (citation omitted)). Its earliest appearance in the common-law courts may have been in reaction to an upsurge in itinerant merchants. The doctrine alerted buyers of the likelihood that their sellers would not be available to respond to customer complaints.

30. A. Rogerson, *Implied Warranty Against Latent Defects in Roman and English Law, in* STUDIES IN THE ROMAN LAW OF SALE 112, 113 (David Daube ed., 1959); WILLIAM L. BURDICK, PRINCIPLES OF ROMAN LAW 445 (1938).

Under an exception to the Roman doctrine of caveat emptor introduced in the fourth century B.C., dealers were required to disclose faults and defects in slaves, as well as cattle, horses, and other drought animals offered for sale in the public marketplace unless the flaws were either so obvious that an ordinary buyer would notice them, or not sufficiently serious as to interfere with the working condition or general usefulness of the slave or animal. JAMES MACKINTOSH, THE ROMAN LAW OF SALE 278-79 (2d ed. 1907). This limited exception was justified by the general rascality of dealers in slaves and animals, who tended to be foreigners with a faculty for rapid disappearance. *Id.* at 279. By the time of Cicero, however, Roman civil law developed to the point where principles of good faith required sellers of land to disclose faults known to them. *Id.* at 279-80. Failure to disclose defective conditions was equated with affirmative misrepresentation. *Id. But see* Leon Rittenberg III, Comment, *Louisiana's Tenfold Approach to the Duty to Inform*, 66 TUL. L. REV. 151, 157 n.22 (1991) ("Scholars debate whether Cicero's view represented the Roman law of the time or, rather, Cicero's opinion of what it should have been.").

was the predominant subject matter of real property transactions.[31] Improvements, if any, were non-complex, and the nature of structural systems was readily apparent to a prospective purchaser.[32] Buyers were fully capable of competent independent investigation to satisfy themselves as to the quality of construction.[33] Therefore, there was no need to rely upon the transfer of information by sellers regarding defective conditions or other matters. In these societies, local marketplace trade "was an arm's length proposition with wits matched against skill."[34] Shoppers tended to carefully inspect the look and feel of commodities offered for sale on the open market, and buyers haggled vigorously with vendors over price.[35] In an economy based on face-to-face dealings, consumers were more likely to feel ashamed of being outsmarted than angry at having been cheated.[36] Real property was exchanged between neighbors in simple face-to-face transactions, and the parties were generally well-acquainted with one another and their respective reputations for veracity.[37] They also were generally familiar with the condition of property being exchanged, the competence of its builder, and the quality of its maintenance and renovation.[38]

Therefore, market prices came to be set in accordance with the principle of caveat emptor. Knowledgeable purchasers of property without benefit of enforceable warranties of quality made allowance for the risk that articles might not be sound by bidding prices down. With prices already discounted to reflect the level of risk being assumed by purchasers, a rule of law imposing liability for nondisclosure of defects would have given buyers a windfall.[39]

The celebrated case of *Chandelor v. Lopus*[40] is often regarded as the origin of the doctrine of caveat emptor under English common law.[41] In *Chandelor*, a London goldsmith sold a jewel to a foreign

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31. Wilhite v. Mays, 232 S.E.2d 141, 142-43 (Ga. Ct. App. 1976), *aff'd*, 235 S.E.2d 532 (Ga. 1977); Holcomb v. Zinke, 365 N.W.2d 507, 511 (N.D. 1985).

32. *See Wilhite*, 232 S.E.2d at 142-43.

33. *See id.*

34. Allison Dunham, *Vendor's Obligation as to Fitness of Land for a Particular Purpose*, 37 MINN. L. REV. 108, 110 (1953).

35. PATRICK S. ATIYAH, THE RISE AND FALL OF FREEDOM OF CONTRACT 179 (1979).

36. *Id.* at 179-80; *see also* MAGNUSON & CARPER, *supra* note 26, at x.

37. Dunham, *supra* note 34, at 110.

38. *Id.* "Of course caveat emptor would be the rule in such a society." *Id.*

39. *See* ATIYAH, *supra* note 35, at 180, 465-66.

40. 79 Eng. Rep. 3, Cro. Jac. 4 (Ex. Ch. 1603).

41. *See, e.g.*, HOWARD O. HUNTER, MODERN LAW OF CONTRACTS ¶ 9.02[3] (rev. ed. 1993).

merchant for £100, a substantial sum of money at the time.[42] The goldsmith asserted that the jewel was a rare "bezar stone."[43] The purchaser, complaining it was not a bezar stone, filed suit for breach of warranty.[44] The court denied relief, holding that the goldsmith had merely affirmed and not warranted the character of the stone.[45] The decision came to be cited for the proposition that English courts were not interested in enforcing the fairness of an exchange because they thought contracting parties should handle such matters themselves.[46]

It seems extraordinary that such a bizarre case would serve as the foundation stone for the principle of caveat emptor.[47] The rather predictable outcome reflects a sensible judicial reluctance to second-guess the parties' estimate of such a strange object, whose value was clearly subjective.[48] Nevertheless, by the early seventeenth century the doctrine of caveat emptor was being applied in England to conveyances in real, as well as personal property.[49] Imported as part of English common law, the doctrine of caveat emptor had become a central governing principle of land conveyancing law in the United States by the nineteenth century.[50]

In its formative period, the doctrine of caveat emptor also served a gate-keeping function, given that claims by disappointed purchasers might have otherwise overburdened the judicial system at the very time law courts were beginning to emerge as an effective organ for

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42. *Chandelor*, 79 Eng. Rep. at 3-4.

43. *Id.* at 4. A bezar, or bezoar, stone, similar to a gallstone, is formed in the stomach or intestines of goats and was once believed to have antidotal or medicinal power. ATIYAH, *supra* note 35, at 179; A.W.B. SIMPSON, A HISTORY OF THE COMMON LAW OF CONTRACT 536 (1975).

44. ATIYAH, *supra* note 35, at 178.

45. *Chandelor*, 79 Eng. Rep. at 4.

46. ATIYAH, *supra* note 35, at 178-79.

47. Indeed, the lineage of the doctrine of caveat emptor in the United States has been traced directly to *Chandelor v. Lopus*. MORTON J. HORWITZ, THE TRANSFORMATION OF AMERICAN LAW 180 & nn.109-10 (1977).

48. *See* ATIYAH, *supra* note 35, at 179 ("In all probability the plaintiff was complaining not that it was not a 'bezoar stone' but that it did not have the magical qualities he had expected.").

49. *See* COKE UPON LITTLETON 102a, *cited in* Hamilton, *supra* note 25, at 1165 ("Note, that by the civil law every man is bound to warrant the thing that he selleth and conveyeth, albeit there be no express warranty; either in deed or in law; but the common law bindeth him not, for *caveat emptor*.").

50. In Barnard v. Kellogg, 77 U.S. (10 Wall.) 383, 388-89 (1870), Supreme Court Justice Davis wrote, "Of such universal acceptance is the doctrine of *caveat emptor* in this country, that the courts of all the States in the Union where the common law prevails, with one exception (South Carolina), sanction it." Indeed, caveat emptor came to be applied even more vigorously in the United States than in England. ATIYAH, *supra* note 35, at 180.

dispute resolution.[51] With the passage from an agrarian to an industrial society, caveat emptor was nourished by the norms of nonintervention and rugged individualism reflected in nineteenth century marketplace morality.[52] Persons entering into contractual relationships were not to expect the law "to stand *in loco parentis* to protect them" if they made a bad bargain by not exercising ordinary business sense.[53] Contracting parties had the responsibility to either rely on their own judgment or require express warranties if they doubted their judgment.[54] A rule of law leveling out informational advantages in transactions conducted in a free marketplace would have been seen as depriving the diligent of the fruits of lawfully acquired superior skill and knowledge.[55]

Laissez faire political economists of the period regarded caveat emptor as a simple, efficient, and self-executing mechanism to prevent the manufacture and sale of defective commodities without interference from vast systems of governmental regulation.[56] The occasional injustice that inevitably resulted from refusing judicial relief to a buyer too careless or foolish to inspect before purchasing thereby educated the general populace. Isolated cases of individual hardship could be expected to decrease in frequency as buyers became familiar with standard operating procedures of the marketplace.

B. Causes of the Decline of Caveat Emptor

With the benefit of hindsight, it is possible to identify with specificity and confidence the societal conditions that fostered erosion of the doctrine of caveat emptor in the law of real property sales during

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51. 2 ALPHONSE M. SQUILLANTE & JOHN R. FONSECA, WILLISTON ON SALES § 15-12, at 364 (4th ed. 1974).

52. *See* LAWRENCE M. FRIEDMAN, A HISTORY OF AMERICAN LAW 540 (2d ed. 1985) ("The maxim *caveat emptor* flattered the manhood and pride of the judges.").

53. Ollerman v. O'Rourke Co., 288 N.W.2d 95, 101 (Wis. 1980).

54. *See, e.g.*, M'Farland v. Newman, 9 Watts 55, 57 (Pa. 1839) ("He who is so simple as to contract without a specification of the terms, is not a fit subject of judicial guardianship.").

55. *Ollerman*, 288 N.W.2d at 101.

56. ATIYAH, *supra* note 35, at 465. This author also notes that:

> If the responsibility for ensuring that a man acquired a reasonable purchase at a fair price were thrown upon the purchaser, they argued, then the purchaser would assuredly take the trouble to examine what he was buying with due care. Shoddy goods would disappear from the market, or if buyers in fact were willing to buy them at prices reflecting their poor quality, then the goods would find a market at that price and deservedly so. All this would follow from throwing the responsibility upon the purchaser, without any legislation or litigation.

Id.

the second half of this century.[57] American courts almost universally adhered to the doctrine of caveat emptor until the middle of the twentieth century.[58] In the era following World War II, however, the doctrine began to unravel.[59] The post-World War II era was characterized by poorer quality homes due to accelerated construction schedules, and a rapidly growing middle class that tended to move more often.[60] As the inability of the average American homebuyer to make a proper structural inspection became evident, courts began to carve out exceptions to the doctrine of caveat emptor in highly sympathetic fact situations.[61] This doctrinal breakdown was heralded by English decisions a decade earlier involving the sale of newly constructed

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57. Notwithstanding that it had ceased to affect personal property transactions, the doctrine of caveat emptor was the staple fare of the law of real estate sales well into the 1960s. *See* Rose, *supra* note 4, at 580; Frona M. Powell & Jane P. Mallor, *The Case for an Implied Warranty of Quality in Sales of Commercial Real Estate*, 68 WASH. U. L.Q. 305, 307 (1990); MILTON FRIEDMAN, CONTRACTS AND CONVEYANCES OF REAL PROPERTY § 1.2(n), at 42-43 (5th ed. 1991).

58. *See* Strawn v. Canuso, 657 A.2d 420, 425 (N.J. 1995) (reviewing the history of caveat emptor and the historical lack of protection afforded purchasers of real property); Cochran v. Keeton, 252 So. 2d 307, 311 (Ala. Civ. App. 1970) (discussing how courts have adapted the role of caveat emptor in Alabama law), *aff'd*, 252 So. 2d 313 (Ala. 1971); Linda M. Libertucci, *Builder's Liability to New and Subsequent Purchasers*, 20 SW. U. L. REV. 219, 220 (1991) (providing a historical overview of the development of the doctrine of caveat emptor).

59. Of course, the process took longer in some jurisdictions than in others. *Compare, e.g.*, Fegeas v. Sherrill, 147 A.2d 223, 227 (Md. 1958) (noting although "the particular case here stated by the plaintiff possesses a certain appeal to the moral sense" it does not justify "imposing upon the frailties of human nature a standard so idealistic" as to require disclosure of active termite infestation by home seller) *with* Obde v. Schlemeyer, 353 P.2d 672, 674-75 (Wash. 1960) (holding that failure by seller to disclose knowledge of termite infestation constituted fraud).

60. *See* McDonald v. Mianecki, 398 A.2d 1283, 1287 (N.J. 1979) (noting that pressure to abandon or modify caveat emptor increased with the post World-War II mass production of homes and the resulting change in home-buying practices); Richard C. Webb, *Liability for Construction Defects in Residential Realty: A Re-Examination in Light of* Kennedy v. Columbia Manufacturing Co., 42 S.C. L. REV. 503, 504 (1991) (asserting that construction of speculative housing after World War II initially encouraged the application of the doctrine of caveat emptor, but eventually led to its downfall).

61. For example, in Ollerman v. O'Rourke Co., 288 N.W.2d 95 (Wis. 1980), the buyer of a vacant building lot claimed that the seller, a corporation engaged in subdivision and development, failed to disclose the existence of a subsurface well that was uncapped in the process of excavation. *Id.* at 97. In order to stop the flow of water and make the subsoil suitable for building, the buyer incurred expenses that exceeded the cost of the land. *Id.* The court held that an unsophisticated buyer, with a reasonable expectation of honesty in the marketplace, may rely on the skill and knowledge of a vendor in the real estate business to disclose material facts not readily discoverable. *Id.* at 112.

housing by vendor-builders,[62] and was influenced by promulgation of the Uniform Commercial Code.[63]

Later, the federal courts, together with the rest of society, responded to the climate of activism created by the civil rights and anti-war movements of the 1960s.[64] As part of Lyndon Johnson's Great Society, federally financed legal services attorneys focused judicial attention on the plight of the urban poor.[65] The result was the implied warranty of habitability in residential landlord-tenant law, derived from jurisprudence by analogy to cases recognizing an implied warranty of suitability in sales by manufacturers of mass-produced chattels.[66] Within a generation, and without closely considering the

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62. The English courts based their decisions not to apply caveat emptor to the sale of new homes on two grounds. First, the application of the doctrine would be unjust because at the time of contract the buyer would be unable to properly inspect a home either under construction or yet to be constructed; and second, the contract of sale was also considered to include an implied covenant that the house would be properly constructed. *See* Perry v. Sharon Dev. Co., 4 All E.R. 390, 395-96 (C.A. 1937) (holding that the purchaser of a house under construction is entitled to rely upon the implied warranty of habitability); Miller v. Cannon Hill Estates, Ltd., [1931] 2 K.B. 113, 122-23 (finding in contract for construction of home both express and implied warranties that house would be fit for habitation).

63. *See* U.C.C. §§ 1-203, 2-314, 2-315 (1995). Consumers who became accustomed to the protection of an implied warranty of merchantability in the sale of goods reasonably expected the law to protect them when they purchased new homes. Joseph C. Brown, Jr., Comment, *The Implied Warranty of Habitability Doctrine in Residential Property Conveyances: Policy-Backed Change Proposals*, 62 WASH. L. REV. 743, 744 (1987).

64. Edward H. Rabin, *The Revolution in Residential Landlord-Tenant Law: Causes and Consequences*, 69 CORNELL L. REV. 517, 546-47 (1984). In a remarkably candid exchange of correspondence, Judge J. Skelly Wright acknowledged that

> I was indeed influenced by the fact that, during the nationwide racial turmoil of the sixties and the unrest caused by the injustice of racially selective service in Vietnam, most of the tenants in Washington, D.C. slums were poor and black and most of the landlords were rich and white. There is no doubt in my mind that these conditions played a subconscious role in influencing my landlord and tenant decisions.

Letter from J. Skelly Wright, U.S. Circuit Judge, to Edward H. Rabin (Oct. 14, 1982), *in* Rabin, *supra*, at 549.

65. Rabin, *supra* note 64, at 550-51.

66. *See, e.g.*, Javins v. First Nat'l Realty Corp., 428 F.2d 1071, 1075 (D.C. Cir.) (Wright, J.) (noting that the decision to extend the implied warranty of habitability reflects a belief that leases of urban dwelling units should be interpreted and construed like any other contract), *cert. denied*, 400 U.S. 925 (1970).

dubious logic,[67] courts imported implied warranty of suitability analysis into the sale of improved real property.[68]

In the 1980s real estate law was revolutionized by the environmental movement.[69] Federal environmental statutes, enforced by a vigorous Environmental Protection Agency and interpreted by a sympathetic federal judiciary, confronted property owners and their lenders with the spectre of joint and several strict liability for environmental contamination, unlimited in amount and without regard to traditional concepts of fault.[70] At the same time, public attention became focused on a new and incurable health concern. As part of the generalized hysteria surrounding Acquired Immune Deficiency Syndrome (AIDS), prospective home purchasers sought to discover the circumstances surrounding the reasons for which a property had come to be placed on the market.[71] In this climate, a rule of law condoning nondisclosure of environmental contamination and public health concerns in real property sales became intolerable.[72]

C. *A Comparative Law Analysis*

Erosion of the doctrine of caveat emptor in the United States is further advanced than in most common-law jurisdictions.[73] Caveat

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67. Extending the logic of the U.C.C.'s implied warranty of suitability of purpose from chattels to the sale of improved real property was unnecessary because the stakes in a real property transaction are so substantially higher than in the sale of chattels that the buyer of real property can reasonably be expected to guard his own interests by, for example, ordering an engineer's report. Rose, *supra* note 4, at 582 n.30 (criticizing the decision in Wawak v. Stewart, 449 S.W.2d 922, 923 (Ark. 1970), in which the court equated the sale of real property to the sale of a mop and applied the same implied warranty logic to both).

68. *See generally* Caryn M. Chittenden, *From Caveat Emptor to Consumer Equity—The Implied Warranty of Quality Under the Uniform Common Interest Ownership Act*, 27 WAKE FOREST L. REV. 571, 578-83 (1992) (tracing the evolution of consumer protection in real estate from caveat emptor to implied warranties of quality).

69. This period also featured new home construction on ground previously considered unsuitable for residential development. Wilhite v. Mays, 232 S.E.2d 141, 143 (Ga. Ct. App. 1976), *aff'd*, 235 S.E.2d 532 (Ga. 1977).

70. *See generally* Steven B. Bass, Comment, *The Impact of the 1986 Superfund Amendments and Reauthorization Act on the Commercial Lending Industry: A Critical Assessment*, 41 U. MIAMI L. REV. 879, 909 (1987) (questioning the soundness of imposing liability for cleanup costs on commercial lenders who have taken no part in the production or release of any hazardous substances).

71. *See infra* text accompanying note 160 and notes 213-215 and accompanying text.

72. *See generally* Omar S. Parker, Jr., *Caveat Emptor Is Further Eroded by Health, Environmental Worries*, NAT'L L.J., Nov. 14, 1988, at 26 (discussing how environmental and health concerns have complicated real estate disclosure issues).

73. In comparison, the French civil code requires that land sellers disclose known defects. BARRY NICHOLAS, THE FRENCH LAW OF CONTRACT 103 (2d ed. 1992) (citing a number of recent decisions in which the court ruled against sellers who failed to disclose, for example, that a parcel of land could never qualify for planning permission, the existence of

emptor remains the basic legal rule of land transfer in modern England and Wales,[74] and "the guiding rule of thumb" of Irish conveyancing.[75]

In 1988 an English legal reform commission recommended abandoning the doctrine of caveat emptor and requiring disclosure of material information by real property vendors.[76] England's land conveyancing professional bodies reacted with strenuous opposition to the proposed radical alteration of the well-understood relationship of parties to the sale of land.[77] What ultimately emerged from this process in 1990 was the "TransAction Protocol," a nonbinding national policy of voluntary seller disclosure to prospective purchasers of standard basic information.[78] The protocol has come under intense

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plans for a piggery near their country house, or the inadequacy of the water supply for the buyer's intended hotel development). The stern simplicity of the common-law doctrine of caveat emptor stood in sharp contrast with the civil law's paternalistic rule that a sound price required a sound commodity. FRIEDMAN, *supra* note 52, at 262-66, 540-41. This divergence was a major factor in California's decision in 1850 to adopt the common law. *Id.* at 540-41. For an excellent comparative analysis of the theoretical models of the legal duty to inform under English common and French civil law, see Rittenberg, *supra* note 30, at 156-58 & nn.19-22.

74. KEVIN GRAY, ELEMENTS OF LAND LAW 245-46 (2d ed. 1993); A.G. GUEST, ANSON'S LAW OF CONTRACT 210 (26th ed. 1984); I.R. STOREY, CONVEYANCING 38 (4th ed. 1993).

English courts have long made an exception in cases involving latent nonphysical defects, such as unrecorded tenancies, easements, and covenants, not reasonably discoverable by purchasers. *See* GRAY, *supra*, at 246; STOREY, *supra*, at 38. Exceptions also have been recognized in cases in which purchasers asked vendors for specific information, the parties occupied a fiduciary relationship, and vendors deliberately concealed physical defects. *See* D.G. BARNSLEY, BARNSLEY'S CONVEYANCING LAW AND PRACTICE 172 (3d ed. 1988).

75. J.C.W. WYLIE, IRISH LAND LAW 112 (2d ed. 1986); *see also* J.C.W. WYLIE, IRISH CONVEYANCING LAW 150 (1978) ("It is not the vendor's duty to disclose defects in the physical condition of his property but rather it is the duty of the purchaser to protect himself by making an inspection of the property and, if necessary, commissioning a survey of the property.").

76. H.W. Wilkinson, *Conveyancer's Notebook: TransAction or OverAction?*, CONV. & PROP. L. 137, 137 (1990) ("[A] vendor of land should be under a positive duty to disclose all material facts about the property he is selling, providing he is aware of those facts or ought reasonably to be aware of them. To this significant extent the *caveat emptor* rule should be reversed.").

77. *Id.* Although, in typical British understatement, the *Conveyancer* noted simply that the proposal was received "without enthusiasm." *Id.* n.1.

78. The protocol envisages that, as soon as property is placed on the market for sale, sellers should supply a range of detailed information described on a standardized form containing the following warning: "IF YOU DO NOT FOLLOW THESE INSTRUCTIONS YOU MAY HAVE TO PAY COMPENSATION TO THE BUYER." *Id.* at 140. However, except for latent nonphysical defects, there is no generalized duty of disclosure in England aside from the protocol, which is not compulsory. GRAY, *supra* note 74, at 245-47. Accordingly, it is unclear why a seller who did not follow the instructions in the disclosure form would incur liability.

criticism from commentators in Great Britain,[79] and it remains uncertain whether the land conveyancing bar will embrace reform.[80]

Until recently, Canadian courts shared their British counterparts' reluctance to impose disclosure duties in real property transactions. For example, following extensive geophysical exploration in the early 1960s, an American mining company, Texas Gulf Sulphur, acquired mineral rights to property in Ontario containing zinc ore with a value of $2 billion.[81] In order to keep its discovery a secret, Texas Gulf took evasive action to throw its competitors off the scent, and managed to conduct its exploration activities in a manner that did not tip off the vendors regarding the extent of the mineral deposits located on their property.[82] After discovering the true value of the deposits, and disappointed by the inadequacy of the consideration received, the vendors filed suit.[83] The Ontario High Court ruled in favor of Texas Gulf, and claimed the company was only doing "what any prudent mining company would have done to acquire property in which it knew a very promising anomaly lay."[84]

However, the real estate brokerage industry in British Columbia and parts of Ontario has recently begun to require sellers to disclose known hidden defects as a condition to gaining access to the multiple

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79. The *Conveyancer* has warned solicitors that the protocol threatens the attorneyclient relationship as sellers react negatively to attorney pressure to comply. Wilkinson, *supra* note 76, at 140. It is "well calculated to put buyer and seller into a state of armed neutrality and mutual suspicion." *Id.* The *Conveyancer* questioned the likely reaction of elderly sellers, widows, "or the simply unorganised" when "faced with the need to recall when the house was last rewired, where the woodworm guarantee is, or whether there has been any building work on the premises in the last four years ('do they mean getting those slates put back?')." *Id.* at 141. Another commentator has warned that unless the protocol achieves widespread adoption, a party selling a home under the protocol and buying another could face a dilemma if his seller does not comply. STOREY, *supra* note 74, at 72-73.

80. STOREY, *supra* note 74, at 72-73 ("It has to be said that, at the time of [this] writing, by no means all the domestic conveyancing transactions conducted by solicitors are protocol transactions.").

81. Leitch Gold Mines, Ltd. v. Texas Gulf Sulphur Co., 1 O.R. 469, 469 (1968).

82. *Id.* at 488-92.

83. *Id.* at 470. To compare and contrast the transferor's legal obligation to disclose material information under the common law of land sales and the federal securities laws, see SEC v. Texas Gulf Sulphur Co., 401 F.2d 833, 848 (2d Cir. 1968) (en banc) (holding that trading based on undisclosed material information violates federal securities laws), *cert. denied*, 404 U.S. 1005 (1971).

84. *Leitch*, 1 O.R. at 493. More recent Canadian decisions recognize a duty to disclose information in the commercial real estate transaction context. *See* Olsen v. Poirier, 111 D.L.R.3d 512 (C.A. 1980) (entitling purchaser to rescission when vendor of dairy farm failed to disclose knowledge of reduction in milk quota upon sale); Tuttahs v. Maciak, 6 Man. R.2d 52 (Q.B. 1980), *available in* CAN. ABRIDGMENT 2D 63, R17D (Supp. 1994), (allowing purchaser of restaurant to rescission and damages when vendor failed to disclose unsuitability of water for cooking and drinking).

listing service, a powerful vehicle for maximizing market exposure.[85] The *Toronto Star* has reported with smug satisfaction that the identical policy reform imposed by governmental fiat in the United States[86] is being achieved through private sector initiative in Canada.[87]

II. THE COMMON-LAW DUTY TO DISCLOSE INFORMATION

It is difficult to imagine custom, practice, or law ever reaching the point where contracting parties will be expected to volunteer everything they know about a subject property in an arm's length real estate transaction.[88] Arguably, an informed party should not be obligated to share informational advantages achieved through deliberate and costly research.[89] Nevertheless, there can be no economic justification for withholding information about a property's defects acquired through no positive investment of resources besides the experience of having resided there. A rule of law requiring disclosure of information casually acquired neither reduces the incentive to produce information nor expropriates any legitimate advantage of skill or shrewdness.[90] When a seller knows that disclosure of material information would correct a mistake as to a basic assumption by the buyer, and when nondisclosure constitutes a failure to act in good faith and in accordance with reasonable standards of fair dealing,[91] the withholding of information may be equated with, and given the same legal effect as, fraudulent misrepresentation.[92]

A. Common-Law Duty to Disclose Physical Defects

During a pre-closing visit to the house he and his wife were considering for purchase, Warren Hill observed a small "ripple" in par-

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85. Silverstein, *supra* note 12.

86. *See infra* notes 187-193 and accompanying text.

87. Silverstein, *supra* note 12.

88. RESTATEMENT (SECOND) OF CONTRACTS § 161 cmt. a (1981); *see, e.g.*, Noss v. Abrams, 787 S.W.2d 834, 838 (Mo. Ct. App. 1990) (holding that a sophisticated real estate developer owed no duty to disclose to seller of single family home that fair market value of property was much higher than contract price).

89. *See* RESTATEMENT (SECOND) OF TORTS § 551 cmt. k (1977) ("To a considerable extent, sanctioned by the customs and mores of the community, superior information and better business acumen are legitimate advantages which lead to no liability."); Anthony T. Kronman, *Mistake, Disclosure, Information, and the Law of Contracts*, 7 J. LEGAL STUD. 1, 33 (1978) (arguing that the law of contracts recognizes a property right in information that results from a deliberate and costly search and that the possesor of such information need not disclose it); *see also* CHARLES FRIED, CONTRACT AS PROMISE 77-85 (1981).

90. RICHARD A. POSNER, ECONOMIC ANALYSIS OF LAW 97 (3d ed. 1986).

91. RESTATEMENT (SECOND) OF CONTRACTS § 161(b) (1981).

92. *Id.* § 161 cmt. b.

quet teakwood flooring on a step leading from the sunken living room to the dining room.[93] As maintenance supervisor at a school district, Hill had seen similar "ripples," which had turned out to be the result of termite damage.[94] Hill asked the sellers, Ora and Barbara Jones, whether the condition he observed could be termite damage.[95] Mrs. Jones replied that a broken water heater had caused water damage in the dining room area necessitating repairs to the floor.[96] Hill was not entirely satisfied with the explanation, but decided to wait for the results of a termite inspection upon which the contract was contingent.[97]

The parties closed the deal after the termite inspection report found neither visible infestation nor evidence of previous treatment or damage.[98] Upon taking possession, the Hills found within the home a pamphlet entitled "Termites, the Silent Saboteurs," learned about past termite infestation from a neighbor, and noticed that the wood on the steps leading to the sunken living room was crumbling.[99] A subsequent termite inspection by the same inspector confirmed the existence of termite damage to the floor, steps, and wood columns of the house.[100]

The Hills filed suit for rescission, claiming that the sellers had fraudulently withheld knowledge of the history of termite infestation and existence of termite damage.[101] At trial, the court granted the sellers' motion for summary judgment.[102] The Arizona Court of Appeals reversed, holding that the sellers owed a duty to disclose their knowledge of termite damage that was unknown to the Hills and materially affected the value of the residence.[103]

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93. Hill v. Jones, 725 P.2d 1115, 1116 (Ariz. Ct. App. 1986).

94. *Id.*

95. *Id.*

96. *Id.*

97. *Id.*

98. *Id.*

99. *Id.*

100. *Id.* When confronted with this information, the termite inspector complained that, in accordance with industry custom, he should have been told of any history of termite infestation and treatment before performing his inspection. *Id.* at 1117; *see also* Mitchell v. Skubiak, 618 N.E.2d 1013, 1019 (Ill. App. Ct. 1993) ("A duty to speak or disclose defects to a professional inspector arises under the same conditions as when a home is inspected by the buyer personally.").

101. *Hill*, 725 P.2d at 1115.

102. *Id.* at 1115-16.

103. *Id.* at 1118. The court noted that an affirmative duty to disclose exists under the following circumstances:

> 1. Disclosure is necessary to prevent a previous assertion from being a misrepresentation or from being fraudulent or material;

Other courts have recognized a duty to disclose information to prospective purchasers in a variety of contexts involving cracked foundations,[104] leaking roofs, structural defects,[105] unstable soil conditions,[106] infestation by cockroaches,[107] and defective sewage disposal.[108] Additionally, nondisclosure of environmental contamination,[109] radon,[110] and asbestos[111] has become a fertile source of litigation in recent years.[112]

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2. Disclosure would correct a mistake of the other party as to a basic assumption on which that party is making the contract and if nondisclosure amounts to a failure to act in good faith and in accordance with reasonable standards of fair dealing;

3. Disclosure would correct a mistake of the other party as to the contents or effect of a writing, evidencing or embodying an agreement in whole or in part;

4. The other person is entitled to know the fact because of a relationship of trust and confidence between them.

Id. (citing RESTATEMENT (SECOND) OF TORTS § 551 (1977)).

104. Thacker v. Tyree, 297 S.E.2d 885, 886 (W. Va. 1982).

105. Johnson v. Davis, 480 So. 2d 625, 629 (Fla. 1985) (imposing duty to disclose leaking roof in three-year-old home).

106. Easton v. Strassburger, 199 Cal. Rptr. 383, 385-86 (Ct. App. 1984); Blake v. Doe, 623 N.E.2d 1229, 1231 (Ohio Ct. App. 1993).

107. Weintraub v. Krobatsch, 317 A.2d 68, 71 (N.J. 1974) (characterizing a no-duty-todisclose case cited by seller as one in "a line of 'singularly unappetizing cases' . . . out of tune with our times" (quoting W. PAGE PROSSER, LAW OF TORTS § 106, at 696 (4th ed. 1971))).

108. Holcomb v. Zinke, 365 N.W.2d 507, 512 (N.D. 1985); Anderson v. Harper, 622 A.2d 319, 324-25 (Pa. Super. Ct. 1993). Latency of defect is a recurring theme in cases imposing a duty to share information. *Anderson*, 622 A.2d at 323. Sewer connections, by their subterranean nature, are not open to inspection. *Id.* at 324.

109. *See* Jane M. Draper, Annotation, *Vendor's Obligation to Disclose to Purchaser of Land Presence of Contamination from Hazardous Substances or Wastes*, 12 A.L.R.5TH 630 (1993).

110. *Compare* Schnell v. Gustafson, 638 P.2d 850, 852 (Colo. Ct. App. 1981) (holding that sellers could be held liable for fraudulent nondisclosure of radon hazard after not taking corrective action following a warning by the health department) *with* Wayne v. Tennessee Valley Auth., 730 F.2d 392, 395 (5th Cir. 1984) (affirming summary judgment dismissing fraudulent concealment claim because the TVA could not reasonably have known of radon hazard that resulted from construction of plaintiffs' house in 1968 using cement blocks made of radon-contaminated phosphate slag), *cert. denied*, 469 U.S. 1159 (1985). *See also* T & E Indus. v. Safety Light Corp., 587 A.2d 1249, 1257-58 (N.J. 1991) (holding that caveat emptor does not bar land purchaser's recovery when seller has engaged in the abnormally dangerous activity of processing radium on the property).

According to the EPA, radon represents the greatest health hazard of any environmental pollutant, ranking behind only cigarette smoking as the second leading cause of lung cancer. Eleanor Charles, *Waterborne Radon Joins Airborne Type as Problem*, N.Y. TIMES, Feb. 19, 1995, § 9, at 11.

111. *See, e.g.*, Heider v. Leewards Creative Crafts, Inc., 613 N.E.2d 805, 817-18 (Ill. App. Ct. 1993) (remanding suit for fraud and tortious interference based on buyer's discovery of asbestos on property).

112. Seriousness of defect is a common feature of cases imposing a duty to share information. *Compare* Anderson v. Harper, 622 A.2d 319, 325 (Pa. Super. Ct. 1993) (holding that sellers had duty to disclose known defective sewage system) *with* Gozon v. Henderson-

A legal duty to "speak up" does not arise simply because two parties may have been sitting across the bargaining table when a deal was struck between them.[113] The common theme running through the nondisclosure jurisprudence is the prevention of situations in which buyers labor under serious misapprehension and are unable to rationally assess the true level of risk involved in the bargain.[114] The duty to disclose arises when contracting parties do not stand on equal footing because one possesses superior knowledge not reasonably available to the other.[115]

This was the case in *Colgan v. Washington Realty Co.*[116] A hard rain fell on the day Donald and Dorothy Colgan closed on the purchase of their new home. Soon after, water seeping through the patio caused the garage roof to collapse onto their automobile.[117] The purchasers had been informed by the sellers that the only water leakage problem previously experienced was a broken water pipe that had since been repaired.[118] The purchasers filed suit, claiming that absence of unresolved water leakage problems was a material inducement to their decision to purchase the property.[119] The trial judge granted the sell-

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Dewey & Assocs., 458 A.2d 605, 607 (Pa. Super. Ct. 1983) (holding that sellers had no duty to disclose non-dangerous patent defects in swimming pool).

113. Jordan v. Duff & Phelps, Inc., 815 F.2d 429, 435 (7th Cir. 1987) ("Strangers transact in markets all the time using private information that might be called 'material' and, unless one has a duty to disclose, both may keep their counsel." (citations omitted)), *cert. dismissed*, 485 U.S. 901 (1988).

114. For example, in a typical formulation, the West Virginia Supreme Court held that,

> [W]here a vendor is aware of defects or conditions which substantially affect the value or habitability of the property and the existence of which are unknown to the purchaser and would not be disclosed by a reasonably diligent inspection, then the vendor has a duty to disclose the same to the purchaser .... [F]ailure to disclose will give rise to a cause of action in favor of the purchaser.

Thacker v. Tyree, 297 S.E.2d 885, 888 (W. Va. 1982).

115. In Osterberger v. Hites Constr. Co., 599 S.W.2d 221 (Mo. Ct. App. 1980), the court held that sophisticated sellers of a single family home owed a duty to disclose the existence of a recorded deed of trust encumbering the property to first-time homebuyers. *Id.* at 227-28. Because the entire transaction was completed within a single day, purchasers had no time to seek assistance from a title insurer or attorney. *Id.* at 228. Instead, a seller with superior knowledge prepared and explained the documentation to purchasers, and although the parties were not in a fiduciary relationship, buyers had relied upon sellers. *Id.* Under these circumstances, the court was not persuaded that, as a matter of public record, the deed of trust was reasonably discoverable. *Id.* at 228-29. *But see* Fairmont Foods Co. v. Skelly Oil Co., 616 S.W.2d 548, 552 (Mo. Ct. App. 1981) (holding the seller owed no duty to disclose impairment of access to subject property by condemnation action to major corporation that had not exercised reasonable care to discover information within its reach).

116. 879 S.W.2d 686 (Mo. Ct. App. 1994).

117. *Id.* at 688.

118. *Id.*

119. *Id.*

ers' motion for summary judgment, noting that purchasers who make independent investigation of the physical condition of real property are presumed to have relied upon the results of their inspection.[120]

The Missouri Court of Appeals reversed, observing that in the vast majority of cases, material information about the condition of a residence will be peculiarly within sellers' knowledge and difficult for purchasers to obtain.[121] Most homebuyers will be unable to achieve parity of information with long-time homeowners, even by conducting a professional building inspection.[122] Judicial recognition that vendors and purchasers are not equal players challenges the basic underlying assumption of the doctrine of caveat emptor.[123]

Where a defective condition is open to observation or otherwise reasonably discoverable, and a purchaser has an opportunity to examine the premises before closing, the seller may be protected by the doctrine of caveat emptor unless, of course, there is evidence of

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120. *Id.* at 690. The purchasers hired an independent professional to inspect the property. *Id.* The inspector's report noted the existence of "small voids" in the grout between patio tiles, and recommended application of silicone sealer to protect against possible leakage into the garage area. *Id.*

121. *Id.* at 691. According to an affidavit by a home improvement worker filed in opposition to their summary judgment motion, the sellers had hired him to paint and caulk the deck, believing that would stop water leakage into the garage. *Id.* at 690. However, he did not know whether the work he had done corrected the problem. *Id.* According to an affidavit by the previous owner of the residence, he had experienced and attempted to correct water leakage on at least two occasions. *Id.* The court held that reasonable minds could conclude, entirely from this circumstantial evidence, that the sellers were aware of active water leakage problems. *Id.*

122. The *Colgan* court made this point by noting that

> a seller, who has lived in a property, as opposed to a mere investor, would have knowledge which is superior to a buyer's knowledge concerning the property's condition. In this case, for example, sellers may have lived in the house through some rainstorms. Buyers, in contrast, sent an inspector into the house for a few hours, an inspector who may or may not have been in the house while it rained. Obviously, the sellers would have a better vantage position of the leakage problem and the severity of the condition.

Id. at 691; *see also* Holcomb v. Zinke, 365 N.W.2d 507, 512 (N.D. 1985) ("While the relationship between seller and buyer may not be a fiduciary or confidential one, it is marked by the clearly superior position of the seller vis-a-vis knowledge of the condition of the property being sold.").

123. *See supra* note 26 and accompanying text.

fraud.[124] Either constructive notice or actual knowledge of the defective condition is a defense to buyer's claim.[125]

This principle is aptly illustrated by *Layman v. Burns.*[126] In *Layman,* the purchasers bought a home only later to discover that the home had a foundation defect.[127] Prior to closing, the purchasers inspected the basement and noticed the I-beams supporting the walls.[128] Assuming the I-beams to be part of the structure, the purchasers bought the home.[129] When the purchasers subsequently tried to resell the house, a broker called their attention to the defective basement walls.[130] Unable to sell, the purchasers defaulted on their mortgage.[131]

In their subsequent lawsuit against the sellers, the trial court awarded the purchasers damages of $40,000.[132] On appeal, the Supreme Court of Ohio reversed, holding that when a defective condition is open to observation or discoverable upon reasonable inspection, and the purchaser has the unimpeded opportunity to examine the property, the defense of caveat emptor remains available to the seller.[133]

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124. Anglo-Saxon common law has long recognized an exception to the doctrine of caveat emptor for causes of action for intentional fraudulent misrepresentation. HUNTER, *supra* note 41, ¶ 9.02(3). Similarly, the defense of caveat emptor is not available when the seller actively and knowingly concealed a material physical defect that could not have been discovered through the exercise of reasonable diligence. Gibb v. Citicorp Mortgage, Inc., 518 N.W.2d 910, 918 (Neb. 1994). Suppression of defective conditions by disguising them, covering them up, or otherwise preventing purchasers from discovering them constitutes fraud. *See, e.g.*, Mitchell v. Skubiak, 618 N.E.2d 1013, 1016 (Ill. App. Ct. 1993) (indoor-outdoor carpeting glued to porch and steps to conceal structural damage); Barylski v. Andrews, 439 S.W.2d 536, 540 (Mo. Ct. App. 1969) (fire damage concealed by paint, paper, plaster, and wallboard); Kracl v. Loseke, 461 N.W.2d 67, 72 (Neb. 1990) (sheetrock placed on basement ceiling to conceal termite damage to wooden floor joists).

125. *But see* Flakus v. Schug, 329 N.W.2d 859, 862-64 (Neb. 1983) (finding that observation of sump pump in basement laundry room was insufficient to charge purchasers with constructive notice of two other sump pumps in basement closets), *overruled on other grounds by* Nielsen v. Adams, 388 N.W.2d 840, 846 (Neb. 1986) (noting buyer's observation of sump pump in basement did not discharge seller's duty to disclose water leakage problem).

126. 519 N.E.2d 642 (Ohio 1988).

127. *Id.* at 642-43. The foundation defect was caused by improper backfilling during construction. *Id.*

128. *Id.* at 643.

129. *Id.*

130. *Id.*

131. *Id.*

132. *Id.*

133. *Id.* at 645. In coming to this conclusion, the court rejected the trial court's finding that the defect was not obviously observable upon reasonable inspection by non-experts, noting that the wall was "bulging" and that other witnesses had detected the bow with little

Real estate vendors were once advised that contractual exculpation clauses would shield them against legal liability for failing to disclose defective conditions.[134] Since the erosion of the doctrine of caveat emptor, however, "as is" and integration clauses are no longer completely dependable, because courts in some instances have imposed liability on sellers for breach of the duty to disclose information notwithstanding these provisions.[135]

B. Common-Law Duty to Disclose Nonphysical Conditions

An action for fraudulent nondisclosure is likely to focus on whether a defective condition is significantly material.[136] A condition that does not affect a property's market value[137] or physical safety[138] may not be considered a material defect.[139] Materiality, a function of the expectation of objectively reasonable purchasers, is the central is-

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effort. *Id.* at 644. The result would have been different under a 1993 Ohio statute requiring seller disclosure of known physical defects. *See infra* note 187.

134. *See generally* Frank J. Wozniak, Annotation, *Construction and Effect of Provision in Contract for Sale of Realty by Which Purchaser Agrees to Take Property "As Is" or in Its Existing Condition*, 8 A.L.R.5TH 312 (1992).

135. *Compare, e.g.*, Stemple v. Dobson, 400 S.E.2d 561, 566 (W. Va. 1990) (holding that "as is" clause did not extinguish buyers' suit for fraudulent concealment) *with* Conahan v. Fisher, 463 N.W.2d 118, 119 (Mich. Ct. App. 1990) (holding that seller owed no duty to disclose termite problem in "as is" sale where buyers' professional inspection revealed no infestation).

In Raskin v. Chrysler Realty Corp., No. 93-1218, 1994 Wis. App. LEXIS 1381, at *1 (Wis. Ct. App. Nov. 8, 1994), the court held that the purchaser of a vacant automobile dealership could not recover damages from the seller for failure to disclose environmental contamination. *Id.* at *14. After purchasing the property, buyer discovered that it contained petroleum-contaminated soil from three tanks that had been removed prior to sale. *Id.* at *8. Under the terms of the contract, buyer agreed to purchase the property in "'as is' condition and subject to all faults of every kind and nature whatsoever whether latent or patent and now or hereafter existing." *Id.* at *3. The court held that the broad disclaimer clause insulated seller from liability for nondisclosure, and shifted the burden to buyer to determine the condition of the property. *Id.* at *14. *Contra* Channel Master Satellite Sys. v. JFD Elec. Corp., 702 F. Supp. 1229, 1232 (E.D.N.C. 1988) (holding that "as is" clause in sales agreement did not release seller from liability for hazardous substance contamination of the subject property).

136. "A fact is material if a reasonable purchaser would attach importance to its existence or nonexistence in determining the choice of action in the transaction in question. . . ." Ollerman v. O'Rourke Co., 288 N.W.2d 95, 107 (Wis. 1980); *see also* RESTATEMENT (SECOND) OF TORTS § 538 (1977).

137. *See* Karoutas v. Homefed Bank, 283 Cal. Rptr. 809, 811 (Ct. App. 1991) (noting that undisclosed facts are considered material if they have a "significant and measurable effect on market value").

138. *See* Gozon v. Henderson-Dewey & Assocs., 458 A.2d 605, 606 (Pa. Super. Ct. 1983) (holding that a leaking swimming pool was neither dangerous nor latent and thus seller had no duty to disclose); Mobley v. Copeland, 828 S.W.2d 717, 725-26 (Mo. Ct. App. 1992) (holding that there was no duty to disclose slight electrical current in swimming pool).

139. Parker, *supra* note 72, at 26.

sue in a controversial line of recent decisions involving nondisclosure of "psychological" defects. Legislative action eventually became necessary to reverse common-law expansion of the concept of materiality into the area of these nonphysical, "psychological" conditions.[140]

1. Psychological Defects.—Well-publicized cases involving murder, AIDS, and poltergeists have focused public and state legislative attention on an evolving legal duty to disclose the existence of nonphysical, psychological defects to prospective purchasers.[141] The market value of affected real estate is significantly reduced once potential purchasers become aware of this information.[142] As a result, these properties are sometimes described as "stigmatized."[143]

The genesis of the doctrine mandating the disclosure of these types of defects was *Reed v. King*.[144] In *Reed*, the seller and the seller's broker failed to disclose that the subject property had been the scene of a multiple axe murder a decade earlier.[145] After learning about the home's gruesome history from a neighbor, the purchaser filed suit for rescission and damages.[146] The trial court granted defendants' motion to dismiss for failure to state a claim.[147] The court of appeals, acknowledging that reputation and history do influence market value,[148] held that the purchaser could recover against the seller and broker for failure to disclose if she could prove that the brutal crime materially reduced the value of the property.[149] Concerned that its holding would "permit[ ] the camel's nose of unrestrained irrational-

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140. *See infra* notes 188-189 and accompanying text.

141. Paula C. Murray, *What Constitutes a Defect in Real Property?*, 22 REAL EST. L.J. 61, 63 (1993) ("Although it may seem bizarre, brokers are routinely asking sellers for this information.").

142. For example, the Los Angeles home where actress Sharon Tate and six others were murdered in 1969 by followers of Charles Manson was recently torn down after years on the market. Suzanne Gordon, *"Stigmatized Houses" Where Crime Strikes, Sometimes Teardown is the Only Answer*, CHI. TRIB., June 3, 1995, at HG14. Furthermore, local real estate agents predict that the condominium owned by the estate of Nicole Brown Simpson is likely to sit vacant for three years before finally selling for 70% of market value. *Id.*

143. Sharlene A. McEvoy, *Stigmatized Property: What a Buyer Should Know*, 48 J. MO. B. 57 (1992).

144. 193 Cal. Rptr. 130 (Ct. App. 1983).

145. *Id.* at 130. The seller represented that the premises were in good condition and were fit for an "elderly lady" living alone. *Id.* at 131. He had even asked a neighbor not to inform the buyer of the crime. *Id.*

146. *Id.* at 130.

147. *Id.* at 131.

148. *Id.* at 133 ("'George Washington slept here' is worth something, however physically inconsequential that consideration may be.").

149. *Id.*

ity admission to the tent,"[150] the court emphasized the fact-specific context of the case at hand.[151]

Nevertheless, as the first case to require disclosure of information about a property's notoriety that would likely affect a purchaser's acquisition decision, *Reed* sent a loud and clear message to real property sellers and their brokers. In the wake of *Reed*, sellers and brokers would need to consider purchaser psychology as well as structural integrity.

Following *Reed*, a New York appellate court decided a celebrated case concerning a seller's duty to disclose a home's reputation for being inhabited by poltergeists.[152] For ten years Helen Ackley publicized an eighteen-room Nyack, New York, residence overlooking the Hudson River as "haunted" by spirits.[153] However, she failed to disclose this information to the eventual purchaser, New York bond trader Jeffrey Stambovsky.[154] Upon discovering the property's notoriety, Stambovsky refused to consummate closing, and filed suit to rescind the contract and recover the $32,500 he had deposited toward the $650,000 purchase price.[155] Noting the continued vitality of the doctrine of caveat emptor in New York,[156] the trial court granted the seller's motion to dismiss.[157] The appellate court reversed on appeal, holding buyer's complaint sufficient to state a cause of action for rescission.[158] Having informed the public of its haunted character, the court held that the seller owed a duty to furnish the home's out-of-town buyer with the same information.[159]

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150. *Id.* at 132.

151. Multiple murder, the court observed, "is highly unusual in its potential for so disturbing buyers they may be unable to reside in a home where it has occurred." *Id.* at 133.

152. Stambovsky v. Ackley, 572 N.Y.S.2d 672 (App. Div. 1991).

153. Prior to offering it for sale, seller promoted the house on a local walking tour as "a riverfront Victorian (with ghost)." *Id.* at 674. She had actively fostered public impression of the haunting through articles published in the *Reader's Digest* and the local press. *Id.*

154. *Id.* at 675.

155. *Id.* at 678.

156. *Id.* at 675. For this proposition the trial court cited London v. Courduff, 529 N.Y.S.2d 874, 875 (App. Div.), *appeal dismissed*, 537 N.Y.S.2d 494 (N.Y. 1988), which involved a seller's failure to disclose knowledge of property's use as landfill. *Id.* The *London* court noted that "[t]he buyer has the duty to satisfy himself as to the quality of his bargain pursuant to the doctrine caveat emptor, which in New York State still applies to real estate transactions." *Id.*

157. *Stambovsky*, 572 N.Y.S.2d at 674.

158. *Id.* at 677. Presumably the court limited the relief available to rescission to test the extent of the buyer's psychological aversion to haunting (not unlike the thinking behind the doctrine of constructive eviction, where tenant must substantiate landlord's breach of the covenant of quiet enjoyment by incurring the hardship of relocation). A. JAMES CASNER & W. BARTON LEACH, PROPERTY 500-01 (3d ed. 1984).

159. The *Stambovsky* court set the standard by noting that

Applying the *Reed* and *Stambovsky* logic to the disclosure of other types of nonphysical psychological "defects," purchasers may in the future seek to rescind or collect damages on the grounds that a home was formerly occupied by a person who died from AIDS-related complications. Although there is no scientific evidence that the AIDS virus is transmitted by contact with a home formerly occupied by an infected person, prospective homebuyers may nevertheless deem it important to know whether a previous occupant had the disease. If it were possible to discover this information, the market value of affected property likely would be reduced. This information, by its very nature, is unlikely to be discoverable during the course of a routine inspection. Therefore, a buyer's reliance upon a seller's disclosure is even greater under these circumstances than in the case of physical defects. Accordingly, and following the logic of *Reed* and *Stambovsky*, the fact that a previous occupant died from AIDS-related complications would seem to require disclosure.[160] The impact of *Reed* and *Stambovsky*, and the uncertainty surrounding the issue of disclosure involving AIDS, have driven the brokerage industry to lobby sympathetic state legislatures nationwide to enact statutes providing that some nonphysical defects are not material and need not be disclosed to prospective purchasers of affected property.[161]

2. *Deleterious Off-Site Conditions.*—During a pre-closing walk-through inspection of the home she was about to purchase, Kitty Van Camp asked about the reason for bars she observed on the basement windows.[162] In the presence of the brokers, owner Connie Bradford responded by describing a break-in that had occurred sixteen years previously, but disclosed neither the rape that had occurred in the residence a few months earlier, nor another rape occurring in a neighboring home a month later.[163] Upon taking occupancy, Van Camp learned of the serious crimes that had occurred in the home

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> [w]here a condition which has been created by the seller materially impairs the value of the contract and is peculiarly within the knowledge of the seller or unlikely to be discovered by a prudent purchaser exercising due care with respect to the subject transaction, nondisclosure constitutes a basis for rescission as a matter of equity.

Stambovsky, 572 N.Y.S.2d at 676.

Statements in subsequent cases have reiterated New York's retention of the doctrine of caveat emptor in residential real estate transactions. *E.g.*, Simms v. Biondo, 816 F. Supp. 814, 820 (E.D.N.Y. 1993); Copland v. Diamond, 624 N.Y.S.2d 514, 521 (Sup. Ct. 1995).

160. *See infra* note 215.

161. *See infra* notes 188-189 and accompanying text.

162. Van Camp v. Bradford, 623 N.E.2d 731, 734 (Ohio C.P. 1993).

163. *Id.* On the day of the second rape, Bradford listed her home for sale. *Id.*

and neighborhood.[164] After being confronted by Van Camp, one of the brokers involved in the sale acknowledged that the owner and both brokers were fully aware of the violent criminal activity at the time of sale.[165]

Van Camp filed suit against the owner and brokers, claiming that they had withheld knowledge of the unsafe character of the residence and area, information that would have influenced her decision to purchase. The court observed that because both seller and purchaser were single mothers with teenage daughters, the seller should have known that the buyer "was 'peculiarly disposed' to attach importance to the subject of female-targeted crimes."[166] The court refused to grant summary judgment for the seller, holding that under the circumstances nondisclosure of neighborhood criminal activity may have constituted a material omission.[167] The court noted that reasonable minds could have construed the buyer's question about the barred basement windows as a specific solicitation of information regarding safety of the residence.[168] The court held that this affirmative inquiry imposed a duty on the seller to speak truthfully about the reason for the bars.[169]

Similarly, the New Jersey Supreme Court recently held that having marketed their housing development as a "peaceful, bucolic setting with an abundance of fresh air and clean lake waters," vendor-builders were liable for failing to disclose to buyers of single-family residences that their homes were located within one-half mile of a

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164. *Id.*

165. *Id.*

166. *Id.* at 740.

167. *Id.* The court granted the brokers' motion for summary judgment holding they owed no duty to disclose knowledge of the crimes simply by reason of being present at the time of Van Camp's inquiry. *Id.* at 741. While the court's distinction between the conduct of seller and brokers may seem tenuous at first glance, it falls squarely within the parameters of the legal definition of "active concealment." *Id.* The seller's representation, accompanied by suppression of facts, conveyed a misleading impression, which had the effect of impliedly representing that the fact concealed did not exist. *Id.* Had the brokers similarly misrepresented or failed to disclose material information in response to an inquiry directed to them, summary judgment would not have been granted. *Id.*

168. *Id.*

169. *Id.* at 740-41. The court identified the following material issues of fact for determination at trial: (1) whether Van Camp inquired about the safety of the premises; (2) whether Bradford failed to disclose a material fact; (3) whether Van Camp relied upon Bradford's withholding of information regarding safety of the residence in forming her purchase decision; (4) whether Van Camp was put on notice that there was a potential problem regarding safety of the residence by the total mix of information available to her notwithstanding Bradford's nondisclosure; (5) whether Van Camp reasonably conducted her duty of inspection and further inquiry when examining the subject property for defects; and (6) the nature and extent of buyer's damages. *Id.*

toxic waste dump.[170] However, in a preemptive strike against hypothetical claims by future disgruntled purchasers, the court sought to distinguish its decision from mere "transient social conditions in the community," such as the proximity of a group home or a neighborhood school in decline.[171] Notwithstanding the attempt to limit its scope, the reasoning behind this holding has potentially far-reaching consequences.[172]

3. Easements, Building Codes, and Ordinance Violations.—The focus in cases involving nondisclosure of easements and building code and local ordinance violations will generally be on the materiality and accessibility of the omitted information. When a court determines that an easement or ordinance violation that is not readily accessible to a reasonably prudent purchaser materially affects the market value of a parcel of property, a duty to disclose is likely to be held to exist.[173] If the omitted information does not constitute a material fact or is readily accessible, there is generally no duty to disclose.[174] However, if a

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170. Strawn v. Canuso, 657 A.2d 420, 429 (N.J. 1995).

171. *Id.* at 431.

172. For example, the California Court of Appeals has been asked to reverse a ruling by a Van Nuys trial judge dismissing the complaint by purchasers of a $592,000 home that their vendor-builder wrongfully withheld information regarding the proximity of a rocket-testing facility, exposing them to potential health hazards from radioactive and chemical contamination. Jim Tranquada, *Court Ruling May Expand Real Estate Disclosure*, FRESNO BEE, May 28, 1995, at D8. But see Blaine v. J.E. Jones Constr. Co., 841 S.W.2d 703 (Mo. Ct. App. 1992), for a case in which buyers of single-family residences sued their vendor-builder for nondisclosure of plans to build an apartment complex at the entrance to the subdivision. *Id.* at 704. Because the seller's intended development would reduce the market value of their homes, the buyers claimed they would not have acquired property in the subdivision if they had been made aware of the seller's plans. *Id.* at 708. Distinguishing between "intrinsic" and "extrinsic" facts, the Missouri Court of Appeals held that the seller had no duty to disclose existence of the development plan, noting that a duty to disclose is more likely to arise in cases involving intrinsic facts, such as a latent physical defect in the subject property itself. *Id.* Here, the seller's intent to build apartments on neighboring property in the future was extrinsic to the purchase of buyers' homes. *Id.*

173. *See, e.g.*, Curran v. Heslop, 252 P.2d 378, 381 (Cal. Dist. Ct. App. 1953) (finding a duty to disclose a building code violation that was a material fact affecting the value of the home); Gamel v. Lewis, 373 S.W.2d 184, 192 (Mo. Ct. App. 1963) (holding that sellers were required to disclose that they had obtained extensions of time to comply with municipal ordinance requirements, and that future improvements would be required to bring property up to code, even though the omitted information was a matter of public record); Lepera v. Fuson, 613 N.E.2d 1060, 1064 (Ohio Ct. App. 1992) (holding that seller may have a duty to disclose that use of property as two-family residence violated local zoning ordinance); Gilbey v. Cooper, 310 N.E.2d 268, 270 (Ohio C.P. 1973) (deciding that easements recorded three days after property was sold could not reasonably have been discovered by purchaser).

174. *See, e.g.*, Equity Capital Corp. v. Kreider Transp. Serv., 967 F.2d 249, 254 (7th Cir. 1992) (holding that nondisclosed information regarding zoning ordinance violation was readily ascertainable at reasonable cost); Randels v. Best Real Estate, Inc., 612 N.E.2d 984,

purchaser inquires directly about these matters, the seller is under a duty to respond truthfully.[175]

C. *Disclosure in Commercial Transactions*

Preparing to close on the acquisition of a sixty-three-acre parcel of raw land in South Florida, the builder of a new home community experienced what surely must be one of the commercial real estate developer's worst nightmares.[176] An archaeological survey revealed that the property was an ancient Native American campsite and burial ground, subsequently determined to be the first home of the Seminole Tribe.[177] The historical and archaeological significance of this property rendered it undevelopable, causing the builder to file suit against the seller on the grounds that the information had been intentionally withheld.[178] The court disagreed with the builder, holding that in the context of a commercial transaction, intentional nondisclosure of known material facts does not state a cause of action.[179]

As this case illustrates, the doctrine of caveat emptor enjoys considerable continued vitality in those states reluctant to abandon the doctrine in commercial real estate transactions.[180] Courts in other

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988-89 (Ill. App. Ct. 1993) (finding that nondisclosed information regarding ordinance requiring that property be disconnected from septic system and hooked into municipal sewer system within five years was discoverable by reasonable investigation); Lawton v. Dracousis, 437 N.E.2d 543, 548 (Mass. App. Ct.) (holding that building code violations were not material), *appeal denied*, 440 N.E.2d 1177 (Mass. 1982); Selvin v. Kelshaw, 611 A.2d 1232, 1238-39 (Pa. Super. Ct. 1992) (finding no duty to disclose existence of unrecorded easement for municipal waterline); Goldfarb v. Dietz, 506 P.2d 1322, 1327 (Wash. Ct. App. 1973) (finding that because purchaser had constructive notice of applicable zoning ordinances, seller was not responsible for failure to disclose that purchaser would be prevented from rebuilding nonconforming home).

175. *See, e.g.*, Kraft v. Lowe, 77 A.2d 554, 557 (D.C. 1950) (noting that seller had a duty to answer truthfully and completely in response to a direct question regarding plumbing).

176. Green Acres, Inc. v. First Union Nat'l Bank, 637 So. 2d 363, 364 (Fla. Dist. Ct. App. 1994).

177. *Id.*

178. *Id.*

179. *Id.* Nevertheless, the court granted leave to amend based on specific contractual language arguably creating a duty to disclose. *Id.* at 364-65.

180. For example, in Haskell Co. v. Lane Co., 612 So. 2d 669 (Fla. Dist. Ct. App.), *appeal dismissed sub nom.* Service Merchandise Co. v. Lane Co., 620 So. 2d 762 (Fla. 1993), a roof collapsed during a severe rainstorm four years after sale of a commercial building, causing significant personal injury to shoppers and property damage. *Id.* at 670. The court held that the seller owed no duty to disclose a latent defect in the roof drainage system, even though the court opined in dicta "that the time has come for a critical evaluation of the merit of continued adherence to the doctrine of caveat emptor" in commercial real estate transactions. *Id.* at 675.

states, however, have extended the common-law duty of disclosure to the commercial context.[181]

While considerations of justice, fair dealing, and sound public policy justify imposition of a duty of disclosure in the residential context,[182] these elements are less persuasive when sought to be applied to commercial transactions.[183] Some commentators have observed, however, that purchasers of "real property for business purposes vary widely in their experience, knowledge, sophistication, bargaining power, wealth and access to outside advisers and experts."[184] Nevertheless, the decision to buy a residence differs from the decision to purchase income-producing commercial property for investment purposes in significant ways that argue for retaining a different legal doctrine.[185]

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181. For example, in Green Spring Farms v. Spring Green Farm Assocs., 492 N.W.2d 392 (Wis. Ct. App. 1992), the cattle on a dairy farm suffered an outbreak of salmonella bacteria two years after the buyer took possession. *Id.* at 394. The outbreak resulted in the destruction of livestock, extensive veterinary care for other dairy cattle, and considerable financial loss. *Id.* As a result, the buyer defaulted on land contract payments and the seller commenced foreclosure proceedings. *Id.* The buyer's counterclaim alleged that the seller knowingly withheld the existence of salmonella contamination. *Id.* Having denied the buyer's request for a jury trial on the issue, the trial court granted summary judgment for the seller. *Id.* at 393. The appellate court reversed, citing Ollerman v. O'Rourke Co., 288 N.W.2d 95 (Wis. 1980), as authority for "a more enlightened rule which rejects strict application of the doctrine of *caveat emptor.*" *Green Spring Farms*, 492 N.W.2d at 396. This more "enlightened rule" states that "[t]he doctrine of *caveat emptor* no longer excuses real estate sellers from fully disclosing to potential purchasers the existence of conditions which may be material to the decision to purchase and which the purchaser is in a poor position to discover." *Id.* at 397.

182. *See supra* notes 90-92 and accompanying text.

183. *See* Easton v. Strassburger, 199 Cal. Rptr. 383, 387-90 (Ct. App. 1984) (noting that "a purchaser of commercial real estate is likely to be more experienced and sophisticated in his dealings in real estate and is usually represented by an agent who represents only the buyer's interests").

184. Powell & Mallor, *supra* note 57, at 333 (footnote omitted); *see also Haskell*, 612 So. 2d at 669; *supra* note 180. The *Haskell* court noted that:

> Many of the policy considerations used to justify a duty to disclose in residential cases apply with equal force to commercial cases . . . . What of the small businessman, or professional in solo practice—do they possess the bargaining power to insist upon express warranties from the seller (or lessor) of a small store or office? Such distinctions may have some merit as to the large corporate purchaser (or lessee), but clearly are inappropriate with regard to a substantial segment of the business community.

Haskell, 612 So. 2d at 675.

185. The purchase of commercial real property for investment purposes is a discretionary decision. After analyzing the comparative advantages of real estate against other available investment opportunities, the investor dispassionately compares the physical and economic features of properties on the market. In contrast, home purchase is frequently occasioned by disorienting changes in either employment or family composition. Additionally, the decision to purchase residential real estate is often affected by the emotional

III. THE IMPACT OF MANDATORY DISCLOSURE STATUTES

Because most dwellings and buildings will possess some sort of "problem" at the time of sale, nearly every transfer of real estate invites litigation instituted by a disappointed buyer. Erosion of the doctrine of caveat emptor has confronted real property sellers with the unhappy prospect of legal liability for conditions their buyers might discover or even imagine after taking possession.[186] Left unchecked, this common-law evolution has the potential to significantly burden the dispute resolution system and the alienability of real property. In response to this, mandatory information-disclosure statutes, recently enacted in approximately half the states, represent a legislative reaction to the erosion of the doctrine of caveat emptor.[187]

These state disclosure statutes accomplish two objectives. First, they allocate to property sellers the burden of providing a detailed accounting of their knowledge about defective conditions to prospective purchasers. Second, they protect sellers from liability for failing to disclose psychologically stigmatizing conditions, such as when a homicide, suicide, felony, or death by AIDS occurred on the property.[188] This is the case because the statutes limit the scope of disclo-

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roller coaster of stressful events surrounding involuntary relocation. Recognizing the personal and financial hardships involved in the purchase of residential real estate, Congress granted relief from federal income taxation to residential home dispositions. I.R.C. § 1034(a) (Supp. 1994) (providing for nonrecognition of gain where taxpayer acquires replacement residence within 24 months of sale of principal residence).

186. *See supra* notes 93-181 and accompanying text.

187. ALASKA STAT. §§ 34.70.010–.200 (Supp. 1994); CAL. CIV. CODE §§ 1102–1102.15 (West Supp. 1995); DEL. CODE ANN. tit. 6, §§ 2570–2578 (1994); HAW. REV. STAT. §§ 508D-1 to -20 (Supp. 1994); IDAHO CODE §§ 55-2501 to -2512 (1994); ILL. ANN. STAT. ch. 765, para. 77/1-77/99 (Smith-Hurd Supp. 1995); IND. CODE ANN. §§ 24-4.6-2-1 to -13 (Burns Supp. 1995); IOWA CODE §§ 558A.1–.8 (1995); KY. REV. STAT. ANN. § 324.360 (Michie/Bobbs-Merrill Supp. 1994); MD. CODE ANN., REAL PROP. § 10-702 (Supp. 1995); MICH. COMP. LAWS §§ 565.951–.966 (Supp. 1995); MISS. CODE ANN. §§ 89-1-501 to -523 (Supp. 1995); NEB. REV. STAT. § 76-2,120 (Supp. 1994); N.H. REV. STAT. ANN. § 477:4-c (Supp. 1994); OHIO REV. CODE ANN. § 5302.30 (Anderson Supp. 1994); OKLA. STAT. ANN. tit. 60, §§ 831–839 (West Supp. 1995); OR. REV. STAT. ANN. §§ 105.465–.490 (Supp. 1994); R.I. GEN. LAWS §§ 5-20.8-1 to -11 (Supp. 1994); S.D. CODIFIED LAWS ANN. §§ 43-4-37 to -44 (Supp. 1995); TENN. CODE ANN. §§ 66-5-201 to -210 (Supp. 1995); TEX. PROP. CODE ANN. § 5.008 (West Supp. 1995); VA. CODE ANN. §§ 55-517 to -525 (Michie 1995); WASH. REV. CODE ANN. §§ 64.06.005–.900 (West Supp. 1995); WIS. STAT. ANN. §§ 709.01–.08 (West Supp. 1994).

The National Association of Realtors' active advocacy of mandatory disclosure legislation has had an influence even in states that have not yet enacted statutes. Real estate brokers in these jurisdictions seek to persuade sellers to complete voluntary disclosure forms to advise prospective purchasers of known defects. *See* ST. LOUIS ASS'N OF REALTORS, SELLER'S DISCLOSURE STATEMENT (1992) (on file with author).

188. The following statute enacted in Connecticut is typical:

> § 20-329cc. "Psychologically impacted" defined. "[P]sychologically impacted" means the effect of certain circumstances surrounding real estate which includes,

sure to defects that are physical in nature and material in significance.[189] Disclosure laws thereby constitute a brake on the erosion of the doctrine of caveat emptor.

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but is not limited to: (1) The fact that an occupant of real property is, or was at any time suspected to be, infected or has been infected with the human immunodeficiency syndrome . . . ; or (2) the fact that the property was at any time suspected to have been the site of a homicide, other felony or a suicide.

§ 20-329dd. Psychological impact. No disclosure required. No cause of action.

(a) The existence of any fact or circumstance which may have a psychological impact on the purchaser or lessee is not a material fact that must be disclosed in a real estate transaction.

(b) No cause of action shall arise against an owner of real estate or his or her agent for the failure to disclose to the transferee that the transferred property was psychologically impacted, as defined in section 20-329cc.

CONN. GEN. STAT. ANN. §§ 20-329cc, -329dd (West Supp. 1995).

See also CAL. CIV. CODE § 1710.2 (West Supp. 1995); COLO. REV. STAT. § 38-35.5-101 (Supp. 1995); DEL. CODE ANN. tit. 24, § 2929 (Supp. 1994); D.C. CODE ANN. § 45-1936(f) (Supp. 1995); FLA. STAT. ANN. § 689.25 (West Supp. 1995); GA. CODE ANN. § 44-1-16 (1991); HAW. REV. STAT. § 508D-8 (Supp. 1994); ILL. ANN. STAT. ch. 225, para. 455/31.1 (Smith-Hurd Supp. 1995); IND. CODE ANN. § 24-4.6-2.1-4 (Burns Supp. 1995); KY. REV. STAT. ANN. § 207.250 (Michie/Bobbs-Merrill 1991 & Supp. 1994); LA. REV. STAT. ANN. § 37:1468 (West 1995); MD. CODE ANN., REAL PROP. § 2-120 (Supp. 1995); MICH. COMP. LAWS § 339.2518 (Supp. 1995); MO. REV. STAT. § 442.600 (Supp. 1995); NEV. REV. STAT. § 40.565 (Supp. 1993); N.H. REV. STAT. ANN. § 477:4-e (Supp. 1994); N.M. STAT. ANN. § 47-13-2 (Michie Supp. 1995); N.C. GEN. STAT. § 39-50 (Supp. 1994); OKLA. STAT. ANN. tit. 59, § 858-513 (West Supp. 1995); OR. REV. STAT. ANN. § 93.275 (1990); R.I. GEN. LAWS § 5-20.8-6 (Supp. 1994); S.C. CODE ANN. § 40-57-270 (Law. Co-op. Supp. 1994); TENN. CODE ANN. § 66-5-207 (Supp. 1995); TEX. PROP. CODE ANN. § 5.008 (West Supp. 1995); UTAH CODE ANN. §§ 57-1-1, -37 (1994); VA. CODE ANN. § 55-524 (Michie Supp. 1994); WIS. STAT. ANN. § 452.23 (West Supp. 1994).

Sellers may still owe a duty to disclose information to buyers sufficiently concerned about such matters and inquiring directly. *E.g.*, Van Camp v. Bradford, 623 N.E.2d 731, 736 (Ohio C.P. 1993) (finding that facts about safety were material and must be disclosed); *see supra* notes 162-169 and accompanying text. *See also* Murray, *supra* note 141, at 64. The typical statute does not insulate sellers from liability for intentional misrepresentation. *See, e.g.*, CAL. CIV. CODE § 1710.2(d) (West Supp. 1994) ("Nothing in this section shall be construed to immunize an owner or his or her agent from making an intentional misrepresentation in response to a direct inquiry from a transferee . . . concerning deaths on the real property."). Oklahoma's statute requires disclosure of nonphysical defects if the buyer advises the owner or broker in writing that knowledge of psychological impact is important to his decision to purchase. OKLA. STAT. ANN. tit. 59, § 858-513 (West Supp. 1995).

189. Indiana's statute, for example, defines "defect" as a "condition that would have a significant adverse effect on the value of the property, that would significantly impair the health or safety of future occupants of the property, or that if not repaired, removed or replaced would significantly shorten or adversely affect the expected normal life of the premises." IND. CODE ANN. § 24-4.6-2-4 (Burns Supp. 1995). Nevertheless, such nonphysical conditions as a neighbor's noisy or hostile behavior may be the subject of mandatory seller disclosure. *See* Alexander v. McKnight, 9 Cal. Rptr. 2d 453, 455 (Ct. App. 1992) (interpreting the California statute requiring disclosure of "neighborhood noise problems or other nuisances").

The disclosure statutes vary widely in their applicability[190] and comprehensiveness,[191] and most are silent on the issue of time limits.[192] Additionally, the statutory obligation to disclose generally cannot be avoided through the use of an "as is" clause. Regardless of whether sellers choose to warrant the condition of their property or sell it "as is," disclosure statutes in most states mandate the disclosure of all known material defects.[193]

In the event that nondisclosure results in litigation, the buyer still bears the burden of proving to the trier of fact that the seller knew of a defect materially affecting market value.[194] This burden will be of little comfort, however, to those legal practitioners who advise sellers

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190. Most disclosure statutes are limited to transactions involving residential property containing up to four dwelling units, whether owner-occupied or held by the seller for investment purposes, on the assumption that buyers engaged in the acquisition of larger properties presumably are in a position to bargain for express seller warranties. *See, e.g.*, CAL. CIV. CODE § 1102 (West Supp. 1995); IND. CODE ANN. § 24-4.6-2-1 (Burns Supp. 1995); OHIO REV. CODE ANN. § 5302.30 (Anderson Supp. 1994). Similarly, most statutes do not apply to the initial sale of newly constructed property, where buyers are generally protected by home warranty programs and common-law implied warranty doctrine. *See, e.g.*, IND. CODE ANN. § 24-4.6-2-1 (Burns Supp. 1995); OHIO REV. CODE ANN. § 5302.30 (Anderson Supp. 1994). Disclosure statutes typically apply to conventional residential land transactions involving contracts of sale, as well as installment land contracts, leases with options to purchase, and option agreements. *See, e.g.*, CAL. CIV. CODE § 1102 (West Supp. 1995); OHIO REV. CODE ANN. § 5302.30 (Anderson Supp. 1994). Properties sold by foreclosure (and the subsequent sale of foreclosed property by lenders) are often exempted, as are transfers between spouses and other co-owners. *See, e.g.*, CAL. CIV. CODE § 1102.1 (West Supp. 1995); IND. CODE ANN. § 24-4.6-2-1 (Burns Supp. 1995); OHIO REV. CODE ANN. § 5302.30 (Anderson Supp. 1994).

191. Some state statutes are comprehensive, mandating general disclosure of property defects from asbestos to zoning. *See, e.g.*, MICH. COMP. LAWS § 565.957 (Supp. 1995); R.I. GEN. LAWS § 5-20.8-2 (Supp. 1994); WASH. REV. CODE ANN. § 64.06.020 (West Supp. 1995). In other states, disclosure is limited to matters such as underground storage tanks, hazardous materials, and other environmental concerns. Sellers in New Hampshire, for example, are required to disclose the presence of radon gas and lead paint, and information about water-supply and sewage-disposal systems. N.H. REV. STAT. ANN. §§ 477:4-a, -c (1992 & Supp. 1994). Many states have promulgated a standardized form for sellers to use. Some versions are more user-friendly than others, allowing sellers to provide information through check-offs rather than written narrative description. *Compare* WASH. REV. CODE ANN. § 64.06.020 (West Supp. 1995) *with* CAL. CIV. CODE § 1102.6 (West Supp. 1995).

192. California specifically excludes any duty to disclose the occurrence of an occupant's death more than three years before the date of the offer to purchase. CAL. CIV. CODE § 1710.2(a) (West Supp. 1995). In other jurisdictions, litigation will be necessary to determine how remote in time the disclosure duty extends.

193. *See supra* note 187 and accompanying text. Additionally, in some states, the rights granted to a purchaser under such a statute may be knowingly and explicitly waived by the parties to the contract of sale. *See, e.g.*, TENN. CODE ANN. § 66-5-202 (Supp. 1995); WASH. REV. CODE ANN. § 64.06.020 (West Supp. 1995); WIS. STAT. ANN. § 709.08 (West Supp. 1994). *Contra* MD. CODE ANN., REAL PROP. § 10-702(j) (Supp. 1995).

194. *See* Johnson v. Davis, 480 So. 2d 625, 629 (Fla. 1985) (holding that sellers' fraudulent concealment of roof problems entitled buyers to rescission of contract).

whether to disclose unfavorable information. From a client-counseling perspective, statutes and case law creating legal rights and remedies for nondisclosure of defective conditions lubricate the slippery slope by which vendors are converted into guarantors of the condition of property.

Doctrinally, statutory and common-law causes of action for nondisclosure require proof of actual personal knowledge of a material undisclosed defect.[195] As noted previously, however, seller knowledge has been allowed to be proven entirely by circumstantial evidence.[196] Courts are being urged to adopt a rule of constructive knowledge that the seller either knew, or should have known, about the defect before attempting to sell the property.[197] Carried to its logical conclusion, this doctrine may be expected to mutate into an implied warranty by all sellers of real property.[198]

As a practical matter, the combined impact of judicial decisions and legislative action has already shifted the burden of structural inspection from buyers to sellers. Before exposing property for sale, sellers are being advised to conduct, at their own expense, professional prelisting inspections in order to discover faults and defects of which they were not aware.[199] Although disclosure statutes do not expressly require independent property inspections, they do encourage the practice by relieving sellers of liability for errors or inaccuracies that are based on reports by home inspectors or other experts.[200]

While the occasional buyer may be willing to accept a seller's disclosure and professional inspection report, most buyers will repeat the

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195. W. PAGE KEETON, PROSSER & KEETON ON TORTS §§ 107–110 (5th ed. 1984); *see also, e.g.*, MICH. COMP. LAWS § 565.955 (Supp. 1995); OHIO REV. CODE ANN. § 5302.30 (Anderson Supp. 1994); WASH. REV. CODE ANN. § 64.06.050 (West Supp. 1995).

196. *See supra* note 121.

197. *Compare* Anderson v. Harper, 622 A.2d 319, 323 (Pa. Super. Ct. 1993) (holding that a seller who repaired a faulty septic system without obtaining required permits could not assume latent and dangerous condition had been corrected and owed duty to purchasers to disclose) *with* Barab v. Plumleigh, 853 P.2d 635, 639 (Idaho Ct. App. 1993) (holding that sellers who visited Sun Valley vacation home approximately five times in seven years of ownership, and used kindling and newspaper to ignite logs in wood stove, were not liable for failure to disclose defective propane lighter).

198. The trend is proceeding exactly as forecast a decade ago by Chief Justice Boyd of the Alabama Supreme Court. Johnson v. Davis, 480 So. 2d 625, 631 (Fla. 1985) (Boyd, C.J., dissenting).

199. Robert J. Bruss, *How Sellers and Their Agents Can Avoid Lawsuits, Give Buyers Written Disclosures of All Home Defects and Consider Offering a One-Year Home Warranty*, CHI. TRIB., Jan. 19, 1995, at YM5.

200. *E.g.*, MD. CODE ANN., REAL PROP. §§ 10-702(d)(4), (h)(3) (Supp. 1995).

process by hiring their own inspectors,[201] who will typically discover additional defects.[202] This duplication of effort maximizes the parties' joint transaction costs, leaving the professional property inspection industry as the principal, albeit unintended, beneficiary of the erosion of the doctrine of caveat emptor.[203] The home warranty services industry is another unintended beneficiary of this erosion process. Buyers are being advised to insist that sellers purchase warranties covering repairs to heating, plumbing, and electrical systems, and roof and other structural components for the year after closing.[204] The importance of these warranties is certainly not downplayed by the brokerage industry. In the intense competition for listings, one brokerage firm even promotes "seller's litigation protection," by offering to pay for home warranty programs.[205]

The insurance industry is the third unintended beneficiary of the erosion of the doctrine of caveat emptor. Fear of liability has given rise to a new insurance product commonly known as "errors and omissions" insurance.[206] This type of insurance covers the cost of investi-

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201. In addition, most real estate agents recommend that sellers conduct a professional radon inspection, even if buyers order their own. Charles, *supra* note 110.

202. Seller disclosure does not replace the need for buyers to conduct property inspections for several reasons. First, disclosure is limited by the extent of the seller's own knowledge about the condition of the subject property, which may be imperfect. In the absence of actual personal knowledge, the seller is not liable for any error, omission, or inaccuracy. Second, some state disclosure statutes limit the scope of liability for negligent disclosure to defective conditions that are not readily observable. *See supra* note 191. Third, the seller is not liable for any error or inaccuracy with respect to information provided by a state or local governmental agency, or licensed person (*e.g.*, engineer, surveyor, geologist, exterminator) working within an area of expertise. *See supra* text accompanying note 200. Finally, the consequences visited upon the seller for violation of the statute may not fully protect the purchaser. For example, a transfer of property may not be invalidated solely by reason of failure to comply with required disclosure. CAL. CIV. CODE 1102.13 (West Supp. 1995). *But see* OHIO REV. CODE ANN. § 5302.30(K)(2) (Anderson Supp. 1994) (expressly granting rescission).

203. Independent professional inspections occur in nearly 60% of California home sales, up from less than 20% before enactment of that state's disclosure statute. Linda Lipman, *Inspector's Eye*, SAN DIEGO UNION-TRIB., Dec. 19, 1993, at H1. *See also Home Inspections Give Home Buyers and Sellers Peace of Mind*, BUS. WIRE, May 11, 1994.

204. Robert J. Bruss, *Don't Be in Hurry to Buy As-Is Home*, TAMPA TRIB., May 27, 1995, at H8; H. Jane Lehman, *New Insurance Covers Home Sellers; Policies Protect Against Lawsuits, but Critics Question Worth*, WASH. POST, Jan. 15, 1994, at F1.

205. *See* Prudential Voges Realtors Advertisement Tearsheet (on file with author). According to the results of one recent survey, 85% of California real estate agents would advise sellers to provide a home warranty. *Home Warranty Lawsuits: Home Warranties Recommended to Provide Protection Against Rising Lawsuits*, BUS. WIRE, May 16, 1994.

206. Homeowners Marketing Services, Inc., a Hollywood, Florida-based company, introduced this type of insurance within the past two years and remains its only source. Lorraine Mirabella, *Disclosure Law Spawns Home Sellers Insurance*, BALT. SUN, May 29, 1994, at K1.

gating, settling, or defending claims based on inadvertent failure to disclose defective conditions, and is available only to sellers who list their property with real estate agents who are themselves insured.[207] A basic policy is offered as part of the package of brokerage services[208] at no additional cost to sellers, and sellers are encouraged to purchase expanded coverage at their own expense.[209]

It is no secret that the real estate sales industry was the principal intended beneficiary of state disclosure laws.[210] The effect of these "broker protection acts" has been to shield real estate agents from liability to purchasers for misstatements and omissions by sellers in complying with their statutory disclosure obligation.[211] The AIDS issue caught conscientious real estate brokers squarely, and painfully, on the horns of a profound dilemma: suffer potential liability to either the purchaser for nondisclosure of an arguably material fact,[212] or to the seller for violation of federal privacy laws against discrimination based on handicap.[213]

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207. Lehman, *supra* note 204; *see also* Michael Gisriel, *Disclaimer Route Favored by Many Realty Agents*, BALT. SUN, Jan. 29, 1995, at L11.

208. The cost to the broker for the basic $25,000 coverage (subject to a $5,000 deductible) is $10 to $30 per client. Lehman, *supra* note 204.

209. For an additional $200 premium payable at closing, sellers may purchase $100,000 of coverage and reduce the deductible to $1,000. *Kiplinger's Money Power Laws Beefing Up After-Sale House Liability*, CHARLESTON GAZETTE, Aug. 9, 1994, at D4. According to one estimate, 20% of sellers who are offered the basic package elect to purchase expanded coverage. Mirabella, *supra* note 206.

210. Loughrin v. Superior Court, 19 Cal. Rptr. 2d 161, 164 (Ct. App. 1993) ("The beneficiaries of the [disclosure] statute were individual buyers of real estate and brokers representing both buyers and sellers."); Bill Lubinger, *Disclosure Rule Rings False Alarm*, PLAIN DEALER (Cleveland), June 26, 1994, at E1.

211. Some states require, as a condition to absolving brokers from disclosure liability, that brokers inform sellers of their statutory disclosure obligation. *See, e.g.*, TENN. CODE ANN. § 66-5-206 (Supp. 1995); VA. CODE ANN. § 55-523 (Michie Supp. 1994).

212. *See supra* text accompanying notes 160-161 and *infra* note 215.

213. Federal law prohibits discrimination on the basis of handicap in the sale or rental of housing. Section 6(a) of the Fair Housing Act makes it unlawful to

> discriminate in the sale or rental, or to otherwise make unavailable or deny, a dwelling to any buyer or renter because of a handicap of (A) that buyer or renter; (B) a person residing in or intending to reside in that dwelling after it is so sold, rented, or made available; or (C) any person associated with that buyer or renter.

42 U.S.C. § 3604(f)(1) (1988). The Fair Housing Act's definition of "handicap" comprehends infection with the AIDS virus. 24 C.F.R. § 100.201(a)(2) (1995); *see also* H.R. REP. No. 711, 100th Cong., 2d Sess. 18 (1988), *reprinted in* 1988 U.S.C.C.A.N. 2173, 2179. However, the protections of the Act appear to extend only to discrimination against buyers and renters, not sellers. Accordingly, it is not at all clear that the Act would prevent disclosure to prospective purchasers of a previous occupant's medical condition. Paula C. Murray, *AIDS, Ghosts, Murder: Must Real Estate Brokers and Sellers Disclose?*, 27 WAKE FOREST L. REV. 689, 701-06 (1992).

Failure to respond to a direct question whether the seller was an AIDS patient remains problematic. By governmental agency regulation, the state of Washington specifically pro-

The hysteria surrounding AIDS coincided with the breakdown of the privity barrier that had once effectively protected brokers from liability for nondisclosure of information to purchasers in residential real estate transactions. It was accepted that brokers' fiduciary duty of loyalty and full disclosure ran only to their seller principals. By the 1980s, however, courts began to acknowledge that real estate brokers, whose product was entirely information, may be liable for negligent misrepresentation and fraudulent nondisclosure to buyers.[214]

This set of circumstances led the real estate brokerage industry to mobilize itself into action.[215] Obligated by the strict fiduciary duty to subsume their self-interest and act in the best interest of vendors, members of the industry collectively opted for self-protection. Intense lobbying in some states by the politically powerful National Association of Realtors and state brokers' associations has succeeded in statutorily limiting the type of disclosure required by real estate agents.[216]

This successful lobbying is aptly illustrated when one notes the timing and legislative history of California's disclosure statute, largely the result of a 1984 appellate decision imposing liability on a broker for failing to competently inspect property and disclose its defective condition to a purchaser.[217] Within a year of this decision, state lawmakers enacted remedial legislation, sponsored by the California

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hibits disclosure of a previous resident's AIDS condition, even in response to a direct question. WASHINGTON STATE HUMAN RIGHTS COMM'N, STAFF POLICY GUIDELINES, AIDS AND REAL ESTATE TRANSACTIONS (Dec. 1986), *cited in* Parker, *supra* note 72, at 26 n.37.

214. Kings Motor Oils, Inc. v. Aviation Petroleum, Inc., No. 91 C 8028, 1993 U.S. Dist. LEXIS 8257, at *12 (N.D. Ill. June 16, 1993); Easton v. Strassburger, 199 Cal. Rptr. 383, 387-91 (Ct. App. 1984).

215. The industry obtained relief in various forms. On May 9, 1990, the General Counsel of the Department of Housing and Urban Development (HUD), Frank Keating, responding to an inquiry from the National Association of Realtors, opined that "unsolicited statements made by a real estate broker or agent that a current or previous occupant of the property has AIDS would violate [the Federal Fair Housing Act]. A broker's unsolicited statements to a prospective buyer or renter would indicate a discriminatory preference or limitation based on handicap." Robert D. Butters, *HUD Says AIDS Disclosure Can Violate Title VIII*, 1 FOR THE RECORD (National Ass'n of Realtors, Chicago, Ill.), Fall 1990, at 2 (quoting Frank Keating, General Counsel, HUD). An interpretation of state statutory or common law that an occupant's AIDS condition was a material fact imposing an affirmative duty on brokers to investigate and disclose would likely be preempted by federal law. *Id.* Mr. Keating further advised that, if asked about an occupant's AIDS condition, brokers should decline to respond. *Id.*

216. Murray, *supra* note 141, at 65; Bradley Inman, *New Laws to Forestall Loan Fraud*, SAN DIEGO UNION-TRIB., Oct. 9, 1994, at H13.

217. *Easton*, 199 Cal. Rptr. at 383. In *Easton*, a portion of the house was built on fill dirt that had not been properly engineered and compacted. *Id.* at 385. Landslides caused by massive earth movement destroyed a portion of the driveway shortly after closing, and wall cracks and warped doorways resulted from subsequent settling. *Id.* The estimated cost to repair and stabilize the property exceeded its purchase price. *Id.*

Association of Realtors,[218] that clarified the type of inspection brokers would be expected to conduct.[219] The following year the legislature enacted a second bill requiring sellers to complete a detailed disclosure statement.[220]

Viewed in the most favorable light possible, state disclosure statutes represent a long overdue attempt by the real estate brokerage industry and the bar to reconcile the divergent perspectives on the land conveyancing process held by members of their respective professions. Attorneys have always considered contract formation to be the decisive event in real estate transactions, with the contract of sale being the critical document. Brokers, on the other hand, have long infuriated real estate lawyers by encouraging the parties to execute a contract prior to seeking legal representation, leaving clients to arrive in the law office already contractually bound.

To some extent, the brokers' attitude reflects a sinister desire to keep parties and lawyers apart. In the brokers' traditional worldview, premature consultation with lawyers will, at best, interfere with the sales momentum and delay contract formation. At worst, an attorney is likely to kill the deal by unnecessarily directing the parties' attention to the remote contingencies (for example, risk of loss from fire or other casualty) that attorneys, by their training, feel compelled to raise.[221]

It is ironic, therefore, that attorneys may be disclosure statutes' final, and least intended, beneficiaries. Broker involvement in complying with statutory disclosure would defeat its principal purpose by exposing them to liability for omissions, inaccuracies, and misstatements. In states where disclosure forms provide for seller indemnity against broker liability,[222] it would be a conflict of interest for brokers

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218. Loughrin v. Superior Court, 19 Cal. Rptr. 2d 161, 164 (Ct. App. 1993).

219. The scope of investigation excluded matters "reasonably and normally inaccessible to such an inspection." CAL. CIV. CODE § 2079.3 (West Supp. 1995).

220. *Id.* §§ 1102–1102.15.

221. In this author's opinion, there is also a more charitable explanation: Real estate brokers and lawyers have tended to view the purpose of the real estate contract of sale very differently. To attorneys, a contract represents the consummation of a long process of negotiation and transfer of essential information about the parties and the property. In other words, once the parties have a contract, they have a deal. To brokers, a contract reflects merely a psychological commitment to undertake the often long and tedious process of back-and-forth renegotiation of the deal as information becomes available to the buyer during the executory period. In other words, once the parties have a contract, they are poised to begin to make a deal.

222. *See, e.g.*, MISS. CODE ANN. § 89-1-509 (Supp. 1995).

to participate in the disclosure process.[223] Furthermore, listing agents are advised not to assist sellers in completing disclosure forms, so most sellers will experience a vague sense of abandonment at an important stage in the process.[224] Additionally, the standardized forms warn that their completion subjects sellers to legal consequences.[225] As a result of these developments, at least some sellers will likely feel the need to fill the "counseling vacuum" by consulting with attorneys for assistance in complying with disclosure obligations.[226]

Disclosure statutes, like statutes of frauds before them, thus offer the potential for serving the important channelling function of directing sellers to sources of legal advice at a meaningful time in the transaction process.[227] If they encourage sellers to consult attorneys, the statutes will inadvertently accomplish the preventive law objective of uncovering points of disagreement, ambiguities, mistakes, and omissions of detail, which may then be corrected prior to contract execution.[228] By focusing the parties' attention on the significant legal issues involved in the contract formation phase of the land conveyancing process, and by placing the transfer of information up-front where it can be a factor in negotiating the purchase price, disclosure statutes may avoid the kind of nasty surprises that lead to disputes both before and after the closing of real estate transactions.

CONCLUSION

The doctrine of caveat emptor in the sale of real property has given way to a societal expectation that sellers disclose material information that cannot reasonably be acquired by buyers without significant investment. This policy serves the remedial purpose of enlightening purchasers laboring under serious misapprehension so they may rationally assess the true level of risk involved in the bargain. Nevertheless, a practice is evolving by which sellers are expected to incur costs to generate information for the purpose of disclosure.

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223. *See* Harris Ominsky, *How to Handle Residential Real Estate Disclosure*, 10 PRAC. REAL EST. LAW. 65, 67-68 (May 1994).

224. Hal Porter, *New Disclosure Laws for Home Sellers*, HOME MECHANIX, Mar. 1994, at 28.

225. *See, e.g.*, ILL. ANN. STAT. ch. 765, para. 77/35 (Smith-Hurd Supp. 1995); MICH. COMP. LAWS § 565.957 (Supp. 1995). Standardized forms in some states specifically suggest that seller may wish to consult with a lawyer in connection with the disclosure process. *See, e.g.*, CAL. CIV. CODE § 1102.6 (West Supp. 1995); ILL. ANN. STAT. ch. 765, para. 77/35 (Smith-Hurd Supp. 1995).

226. Deborah L. Wood, *Sellers Must Reveal Troubles—Or Else; Law Protects Buyers from Known Defects*, CHI. SUN-TIMES, Oct. 9, 1994, at 3.

227. Joseph M. Perillo, *The Statute of Frauds in the Light of the Functions and Dysfunctions of Form*, 43 FORDHAM L. REV. 39, 57-58 (1974).

228. *Id.* at 57.

Approximately half the states have recently enacted mandatory information-disclosure statutes.[229] These statutes, ostensibly designed to enhance the information available to purchasers, in fact represent a legislative reaction, inspired by the real estate brokerage industry, to the uncontrolled erosion of the doctrine of caveat emptor by common-law development.

Economic efficiency dictates that transaction costs of the land conveyancing process be limited. The first generation of state disclosure statutes violates this principle. These statutes encourage the production of unnecessary and duplicative information, exacerbating the already costly burden of real estate settlement.[230] In the aggregate, it may be less costly for society as a whole simply to absorb the loss caused by allowing occasional unintentional misrepresentation to continue.[231]

Fortunately, there is an alternative. In an interesting variation, three states have embraced a market-driven approach.[232] Sellers of residential real property in Maryland, Oregon, and Virginia are offered an option: A seller may elect to furnish either a statement describing known latent defects or a disclaimer informing the prospective purchaser that the seller is making no representations or warranties, and is selling the property "as is" with all existing defects.[233] It remains to be seen whether a seller's decision to disclose or disclaim will affect marketability.[234] Presumably, absent a sufficient explana-

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229. *See supra* note 187 and accompanying text.

230. Brokers, loan officers, appraisers, title assurance personnel, surveyors, and escrow agents must all be compensated for their participation in the land conveyancing process. As a result, total settlement costs average 10% of contract sales price. PAUL GOLDSTEIN & GERALD KORNGOLD, REAL ESTATE TRANSACTIONS 12 (3d ed. 1993). Each incremental increase effectively prices some buyers out of the market, and forces others to seek lower priced housing that is less suited to the needs of their household. *Id.* at 13.

231. By following the advice they receive to obtain a pre-listing structural inspection, radon test, warranty, and errors and omissions insurance in order to safely comply with their statutory disclosure obligations, risk-averse sellers will incur additional transaction costs of about $1200. *See supra* notes 199-209 and accompanying text. According to a recent estimate by the National Association of Realtors, 3.5 million previously owned single family homes are sold annually. *Used-Home Sales Sag to Hit a 2-Year Low*, ORLANDO SENTINEL, Mar. 28, 1995, at B1. If the brokerage industry succeeds in its nationwide lobbying efforts, statutory disclosure carries a potential price tag of $4.2 billion on the basis of the above estimates.

232. MD. CODE ANN., REAL PROP. § 10-702 (Supp. 1995); OR. REV. STAT. ANN. §§ 105.465–.490 (Supp. 1994); VA. CODE ANN. §§ 55-517 to -525 (Michie Supp. 1994).

233. MD. CODE ANN., REAL PROP. § 10-702(b)(1) (Supp. 1995); OR. REV. STAT. ANN. § 105.465(2) (Supp. 1994); VA. CODE ANN. § 55-519 (Michie Supp. 1994).

234. Given the choice between disclosing or disclaiming, one-fourth of sellers doing business at one Maryland realty company were opting to give the disclaimer during the

tion, buyers will be suspicious of property offered for sale without disclosure.

The Maryland, Oregon, and Virginia statutes provide a model for second generation disclosure statutes consistent with voluntary policies recently adopted in other English-speaking jurisdictions.[235] To the extent other states follow this example, the legacy of the statutory disclosure experiment will have been the revival of the doctrine of caveat emptor—with a twist. Sellers interested in purchase price maximization may elect to incur the additional expense of generating and disclosing relevant information. Or, sellers will be required to inform all buyers what sophisticated purchasers knew all along: There is information about this property that you do not know; you should assume the worst, and govern yourself accordingly in contract negotiations. In other words, buyer beware.

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new statute's first few months of operation. Adriane B. Miller, *Disclosure Law Mystifies Market*, BALT. SUN, May 1, 1994, at L1.

235. *See supra* notes 78-80, 85-87 and accompanying text.