

1969

Federal Regulation of Land Sales: Full Disclosure Comes Down to Earth

Ronald J. Coffey

James d'A. Welch

Follow this and additional works at: <https://scholarlycommons.law.case.edu/caselrev>



Part of the [Law Commons](#)

Recommended Citation

Ronald J. Coffey and James d'A. Welch, *Federal Regulation of Land Sales: Full Disclosure Comes Down to Earth*, 21 Case W. Res. L. Rev. 5 (1969)

Available at: <https://scholarlycommons.law.case.edu/caselrev/vol21/iss1/4>

This Article is brought to you for free and open access by the Student Journals at Case Western Reserve University School of Law Scholarly Commons. It has been accepted for inclusion in Case Western Reserve Law Review by an authorized administrator of Case Western Reserve University School of Law Scholarly Commons.

Federal Regulation of Land Sales: Full Disclosure Comes Down to Earth

Ronald J. Coffey

James d'A. Welch

I. INTRODUCTION

IT IS ARGUABLE — if not beyond cavil — that state and federal securities laws have effectively diminished the opportunities for reaping overnight bonanza profits from the sale of “blue sky” to uninformed or misinformed investors.¹ However, the “security” concept has not been developed to embrace all the tantalizing “pies-in-the-sky” served up by poorly financed, inept, or downright mendacious promoters. Outside the protective purview of securities regulation falls the burgeoning, multifaceted real estate business,² encompassing the sale of a house between neighbors as well as the sight-unseen marketing of wilderness by “boilerroom” pitch-

THE AUTHORS: RONALD J. COFFEY (A.B., Xavier University; LL.B., University of Cincinnati; LL.M., Harvard University) is an Associate Professor of Law at Case Western Reserve University and is admitted to the Ohio and Federal Bars. His teaching specialties are *Corporations*, *Securities Regulation*, and *Business Planning*. JAMES D'A. WELCH (B.A., Colorado College; J.D., Case Western Reserve University) is a practicing attorney in Cleveland, Ohio and is admitted to the Ohio Bar.

men who dun their citified and susceptible prospects by WATS telephone.³ Between these extremes lie the many forms of real estate mongering, some innocent and straightforward enough, but others so fraught with opportunities for sharp practice or outright fraud that legislative reaction, in retrospect, seems to have been almost inevitable.

¹ Regarding the effects of disclosure in the federal scheme, see SEC, REPORT ON DISCLOSURE TO INVESTORS — A REAPPRAISAL OF FEDERAL ADMINISTRATIVE POLICIES UNDER THE '33 AND '34 ACTS 46-54 (CCH ed. 1969) [hereinafter cited as WHEAT REPORT].

² Not all sales of real estate are beyond the ambit of securities regulation. In fact, many real property transactions which have escaped the notice of securities agencies might very well constitute securities. See text accompanying notes 42-53 *infra*.

³ For the uninitiated, a “boiler room” typically consists of a group of high pressure salesmen who spend their days making hard sell telephone calls to prospective purchasers of land. The land promoters frequently use the “wide area telephone service” (WATS), an arrangement whereby they are permitted to make any number of long

Congress' latest bout with the real estate industry began with hearings before the Senate Special Committee on Aging in early 1963.⁴ The testimony laid bare an industry, ambitious and adolescent, actively engaged in marketing raw and semideveloped subdivided land to the "sunset set" by means of the mails, magazines, newspapers, and personal or telephone solicitations.⁵ The origin of the 20th century land sales phenomenon was traced to a short-lived boom during the 1920's.⁶ Revitalized in the forties, the industry has attained spectacular proportions over the last fifteen years.⁷ From the 1963 Hearings, one thing was abundantly clear: Untold thousands were being flimflammed into purchasing parcels which could not be inhabited without serious threat of death from either thirst or drowning.⁸ While the volume of sight-unseen land sales was uncertain, it was pegged at \$500 million annually in 1963⁹ — a figure which was to be revised to \$700 million in 1964¹⁰ and to \$1 billion in 1967.¹¹

Early in the federal legislative history, and throughout the hearings and floor proceedings thereafter, one finds repeated agreement that abuses in land sales could be laid at the door of only a minority of the industry. The precise ratio of bad apples to good never

distance calls within given boundaries for a flat monthly fee. See SENATE SUBCOMM. ON FRAUDS AND MISREPRESENTATIONS AFFECTING THE ELDERLY, 89TH CONG., 1ST SESS., REPORT ON FRAUDS AND DECEPTIONS AFFECTING THE ELDERLY 36-37 (Comm. Print 1965) [hereinafter cited as 1965 REPORT].

⁴ *Hearings Before the Senate Special Comm. on Aging*, 88th Cong., 1st Sess. (1963) [hereinafter cited as 1963 *Hearings*].

⁵ *Id.* at 141-50, 162, 184-235, 238-47, 253, 299-310, 482-89. Thus, while the term "mail-order" sales was used to describe the marketing process, that phrase was simply a shorthand convention for referring to many modes of merchandising property sight (and site) unseen. As the hearings wore on over the years, legislative interest expanded to encompass the sale of undeveloped or semideveloped land which the buyer had been given an opportunity to "inspect." See text accompanying notes 20-25 *infra*.

⁶ *Id.* at 302-03, quoting Address by Attorney General Walter F. Mondale, National Association of License Law Officials, in Minneapolis, May 10, 1962.

⁷ *Id.* at 302. It has been asserted that the American land sales boom was set off by Christopher Columbus' letters to Ferdinand and Isabella. *Hearings Before the Subcomm. on Frauds and Misrepresentations Affecting the Elderly of the Senate Special Comm. on Aging*, 88th Cong., 2d Sess. 343 (1964) [hereinafter cited as 1964 *Hearings*]. Two of history's most famous land promoters, George and Lawrence Washington, sold lots in Virginia on the installment plan. *Id.* at 344. The year 1962 appears to be when state authorities decided to take concerted action against land promotion activities. 1963 *Hearings* 230.

⁸ 1963 *Hearings* 148-49.

⁹ *Id.* at 291.

¹⁰ 1964 *Hearings* 3.

¹¹ *Hearings on S. 275 Before the Subcomm. on Securities of the Senate Comm. on Banking and Currency*, 90th Cong., 1st Sess. 2 (1967) [hereinafter cited as 1967 *Hearings*].

became clear. However, testimony indicates that overreaching was more prevalent than anyone, including Congress, was willing to admit.¹² Moreover, while elderly purchasers were the initial concern of congressional inquiry, it soon became clear that a much broader group was being exploited by the disreputable sector of the real estate industry.¹³

And so, in 1963, the stage was set for a five-year period of legislative rumination, during which the congressional mind (or, more precisely, the minds of that smaller group of senators who pondered the need for land sales legislation) would reevaluate the basic philosophies of protective regulation — the same philosophies which were examined nearly 40 years ago in connection with the passage of the federal securities laws. What follows is an elaboration of the factual and policy antecedents which appear to have influenced Congress' deliberations in reaching a solution to the land sales problem. It is only through an appreciation of this background that one can savor the true intent and meaning of the final legislative product — the Interstate Land Sales Full Disclosure Act.¹⁴

II. LEGISLATIVE AIMS AND POLICIES

A. *Offensive Practices*

Congressional concern over real estate sales practices seems to have emanated from several principal sources. First, the physical state or character of the land being sold clearly constituted a worrisome factor. The Senate hearings were dominated by testimony and discussion concerning large tracts of utterly raw "investment acreage" and primitively subdivided "homesites."¹⁵ It is this type of land which is least likely, in its natural state, to serve as a comfortable residential environment.¹⁶ Large tracts of undeveloped

¹² "Many of the offerings are good merchandise, fairly presented. Numerically, more are not." Letter from Robert R. Peacock to Harrison A. Williams, Jan. 11, 1963, in 1963 *Hearings* 142. "[W]hile it is a cliché that every industry is 90 percent legitimate and dangers are posed only by a small minority on the periphery of the industry, I do not believe this is true of the mail-order real estate industry." 1964 *Hearings* 90.

¹³ For example, servicemen abroad. See 1963 *Hearings* 188. By 1966, it was clear that there had been a conscious broadening of interest. *Hearings on S. 2672 Before the Subcomm. on Securities of the Senate Comm. on Banking and Currency*, 89th Cong., 2d Sess. 2 (1966) [hereinafter cited as 1966 *Hearings*].

¹⁴ 15 U.S.C.A. §§ 1701-20 (Supp. 1969).

¹⁵ A distinction is drawn between "homesites," which are offered as potential building parcels, and "investment acreage," which is offered as an appreciation speculation. See 1966 *Hearings* 7, 120; 1965 REPORT 33.

¹⁶ Vast acreage offerings frequently involve "swamps, deserts, high arid plateaus, mountains, remote valleys, and — in some cases — actual jungles or lava beds outside

land also present the greatest uncertainty and risk in terms of future development and use. Even where there are no serious barriers to human habitation — such as heat so intense and water so scarce that even jackrabbits carry canteens¹⁷ — the costs of opening up an undeveloped expanse may be enormous, requiring the energies of a skilled and well-financed developer. However, while the sale of bulk land located in hostile settings presents the most extreme case for concern, it is clear that congressional solicitude extended to purchasers of other types of property as well.¹⁸ Congress, responding at first to febrile outcries against swamp and desert merchants, gradually came to realize that many of the evils which attend the marketing of remote land might also pervade the sale of subdivided agricultural tracts on the fringe of a large city.¹⁹

Second, it was obvious that sales methods bulked large as a cause for congressional intrusion into the real estate sector. Perhaps the most disturbing aspect of the marketing process was the widespread use of sight-unseen sales tactics. Mail-order, buy-by-telephone, and “sales party” techniques were viewed as enhancing the opportunities for fraud and sharp practice.²⁰ If a buyer must rely on second-hand descriptions, he quite naturally becomes easy prey for those who would lure him into a deal by means of half-truths or omissions, not to mention lies. And, where a substantial distance separates the potential buyer from the property, he may be more receptive (especially if his resources are limited) to suggestions that the seller handle the “legal technicalities” of the sale. Thus, not only may the nature of the land lie veiled behind the seller’s representations, but the process of acquisition and the quality of title may also be shrouded by the seller’s unfettered control over matters relating to transfer.²¹ Further, it was understood that the sight-unseen problem, as such, did not depend on whether the

the continental United States.” See 113 CONG. REC. 315, 3529 (1967) (remarks of Senator Williams).

¹⁷ 1963 *Hearings* 203.

¹⁸ When introducing an earlier version (S.275, 90th Cong., 1st Sess. (1967), of the Act in 1967, Senator Williams of New Jersey stated: “We are concerned not only with retirement havens, but also with other kinds of promotion. Installment buyers, for example, are now purchasing vacation lots, undeveloped ‘investment acreage,’ *homesites in developing communities, and even farmland . . .*” 113 CONG. REC. 315 (1967) (emphasis added).

¹⁹ It is noteworthy that an “urban proximity” exemption suggested in 1963 was never incorporated into the Act. Compare 1963 *Hearings* 304-05, with 1966 *Hearings* 303-04.

²⁰ 1966 *Hearings* 46-51.

²¹ *Id.* at 46-50, 366-67.

land and the purchaser were in two different states.²² Here again, however, the focus of investigation, narrow at first, widened as the hearings wore on. Several witnesses noted that on-site inspection by a prospective purchaser might not, in practice as well as theory, obviate the need for special protection where investment acreage or subdivided parcels are involved.²³ A first hand look, it was argued, does not reveal the land's legal attributes, its hidden physical characteristics, or its surrounding environment at times other than when the prospective buyer observes it.²⁴ Moreover, the inspecting purchaser, frequently away from home and anxious to return, is more vulnerable to the "make up your mind now" selling pressures of the hustling salesman.²⁵

A third factor troubling the legislative conscience was the land-use planning problem raised by the ill-controlled marketing of thousands upon thousands of subdivided parcels, many of which were unfit for habitation either presently or in the near future.²⁶ When a large tract of marginal land is subdivided into hundreds of small lots by means of the unimaginative grid pattern, a chain reaction of planning problems is triggered. A tremendous demand is immediately imposed upon local government for the speedy development of proper drainage, sanitation, and roads, together with adequate public utilities and facilities such as schools, police, and fire protection. But the area generally does not have a tax base sufficient to support such rapid expansion and improvement. This unfortunate state of affairs may lead to haphazard and patchwork community growth. It could also stymie development altogether. And, worst of all, it is extremely difficult for a new developer to reassemble the tract for some sensible use. The fast-buck developer, who originally subdivided the tract into thousands of non-viable lots, has created a "legal wasteland"²⁷ — a long-term clog on planning for a high quality living environment.

Fourth, Congress apparently felt that something had to be done to restore public confidence in the land sales industry. When Senator Williams introduced the first of the Act's predecessors in 1965,

²² *Id.* at 65-67.

²³ *Id.* at 105, 131-32, 303.

²⁴ 1967 *Hearings* 167.

²⁵ 1964 *Hearings* 168.

²⁶ 1965 REPORT 40; 1966 *Hearings* 44.

²⁷ See 1964 *Hearings* 93, 157-58. "A situation therefore can develop which precludes use of the land by the small parcel owners; prohibits reassembly for either a private or public purpose; and, indeed, makes it impractical even for agricultural pursuits." *Id.* at 158.

he sounded the theme, harking back to the birth of the Securities Act of 1933 and the nadir to which public confidence in the securities industry had fallen at that time.²⁸ The rationale was repeated by Senator Williams in 1967²⁹ and referred to in that same year by Manuel Cohen, then Chairman of the Securities and Exchange Commission (SEC).³⁰ Of course, the fear of waning public confidence stems from a recognition of the fact that land development will not proceed apace if investor interest flags.³¹ Implicit also is the assumption that the business of subdividing and selling small parcels of land is a national good, which is to be encouraged in its most desirable manifestations.³² Hence the classic legislative dilemma: how to regulate an industry in order to save it — how to accommodate the antinomies that result from a desire to purge abuses, without, at the same time, imposing stifling regulatory burdens.

The fifth factor at work in the legislative deliberations was also based on the apparent feeling that mass marketing of lots in undeveloped tracts is, shorn of its reprehensible aspects, a basically useful economic activity. Senator Williams, a chief exponent of federal legislation, was wont to point out how corrective laws would place reputable and ethical developers on a par with the so-called hucksters and bilkers.³³ The rationale is that developers who use full and accurate selling literature are put at a competitive disadvantage because detailed informational material costs more to prepare and because full disclosure gives the potential buyer a sporting chance to bargain intelligently with the developer's sales agent — a circumstance that may require an extended selling effort or result in a lower selling price.

The preceding array of industry ills and evils was in the forefront of the congressional dialogue which sprang to life in 1963 and came to fruition in 1968. Along the way, of course, the laws already on the books had to be examined to ascertain whether reformulation of "on the shelf" nostrums might provide a cure, or whether stronger (or at least novel) medicine should be developed.

²⁸ 111 CONG. REC. 27,310-11 (1965).

²⁹ 113 CONG. REC. 315 (1967).

³⁰ 1966 *Hearings* 86.

³¹ See 1964 *Hearings* 2; 1965 REPORT 29.

³² 1965 REPORT 29.

³³ 111 CONG. REC. 27,311 (1965); 113 CONG. REC. 3529 (1967).

B. Existing Protections

1. *Mail Fraud Statutes*.— During the 1963 Hearings, representatives of the Post Office Department described their line of attack against fraudulent land sales practices involving the mails.³⁴ The two important weapons in the mail fraud arsenal are the criminal sanction, providing fines and penalties for fraudulent use of the mails,³⁵ and the “fraud order” provision, which authorizes the Postmaster General, upon a finding that the mails are being used to conduct a fraudulent scheme, to direct local postmasters to intercept mail addressed to the perpetrator of the fraud, to return such mail to its senders, and to refuse payment of money orders and postal notes drawn to the order of the violator.³⁶ The mail fraud approach to solving land sales abuses was thought to be deficient in several respects. First, the mails, as contrasted with interstate facilities, have to be used as part of the scheme. Second, a rather specific intent to defraud must be demonstrated not only to obtain a criminal conviction (as one would expect), but also to justify the entry of a fraud order by the Post Office.³⁷ And, because considerable investigation must be made to build a case for specific intent, the transgressing promoter may be able to strew a great deal of wreckage in his path before he is brought up short.³⁸ Finally, it is small comfort to a defrauded buyer that his seller has been fined or jailed or that further mail solicitations have been blocked.³⁹

2. *Federal Trade Commission Act*.— The Federal Trade Commission (FTC) can proceed administratively against deceptive land sales literature under section 5 of the Federal Trade Commission Act (FTCA).⁴⁰ However, regardless of how cogent the case for provisional relief might be, the FTC is not authorized to issue tem-

³⁴ 1963 *Hearings* 235-58.

³⁵ 18 U.S.C. § 1341 (1964).

³⁶ 39 U.S.C. § 4005 (1964).

³⁷ *Reilly v. Pincuss*, 338 U.S. 269 (1949). See also 1963 *Hearings* 239-45.

³⁸ Senator Mondale (then Attorney General of Minnesota) in his testimony noted: “Time consuming criminal investigations and prosecutions are not a total ‘cure.’ Too often we are too late to prevent the victimizing of a large group of our public. Even the preventatives of postal fraud orders . . . do not provide complete protection. In the end it is little solace to the public who has lost millions of dollars that the culprit is now in jail or, that he can no longer operate under his present business label.” Statement of Attorney General Mondale of Minnesota, 1963 *Hearings* 301, quoting Remarks by Mr. Nathaniel Kossack, Chief of Fraud Section of Criminal Division of the Department of Justice, at the National Conference on Interstate Land Sales.

³⁹ 1967 *Hearings* 79-80.

⁴⁰ 15 U.S.C. § 45 (1964).

porary cease-and-desist orders to prevent the continuation of deceptive trade practices during administrative proceedings and judicial review of final orders.⁴¹ Like the mail fraud statutes, the FTCA process is not primarily prophylactic.

3. *Federal and State Securities Regulation.*— In order to invoke the protections of federal and state securities laws, it would be necessary to find that land sale transactions are "securities." Historically, except where state blue sky laws specifically refer to real estate transactions,⁴² the typical land agreement, at least the non-installment type, has not been generally thought of as a security.⁴³ Notwithstanding, certain dispositions of real estate may in fact possess all the elements of a security.⁴⁴ While William Cary and Manual Cohen, both prior Chairmen of the SEC, tended to gloss over the possibility that lump-sum and installment land sales agreements might well constitute securities under long-standing criteria,⁴⁵ it is likely that many of the transactions described at the hearings were subject to existing securities laws.⁴⁶ For example, certain lots were sold on the representation that oil explorations were being conducted in surrounding areas.⁴⁷ In such circumstances, it is likely that the purchase price included a component which represented the future, but yet unrealized success of an enterprise over which the buyers of lots exercised no control. All the indicia of a security are present in such a transaction, even where the purchaser acquires an immediate interest in the fee.⁴⁸ The same analysis should apply where a developer sells a lot at a price which is realistic only if he successfully completes all the improvements which he promises for the entire development. Here, the initial value furnished by the purchaser includes an element which is critically dependent on the success of the developer's own enterprise. In other words, the developer is actually using part of the purchase

⁴¹ 15 U.S.C. § 45(b)(C) (1964). See also 1964 Hearings 296; 1963 Hearings 287-92.

⁴² See, e.g., OHIO REV. CODE ANN. § 1707.01(B) (Page 1964).

⁴³ But see *Chaney v. Western States Title Ins. Co.*, 292 F. Supp. 376 (D. Utah 1968), where, apparently, a lump sum land sales agreement was held to be a security.

⁴⁴ See Coffey, *The Economic Realities of a "Security": Is There a More Meaningful Formula?*, 18 W. RES. L. REV. 367, 386-92 (1967).

⁴⁵ 1967 Hearings 51; 1966 Hearings 85; 1963 Hearings 487.

⁴⁶ 1966 Hearings 367-68; 1964 Hearings 326.

⁴⁷ 1966 Hearings 39.

⁴⁸ See Coffey, *supra* note 44, at 391-92. See also 1 L. LOSS, SECURITIES REGULATION 491-92 (2d ed. 1961), (Supp. 1969).

price to finance completion of developments which will ultimately make the lot worth what the buyer paid for it.⁴⁹

As for the so-called installment lot transactions, the testimony revealed that buyers were actually acquiring very little more than creditors' claims against the developers under the guise of multi-payment conditional sales contracts. To illustrate: The buyer's payments were not escrowed to guarantee their application against encumbrances; no contract was recorded; no title passed until all payments were made; the buyer was not entitled to possession until final payment was made; penalties were imposed for advance payment; and no title search or insurance were provided for.⁵⁰ Given these terms, it is difficult to characterize the purchaser's payments as much more than a loan to the developer. In essence, the developer is selling a debt instrument coupled with a specious commitment to repay by means of specific property. Such a transaction differs considerably from the installment sale of a residence, where the purchaser takes possession of the property, and the entire deal is viewed as a loan by the seller to the purchaser, with the vendor retaining title as security for payment.⁵¹

It remains unclear just why Chairmen Cary and Cohen gave such short shrift to the possible applicability of the securities laws to certain sales of lots, but their views can in no way remove the likelihood that such laws will continue to hang threateningly above the heads of those who peddle lots in a manner that calls for securities law protection. Thus, with the advent of the Interstate Land Sales Full Disclosure Act, certain developers may face double compliance requirements at the federal level.⁵² Moreover, it is unlikely that registration under the Securities Act of 1933 will satisfy the requirements of the Land Sales Act, or vice versa, since the former is aimed primarily at disclosure of facts about the issuing enterprise (here, the developer), while the latter is concerned principally with facts concerning the land which the developer is marketing. Furthermore, when lots are subject to both the securities laws and the Land Sales Act, the developer will face a rather

⁴⁹ One statement referred to sale of land at a premium as a "method of financing." See 1966 *Hearings* 74, 362-66. Indeed, it appears that some lots were being sold at 1000 times their present value. 1963 *Hearings* 309.

⁵⁰ 1966 *Hearings* 46-50, 366-68; 1965 REPORT 30-36.

⁵¹ See *Contract Buyers League v. F. & F. Inv.*, [Current Binder] CCH FED. SEC. L. REP. ¶ 92,417 (N.D. Ill. May 21, 1969) (installment conditional sale of residence occupied by the purchaser held not to be a security).

⁵² Perhaps dual registration will be required at the state level also, except in those cases where the state blue sky law is the only vehicle by which land sales are controlled.

frightening array of fraud remedies, each with its own peculiarities of application and interpretation.⁵³

In any event, the Senate committees were not satisfied that existing securities laws could afford adequate protection in the land sales context.

4. *State Regulation of Lot Sales.*— When discussing state land legislation, a distinction must be drawn between “land contract” sales statutes, which are directed toward regulation and disclosure of the contractual and property relationships between the vendor and vendee,⁵⁴ and lot sales regulation, which requires that the prospective purchaser be given a complete picture of the land he is about to buy. The latter type of state law is central to this discussion, although it must be realized that the “land contract” brand of legislation represents yet another form of regulation with which an *installment* lot seller may have to deal.⁵⁵

In 1963, the existence of state lot sales legislation was spotty and uneven, and remained so through the passage of the Land Sales Act. Many states had no such laws, and those that did differed considerably in approach.⁵⁶ In substance and content, state laws fell basically into three categories: those that required registration of land information;⁵⁷ those that required registration plus the use of administratively approved selling reports (in which the state agency might editorialize with respect to the quality of the land offered);⁵⁸ and those involving a combination of registration, use of property reports (editorialized or not), and administrative power to prohibit offerings which are not “fair, just, and equitable.”⁵⁹

Aside from the complete absence of legislation in certain jurisdictions and the substantive variation among existing state laws, there was the question of the extent to which a particular state is able or willing to apply its laws when the land offerings are interstate. There is not much difficulty where the “situs” state, *S* (the

⁵³ See text accompanying notes 274-379 *infra*.

⁵⁴ E.g., OHIO REV. CODE ANN. §§ 5313.01-.10 (Baldwin Supp. 1969).

⁵⁵ FED. RES. BD. REG. Z, 12 C.F.R. §§ 226.1-.12 34 Fed. Reg. 2002-11 (1969), will also apply where the installment contract truly constitutes the equivalent of a loan by the seller to the buyer. *Id.* § 226.2(z).

⁵⁶ For lists of states and types of laws, see 1967 *Hearings* 218; 1966 *Hearings* 53-54; 1965 REPORT 38-39; 1964 *Hearings* 320-33.

⁵⁷ See 1967 *Hearings* 218; 1966 *Hearings* 53-54; 1965 REPORT 38-39; 1964 *Hearings* 320-33.

⁵⁸ See 1967 *Hearings* 218; 1966 *Hearings* 53-54; 1965 REPORT 38-39; 1964 *Hearings* 320-33.

⁵⁹ See 1967 *Hearings* 218; 1966 *Hearings* 15, 53-54, 120; 1965 REPORT 38-39; 1964 *Hearings* 320-33.

state where the offered land is located), has a lot sales law and where both the developer and the offeree are located there. But even slight variants of this case — where the developer operates from another state, *D*, or where the offeree is in another state, *I* — raise problems of enforcement.⁶⁰ At the other end of the spectrum lies the case where the developer, operating from state *D*, makes his offer of land, located in situs state *S*, to offerees located in investor state *I*, which is the only one of the three having lot sales regulation. In such a fact pattern, *I* authorities will face the issues of: jurisdiction for service of process; jurisdiction to regulate (with its commerce clause implications); choice of law; full faith and credit; and practical enforcement.⁶¹ This lineup of thorny problems caused state authorities to cry out for federal legislation to solve the interstate puzzle.⁶² While California and New York, for example, claimed they had theoretical jurisdiction to regulate offers of lots emanating from other states,⁶³ they admitted that enforcement was a serious practical problem.⁶⁴

The intricacies of state law applicability to interstate transactions was further compounded by the peculiarities of the express coverage of certain statutes. To illustrate, the Florida law was applicable only to installment sales, not lump-sum purchases,⁶⁵ and the New Jersey law was specifically limited to sales completed within its borders.⁶⁶

Two major uniform state laws were adopted⁶⁷ in an attempt to encourage passage of legislation by more states, attain uniformity of substantive content, and unscramble some of the complexities of interstate coverage. As of 1968, however, satisfactory progress toward these goals had not been made — not, at least, in the opinion of Congress.

Besides the rather substantial lacunae in state legislation and the vexing problems of the interstate tangle, there is the question

⁶⁰ For instance, property reports required by the situs state might not be used by the developer when offering to residents of the investor state. 1967 *Hearings* 115-16.

⁶¹ See generally 1 L. LOSS, *supra* note 48, at 67-85. In connection with pending lot sales legislation, Massachusetts authorities prepared an interesting and thoughtful memorandum on jurisdictional problems. 1964 *Hearings* 312-33.

⁶² See 113 CONG. REC. 318 (1967); 1964 *Hearings* 254.

⁶³ 1966 *Hearings* 113, 121; 1964 *Hearings* 18-19.

⁶⁴ See notes 60-61 *supra*.

⁶⁵ 1966 *Hearings* 36-37.

⁶⁶ *Id.* at 47.

⁶⁷ UNIFORM LAND SALES PRACTICES ACT, published in 1967 *Hearings* 229-53; MODEL SUBDIVISION SALES CONTROL LAW, published in 1964 *Hearings* 335-38.

of the states' fiscal ability to administer and enforce lot sales laws. The blue sky law experience has taught that the best state statute may lie dormant without a well-financed agency to vivify it. The same point was made with respect to lot sales laws.⁶⁸

And so, despite industry attempts to portray the state system as an adequate source of protective legislation, the scene painted at the hearings was at best clouded and ambiguous.

5. *Industry Self-Regulation.*— Whenever an entire industry faces the prospect of sweeping new regulation at the federal level, the traditional and inevitable response seems to be a request for time to secure voluntary self-discipline. With respect to the Land Sales Act, it must be said that advocates of self-regulation had more than a sporting chance to initiate and establish industry standards in order to head off federal legislation. Indeed, Congress played a waiting game; five years intervened the commencement of hearings and the passage of the Act. Yet, at both ends of that period, the appraisal of industry efforts to correct abuses from within was the same — a dismal failure.⁶⁹ The more reputable operators, while publicly disfavoring federal legislation, probably did not care whether it was passed or not. They were informally furnishing purchasers with full disclosure already. The less reputable promoters, on the other hand, were certainly not willing to give up the slick trade practices which enabled them to compete on a shoe-string. Thus, the case of a house divided against itself.

C. *Federal Regulation: What Form Should It Take?*

From the foregoing, it is reasonably clear that in 1968 the time was ripe for *some kind* of federal legislation. In all fairness, it must be said that members of the senatorial committees, alarmed by the testimony which they had heard, were nonetheless sensitive to the policy arguments against regulative heavy-handedness in the field of land sales. As already noted, they viewed the industry as essentially beneficial to the economy.⁷⁰ They heard again, almost as an echo out of the thirties, the claim that the West would not have been won had modern legal strictures then been in force.⁷¹

⁶⁸ 1967 *Hearings* 80; 1966 *Hearings* 15, 132.

⁶⁹ 1966 *Hearings* 62-64, 127; 1965 *REPORT* 42-44; 1964 *Hearings* 89-90, 285.

⁷⁰ See text accompanying notes 31-32 *supra*. It is interesting to observe how hostilities subsided when certain industry witnesses convinced senators that their testimony constituted a good faith attempt to explain the risks and burdens of land development and the necessity for leeway in marketing practices. See 1966 *Hearings* 221-37.

⁷¹ See 1964 *Hearings* 239.

Moreover, they knew full well that state authorities were in a better position to inspect and control the sale of land, simply because of their physical proximity to the problem.⁷² However, it was equally clear that there existed some very substantial justifications for additional action at the federal level. Thus, the question was: What should the federal law look like? For those readers with securities law backgrounds, the following will read (if the preceding has not) like a page out of history, one score and sixteen years ago.⁷³

1. *Preemption vel non.*— The land sales industry, as a sort of rear guard action, took up the cudgel for federal preemption of regulation in the field. There were arguments for absolute preemption and, in the alternative, exemption from state laws for those who complied with federal requirements.⁷⁴ Absolute preemption would have benefited the industry by establishing uniform compliance and by removing the discomfiting uncertainties created by the application of state law to interstate transactions. Preemption was also urged on the further premise that non-preemptive federal law would tend to lull state agencies into laxity with respect to their own statutes.⁷⁵ But Congress was sensitive to the factors militating against a complete federal takeover. Whether the federal law was full disclosure oriented or highly paternalistic (*i.e.*, going beyond full disclosure to allow administrative comment on, or prohibition of, land offerings), preemption would have been a political impossibility. Representatives and senators from states with highly regulatory legislation would not support federal preemption based on a full disclosure philosophy.⁷⁶ But if the federal law were itself highly regulatory, preemption would be fought by members of Congress from states having no laws, or laws requiring full disclosure only.⁷⁷

Thus, thoughts of preemption were repressed, indicating, perhaps, that the concept of the states as laboratories for local experiment is alive and reasonably well — at least in the land sales area.

2. *Full Disclosure Versus Paternalism.*— Led by New Jersey's Senator Williams, the proponents of substantial new legislation showed a marked predilection for full disclosure rather than paternalism. Under the full disclosure philosophy, it is enough to re-

⁷² *Id.* at 168.

⁷³ See generally 1 L. LOSS, *supra* note 48, at 121-28.

⁷⁴ 1966 *Hearings* 150, 205; 1963 *Hearings* 310.

⁷⁵ 1966 *Hearings* 173.

⁷⁶ *Id.* at 119-20.

⁷⁷ *Id.* at 161-62.

quire a comprehensive informational registration, followed by administrative processing of the information and a mandatory delivery of a complete and structured property report to potential buyers. Unlike the paternalistic approach, there is no need for the agency to interject its own evaluation of the land. Even less is there need for administrative power to prohibit offerings when they are thought to be "unfair," though not fraudulent. Light the threshold, but don't lock the door.⁷⁸ Inform the buyer fully and give him liberal fraud remedies, but don't babysit with him.⁷⁹

The considerable bias in favor of full disclosure (and against paternalism) was supported and reinforced by Manuel Cohen, then Chairman of the SEC.⁸⁰ When asked whether he would want the power to editorialize on the quality of lots if his agency were given charge of the Land Sales Act, Chairman Cohen responded: "We would respectfully decline."⁸¹ Reacting to misgivings about the adequacy of a property report not including "fair comment" by an administrative agency,⁸² Chairman Cohen stated that, if his agency fell heir to administration of the Act, a meaningful selling document could be prepared without resorting to paternalistic techniques.⁸³ In this regard, he referred to the SEC practice of requiring the issuer to include an "introductory statement" or "poison paragraph" at the beginning of its prospectus (a practice itself somewhat tinged with paternalism), where such issuer is unseasoned and the security offering is unusually risky.⁸⁴ It is also important to note that the SEC wields a fair amount of power over the content of a securities registration statement and the terms of the offering (*i.e.*, it waxes paternalistic now and then) by means of its discretionary power to accelerate the effective date of a registration and its authority to grant exemptions.⁸⁵

Still, it can be argued that full disclosure to prospective land buyers by use of a prospectus-like selling document will not function as well as it does in the securities context. Unlike the typical sale of lots, many securities offerings, before they reach the "pub-

⁷⁸ 1963 *Hearings* 191.

⁷⁹ 1966 *Hearings* 23.

⁸⁰ 1967 *Hearings* 51-52, 59.

⁸¹ 1966 *Hearings* 99.

⁸² 1967 *Hearings* 73-74; 1966 *Hearings* 30-31, 69-70.

⁸³ 1966 *Hearings* 97-100. See also Note, S. 275 — *The Interstate Land Sales Full Disclosure Act*, 21 RUTGERS L. REV. 714, 729 (1967).

⁸⁴ 1966 *Hearings* 99.

⁸⁵ See SEC Rules 253(c), 460, 17 C.F.R. §§ 230.253(c), 460 (1969).

lic," filter through a superstructure of financial sophisticates (brokers and dealers), to whom the maze of prospectus information is presumably meaningful.⁸⁶ But what of the securities offerings that do not involve a large selling group or broad aftermarket — or which do not involve underwriters or dealers at all? Are we to conclude that full disclosure in these situations is useless? Probably not. The SEC certainly strives to make the Securities Act prospectus a document meaningful to the average investor.⁸⁷ Moreover, a prospectus regarding the character of land may not be as complex as one referring to securities.

Finally, regardless of its effect on those who see or understand it, a prospectus has an immediate purifying effect on the one disclosing. The thought of being exposed to the light of day, in terms that even a few can decipher, tends to reshape one's notions of what is ethical and what is not.⁸⁸

3. *The Securities Act Paradigm.*— With full disclosure taking an early lead in the struggle over philosophy and approach, Senator Williams introduced, in 1965, Senate bill 2672,⁸⁹ which, to the amusement of some and the chagrin of others, was simply a truncated version of the Securities Act of 1933, adapted for application to the sale of lots. Nor could its collateral ancestry be mistaken, for it was explicitly described as paralleling and being patterned after the Securities Act.⁹⁰ The bill provided two basic levels of protection: first, liberalized fraud remedies; and second, a requirement for full disclosure (by way of registration and use of a prospectus) far beyond mere avoidance of fraud, either in the common law sense or within the meaning of the bill's own expanded fraud concepts. Indeed, Senate bill 2672 so closely followed the Securities Act that the words "registration statement" and "prospectus" were preserved as the designators of the two principal full disclosure documents.⁹¹ In 1967, the bill was succeeded by Senate bill 275,⁹² and, while some minor changes could be observed, the motif was still Securities Act, vintage 1933.⁹³

Of course there were objections. Land, it was said, is not like

⁸⁶ See G. LEFCOE, LAND FINANCE LAW 1178 (1969).

⁸⁷ See WHEAT REPORT, *supra* note 1, at 46-54.

⁸⁸ *Id.*

⁸⁹ 111 CONG. REC. 27,310-13 (1965). See also 1966 Hearings 243-75.

⁹⁰ 111 CONG. REC. 27,310 (1965).

⁹¹ 1966 Hearings 91-100, 247.

⁹² 113 CONG. REC. 315-24 (1967). See also 1967 Hearings 4-36.

⁹³ 113 CONG. REC. 316 (1967); 1967 Hearings 2.

securities. The purchaser of securities cannot see the enterprise underlying his interest, while the purchaser of land can view and touch his "goods."⁹⁴ Query, whether this is a realistic distinction? What of those who buy sight-unseen in response to high pressure sales maneuvers? And what of those who have the opportunity to inspect raw land? Even an assiduous survey of a lot may fail to reveal such things as quality of title, year-round environment, hidden physical characteristics, or the dependability of a developer who promises extensive improvements. The kinship of raw land to securities may be close indeed.

Industry seers portended great increases in the cost of land as a result of federal registration and prospectus requirements.⁹⁵ But SEC Chairman Cohen put the lie to these gloomy forecasts by noting that legitimate developers were already preparing similar materials, either voluntarily or in compliance with state law.⁹⁶

Alternatives were offered. In the name of "creative federalism,"⁹⁷ it was suggested that federal criminal penalties be imposed,⁹⁸ or state authorities be afforded the right to sue in federal court, when state laws are violated in interstate commerce.⁹⁹ An additional proposal would have empowered a federal agency to proceed against a developer who was violating a state law.¹⁰⁰ However, these options would have put federal decision-makers in the business of interpreting, applying, and developing state law. Besides, where no state law existed, the very gaps in legislation which prompted congressional concern would be left unfilled. With respect to the suggestion that state authorities be given a federal forum for enforcement of their laws, there is always the problem of the under-financed state administrator, who could not afford to take advantage of the federal privilege. Finally, and perhaps most importantly, these alternatives lacked the badly needed preventive mechanism of full disclosure and the opportunity for individual recovery.¹⁰¹

In any event, in 1968, the Interstate Land Sales Full Disclosure

⁹⁴ 1966 *Hearings* 67.

⁹⁵ 1967 *Hearings* 160-61, 181.

⁹⁶ 1967 *Hearings* 52; 1966 *Hearings* 303.

⁹⁷ 1966 *Hearings* 116.

⁹⁸ 1967 *Hearings* 40, 219-20.

⁹⁹ 1966 *Hearings* 115-16; 1964 *Hearings* 27.

¹⁰⁰ 1966 *Hearings* 121.

¹⁰¹ 1967 *Hearings* 55-57, 153-54.

Act¹⁰² was quietly passed, its striking resemblance to the Securities Act still intact. The Department of Housing and Urban Development (HUD) was made its guardian, and the Secretary forthwith set up the Office of Interstate Land Sales Registration to handle matters of compliance.¹⁰³ History had, in a very substantial way, repeated itself, and the body of law developed under the Securities Act (and, to some extent the Securities Exchange Act) was to become apposite, more or less, to a whole new industry.

III. THE JURISDICTIONAL MEANS

Section 1404(a) provides that it is "unlawful for any developer or agent, directly or indirectly, to make use of any means or instruments of transportation or communication in interstate commerce, or of the mails"¹⁰⁴ to dispose of realty in violation of the Act. This language provides the jurisdictional base with respect to the requirements of a statement of record and a property report, as well as the antifraud provisions. Although it may initially appear that the burdens of the Act may be circumvented by refraining from the use of the jurisdictional means, it is apparent from the cases interpreting substantially similar language in the Securities Act that this would be a difficult and risky undertaking.

Clearly, the use of the mails,¹⁰⁵ telephone,¹⁰⁶ railroad,¹⁰⁷ an air-

¹⁰² 15 U.S.C.A. §§ 1701-20 (Supp. 1969).

¹⁰³ 24 C.F.R. §§ 1700.1-.85, 34 Fed. Reg. 5722-23 (1969).

¹⁰⁴ Since section 1404(a) is the pivotal provision of the entire Act, it is set out below:

(a) It shall be unlawful for any developer or agent, directly or indirectly, to make use of any means or instruments of transportation or communication in interstate commerce, or of the mails—

(1) to sell or lease any lot in any subdivision unless a statement of record with respect to such lot is in effect in accordance with section 1407 and a printed property report, meeting the requirements of section 1408, is furnished to the purchaser in advance of the signing of any contract or agreement for sale or lease by the purchaser; and

(2) in selling or leasing, or offering to sell or lease, any lot in a subdivision—

(A) to employ any device, scheme, or artifice to defraud, or

(B) to obtain money or property by means of a material misrepresentation with respect to any information included in the statement of record or the property report or with respect to any other information pertinent to the lot or the subdivision and upon which the purchaser relies, or

(C) to engage in any transaction, practice, or course of business which operates or would operate as a fraud or deceit upon a purchaser. 15 U.S.C.A. § 1703(a) (Supp. 1969).

¹⁰⁵ *Burns v. United States*, 286 F.2d 152 (10th Cir. 1961); *MacClain v. Bules*, 275 F.2d 431 (8th Cir. 1960); *Blackwell v. Bentsen*, 203 F.2d 690 (5th Cir. 1953), *cert. denied*, 347 U.S. 925 (1954).

plane,¹⁰⁸ or even one's personal automobile¹⁰⁹ between states would constitute the use of the jurisdictional means. However, the scope of this provision may be considerably broader. Although section 1404(a) uses the term "in" interstate commerce, rather than the more encompassing words "of" or "affecting," the operation of this language has not been limited to the use of interstate facilities across state lines. "Interstate commerce," when defined as "trade or commerce among the several States,"¹¹⁰ has been interpreted to include the *intrastate* use of *interstate* facilities, such as an *intrastate* telephone call¹¹¹ or the *intrastate* use of the mails.¹¹²

More specifically, section 1404(a)(1)¹¹³ makes it unlawful for a developer to use the jurisdictional means "to sell or lease" realty covered by the Act, unless a "statement of record" is in effect and the prospective purchaser has been furnished with a "property report." Presumably this provision encompasses more than merely the use of the jurisdictional means in the *act* of selling or leasing. There is a shift in language from "to sell" in section 1404(a)(1) to "in selling . . . or offering" in section 1404(a)(2),¹¹⁴ but the modulation is readily explained by the fact that to include offers in subparagraph (1) would prohibit the making of offers unless the disclosure requirements were satisfied. This does not indicate an intent to exclude from the disclosure requirements those transactions which are not *executed* by the use of the jurisdictional means. This same language, appearing in a similar context in the Securities Act,¹¹⁵ has been interpreted to mean "in order to" and includes the

¹⁰⁶ *Matheson v. Armbrust*, 284 F.2d 670 (9th Cir. 1960), *cert. denied*, 365 U.S. 870 (1961); *Nicewarner v. Bleavins*, 244 F. Supp. 261 (D. Colo. 1965).

¹⁰⁷ *Moore v. Gorman*, 75 F. Supp. 453 (S.D.N.Y. 1948).

¹⁰⁸ *Ellis v. Carter*, 291 F.2d 270 (9th Cir. 1961).

¹⁰⁹ *Moses v. Michael*, 292 F.2d 614 (5th Cir. 1961); *MacClain v. Bules*, 275 F.2d 431 (8th Cir. 1960) (use of interstate transportation inferred from personal delivery from one state to another); *Stadia Oil & Uranium Co. v. Wheelis*, 251 F.2d 269 (10th Cir. 1957); *Schamber v. Aaberg*, 186 F. Supp. 52 (D. Colo. 1960); *Collier v. Mikel Drilling Co.*, 183 F. Supp. 104 (D. Minn. 1958).

¹¹⁰ 15 U.S.C.A. § 1701(7) (Supp. 1969).

¹¹¹ *Myzel v. Fields*, 386 F.2d 718 (8th Cir. 1967), *cert. denied*, 390 U.S. 951 (1968); *Lennerth v. Mendenhall*, 234 F. Supp. 59 (N.D. Ohio 1964); *Nemitz v. Cunny*, 221 F. Supp. 571 (N.D. Ill. 1963). *But see* *Rosen v. Albern Color Research, Inc.*, 218 F. Supp. 473 (E.D. Pa. 1963).

¹¹² *Shaw v. United States*, 131 F.2d 476 (9th Cir. 1942); *SEC v. Bennett & Co.*, 207 F. Supp. 919 (D.N.J. 1962); *SEC v. Timetrust, Inc.*, 28 F. Supp. 34 (N.D. Cal. 1939); *United States v. Alluan*, 13 F. Supp. 289 (N.D. Tex. 1936).

¹¹³ 15 U.S.C.A. § 1703(a)(1) (Supp. 1969).

¹¹⁴ *Id.* § 1703(a)(2).

¹¹⁵ Securities Act § 5(a)(1), 15 U.S.C. § 77e(a)(1) (1964).

use of interstate facilities in the furtherance of the transaction from its inception to its final consummation.¹¹⁶

The scope of subparagraph (2) of section 1404(a), the anti-fraud provision, is somewhat more debatable. Query: Does the provision apply to transactions where the jurisdictional means are used at some stage of the transaction but not to transmit the deceptive information; or is the scope of the section limited to those situations where an interstate facility is used to communicate the fraudulent statements? The difficulty posed is relatively minor when viewed in light of the clear purpose of the Act — to prevent frauds as well as to compel full disclosure. A restrictive reading of this section would lead to the anomalous result of confining the jurisdictional base of the antifraud provisions to a narrower scope than that afforded the disclosure provisions. Nor is there a serious doubt as to the power of Congress to prevent the use of the mails or interstate facilities for purposes which it deems contrary to public policy.¹¹⁷ Rather than invoking handy Latin aphorisms of statutory construction or engaging in the futile effort of divining virtually nonexistent legislative history on this point,¹¹⁸ it is probably sufficient to note that in the securities context, where this issue has

¹¹⁶ *United States v. Wolfson*, 405 F.2d 779 (2d Cir. 1968), *cert. denied*, 394 U.S. 946 (1969) (mails used to transmit an offer and sales literature, to remit the proceeds, and to confirm the transaction); *Roe v. United States*, 316 F.2d 617 (5th Cir. 1963) (letter mailed to purchasers); *Stadia Oil & Uranium Co. v. Wheelis*, 251 F.2d 269 (10th Cir. 1957) (personal delivery of proceeds by means of interstate transportation); *United States v. Kane*, 243 F. Supp. 746 (S.D.N.Y. 1965) ("to sell" interpreted to mean "in connection with," and includes the use of the mails to transmit an offer and sales literature, to deliver the securities after sale, to send a confirmation, and to remit the proceeds to the seller); *Lennerth v. Mendenhall*, 234 F. Supp. 59 (N.D. Ohio 1964) (*intra*-state telephone call to arrange a meeting; mails used to deliver payment to seller); *Schamber v. Aaberg*, 186 F. Supp. 52 (D. Colo. 1960) (seller induced buyer to drive to another state for the purpose of being solicited); *Repass v. Rees*, 174 F. Supp. 898 (D. Colo. 1959) (telephone used to make an offer); *Collier v. Mikel Drilling Co.*, 183 F. Supp. 104 (D. Minn. 1958) (seller's transportation of buyers by automobile between states at the negotiation stage); *Dupler v. Simmons*, 163 F. Supp. 535 (D. Wyo. 1958) (telephone used for negotiations; mails used to remit payment); *SEC v. Truckee Showboat, Inc.*, 157 F. Supp. 824 (S.D. Cal. 1957) (newspaper containing advertisement sent through the mails). See also cases cited note 112 *supra*.

¹¹⁷ See *Kann v. United States*, 323 U.S. 88 (1944); *Nemitz v. Cunny*, 221 F. Supp. 571 (N.D. Ill. 1963); *SEC v. Timetrust, Inc.*, 28 F. Supp. 34 (N.D. Cal. 1939). See generally 3 L. LOSS, *supra* note 48, at 1519-28.

¹¹⁸ Reference to the use of the jurisdictional means is contained in HOUSE COMM. ON BANKING AND CURRENCY, 90TH CONG., 2D SESS., SUMMARY OF THE HOUSING AND URBAN DEVELOPMENT ACT 60 (Comm. Print 1968), which states that it is "unlawful for any developer or agent engaged in interstate commerce" to violate the provisions of section 1404(a) (emphasis added). This is broad language indeed.

arisen with respect to substantially similar language,¹¹⁹ the broader construction has been adopted.¹²⁰

Finally, section 1404(a) provides that it is unlawful for a "developer or agent, *directly or indirectly*" to use the jurisdictional means to violate the disclosure and antifraud provisions. Thus, if a developer were to accept a purchase contract and mail a copy of it to the purchaser, jurisdiction would be established. But, so long as the use of the jurisdictional means is foreseeable and in the furtherance of the transaction, it would also be sufficient if the purchaser mailed the proceeds to the developer,¹²¹ or even if the escrow agent mailed the deed and payment to the proper parties.¹²² Indeed, where payment is by check, it may be sufficient if the depository bank used the mails in the collection process.¹²³

¹¹⁹ Compare 15 U.S.C.A. § 1703(a)(2) (Supp. 1969), with section 17(a) of the Securities Act of 1933, 15 U.S.C. § 77q(a) (1964), and Rule 10b-5, promulgated by the SEC pursuant to the Securities Exchange Act of 1934, 17 C.F.R. § 240.10b-5 (1969).

¹²⁰ *Myzel v. Fields*, 386 F.2d 718 (8th Cir. 1967), *cert. denied*, 390 U.S. 951 (1968) (*intrastate* telephone call to solicit purchasers); *Ellis v. Carter*, 291 F.2d 270 (9th Cir. 1961) (personal delivery by use of commercial airplane); *MacClain v. Bules*, 275 F.2d 431 (8th Cir. 1960) (delivery through the mails); *Matheson v. Armbrust*, 284 F.2d 670 (9th Cir. 1960), *cert. denied*, 365 U.S. 870 (1961) (telephone call to arrange initial meeting); *Blackwell v. Bentsen*, 203 F.2d 690 (5th Cir. 1953), *cert. denied*, 347 U.S. 925 (1954) (delivery through the mails); *Nicewarner v. Bleavins*, 244 F. Supp. 261 (D. Colo. 1965) (incidental use of telephone by seller and of the mails by purchaser); *Belhumer v. Dawson*, 229 F. Supp. 78 (D. Mont. 1964) (use of mails for correspondence between codefendant sellers); *SEC v. Gulf Intercontinental Fin. Corp.*, 223 F. Supp. 987 (S.D. Fla. 1963) (newspaper containing advertisement sent through the mails); *SEC v. Bennett & Co.*, 207 F. Supp. 919 (D.N.J. 1962) (solicitations by *intrastate* use of telephone, *intrastate* use of mails to send advertising literature to confirm sales, and by purchasers to remit proceeds); *Schamber v. Aaberg*, 186 F. Supp. 52 (D. Colo. 1960) (telephone call by seller to a third person for the purpose of having this third person affirm the seller's good reputation to the buyer); *Moore v. Gorman*, 75 F. Supp. 453 (S.D.N.Y. 1948) (personal delivery via railroad). See also *Roe v. United States*, 316 F.2d 617 (5th Cir. 1963) (use of mails after consummation of transaction to reassure purchaser may be sufficient) (*dictum*). See generally 3 L. LOSS, *supra* note 48, at 1526-27.

¹²¹ *Creswell-Keith, Inc. v. Willingham*, 264 F.2d 76 (8th Cir. 1959); *Nicewarner v. Bleavins*, 244 F. Supp. 261 (D. Colo. 1965) (ancillary use of mails by purchaser); *Lennerth v. Mendenhall*, 234 F. Supp. 59 (N.D. Ohio 1964) (check mailed to seller); *SEC v. Bennett & Co.*, 207 F. Supp. 919 (D.N.J. 1962); *Schamber v. Aaberg*, 186 F. Supp. 52 (D. Colo. 1960) (seller induced buyer to travel by means of interstate highway for the purpose of being solicited).

¹²² *McDaniel v. United States*, 343 F.2d 785 (5th Cir.), *cert. denied*, 382 U.S. 826 (1965) (foreseeable use of mails by agent); *Sherwood v. United States*, 300 F.2d 603 (5th Cir.), *cert. denied*, 371 U.S. 838 (1962) (use of mails by codefendant); *Ellis v. Carter*, 291 F.2d 270 (9th Cir. 1961) (foreseeable use of jurisdictional means by escrow agent); *Burns v. United States*, 286 F.2d 152 (10th Cir. 1961) (foreseeable use of mails by partner); *Danser v. United States*, 281 F.2d 492 (1st Cir. 1960) (foreseeable use of mails by underwriter for delivery to purchaser).

¹²³ *Little v. United States*, 331 F.2d 287 (8th Cir.), *cert. denied*, 379 U.S. 834 (1964); *United States v. Carruthers*, 152 F.2d 512 (7th Cir. 1945), *cert. denied*, 327 U.S. 787 (1946); *United States v. Reidel*, 126 F.2d 81 (7th Cir. 1942); *United States v.*

It should be abundantly clear that any attempt to avoid the burdens of the Act on jurisdictional grounds would probably be unsuccessful. From a highly theoretical point of view, one might finesse the jurisdictional base if all the steps in an intrastate transaction were accomplished in person. However, the risk that the *purchaser* might utilize the jurisdictional means, not to mention the inconvenience of being foreclosed from use of the mails and telephone, would render such a scheme impractical.

It is important to appreciate the precise function of the jurisdictional provision of the Act. Congressional power to regulate is established whenever the mails or other interstate facilities are used in connection with an offer, sale, or lease of land. Regulation is not dependent upon the relative locations of the offeror, offeree, or the land. Thus, the requirement that interstate facilities or the mails be used does *not* limit application of the Act to situations where property in one state is offered, sold, or leased to persons in another state.¹²⁴ At the same time, it must be recognized that separation of the offeror, offeree, or the land by state boundaries may well be relevant to the availability of the intrastate exemption discussed later.¹²⁵ In that context, the term "interstate" (the presumed logical contradictory of "intrastate") depends upon the domiciles of the parties and the location of the land. It appears, therefore, that there is a tricky bit of equivocation lurking in the Act.

IV. THE REGISTRATION PROCESS

Section 1404(a)(1) makes it unlawful for a developer to sell or lease a lot in a subdivision unless a *statement of record* is *in effect* and a *property report* has been furnished to the purchaser prior to the signing of the agreement. Failure to comply with these requirements may result in administrative action,¹²⁶ as well as criminal¹²⁷ and civil¹²⁸ liability.

Robertson, 181 F. Supp. 158 (S.D.N.Y. 1959), *aff'd mem.*, 298 F.2d 739 (2d Cir. 1962); United States v. Vidaver, 73 F. Supp. 382 (E.D. Va. 1947). *But see* Kann v. United States, 323 U.S. 88 (1944). *See generally* H. BLOOMENTHAL, CASES AND MATERIALS ON SECURITIES LAW 108-19 (1966); 3 L. LOSS, *supra* note 48, at 1525-28.

¹²⁴ Congress knew full well that, by using the jurisdictional language of the Securities Act, it was extending coverage of the Land Sales Act to transactions where the land and the purchaser were either both in one state or separated by short distances. The point was brought up several times. 1966 *Hearings* 67, 103-09; 1964 *Hearings* 73. Senators Bennett, Tower, and Hickenlooper commented: "We want to point out our concern, however, that the bill still deals with promotional plans not for the purpose of selling land interstate." S. REP. NO. 1123, 90th Cong., 2d Sess. 199 (1968).

¹²⁵ *See* text accompanying notes 223-49 *infra*.

¹²⁶ 15 U.S.C.A. § 1714 (Supp. 1969).

¹²⁷ *Id.* § 1717.

A. *Filing*

The statement of record, which must fully disclose all material information pertinent to the offered land,¹²⁹ must be filed with the Secretary.¹³⁰ "Filing" occurs on the date of receipt by the Secretary.¹³¹

B. *Waiting Period*

The statement of record is then examined, and, if it appears to be free from defects, it automatically becomes "effective" on the 30th day after filing.¹³² The Secretary has the discretion to "accelerate" the effectiveness to such earlier date as he may approve.¹³³ Of course, it is too early to ascertain the details of administrative practice with respect to acceleration, and no guidelines have been established by regulation.¹³⁴ However, it may be speculated that effectiveness will be accelerated to a date requested by the developer as soon as any deficiencies raised by the Examination Division have been corrected.¹³⁵

The effective date may also be delayed under certain circumstances. If the developer takes the initiative to file an amendment, a new waiting period commences and the statement of record does not become effective until its expiration unless accelerated by the Secretary.¹³⁶ On the other hand, where an amendment is filed pur-

¹²⁸ *Id.* § 1709(b)(1).

¹²⁹ The information required to be disclosed in the statement of record is contained in section 1406, 15 U.S.C.A. § 1705 (Supp. 1969), and 24 C.F.R. §§ 1710.20, .105-.110, 34 Fed. Reg. 5931, 5933, 5938 (1969).

¹³⁰ 15 U.S.C.A. § 1704(a) (Supp. 1969). More specifically, the Examination Division, Office of Interstate Land Sales Registration, Washington, D.C. See 24 C.F.R. § 1700.80, 34 Fed. Reg. 5722 (1969).

¹³¹ 15 U.S.C.A. § 1704(c) (Supp. 1969).

¹³² *Id.* § 1706(a). As is the case under the Securities Act, effectiveness is not to be taken as HUD approval of the land offering. Nor is it to be construed as an indication that the statement of record is true and accurate. *Id.* § 1716. It is a crime to wilfully make a representation to the contrary, *id.* §§ 1716, 1717, and the Regulations require that the property report bear a legend disclaiming HUD approval of the offering. 24 C.F.R. § 1710.110, 34 Fed. Reg. 5938 (1969).

¹³³ 15 U.S.C.A. § 1706(a) (Supp. 1969).

¹³⁴ The Regulations merely provide for acceleration with respect to sales in progress when the Act became effective on April 28, 1969. 24 C.F.R. § 1710.40, 34 Fed. Reg. 5932 (1969).

¹³⁵ This is the general practice under the Securities Act § 8(a), 15 U.S.C. § 77h(a) (1964). See SEC Rules 460, 461, 17 C.F.R. §§ 230.460, .461 (1969).

¹³⁶ 15 U.S.C.A. § 1706(a) (Supp. 1969). Similar language in the Securities Act provided the vehicle by which the Securities and Exchange Commission was able to gain additional time for processing the "registration statement," the federal securities law analogue of the statement of record. When additional time is needed, it is obtained

suant to an "order" or with the "consent" of the Secretary, the effective date is not delayed beyond the end of the then running 30-day period, and, what is more, it may be accelerated.¹³⁷

If it appears to the Secretary that the statement of record or any amendment thereto is "incomplete or inaccurate in any material respect," the Examination Division, by sending a deficiency notice to the developer, can suspend the effective date "until thirty days after the developer files *such additional information* as the Secretary shall require."¹³⁸ Upon receiving a suspension notice, the developer has two options: He can contest the Secretary's deficiency comment by pursuing his administrative and judicial remedies;¹³⁹ or he can comply with the order by sending the requested information.

The question arises whether amendments filed to correct defects in the original statement of record should be considered "additional information." It appears that the power to toll the running of the waiting period by a deficiency notice was designed for administrative convenience. This power enables the Secretary to compel the developer to supply any information which may be needed to verify the accuracy of the statement of record, and it provides him with sufficient time to conduct the examination.¹⁴⁰ In the event that

by way of a "delaying amendment," *i.e.*, an amendment filed at the initiative of the applicant which starts a new waiting period. This informal procedure avoids the necessity of resorting to the formal and time consuming suspension procedure. See SEC Rule 473, 17 C.F.R. § 230.473 (1969); 1 L. LOSS, *supra* note 48, at 273. Since this Act, unlike the Securities Act, provides for suspension of the waiting period upon the issuance of a "deficiency notice" by the Division of Examination, *see* note 140 *infra*, the only situation in which a delaying amendment would be required is where the Division finds it impossible to finish its inspection of the statement of record within 30 days.

¹³⁷ 15 U.S.C.A. § 1706(a) (Supp. 1969). The same rule applies under the Securities Act. In order to obtain "consent" to an amendment, a written request must be made. It is granted only pursuant to a specific order. 1 L. LOSS, *supra* note 48, at 269-70.

¹³⁸ 15 U.S.C.A. § 1706(b) (Supp. 1969) (emphasis added).

¹³⁹ Receipt of the suspension notice triggers the developer's right to request a hearing which must be held (but presumably not completed) within 20 days of the receipt of the request. *Id.* The Secretary's determination may be appealed to the court of appeals and the United States Supreme Court. *Id.* § 1710(a).

¹⁴⁰ *Id.* § 1706(b). Before effectiveness of the statement of record, the Secretary does not seem to have direct authority to *order* a developer to supply "additional information" pursuant to a deficiency notice. However, he can sue to enjoin the developer from making sales in the absence of an effective statement of record. *Id.* § 1714(a). Indeed, a recalcitrant developer might refuse to supply the requested information and withdraw the statement of record. *But see id.* §§ 1714(b), (c), wherein the Secretary is given authority to conduct investigations which he deems necessary for the enforcement of the Act. By this route, the Secretary could probably obtain any information he desires. *Cf.* 3 L. LOSS, *supra* note 48, at 1948-56. If the developer initiated a hearing on the deficiency notice, he may forfeit his right to withdraw the statement of record with-

the Examination Division does not need the full 30-day period after the developer furnishes additional information, the suspension period may be shortened by acceleration.¹⁴¹ If the Secretary determines that a corrective amendment is necessary, he would presumably notify the developer, and the amendment filed pursuant to this notice would seem not to require extensive examination. If the corrective amendment is considered "additional information," its filing would commence a new waiting period.¹⁴² This, however, would serve no administrative purpose and would needlessly postpone the date when the developer could make sales. Although the Secretary might exercise his discretion and accelerate the effective date, this should not be necessary. The corrective amendment should be considered an amendment filed pursuant to an "order" of the Secretary rather than "additional information," thereby avoiding the commencement of another waiting period.¹⁴³

Of course, if the phrase "additional information" does not refer to — and therefore need not include — a corrective amendment, there is the possibility that the statement of record may become effective 30 days after the filing of the original additional information requested by the Secretary, regardless of whether a corrective amendment was filed. However, if the developer failed to make a corrective amendment as requested by the Examination Division and commenced sales after the effective date, the Secretary could initiate injunctive proceedings,¹⁴⁴ thus exposing the developer to civil and criminal liability for having on file a false or misleading statement of record¹⁴⁵ or for using a false or misleading property report.¹⁴⁶

out administrative approval. Cf. SEC Rule 477, 17 C.F.R. § 230.477 (1969); 1 L. LOSS, *supra* note 48, at 310-16.

¹⁴¹ 15 U.S.C.A. § 1706(a)(2) (Supp. 1969); 24 C.F.R. § 1710.45(a)(2), 34 Fed. Reg. 5933 (1969).

¹⁴² 15 U.S.C.A. § 1706(b) (Supp. 1969).

¹⁴³ *Id.* § 1706(a). There could also be acceleration to a point before the end of the waiting period running at the time when such amendment is filed.

¹⁴⁴ *Id.* § 1714(a).

¹⁴⁵ Section 1410(a), *id.* § 1709(a), provides an express right of action for having on file a false or misleading statement of record. Criminal penalties are found in section 1418, *id.* § 1717.

¹⁴⁶ Section 1410(b)(1), *id.* § 1709(b)(1), creates a civil action for using a false or misleading property report in violation of the general antifraud provision, section 1404(a)(2), *id.* § 1703(a)(2). See also *id.* § 1709(b)(2). Criminal liability for willful violations of section 1404(a)(2), *id.* § 1703(a)(2), is possible under section 1418, *id.* § 1717.

C. *Post Effective Period*

1. *Property Report*.— Although a developer may engage in promotional activities at any time, he may not make sales unless the statement of record is in effect.¹⁴⁷ In order to consummate a sale, the developer or his agent must furnish the purchaser with a copy of the property report "in advance of the signing of a contract or agreement."¹⁴⁸ Failure to do so gives the purchaser a right to rescission¹⁴⁹ or damages.¹⁵⁰ If the purchaser receives the property report less than 48 hours prior to signing the agreement, he may revoke his obligation within the next 48 hours.¹⁵¹ This right of revocation, however, may be waived in the contract by a purchaser who acknowledges that prior to signing he had received, read, and understood the property report and had inspected the lot.¹⁵²

2. *Post Effective Amendments*.— Assume for the present that the statement of record and property report were materially inaccurate on the effective date. It is clear that in such circumstances the developer, if sales were made after the effective date, may be in violation of sections 1404(a)(2)(B) (sales made in violation of the antifraud provisions),¹⁵³ 1410(a) (sales made after the effective date where the statement of record was materially deficient when it became effective),¹⁵⁴ and 1410(b)(2) (sales made by means of a property report which misstated or omitted material facts).¹⁵⁵ Although the developer may be able to protect himself from liability under sections 1404(a)(2)(B) and 1410(a) by informing prospective purchasers of the error *before sale*,¹⁵⁶ he could not

¹⁴⁷ *Id.* § 1703(a)(1). Earlier versions of the Act forbade the making of "offers," as broadly defined in section 1402(10), *id.* § 1701(10), before the effectiveness of the statement of record. See 1967 *Hearings* 8; 1966 *Hearings* 247. See also text accompanying notes 169-83 *infra*.

¹⁴⁸ 15 U.S.C.A. § 1703(a)(1) (Supp. 1969). The contents of the property report are specified in section 1408(a), *id.* § 1707(a), and by Regulation in 24 C.F.R. § 1710.110, 34 Fed. Reg. 5938 (1969). The property report is actually a part of the statement of record. *Id.* §§ 1710.20, .110, 34 Fed. Reg. 5931-32, 5938-39 (1969).

¹⁴⁹ 15 U.S.C.A. § 1703(b) (Supp. 1969).

¹⁵⁰ *Id.* §§ 1703(a)(1), 1709(b)(1), (c).

¹⁵¹ *Id.* § 1703(b).

¹⁵² *Id.*

¹⁵³ *Id.* § 1703(a)(2)(B). For the full text of subsection (a), see note 104 *supra*.

¹⁵⁴ *Id.* § 1709(a).

¹⁵⁵ *Id.* § 1709(b)(2).

¹⁵⁶ Under section 1410(a), *id.* § 1709(a), the developer can exculpate himself by proving that the purchaser knew of the untruth or omission at the time of the acquisition; section 1404(a)(2)(B), *id.* § 1703(a)(2)(B), requires that the purchaser rely on the material misrepresentation contained in the property report.

avoid liability under section 1410(b)(2) unless he filed a corrective amendment to the statement of record. Even then he could avoid liability only with respect to sales made after the effective date of the amendment and where a newly corrected property report is used.¹⁵⁷ Nor is it possible, by using an informally corrected property report, to avoid liability with respect to sales made while a defective statement of record is on file. The property report is a part of the statement of record,¹⁵⁸ and it must be used in its entirety.¹⁵⁹ Thus, if the original property report contained a misstatement, it could not be corrected by merely striking out the error; and, further, if material facts were omitted, it would not suffice to attach an addendum. Sales by means of such altered (and unlawful) property reports would unavoidably violate section 1404(a)(1).¹⁶⁰ To avoid any further liability of the sort already described (not to mention administrative as well as criminal actions),¹⁶¹ the developer must file a corrective amendment to *both* the statement of record and the property report contained therein. Although there is no direct statutory authority for filing post effective amendments to cover preeffective errors, the right and duty of the developer to do so clearly follow considering the liability which attaches if he is remiss.¹⁶²

Assume now that the statement of record was free from defects when it became effective but that subsequently a change occurred affecting a material fact required to be stated therein. In accordance with the policy of protecting purchasers through full disclosure, section 1407(c)¹⁶³ requires that the statement of record be continuously complete and accurate. Further, it imposes upon developers the duty to promptly file amendments reflecting all material post effective changes.¹⁶⁴ Upon receipt of such amendments, the Secretary has the discretionary power to suspend the statement of

¹⁵⁷ Section 1410(b)(2), *id.* § 1709(b)(2), does not afford a developer who sells by means of an inaccurate property report a reliance defense.

¹⁵⁸ 24 C.F.R. §§ 1710.20, .110, 34 Fed. Reg. 5931-32, 5938-39 (1969).

¹⁵⁹ 15 U.S.C.A. § 1707(b) (Supp. 1969).

¹⁶⁰ *Id.* § 1703(a)(1).

¹⁶¹ *Id.* §§ 1706(d), 1714(a), 1717.

¹⁶² Section 1407(c), *id.* § 1706(c), seems to refer to post effective amendments required by post effective changes. However, section 1410(a), *id.* § 1709(a), clearly implies that the developer should file post effective amendments to correct *any* error (pre- or post effective) in the statement of record.

¹⁶³ *Id.* § 1706(c).

¹⁶⁴ *Id.* The amendment, like the original statement of record, becomes effective 30 days after filing, unless its effectiveness is accelerated. *Id.* § 1706(a). It is also subject to the deficiency notice process. *Id.* § 1706(b).

record until the amendment becomes effective.¹⁶⁵ Alternatively, if the developer fails to file a corrective amendment, the Secretary may initiate suspension proceedings.¹⁶⁶ Clearly, sales made during a period of suspension would violate section 1404(a)(1),¹⁶⁷ since a statement of record would not be "in effect." However, regardless of whether the statement of record is suspended, if the post effective change materially affects the content of the property report, the developer would, as a practical matter, be foreclosed from making sales until the amendment became effective, at which time he could use a corrected property report.¹⁶⁸

D. *Marketing Problems*

There remains to be considered the point in time at which a developer may commence his advertising campaign. Section 1404(a)(1)¹⁶⁹ prohibits the making of *sales or leases* prior to the effective date of the statement of record and unless the purchaser has been furnished with a copy of the property report prior to signing the agreement. Unfortunately, the terms "sales" and "leases" are not defined either in the Act or by regulation. Although these words may include all the constituent as well as ancillary elements of a transaction for the purpose of establishing the jurisdictional base,¹⁷⁰ this same language, as it pertains to fulfilling the disclosure requirements, presumably refers to mutually binding contracts, executory as to performance. Under this interpretation, developers may engage in promotional activities prior to the effective date. Read in this manner, the section differs substantially from its counterpart in the Securities Act which expressly prohibits all promotional activities prior to filing and allows only prospectus-type written promotional materials to be used during the waiting period.¹⁷¹ The objective of the Securities Act is clear: Even though no legally

¹⁶⁵ *Id.* § 1706(c).

¹⁶⁶ *Id.* § 1706(d). After notice, the Secretary has 15 days in which to hold a hearing and issue an order. *Id.* The order is reviewable in the court of appeals and the Supreme Court. *Id.* § 1710(a).

¹⁶⁷ *Id.* § 1703(a)(1).

¹⁶⁸ Because the statement of record was correct as of its effective date, the developer would not be subject to liability under section 1410(a), *id.* § 1709(a). He would, however, by making sales after a post effective change, but prior to the effectiveness of a corrective amendment, be opening himself up to civil (both private and governmental) and criminal fraud actions. *Id.* §§ 1703(a)(2), 1709(b)(1), (2), 1714, 1717.

¹⁶⁹ *Id.* § 1703(a)(1). See note 104 *supra*.

¹⁷⁰ See text accompanying notes 104-25 *supra*.

¹⁷¹ See 15 U.S.C. §§ 77e(b), 77e(c) (1964).

binding sales are permitted before the effective date, prospective purchasers might, in response to selling pressure and personal proclivity, become "committed" to buy. To inhibit the formation of these psychological obligations before disclosure is available, sellers may not begin their attempts to dispose of securities until after filing, and, during the waiting period, may use only structured written materials meeting statutory and administrative standards.¹⁷²

Congress has abandoned this approach with respect to land sales, apparently on the theory that there is less danger of non-legal commitment before a property report is shown to the buyer. The wisdom of allowing a developer to conduct an unbridled sales campaign before his purchasers receive a statutory property report (or, worse still, before a statement of record is on file) is certainly open to question. To be sure, the purchaser of land is quite unlike the purchaser of securities in certain respects. In many securities distributions, a purchaser must make up his mind whether he wants to purchase at the public offering price by (or soon after) the time the securities go "out the window." Land, on the other hand, is not distributed in a single "burst" of activity; rather, it is sold piecemeal, over a longer period. Thus, in the securities context, the limited decision-making period, together with the concerted efforts of the selling group to "find a home" for securities prior to the actual offering of a new issue, supplies an apparent justification for more stringent controls during the preeffective period. There is the further likelihood that a prospective buyer of securities might hesitate to withdraw his informal commitment to buy, once he has indicated his interest to a broker with whom he regularly does business. Compunctions over renegeing on a deal, albeit not legally binding, may not be felt by a purchaser of land who will rarely have repeated contacts with his seller. However, these generalized distinctions between securities and land, ostensibly valid on the basis of an a priori analysis, may tend to fade and blur in particular cases. For instance, an offering of lots may be advertised as containing a limited number of "superior" or "prime" parcels, sufficient to satisfy only a small group of purchasers having the perspicacity to seize the opportunity "while the supply lasts."¹⁷³ An offeree who is sub-

¹⁷² The wisdom of forbidding "gun jumping" offers (attempts to dispose of securities before structured information is available to the public) has recently been re-evaluated and reaffirmed. See WHEAT REPORT, *supra* note 1, at 127-35.

¹⁷³ Such tactics remind one of the methods used in the past by carnival barkers and announcers for radio adventure serials. One of the writers, at least, recalls the days when attentive, infant devotees of such programs as "Jack Armstrong" and "Captain Midnight" were regularly admonished by excited voices: "Be the first on your block to

jected to such a sales device may well believe that he must make his choice while the time is ripe. Moreover, if significant selling pressure is applied, the whole pattern is very much akin to the securities distribution. Congress, however, wisely or not, has chosen a different tack for the land sales industry.

Had Congress intended to proscribe advertising during the pre-effective period, it could have included the term "offer"¹⁷⁴ in section 1404(a)(1)¹⁷⁵ as it did in section 1404(a)(2)¹⁷⁶ with respect to fraudulent transactions. The congressional decision to allow offers prior to the effective date does not render the foregoing discussion moot, however. Rather, attention is drawn to the need for vigilant enforcement of the general antifraud provision of the Act,¹⁷⁷ which applies to *all* oral and written representations made to the buyer prior to sale, including those made in the preeffective period. Similarly, the developer's freedom to "condition the market" prior to the effective date calls for stringent enforcement of standards governing preparation of the property report. Indeed, it is the only document which might counterbalance the effects of the developer's own selling literature. Even when the language of the Act forbade offers prior to the effective date, concern was expressed over the need for a comprehensive, yet uncomplicated property report which would maintain the equilibrium in the selling process.¹⁷⁸ In 1966, SEC Chairman Cohen assured anxious senators that an effective and intelligible property report could be produced with proper administrative guidance and prodding.¹⁷⁹ Later, however, the Chairman suggested specific statutory authority to regulate all selling literature.¹⁸⁰ Perhaps this could be accomplished under the general rulemaking authority granted to the Secretary.¹⁸¹ In any event, the

own a magic ring (or secret decoder, or some such thing)." It is not difficult to visualize the real estate pitchman using the same gambit at a county fair, the only difference being that his line would read simply: "Be the first on your block."

¹⁷⁴ "The term offer includes any inducement, solicitation, or attempt to encourage a person to acquire a lot in a subdivision." 15 U.S.C.A. § 1701(10) (Supp. 1969).

¹⁷⁵ *Id.* § 1703(a)(1). See also note 147 *supra*. The property report will *not*, as originally intended, serve as a "companion piece" to selling literature during the preeffective period. See 111 CONG. REC. 27,311 (1965).

¹⁷⁶ *Id.* § 1703(a)(2).

¹⁷⁷ *Id.* See text accompanying notes 336-63 *infra*.

¹⁷⁸ 1966 *Hearings* 24, 30, 69.

¹⁷⁹ *Id.* at 98-99. Chairman Cohen mentioned specifically the use of the "poison paragraph," wherein an issuer of securities may be required to state, succinctly and prominently at the beginning of the prospectus, all unfavorable information about its enterprise. *Id.*

¹⁸⁰ 1967 *Hearings* 53. It was not given.

¹⁸¹ 15 U.S.C.A. § 1718 (Supp. 1969).

Secretary can control preeffective shenanigans by using his discretionary power to refuse acceleration when it is not in the public interest.¹⁸²

In conducting promotional activities prior to the effective date, developers must be careful lest their advertisements rise to the dignity of a common law offer, which, if accepted in writing before a copy of the property report is furnished, would clearly result in an illegal contract. Nor could this result be avoided if the developer solicits written offers to buy during the preeffective period and then accepts them after the effective date, since the purchaser would not have received the property report prior to signing the agreement. Thus, although offers may be extended prior to the effective date, the risk that they may be accepted prior to compliance with the disclosure requirements will substantially circumscribe this practice.

A different problem is posed with respect to oral contracts. Although the difficulties of enforcement raised by the Statute of Frauds may be overcome by part performance,¹⁸³ it remains to be decided whether the terms "sales" and "leases" encompass oral as well as written contracts. If not — a very dangerous assumption — then developers could make oral sales at any time whether or not a statement of record was in effect. Furthermore, since there would be no "signing," a property report would not be required. However, where the oral contract is evidenced by a check signed by the purchaser, the disclosure policies of the Act could be fulfilled if it were concluded that the check, being essential to the transaction, constitutes a signed agreement which pursuant to the Act must be preceded by a property report.

V. COVERAGE OF THE ACT

A. *Definitional Coverage*

In general, the reach of the Act extends to "lots" in a "subdivision."¹⁸⁴ The term "subdivision" in turn is given a rather elaborate definition.¹⁸⁵ Basically, a subdivision is "land which is divided or *proposed* to be divided into fifty or more lots . . . for the purpose of sale or lease as part of a common promotional plan."¹⁸⁶ Thus, the

¹⁸² *Id.* § 1706(a).

¹⁸³ See generally 8A G. THOMPSON, REAL PROPERTY § 4463 (1963).

¹⁸⁴ 15 U.S.C.A. § 1703(a) (Supp. 1969).

¹⁸⁵ *Id.* § 1701(3) (emphasis added).

¹⁸⁶ *Id.* (emphasis added). Earlier versions of the Act set the lot minimums at 5 and 25. 111 CONG. REC. 27,312 (1965) (five); 1967 *Hearings* 5 (twenty-five); 1966

sale of a lot in a tract planned for a 50-lot breakdown would be within the purview of the Act, even though the engineering and recording for all 50 parcels had not yet been completed. Individual parcels making up the 50 lots need not be "contiguous" so long as they will be offered as part of a common promotional plan.¹⁸⁷ For example, two tracts of 25 lots each, though separated by many miles, may be conglomerated and counted as a 50-lot tract for purposes of the Act, if they are offered as part of a common promotional plan. Furthermore, they will be presumed to be part of such a plan if they are offered by a "single developer, or group of developers acting in concert," and are "known, designated, or advertised as a common unit or by a common name."¹⁸⁸ One can only speculate as to the rebuttable or irrebuttable nature of the presumption. For example, if X offers 25 lots on each of two sides of town under the single name Blackacre Estates, the courts and HUD should have some flexibility in determining whether the Act applies. The physical size of each of the two tracts is not statutorily sufficient to raise difficulties about the nature of the land and the possible need for full disclosure through registration. Moreover, it may happen that each tract lies within well-developed, low risk surroundings. In these circumstances, the protections of the Act may well be superfluous.¹⁸⁹

Similarly, it does not appear that contiguous parcels need always be counted together, if the lots contained therein are not to be offered as part of a common promotional plan. However, if par-

Hearings 244 (twenty-five). The size requirement is, at best, merely a threshold at which a *prima facie* case for protection is established. It is a rough gauge, based on the general assumption that tracts containing more than a given number of lots will, in their most frequent manifestations, have enough troublesome characteristics to create a need for buyer protection. The premise was challenged by a witness before the Senate Securities Subcommittee: "I . . . would like to see some more work done on [defining exemptions], and not just by changing the number from 5 to 25 or 50 or 300 or what, because these birds operate in all numerical levels, so it has to be something better than that for a definition." *1966 Hearings 70*.

¹⁸⁷ *Id.*

¹⁸⁸ *Id.*

¹⁸⁹ The presumption, if irrebuttable, might be circumvented by use of the specific exemption granted to "the sale or lease of real estate not pursuant to a common promotional plan to offer or sell fifty or more lots in a subdivision." 15 U.S.C.A. § 1702(a)(1) (Supp. 1969). But if, by dint of section 1402(3), *id.* § 1701(3), lots are deemed to be in a "subdivision" (and therefore within the coverage of the Act) because they *are* offered as part of a common promotional plan, how can the same lots be exempted from the provisions of the Act, under section 1403(a)(1), *id.* § 1702(a)(1), on the ground that they are *not* offered pursuant to such a plan? It is true that the definitional provision uses the words "part of" (section 1402(3)), while the exemptive paragraph uses "pursuant" (section 1403(a)(1)), but it will be cutting a fine line indeed if such a slim difference creates a distinction.

cels are contiguous¹⁹⁰ and offered by a "single developer, or a group of developers acting in concert," they are presumed to be offered as part of a common promotional plan and are thus counted together toward the 50-lot minimum.¹⁹¹

B. *Specific Exemptions*

Section 1403(a) exempts certain lots, offerings, and transactions.¹⁹² Among these are dispositions of land pursuant to a court order, transfers of mortgages, the sale of securities in a real estate investment trust, the sale or lease of real estate by any government or governmental agency, the sale of cemetery lots, and transactions with commercial builders.¹⁹³ The rationale for these exemptions is clear: Such lots and transactions are either essentially commercial in character, adequately governed by other laws, or unlikely to involve a home-building or investment acreage purchaser. However, it is evident that a developer could conceivably cast an ordinary consumer transaction in the form of one of these exemptions in an attempt to thwart the purposes of the Act. This possibility was anticipated, and consequently the availability of any specific exemption is conditioned upon the developer's not having adopted an exempt form of disposition "for the purpose of evasion" of the Act.¹⁹⁴ Presumably, the developer would have the burden of proving the applicability of an exemption,¹⁹⁵ including absence of evasive purpose, but in the normal transaction this should not be too difficult. Problems arise when it appears that a particular transactional form deviates from usual business practices and bears little relation to commercial realities. While Congress did not intend to impose additional burdens with respect to the normal conduct of these transactions, neither did it intend to allow form to reign over substance. Thus, these exemptions should be applicable only upon

¹⁹⁰ And one can only assume that "contiguity" may refer to having a common planar point. Query, whether two plots, both having separate points in common with a third, but not with each other, are contiguous within the meaning of the statute.

¹⁹¹ 15 U.S.C.A. § 1701(3) (Supp. 1969).

¹⁹² *Id.* § 1702(a). The Regulations repeat the statutory exemptions and add others. See 24 C.F.R. § 1710.10, 34 Fed. Reg. 5931 (1969). The Secretary has exemptive power for "subdivisions" or "lots" where application of the Act is not necessary "in the public interest . . . by reason of the small amount involved or the limited character of the public offering." 15 U.S.C.A. § 1702(b) (Supp. 1969).

¹⁹³ 15 U.S.C.A. § 1702(a) (Supp. 1969).

¹⁹⁴ *Id.*

¹⁹⁵ At least if the securities analogy is followed. See 1 L. LOSS, *supra* note 48, at 712-13.

a showing that the form was consistent with normal business practices, and in this respect the burden of proof should not be severe. However, when it appears that there has been a departure from accepted business behavior, the developer ought to explain his conduct clearly in terms of purposes other than evasion of the Act.

Section 1403(a)¹⁹⁶ also exempts certain types of transactions which, unless carefully circumscribed, may provide developers with a ready escape from the provisions of the Act. The first of these is the rather curious specific exemption for those transactions excluded from the definition of subdivision.¹⁹⁷ The exemption is enigmatic because the Act applies only to transactions involving lots in a "subdivision,"¹⁹⁸ which is defined as "any land which is divided or proposed to be divided into fifty or more lots, whether contiguous or not, for the purpose of sale or lease as a part of a common promotional plan."¹⁹⁹ Nonetheless, section 1403(a)(1) *specifically* exempts "the sale or lease of real estate not pursuant to a common promotional plan to offer or sell fifty or more lots in a *subdivision*," unless, of course, the method of disposition is adopted for the purpose of evasion of the Act.²⁰⁰ Ordinarily, one would assume that all transactions not covered by the definition would be excluded without resort to an exemptive provision. *E converso*, one would not expect that lots brought within the pale of the Act, upon a necessary finding that they were offered as part of a common promotional plan, could then be exempted on the ground that they were not so offered. Even without the exemption, a developer who is marketing a tract composed of 20 lots (or, for that matter, 100 lots not pursuant to a common promotional plan) would not be covered by the Act. Unfortunately, there is no discussion of this point in any of the committee reports, nor was it brought out at the hearings.²⁰¹ Nevertheless, the restatement of the definitional exclusion in the form of an exemption, *subject to the evasive purpose caveat*, presents some interesting possibilities for expanding the scope of the Act.

For example, suppose a developer owns a tract of land which could be subdivided with equal convenience into either 30 one-acre lots or 60 half-acre lots, and that he elects the former. Clearly,

¹⁹⁶ 15 U.S.C.A. § 1702(a) (Supp. 1969).

¹⁹⁷ *Id.* § 1702(a)(1).

¹⁹⁸ *Id.* § 1703(a).

¹⁹⁹ *Id.* § 1701(3).

²⁰⁰ *Id.* § 1702(a)(1) (emphasis added).

²⁰¹ See note 189 *supra*.

he is outside the definition of "subdivision."²⁰² However, unless he can show that he did not have an evasive purpose, he would not be entitled to the exemption. He could argue, with great logical force, that he need not claim the benefit of the exemption (with its "purpose" limitation), because he is outside the Act *definitionally*. That is, one need tackle the evasive purpose issue of the exemption only if one cannot avoid the Act by not falling within the definition of "subdivision." But such an analysis might very well convert the section 1403(a)(1)²⁰³ exemption into mere surplusage. Alternatively, the two provisions can be read as being necessarily interdependent, resulting in an exclusion by way of the "subdivision" definition only if the failure to fulfill the terms of the definition is not the result of an evasive purpose. For example, it was early speculated that developers might attempt to bypass the Act by blocking acreage into subdivisions of less than 50 lots to be sold by separate but affiliated businesses.²⁰⁴ If it were impossible to bring such a practice within the coverage of the Act through a finding that the affiliates are "a group of developers acting in concert,"²⁰⁵ then, as an alternative, the evasive purpose clause could be invoked to prevent operation of both the definitional exclusion and the exemption.²⁰⁶

A second exemption applies to a subdivision where each individual lot is five acres or larger in size.²⁰⁷ This, indeed, is a deviation from the policies of the Act. The evidence adduced during the hearings tended to show that some of the worst frauds involved the sale of "investment acreage."²⁰⁸ In fact, one repeatedly condemned development was apparently marketed in two, five, and ten

²⁰² 15 U.S.C.A. § 1701(3) (Supp. 1969).

²⁰³ *Id.* § 1702(a)(1).

²⁰⁴ 1966 *Hearings* 304.

²⁰⁵ 15 U.S.C.A. § 1701(3) (Supp. 1969).

²⁰⁶ And, of course, a common promotional plan could be found, notwithstanding a failure to find that the affiliates were acting in concert. But the presumption of section 1402(3) would not be operative in this instance. Still a fourth method of blocking a split-business ploy would be to consider all the lots offered by the affiliates as offered "indirectly" by the common owners of the several businesses. Thus, such common owners would constitute a single "developer" within the meaning of section 1402(4). There might be some difficulty with this last analysis because the definition of developer seems to assume the presence of a "subdivision." This would indicate that the definition of developer cannot be used to determine whether or not there is a subdivision. But the same insoluble difficulty exists with respect to the definition of "subdivision," wherein the word "developer" appears twice.

²⁰⁷ *Id.* § 1702(a)(2).

²⁰⁸ See note 15 *supra*.

acre lots.²⁰⁹ A subdivision composed of 50 five-acre lots would be only three-eighths of a square mile — hardly beyond the capacities of most developers. In subdividing such a tract, a developer might be tempted to make all of the lots five acres or larger in order to avail himself of the exemption. Indeed, he may have this flexibility because of the nature of the land and the character of the real estate market. Furthermore, the unscrupulous developer who is selling uninspected parcels may not even consider the topography of the land in subdividing it. Thus, it is clear that, unless the evasive purpose test is given substantial content, this exemption gives the large tract developer the option of avoiding the Act simply by creating large lots.

In other cases — where the land is subject to a zoning law specifying a minimum lot size — it may appear that the only way the land can be marketed is in parcels of five acres or more. In this situation, the exemption may not be objectionable assuming that land subject to such restrictions is typically desirable and frequently located in prestigious areas. However, such an assumption will not always be verified, and, as indicated above, where the quality or potential of the land is more doubtful and evasiveness can otherwise be shown, compliance with the Act may be appropriate.

A third exemption embraces the sale or lease of a lot in a subdivision where the purchaser or his spouse personally inspects the parcel.²¹⁰ The history of this exemption furnishes a provocative study in the subtleties of the legislative process. Apparently, the Act was created primarily in reaction to fraudulent sales of land where purchasers were solicited by mail or telephone and did not see the land they were buying. Recognizing the early congressional preoccupation with sight-unseen sales, lobbyists strenuously argued for a personal inspection exemption. However, this recommendation was not incorporated into earlier versions of the Act. While the lobbyists may have been correct in their assertion that sight-unseen sales furnished the original stimulus for legislative investigation, it is equally apparent that the Act's evolving disclosure policy extended considerably beyond the mere dissemination of informa-

²⁰⁹ 1966 *Hearings* 37-38. The California Real Estate Commissioner commented: "Offerings of recreational, agricultural, and purely speculative subdivision lots carry the greatest dangers to the purchasing public." *Id.* at 120. It is also interesting to note that this exemption did not appear in the earlier drafts of the Act and was incorporated, without explanation, in the 1968 version. 1967 *Hearings* 4-36; 1966 *Hearings* 243-75.

²¹⁰ 15 U.S.C.A. § 1702(a)(10) (Supp. 1969).

tion that could be obtained by personal inspection.²¹¹ By requiring that purchasers be furnished with a property report prior to signing a contract, the Act assures that purchasers will be exposed to information which they need to know in order to make an intelligent decision. The property report must include the following information: (1) the extent to which a buyer is exposed to the risk of losing his investment in the event of the developer's bankruptcy; (2) the impact on the buyer in the event a blanket mortgage or other lien is foreclosed against the developer; (3) the arrangements made, if any, to assure the completion of proposed improvements;²¹² (4) the availability of such facilities as gas, water, sewage disposal, electricity, and telephones; and (5) the necessity for subsurface improvements or special foundations.²¹³ This information is not disclosed by visual inspection. Moreover, even if the inspecting purchaser requests such information, the developer may never give a reasonably intelligible reply but may, instead, resort to the very kind of evasive doubletalk which the Act was meant to prevent.²¹⁴ Since an exempt developer is not even required to supply purchasers with such information, severe evidence problems are presented in the event of alleged fraud.

At any rate, during consideration of the Act by the Senate, Senator Fulbright (who incidentally was not a member of the committees which had held the hearings) introduced this exemption, which strangely enough was substantially similar to one proposed by a lobbyist.²¹⁵ The amendment was passed with no debate whatsoever directed to its merits. In assessing the congressional intent underlying the exemption, it should be pointed out that the Act was merely one of 17 titles of the Housing and Urban Development Act of 1968,²¹⁶ which was considered in its entirety by the Senate.²¹⁷

²¹¹ See text accompanying notes 23-25 *supra*.

²¹² On this point, one witness noted that the developer's diminishing cash flow in the latter stages of development frequently makes it difficult for him to complete all the improvements promised. See 1966 *Hearings* 168.

²¹³ 15 U.S.C.A. §§ 1705, 1707(a) (Supp. 1969); 24 C.F.R. §§ 1710.105-110, 34 Fed. Reg. 5933, 5938 (1969).

²¹⁴ The policy deficiencies of this exemption are somewhat, but by no means wholly, ameliorated by the requirement that the land sold pursuant thereto be "free and clear of all liens, encumbrances, and adverse claims," except reservations for such things as roads and utilities and liens arising from taxes and assessments. 15 U.S.C.A. § 1702 (a)(10) (Supp. 1969).

²¹⁵ 114 CONG. REG. 15,270-72 (1968).

²¹⁶ 82 Stat. 476, published in 1968 U.S. CODE CONG. & AD. NEWS 547.

²¹⁷ This followed its being reported out by the Senate Committee on Banking and Currency. S. REP. NO. 1123, 90th Cong., 2d Sess. (1968).

Subsequently, the entire Housing and Urban Development Act was referred to Conference Committee to resolve the differences between the House and Senate versions.²¹⁸ However, the report from this Conference does not further delineate the purpose of the exemption.

Throughout the hearings, it became quite evident that even the "reputable" developers were using selling methods approaching "high pressure" tactics. It is not inconceivable that even a cautious person might have his doubts suppressed under similar circumstances. Indeed, one self-proclaimed ethical developer objected to giving purchasers a 48-hour grace period in those instances where the property report is received within 48 hours before the signing of an agreement.²¹⁹ Thus, while personal inspection may protect against the more obvious frauds, this exemption seems to gloss over the ingenious, subtle ones that can be equally devastating. It is submitted that, if the full disclosure policies of the Act are to be fulfilled, this exemption ought to be limited via the evasive purpose test to those situations where the type of information included in the property report is made available to prospective purchasers, or, at the very least, where the purchaser is completely protected against the risk of the developer's potential failures.

The doubtful value of personal inspection also underlies the specific exemption for the sale or lease of lots "on which there is a residential, commercial, or industrial building," or a sale or lease which obligates "the seller to erect such a building thereon within a period of two years."²²⁰ A partial justification for this exemption seems to be that, when a purchaser is buying a house (as opposed to a naked plot of land), he will likely take the time to inspect the property.²²¹ Once again, the basic premise of the exemption can reasonably be disputed,²²² though it must be conceded that a home buyer is not only likely to inspect his property but also to take additional protective steps, such as hiring a lawyer. As a theoretical matter, then, exemption for home-builder purchases ought to extend only to those situations where the developer can clearly show that his purchasers do not need the protections afforded by the Act. For

²¹⁸ See H.R. REP. NO. 1785, 90th Cong., 2d Sess. 161-62 (1968). See also HOUSE COMM. ON BANKING AND CURRENCY, 90TH CONG., 2D SESS., SUMMARY OF THE HOUSING AND URBAN DEVELOPMENT ACT OF 1968, at 59-60 (Comm. Print 1968).

²¹⁹ 1966 *Hearings* 103-09. See 15 U.S.C.A. § 1703(b) (Supp. 1969).

²²⁰ 15 U.S.C.A. § 1702(a)(3) (Supp. 1969).

²²¹ 1963 *Hearings* 304.

²²² 1967 *Hearings* 96-97.

instance, he might show that he has made information available to prospective purchasers which is substantially similar to that contained in the property report. Alternatively, he might show that since he has completed general improvements which are sufficient for the needs of the development, there is no need for any detailed information. In establishing the standards of proof in such cases, it must be remembered that a statutory exemption also provides immunity from the fraud provisions, and a purchaser in a statutorily exempt transaction is not necessarily more protected than other purchasers. Under normal circumstances, lots are sold prior to or during construction, and purchasers critically need information pertaining to the developer's plans and particularly regarding arrangements he has made to assure completion. They should be apprised of the anticipated costs of completing all improvements (no mean sum in many instances), should the developer fall upon hard times. Indeed, the value of individual lots may be largely determined with reference to a completed subdivision, since the worth of overall improvements accrues to the value of the lots. And it should not be forgotten that the property report, by informing prospective purchasers about the *bad* things of a development, serves to counterbalance the seductive poetry of salesmen. As a practical matter, application of the home-builder exemption according to the foregoing analysis may be impossible, because it will be difficult to charge the seller with choosing to sell lots with homes — rather than lots without homes — in order to evade the Act. Nevertheless, the Secretary should not hesitate to use the evasive purpose test, where possible, as a device for requiring developers to shoulder a heavy burden in demonstrating that they are entitled to such an exemption, especially where the theoretical justification for dispensing with compliance is not likely to be verified.

Finally, by Regulation, the Secretary has created an "intrastate" exemption.²²³ It is interesting to ponder the reasons why this exemption was not contained in the Act. The first two versions of the Act expressly provided for such an exemption,²²⁴ patterned closely after section 3(a)(11) of the Securities Act.²²⁵ While the express exemption was dropped from the Act as passed, its reappearance in regulatory form may have been a response to certain legislative re-

²²³ 24 C.F.R. § 1710.10(d), 34 Fed. Reg. 5931 (1969).

²²⁴ 1967 *Hearings* 7-8; 1966 *Hearings* 246.

²²⁵ 15 U.S.C. § 77c(a)(11) (1964).

marks which called upon the Secretary to furnish relief for intrastate offerings.²²⁶

The initial query is whether the Regulation was legitimately promulgated.²²⁷ In adopting the exemption, the Secretary must have invoked his rulemaking power under either section 1403(b)²²⁸ (referring to exemptive power in the case of small offerings or limited public offerings) or section 1419²²⁹ (general rulemaking authority). Section 1403(b), notwithstanding senatorial remarks to the contrary, does not appear to sanction administrative exemptions premised on the interstate or intrastate character of the offering. Rather, it authorizes exemptions based on size (presumably money²³⁰ or the number of lots²³¹) or the "limited character of the public offering." This latter phraseology could quite reasonably be read to refer to the extent to which the offering is public, *i.e.*, whether the lots, though many in number, will be offered to a relatively small group. Actually, this interpretation is well nigh inescapable. The same language appears in section 3(b) of the Securities Act,²³² and there has never been a suggestion that it authorizes the promulgation of an intrastate exemption by the SEC. That this terminology was not meant to function as a basis for an intrastate exemption is clear from the fact that it was included in the Securities Act, even though that Act contained a *statutory* intrastate exemption.²³³ This seems to suggest rather forcefully that the "limited character of the public offering" phraseology describes something besides "intrastate" character. This interpretative clash originated in the formative drafts of the Land Sales Act. Evincing a clear parallel to the Securities Act, the early drafts contained a specific statutory exemption for intrastate offerings.²³⁴ These original drafts also included

²²⁶ S. REP. NO. 1123, 90th Cong., 2d Sess. 111, 199-200 (1968) (combined views of Senators Bennett, Tower, and Hickenlooper); H.R. REP. NO. 1785, 90th Cong., 2d Sess. 161 (1968).

²²⁷ Whereas the proposed statutory exemption would have required a *wholly intrastate* offering before the exemption would apply, regulatory exemption is now extended where the offering is "entirely or almost entirely intrastate." 24 C.F.R. § 1710.10(l), 34 Fed Reg. 5931 (1969).

²²⁸ 15 U.S.C.A. § 1702(b) (Supp. 1969).

²²⁹ *Id.* § 1718.

²³⁰ *E.g.*, 24 C.F.R. § 1710.10(k), 34 Fed. Reg. 5931 (1969).

²³¹ For example, the situation where a developer currently intends to sell only three of the 50 lots in his subdivision.

²³² 15 U.S.C. § 77c(b) (1964).

²³³ *Id.* § 77c(a)(11).

²³⁴ See note 224 *supra* & accompanying text.

the administrative exemptive power,²³⁵ which certainly, in those drafts, was not meant to authorize a regulatory intrastate exemption. Thus, it seems quite clear that, by deleting the exemption from the statute before it was passed, Congress left the Act with no legislative exemption and with no administrative power to create one. Of course, one could ignore the analogy to the Securities Act and the draft history of the Land Sales Act, leaving the plain meaning of the exemptive provision as the sole focus of discussion. However, as already noted, the words themselves do not relate well to the notion of an exemption based on the intrastate nature of the offering, unless one adopts the view that confining an offer to a single state causes its "public" character to be "limited." This argument might have slight merit in sparsely populated states. However, as a general proposition, the thesis is considerably strained.

Perhaps authorization could be founded on the general rule-making power of the Secretary.²³⁶ However, this line of analysis runs seriously afoul of the maxim of statutory construction that Congress, by expressly providing an exemptive power in one section, implicitly excluded the inference of such exemptive authority from other sections. It is true that section 1419 gives the Secretary power to "classify,"²³⁷ but classification *within* the operation of the Act is quite different from avoidance of its application.

If the intrastate exemption is eventually held invalid, some developers who have relied on it may find themselves facing a number of damage or rescission actions under sections 1404(a)(1) and 1410(b)(1) for failure to register.²³⁸ Unfortunately, the Land Sales Act does not, like the Securities Act, provide a shield for those who rely in good faith on rules and regulations promulgated by the Secretary.²³⁹

Admitting, *arguendo*, the Secretary's power to promulgate the exemption, it may be fortunate that it arose through the administrative process, because the Secretary did what the drafters of the earlier versions failed to do: He framed the exemption so that it applies only with respect to the registration provisions of the Act and does not insulate qualifying developers from the fraud provi-

²³⁵ 15 U.S.C.A. § 1702(b) (Supp. 1969).

²³⁶ *Id.* § 1718.

²³⁷ *Id.*

²³⁸ *Id.* §§ 1703(a)(1), 1709(b)(1).

²³⁹ Compare Securities Act § 19(a), 15 U.S.C. § 77s(a) (1964), *with* 15 U.S.C.A. § 1718 (Supp. 1969).

sions.²⁴⁰ Thus, with respect to this one exemption, at least, the exemptive structure maintains its fidelity to the Securities Act philosophy — not relieving the seller of his liabilities under the fraud provisions simply because he need not comply with the plenary full disclosure requirements of registration.²⁴¹ This result would seem to depart, however, from the expectations of the committees who held hearings on the Act. They probably expected that this exemption would provide immunity from the entire Act, just as the other statutory exemptions do. The reason for total immunity under the statutory exemptions is a matter for conjecture. When Manuel Cohen, then Chairman of the Securities and Exchange Commission, testified, he urged that qualifying developers should not be exempt from the fraud provisions,²⁴² but his efforts were in vain. However, the Secretary apparently heeded the Chairman's suggestion, at least with respect to the "intrastate" exemption.

The language of this exemption is fraught with troublesome terminology which no doubt will produce more than a few interpretative hassles. It states that "[t]he sale or lease of lots where the offering is entirely or almost entirely intrastate" shall be exempt from the registration provisions, subject to the evasive purpose condition.

Initially, the "intrastate-interstate" concepts connected with the exemption should not be confused with the similar-sounding notions involved in the jurisdictional means context.²⁴³ The exemption may apply (*i.e.*, the offering may be "intrastate") even though the jurisdictional means (interstate facilities or the mails) are used. The requirement of the exemption is that the promotional campaign (as contrasted with actual sales) must not extend significantly beyond the borders of a given state. The thrust of the exemption is premised on the assumption that when land is being *offered* to local persons, there is no need to require registration since they would have the opportunity to evaluate the quality of the development themselves.²⁴⁴ Query, however, whether this rationale is sound considering that in many states a prospective purchaser might

²⁴⁰ 24 C.F.R. § 1710.10(*l*), 34 Fed. Reg. 5931 (1969).

²⁴¹ See Securities Act §§ 3, 4, 12(2), 17(a), (c), 15 U.S.C. §§ 77c, d, 1(2), q(a), q(c) (1964).

²⁴² 1967 *Hearings* 55; 1966 *Hearings* 89.

²⁴³ See text accompanying notes 104-25 *supra*.

²⁴⁴ Since the exemption refers to the character of the "offering," the conclusion is inexorable that the location of the *offerees* (not the ultimate purchasers alone) is critical. See 1 L. LOSS, *supra* note 48, at 655-56.

have to drive several hundred miles to inspect his land. Moreover, if land located in state X is offered entirely within state Y, the exemption, on its face, would seem to be apposite.²⁴⁵ However, this problem could be avoided by reading the exemption to apply only when the offering is intra the state in which the land is located.²⁴⁶

The exemption does leave to the states the exclusive power to regulate offerings taking place entirely or almost entirely within their borders, but this justification is not without its difficulties. For instance, suppose land located in state X is offered entirely within that state by a developer operating out of state Y. State X (which is both the investor and the situs state) might have a law governing the sale of subdivisions. However, it may choose not to enforce its law against the developer, either because it feels it lacks jurisdiction or because it lacks the resources to police offers coming across its borders.²⁴⁷ To minimize this problem, the exemption could be further limited to apply only when the offering is intra the state in which the land *and* the offeror are located.²⁴⁸ All this might be accomplished either by amending the Regulation or by invoking the evasive purpose condition on the exemption.

It is notable that this exemption, unlike its analogue in the Securities Act, does not expressly require that the offerees be "residents" — a term interpreted to mean domiciliaries.²⁴⁹ However, unless the exemption is limited to residents of some sort, it will be possible to direct offers to transients and vacationers, who are not localized in outlook and knowledge.

The foregoing discussion has stressed the notion that a broad application of certain exemptions will result in an unwarranted denial of the protections of the Act. Conversely, it should be noted that the lack of an exemption does not deprive a developer of the right to sell his land, but merely requires that he furnish full disclosure and avoid fraud. The vehicle by which these exemptions are kept within bounds is the evasive purpose condition. The normal procedure for interpreting this phrase would be to refer to its legislative history, but, unfortunately, this source is silent. Refer-

²⁴⁵ 24 C.F.R. § 1710.10 (*l*), 34 Fed. Reg. 5931 (1969).

²⁴⁶ Similarly, securities must be offered intra the state in which the issuer is doing business in order for the Securities Act intrastate exemption to apply. 15 U.S.C. § 77c(a)(11) (1964).

²⁴⁷ On the question of state regulation and the jurisdictional issues and inhibitions involved therein, see text accompanying notes 60-68 *supra*.

²⁴⁸ Cf. 15 U.S.C. § 77c(a)(11) (1964).

²⁴⁹ For a short but informative analysis of section 3(a)(11), see Sowards, *The Intra-state Exemption*, 2 REV. SEC. REG. 922 (1969).

ence to the original drafts of the Act reveals that the evasive purpose clause was not inserted until the final version.²⁵⁰ The same terminology appears in the *Uniform Land Sales Practices Act*, which was approved by the Commissioners on Uniform State Laws in 1966.²⁵¹ Again the proceedings and the comments fail to provide any insight.²⁵² Thus, the phrase is amenable to construction in accordance with the general policies of the Act.

As an original proposition, the term "evasion" could be read to convey the notions of "sole" purpose and a rather specific untoward intent. On the other hand, it could be equated with the term "avoidance," thus eliminating the elements of scheme, artifice, or contrivance. The latter interpretation would seem to be preferred, since, under the former, a developer could avail himself of an exemption upon a showing of *any* legitimate business purpose, no matter how obscure. The preferred test would require a developer to show that his knowledge of the consequences of an exemption did not materially contribute to his decision, *i.e.*, that other legitimate considerations were primarily determinative. In short, the developer would have to demonstrate that an exempted form was the only practical way to market his land, or at least, that it was significantly more advantageous than a form which would bring the transaction within the Act.²⁵³ Another more lenient formulation of the evasive purpose test would necessitate a showing that avoidance was not a dominant or principal purpose, *i.e.*, that some legitimate considerations were of at least equal importance.

In establishing the dimensions of the evasive purpose limitation, the courts and the Secretary should remain mindful of the following: First, the denial of an exemption does not prohibit the developer from adopting a particular means of marketing his land; it merely subjects him to the coverage of the Act, thus affording protection to the purchaser. Second, developers possess differing degrees of flexibility in choosing the manner in which they wish to dispose of their lots. Some developers may rather freely determine the mode of marketing their land; others have little range of choice.

²⁵⁰ 1967 *Hearings* 7; 1966 *Hearings* 245.

²⁵¹ UNIFORM LAND SALES PRACTICES ACT § 3, *published in* 1967 *Hearings* 235.

²⁵² *Id.*

²⁵³ By referring to "*the* purpose of evasion," 15 U.S.C.A. § 1702(a) (Supp. 1969) (emphasis added), Congress could be held to have meant "any" or "a" purpose, and not a sole or even dominant purpose. *Cf.* *United States v. Donruss Co.*, 393 U.S. 297 (1969). In situations where a developer is in doubt about the availability of any exemption, he can seek an "exemption advisory opinion" from the Secretary. 24 C.F.R. § 1710.15, 34 Fed. Reg. 5931 (1969).

Third, the complexity of the decision-making process and the difficulty of weighing factors which might influence the formation of intent point up the need for objective criteria.

Finally, there is nothing in the Act to suggest that the evasive purpose test must be used on an all-or-nothing basis. To illustrate, where there is evidence of evasive purpose in connection with the subdivision of a tract into 49 lots instead of 50, the courts and the Secretary might take the position that the developer was exempt from the statement of record and property report requirements of the Act, but not free from coverage of the general antifraud provision.²⁵⁴

C. *Coordination with State Compliance*

The Act does not preempt the role of the states in the regulation of subdivision sales.²⁵⁵ Indeed, the Secretary is authorized to accept certain state materials in fulfillment of the statement of record and property report filing requirements of the Act, if he finds such action to be in the public interest and for the protection of purchasers.²⁵⁶ Thus far, the Secretary has made such a finding with respect to California, Florida, New York, Hawaii, and Illinois.²⁵⁷ This approach, the reverse of the style of coordination prevalent in the securities industry,²⁵⁸ was apparently intended to encourage state legislation.²⁵⁹ Whether the Act will actually stimulate state regulation is a debatable matter. Some have suggested that it will have precisely the opposite effect.²⁶⁰

²⁵⁴ 15 U.S.C.A. § 1703(a)(2) (Supp. 1969). In its penultimate version (S. 275, 90th Cong., 1st Sess. (1967)), the Act did not contain an evasive purpose limitation on exemptions. Like the Act as finally passed, however, it did not specifically preserve the coverage of the antifraud provisions where exemptions were available. Thus, S. 275 allowed no leeway for "splitting" the applicability of the registration and antifraud sections, so that one might apply when the other didn't. This result was criticized on the theory that the fraud section ought to be left active in many cases where registration is excused. See Note, *supra* note 83, at 730-31. The evasive purpose circumscription on exemptions could furnish the statutory handle for the desired flexibility of coverage.

²⁵⁵ 15 U.S.C.A. § 1708(b) (Supp. 1969).

²⁵⁶ *Id.* § 1708(a).

²⁵⁷ 24 C.F.R. § 1710.25, 34 Fed. Reg. 9757 (1969).

²⁵⁸ Where the use of federal materials is allowed as compliance with state requirements. See 1967 *Hearings* 59; UNIFORM SECURITIES ACT § 303.

²⁵⁹ 111 CONG. REC. 27,311 (1965); 113 CONG. REC. 316 (1967).

²⁶⁰ It is argued that investor-only states would be happy to stay out (or get out) of the business of regulating offers involving developers and land located outside their borders, because such offers are primarily interstate and raise unwieldy administrative as well as theoretical problems. See 1966 *Hearings* 52, 150. Situs states, too, might be tempted to reduce enforcement of their laws when sellers and buyers reside outside their boundaries.

In any event, the coordination technique of the Act should reduce the cost of compliance somewhat by eliminating duplicative filings where the Secretary accepts state materials. Furthermore, the Act does constitute an improvement over the approach taken in the 1964 Amendments to the Securities Exchange Act of 1934.²⁶¹ The Exchange Act grants certain exemptions for securities subject to state regulations equivalent to their federal counterparts.²⁶² However, the issuers of the securities are left to guess whether the state regulation is "equivalent enough."²⁶³ Under the Land Sales Act, a finding of the Secretary regarding the acceptability of state materials is authorized and required.

It is also fairly clear that the coordination process of the Act will not accomplish the substantial monetary saving and uniformity that would have resulted from federal preemption and that might have accompanied a practice whereby state authorities could adopt federal compliance as their own.²⁶⁴

VI. ENFORCEMENT PROVISIONS

Violation of the Land Sales Act may expose a developer and his agents to a host of sanctions — administrative, civil, and criminal. Prior to the Act, federal jurisdiction over real estate frauds was asserted mainly under the mail fraud statutes, the FTCA, and the securities laws.²⁶⁵ However, these avenues of attack were largely ineffective primarily because of the time involved in obtaining convictions, the impotency of both the Post Office "fraud order" and the FTC stop order, the total absence of private civil remedies, and the general lack of prophylaxis.²⁶⁶ During the hearings on the Land Sales Act, it was suggested that real estate frauds should be dealt with by amending the mail fraud statutes and the FTCA rather than by creating a new act. This was rejected. Instead, Congress passed the Interstate Land Sales Full Disclosure Act equipped with broad disclosure and antifraud requirements to be implemented via its extensive enforcement machinery.

²⁶¹ 15 U.S.C. § 78a *et seq.* (1964).

²⁶² *Id.* § 78l(g) (2) (G).

²⁶³ *See* 1967 *Hearings* 52, 57-58.

²⁶⁴ Unless, of course, the Act encourages many states to repeal their own land sales laws.

²⁶⁵ *See* text accompanying notes 34-53 *supra*.

²⁶⁶ *Id.*

A. *Administrative and Criminal Proceedings and Actions*

The Secretary is authorized to make investigations to determine whether any person has violated, or is about to violate, the Act.²⁶⁷ For this purpose, he may subpoena witnesses, compel their attendance and testimony, and require the production of records.²⁶⁸ If a witness refuses to comply, the Secretary may seek a court order, a violation of which may be enforced by contempt proceedings.²⁶⁹ Furthermore, a witness is not excused from complying with the order of the Secretary merely by invoking the fifth amendment privilege against self-incrimination.²⁷⁰ However, if he is compelled to testify or produce records, after invoking the privilege, he is immune from criminal prosecution.²⁷¹ Nevertheless, he would not be immune from civil actions for injunctive relief or damages based upon such evidence. Thus, the Secretary may well utilize his investigative powers to gather evidence as an aid to defrauded parties, who, individually, might not have been able to undertake this expensive process. Most importantly, the Secretary may use such evidence to commence an injunctive proceeding against persons who have violated, or who are about to violate, the Act.²⁷² Moreover, a developer may be criminally prosecuted for willful violations of any of the provisions of the Act or the Regulations, and upon conviction fined up to \$5,000 and imprisoned for five years.²⁷³

B. *Private Civil Liabilities*

The Land Sales Act imposes liability on developers for a wide range of deceptive conduct and provides remedies for purchasers in a variety of situations. To enforce his rights under the Act, a purchaser may select either a federal or state forum, since both have concurrent jurisdiction.²⁷⁴ It is probably more desirable to commence such an action in federal court. Here, of course, one has the advantage of nationwide service of process and broad venue provisions which allow suits to be brought in any district where "the defendant is found or is an inhabitant or transacts business, or in the

²⁶⁷ 15 U.S.C.A. § 1714(b) (Supp. 1969).

²⁶⁸ *Id.* § 1714(c).

²⁶⁹ *Id.* § 1714(d).

²⁷⁰ *Id.* § 1714(e).

²⁷¹ *Id.*

²⁷² *Id.* § 1714(a).

²⁷³ *Id.* § 1717.

²⁷⁴ *Id.* § 1719.

district where the offer or sale took place.”²⁷⁵ The jurisdiction of the federal courts is not affected by the amount in controversy or the citizenship of the parties.²⁷⁶

Nor do the remedy provisions of the Act preempt the field; a plaintiff may avail himself of “any and all other rights and remedies that may exist at law or in equity”²⁷⁷ — most notably, the remedies provided by state statutes regulating the sale of land in subdivisions²⁷⁸ and actions for damages or rescission based on common law or equitable fraud. Because of the different types of relief allowed, it may be desirable to base a claim on several different theories of recovery. If successful, a plaintiff might, for example, be granted damages under the Land Sales Act²⁷⁹ as well as punitive damages based on common law fraud.

1. *Common Law Fraud: A Basis for Comparison.*— The full significance of the Act’s private civil remedies can best be appreciated by comparing them with the traditional common law and equitable remedies. As will become apparent shortly, the normal elements of these actions have been substantially modified and in some cases even eliminated by the Act.

In a common law fraud action, one would have to elect either rescission, founded in equity, or the legal tort of deceit. Rescission seeks to restore the status quo; a plaintiff must allege and prove (1) a misrepresentation of (2) a material (3) fact (4) on which he relied.²⁸⁰ In addition, the parties must be in privity of contract, and the plaintiff must be able to tender the property. Moreover, the party pursuing the action must be able to avoid the affirmative defenses of laches, estoppel, waiver, and ratification.²⁸¹ An action for deceit, on the other hand, allows a more generous measure of

²⁷⁵ *Id.* On the meaning of similar language under the federal securities laws, see *Zorn v. Anderson*, 263 F. Supp. 745 (S.D.N.Y. 1966).

²⁷⁶ Language virtually identical to section 1420(a), 15 U.S.C.A. § 1719(a) (Supp. 1969), in Securities Act section 22(a), 15 U.S.C. § 77v(a) (1964), has been interpreted as giving the federal courts jurisdiction “irrespective of the amount in controversy or the citizenship of the parties.” *Deckert v. Independent Shares Corp.*, 311 U.S. 282, 289 (1940) (Securities Act § 12(2)); *Wilco v. Swan*, 346 U.S. 427, 431 (1953) (same). See generally 1 L. LOSS, *supra* note 48, at 2005-07.

²⁷⁷ 15 U.S.C.A. § 1713 (Supp. 1969).

²⁷⁸ In Ohio, for example, the blue sky law which regulates the sale of securities in the state defines the term “security” as including “real estate not situated in this state and any interest in real estate not situated in this state.” OHIO REV. CODE ANN. § 1707.01(B) (Page 1953). See also text accompanying notes 56-59 *supra*.

²⁷⁹ 15 U.S.C.A. § 1709(c) (Supp. 1969).

²⁸⁰ RESTATEMENT OF CONTRACTS § 471 (1932); RESTATEMENT OF RESTITUTION § 8 (1937).

²⁸¹ RESTATEMENT OF CONTRACTS §§ 482-85 (1932).

recovery and is not subject to the equitable defenses or the privity requirement.²⁸² In spite of its freedom from some of the impediments to rescissional relief, an action in deceit involves a more complex set of elements: (1) A misrepresentation of (2) a material (3) fact; (4) scienter (*i.e.*, that the defendant knowingly made a false statement to induce reliance); (5) justifiable reliance by the plaintiff, (6) causing (7) damage; and (8) malice, if punitive damages are sought.²⁸³ In view of these requirements the proof in support of a claim for deceit is greater than that required to support a claim for rescission. To obtain rescission, a plaintiff need not prove a causal relationship between the misrepresentation and the damage. Indeed, it is not even necessary that there be any damage.²⁸⁴ Furthermore, rescission may be granted without proof of the seller's fraudulent intent, but, if this fact is shown, materiality need not be proven.²⁸⁵

It is against this background of common law fraud and equitable rescission that the remedies under the Land Sales Act will be analyzed. At the outset, it should be recognized that Congress felt that the traditional common law and equitable remedies were inadequate in the land sales context.²⁸⁶ Thus, powerful new anti-fraud weapons were created. In addition, Congress provided new mechanisms to enforce the full disclosure requirements of the Act (*i.e.*, those portions of the Act calling for disclosure over and above mere avoidance of fraud). These devices operate to relieve a defrauded or uninformed party of many of the burdens he was subjected to at common law.

2. *Effective Registration Statement and Timely Delivery of a Property Report.*— The Act prohibits sales or leases of land at any time prior to the effective date of the statement of record and requires that the property report be furnished to the prospective purchaser or lessee prior to his signing an agreement.²⁸⁷ A viola-

²⁸² W. PROSSER, HANDBOOK OF THE LAW OF TORTS § 102 (3d ed. 1964). It is sufficient that the plaintiff was one of the class of persons intended to be misled. In addition, there has been a tendency to extend liability to those persons whose reliance upon the representation may be reasonably anticipated, without regard to intent. *Id.*

²⁸³ *Id.* at § 100. RESTATEMENT OF CONTRACTS § 476, comment *c* (1932).

²⁸⁴ 3 J. POMEROY, EQUITY JURISPRUDENCE § 898a (1941).

²⁸⁵ RESTATEMENT OF CONTRACTS § 470 (1932); RESTATEMENT OF TORTS § 538, comment *g* (1938). If the seller makes an intentional misrepresentation of a material fact, he has the burden of proving that the purchaser did not rely on such statement. RESTATEMENT OF CONTRACTS § 479 (1932).

²⁸⁶ See 111 CONG. REC. 27,311-12 (1965); 1965 REPORT 30-36; 1963 *Hearings* 235; 113 CONG. REC. 315, 3529 (1967); 1966 *Hearings* 68, 79-80, 221.

²⁸⁷ Section 1404(a)(1) makes it unlawful for any developer or agent "to sell or lease

tion of these provisions entitles the purchaser or lessee to either rescission or damages.²⁸⁸

If the prospective purchaser signs the contract prior to receiving a copy of the property report, his right to rescind the contract is absolute.²⁸⁹ The absence of statutory affirmative defenses in favor of the developer (except for a statute of limitations) gives the purchaser an exclusive option to exercise his right to void the contract. Failure to deliver the property report is the gravamen of the offense. The purchaser, therefore, need not prove anything more than the fact that he signed the contract before he received the property report. None of the other elements which are essential to recovery under other provisions of the Act or at common law are relevant. The exercise of this right provides the purchaser with a defense for his failure to perform as well as giving him the right of restitution in the event that he fulfills the contract. Alternatively, if the purchaser should decide that he would rather retain the land, he may institute an action for statutory damages.²⁹⁰

The developer does not fulfill his obligation merely by furnishing a property report *shortly* before the buyer signs the contract. Since a property report hardly performs its disclosure function unless there is sufficient time to read and understand it, the purchaser is allowed to rescind his obligation when the property report is furnished less than 48 hours prior to signing the agreement, and this statutory privilege must be expressly stated in the agreement. This right, however, is only exercisable for 48 hours after signing,²⁹¹ and

any lot in any subdivision unless a statement of record with respect to such lot is in effect in accordance with section 1407 and a printed property report, meeting the requirements of section 1408, is furnished to the purchaser in advance of the signing of any contract or agreement for sale or lease by the purchaser . . .” 15 U.S.C.A. § 1703(a)(1) (Supp. 1969).

²⁸⁸ *Id.* §§ 1703(b), 1709(b)(1), (c). Where the action is based on the non-effectiveness of a statement of record at time of purchase, sections 1404(a)(1), 1410(b)(1), and 1410(c), *id.* §§ 1703(a)(1), 1709(b)(1), (c), are apposite. Although none of these sections speaks of rescission, the use of the word “may” in the damage provision, section 1410(c), would indicate that the equitable action of rescission is also available.

²⁸⁹ Section 1404(b), *id.* § 1703(b), provides: “Any contract or agreement for the purchase or leasing of a lot in a subdivision covered by this title, where the property report has not been given to the purchaser in advance or at the time of his signing, shall be voidable at the option of the purchaser.” This option is presumably enforceable through section 1410(b)(1), *id.* § 1709(b)(1).

²⁹⁰ *Id.* § 1709(c).

²⁹¹ Section 1404(b), *id.* § 1703(b), provides:

A purchaser may revoke such contract or agreement within 48 hours, where he has received the property report less than 48 hours before he signed the contract or agreement, and the contract or agreement shall so provide, except that the contract or agreement may stipulate that the foregoing revocation authority shall not apply in the case of a purchaser who (1) has received the property re-

it may be negated if the purchaser signs a statutory waiver of the privilege.²⁹² The foregoing provisions are applicable to both the developer and his "agents."²⁹³

3. *False Statements of Record and Property Reports.*— Sections 1410(a) and (b)(2) set forth the enforcement machinery of the full disclosure requirements of the Act.²⁹⁴ They are stiff relief provisions meant to assure that the statement of record and the property report are prepared with extraordinary diligence. They impose liability if the statement of record, when it became effective, or the property report, at the time of sale, "contained an untrue statement of material fact or omitted to state a material fact required to be stated therein [or necessary to make the statement therein not misleading]."²⁹⁵ The quoted language deviates from its analogues in the Securities Act²⁹⁶ in one important respect: The bracketed language was deleted in the Land Sales Act. Since this language functions in the Securities Act to prohibit half-truths, the omission could have seriously weakened the Land Sales Act. However, pursuant to his authority to specify the content of statements of record and property reports,²⁹⁷ the Secretary has incorporated the bracketed language in his Regulations.²⁹⁸

Reading sections 1410(a) and 1410(b)(2) in conjunction with the itemized disclosure requirements of the Act and the regula-

port and inspected the lot to be purchased or leased in advance of signing the contract or agreement, and (2) acknowledges by his signature that he has made such inspection and has read and understood such report.

²⁹² *Id.*

²⁹³ *Id.* §§ 1703(a)(1), 1709(b)(1). See section 1402(5), *id.* § 1701(5), for the definition of "agent." Query, whether a paid publisher of advertisements is the agent of the developer.

²⁹⁴ The section provides in part:

(a) Where any part of the statement of record, when such part became effective, contained an untrue statement of a material fact or omitted to state a material fact required to be stated therein, any person acquiring a lot in the subdivision covered by such statement of record from the developer or his agent during such period the statement remains uncorrected (unless it is proved that at the time of such acquisition he knew of such untruth or omission) may, either at law or in equity, in any court of competent jurisdiction sue the *developer*. (b) Any *developer* or *agent*, who sells or leases a lot in a subdivision . . . (2) by means of a property report which contained an untrue statement of material fact or omitted to state a material fact required to be stated therein, may be sued by the purchaser of such lot. *Id.* §§ 1709(a), (b)(2) (emphasis added).

²⁹⁵ *Id.* § 1709(b)(2).

²⁹⁶ 15 U.S.C. §§ 77k(a), 77l(2) (1964).

²⁹⁷ 15 U.S.C.A. §§ 1705(12), 1707(a) (Supp. 1969).

²⁹⁸ 24 C.F.R. § 1710.105, 34 Fed. Reg. 5933 (1969).

tions,²⁹⁹ a developer is under a duty to avoid the use of patent falsities and half-truths. Furthermore, he is under an affirmative duty to disclose specifically designated items of information. In this latter respect, the Act imposes duties in excess of those prevailing at common law. Traditionally, actionable misrepresentations have included, in addition to outright lies,³⁰⁰ half-truths (*i.e.*, those statements which are true as far as they go, but are misleading because of the absence of pertinent qualifications) and ambiguous statements (*i.e.*, those which are capable of two interpretations, one true and the other false).³⁰¹ However, there was no liability for omissions, except where there was a duty of disclosure based upon a fiduciary relationship, an implied representation of fair dealing, superior access to information, or a statutory requirement.³⁰²

Just as the Act and Regulations require disclosure of information which would probably not have been required at common law, in certain cases the general notions of the common law may be invoked to impose a duty to disclose matters not expressly required to be mentioned in itemized schedules. Although the itemized requirements are quite comprehensive, they are not exhaustive. Indeed, it is entirely conceivable that developers may possess material information which is not specifically enumerated. In these instances, recourse may be had to the common law, where sellers of real estate are under an affirmative duty to disclose in several situations: where the seller has superior knowledge of extraordinary conditions; where the seller knows facts which the purchaser has no reasonable means of discovering; where the seller discovered information by undertaking an investigation, even though there was no initial need to investigate; and where the purchaser does not have an opportunity to acquire information, such as concealed facts known to the seller.³⁰³ Disclosure of these types of

²⁹⁹ 15 U.S.C. §§ 1705, 1707 (Supp. 1969); 24 C.F.R. §§ 1710.20, .105, .110, 34 Fed. Reg. 5931-32, 5933-39 (1969).

³⁰⁰ RESTATEMENT OF TORTS § 527 (1938).

³⁰¹ *Id.* § 529.

³⁰² RESTATEMENT OF CONTRACTS § 472 (1932); RESTATEMENT OF RESTITUTION § 8, comment *b* (1937); RESTATEMENT OF TORTS § 551 (1938).

³⁰³ For cases holding that a seller of real estate committed actionable fraud by failing to disclose subsurface defects which were known to him and where such information was not reasonably available to the purchaser, see *Buist v. Dudley DeVelbiss Corp.*, 182 Cal. App. 2d 671, 6 Cal. Rptr. 259 (1960) (failed to disclose that the lot was known to be in an area of underground water and in an area of an ancient slide); *Central Mut. Ins. Co. v. Schmidt*, 152 Cal. App. 2d 671, 313 P.2d 132 (1957); *Coen v. Vivian*, 141 Colo. 443, 349 P.2d 336 (1960); *Ramel v. Chasebrook Constr. Co.*, 135 So. 2d 876 (Dist. Ct. Fla. 1961); *Brooks v. Ervin Constr. Co.*, 253 N.C. 214, 116 S.E.2d 454 (1960). For additional cases construing the scope of common law fraud, see Gil-

data in the statement of record and property report may be required by sections 1410(a) and 1410(b)(2) on the ground that they are matters "required to be stated therein." Such a construction would be in line with Congress' concern over "omissions"³⁰⁴ and clearly recognizes that duties of disclosure may arise from sources of law independent of the *express* requirements of the Act.³⁰⁵

In the event of an omission, the question arises whether the developer should be held liable when the failure to disclose was innocent rather than negligent or intentional. This consideration raises the problem of scienter, an element essential to recovery for common law deceit.³⁰⁶ With respect to the itemized disclosure requirements of the Act, the issue is irrelevant since sections 1410(a) and (b)(2) make no reference to the element of intent.³⁰⁷ To the extent that the Act requires itemized disclosure of specific facts, the developer is under an absolute duty to provide accurate information. He is responsible for undertaking investigations to ascertain these facts, and, to the extent that he makes affirmative representations, he is held absolutely accountable. If a developer states that he has

bert v. Corlett, 171 Cal. App. 2d 116, 339 P.2d 960 (1959) (failure to make known the content of an engineering report indicating that the property had little value due to subsidence); Whiten v. Orr Constr. Co., 109 Ga. App. 267, 136 S.E.2d 136 (1964) (nondisclosure of a large sewer on the premises, resulting in damages to the house constructed thereon and to the land itself); Walsh v. Edwards, 223 Md. 552, 197 A.2d 424 (Ct. App. 1964) (failure to disclose likelihood of a nearby creek flooding); Gamel v. Louis, 373 S.W.2d 184 (Mo. Ct. App. 1963).

³⁰⁴ See note 286 *supra*. Cf. SEC v. Great Am. Indus., Inc., 407 F.2d 453 (2d Cir. 1968), *cert. denied*, 395 U.S. 920 (1969) (general antifraud section, such as section 1404(a)(2), 15 U.S.C.A. § 1703 (a)(2) (Supp. 1969), superimposed on itemized disclosure requirements).

³⁰⁵ Especially when the developer has engaged in a heavy selling campaign before the effectiveness of the statement of record and the use of a property report. See text accompanying notes 169-83 *supra*. The question of whether compliance with the *itemized* disclosure requirements of the Securities Act avails an issuer of a safe harbor or merely fulfills the issuer's minimum duty has not been resolved. See 3 L. LOSS, *supra* note 48, at 1702.

³⁰⁶ At common law, a seller was liable for old style deceit only if he knew that his statement was false and made such statement with the intention of misleading the purchaser. RESTATEMENT OF TORTS § 526, 531 (1938). However, in an action for rescission, a seller was liable even for innocent material misrepresentations. RESTATEMENT OF CONTRACTS § 476, comment *b* (1932).

³⁰⁷ The scienter element was eliminated from sections 11 and 12(2) of the Securities Act, 15 U.S.C. §§ 77k, l(2) (1964), and the defense of the issuer's due diligence was substituted. Thus, most defendants under those sections were protected from liability for nondisclosure of information which could not reasonably be discovered. See, e.g., Escott v. BarChris Constr. Corp., 283 F. Supp. 643 (S.D.N.Y. 1968). However, *even the due diligence defenses have been dropped from the Land Sales Act*. In this connection, it is important to note that earlier versions of the Act contained virtual copies of Securities Act sections 11 and 12(2). See 1967 *Hearings* 19-26. Then, suddenly, present sections 1410(a) and 1410(b)(2), 15 U.S.C. §§ 1709(a), (b)(2) (Supp. 1969), were substituted, devoid of all the qualifying language contained in their predecessors.

clear legal title to the property in question, he is held strictly to the accuracy of that representation. If it later turns out that there is a paramount title holder, the existence of which the developer could not have ascertained by reasonable investigation, he is held liable nonetheless.³⁰⁸ In this respect, the Act shifts the risk of loss to the developer.

The situation is somewhat different with respect to the incorporation of the common law duties of disclosure. If it is held that the statement of record and property report must contain information beyond the itemized data, reference should be made to the common law to determine the scope of the duty to disclose such additional information.³⁰⁹ In common law deceit, the information must be *known* to the seller and unavailable to the purchaser.³¹⁰ If the developer states that his information is based upon his own investigation, he will be held liable for misstatements resulting from a negligent investigation, based upon the implied representation that the investigation was undertaken with due care.³¹¹ However, the common law does not hold a developer liable for not disclosing information of which he has no knowledge, regardless of how significant it may be. Moreover, it does not seem to matter whether his ignorance stems from an actual failure to investigate or from an oversight in a negligent investigation. In the securities cases, there is considerable dicta which would impose liability, even in the case of innocent or negligent nondisclosure. But this approach seems to be predicated on the concept of corporate fiduciary duty, particularly the presumption that corporate management personnel, being in control of the corporation, are knowledgeable about the business.³¹² However, in real estate transactions, this relationship does not exist. Unlike his counterpart in the securities area, the developer lacks physical mastery over the realty that he sells. There are numerous latent defects that can only be discovered by expensive and frequently useless surveys. The Land Sales Act should not attempt to make the developer an insurer of the land he sells; rather, it should seek to compel him to deal fairly with the purchaser and

³⁰⁸ It remains to be seen whether a developer can protect himself by making qualified statements to the effect that no outstanding legal interests appear in its chain of title, even though there may be such interests outside its chain of title.

³⁰⁹ Since sections 1410(a) and 1410(b)(2), 15 U.S.C.A. §§ 1709(a), (b)(2) (Supp. 1969), are so absolute in nature, it is arguable that only the elements of the claim and defenses expressly stated therein should apply, even to the disclosure beyond the itemized type specified by the Act and Regulations.

³¹⁰ See cases cited note 303 *supra*.

³¹¹ W. PROSSER, *supra* note 282, at 724-29.

³¹² See *Ellis v. Carter*, 291 F.2d 270 (9th Cir. 1961).

to place both the buyer and seller on equal informational levels by affording the former access to the seller's information. Providing the purchaser with such information enables him to make an intelligent decision. If a destructive earthquake occurs because of a fault unknown to the seller, there is no reason why the risk of loss should be placed upon the developer. However, if the developer knew of or suspected the existence and significance of the fault, he should be held liable.

At common law, as well as under the Act, the facts which must be disclosed completely and accurately are those which are *material*. The significance of the data available to the purchaser is judged by an objective standard reflecting the policy that facts which are unlikely to influence average purchasers should not be actionable. Imposing upon the seller the duty of ascertaining the accuracy of statements about such facts, much less remembering to disclose them, would be too great a burden. Thus, the law looks to that faceless fiction — the reasonable man — to determine the significance of particular facts. At common law, materiality appears to be a rather stable concept. Essential to the right of recovery is "fault," a label which the courts are hesitant to apply, particularly in cases of alleged fraud. However, by gerrymandering the scope of materiality, the courts can tailor the remedy to the situation. If a misrepresentation is made with actual knowledge that it would be regarded as significant by a purchaser, it is automatically material.³¹³ Otherwise, a fact is not material unless "its existence is a matter to which a reasonable man *would* attach importance in determining his choice of action in the transaction in question."³¹⁴ Although this test is not as stringent as it might be, it does require a degree of certainty that the facts, as represented, would ordinarily enter into a reasonable purchaser's decision-making process.

This standard may be appropriate for purposes of the common law, especially since it was designed to apply to a variety of situations. However, it is submitted that the policies of the Land Sales Act require a broader standard. It must be remembered that this is a disclosure-type statute which is designed to expose the purchaser to extensive, but distilled, information. Its purpose is to place the buyer and the seller on equal informational levels, and to provide the purchaser with accurate information upon which he can base a well-reasoned decision. Consequently, the Act should afford very

³¹³ RESTATEMENT OF TORTS § 538(2) (b) (1938).

³¹⁴ *Id.* § 538(2) (a) (emphasis added).

little latitude for erroneous information, and the standard of materiality should be applied with this in mind. In formulating a criterion, reference must be made to the type of person which the Act was designed to protect. Is it a sophisticated businessman, an educated person, a speculator, or your Aunt Jenny? Most likely the latter, particularly if she is elderly.³¹⁵

In answering this query, one can look to the groundwork laid by analogous developments under the Securities Act. The SEC has defined as material those matters as "to which an average prudent investor *ought* reasonably to be informed before purchasing."³¹⁶ This definition and its application represent several substantial deviations from the common law standard. The language has been variously interpreted to include: (1) those matters which an average prudent investor "needs to know before he can make an intelligent, informed decision;"³¹⁷ (2) "a fact which, if it had been correctly stated or disclosed, *would* have deterred or *tended* to deter the average prudent investor;"³¹⁸ (3) any fact "which in reasonable and objective contemplation *might* affect the value of the corporation's stock or securities;"³¹⁹ and (4) facts "which *may* affect the desire of investors to buy, sell or hold companies' securities."³²⁰ Although these constructions appear to be exercises in semantics, more pleasurable perhaps to the philosopher than to the lawyer, they do reflect a broadening of the range of materiality. Furthermore, the reference point is not limited to persons of moderate financial intelligence. The Securities Act was created for the very purpose of protecting those who lack business acumen.³²¹ Thus, if Securities Act patterns are followed, a developer will have to meet higher materiality standards under the Land Sales Act than he would at common law.

Reliance, an element necessary to traditional legal and equitable relief,³²² has been eliminated as an ingredient of the claim

³¹⁵ See text accompanying notes 4-12 *supra*.

³¹⁶ 17 C.F.R. § 230.405 (1969) (emphasis added).

³¹⁷ *Escott v. BarChris Constr. Co.*, 283 F. Supp. 643, 681 (S.D.N.Y. 1969).

³¹⁸ *Charles A. Howard*, 1 S.E.C. 6, 8 (1934) (emphasis added).

³¹⁹ *List v. Fashion Park, Inc.*, 340 F.2d 457, 462 (2d Cir.), *cert. denied*, 382 U.S. 811 (1965) (emphasis added).

³²⁰ *SEC v. Texas Gulf Sulphur Co.*, 401 F.2d 833, 849 (2d Cir. 1967), *cert. denied*, 394 U.S. 976 (1969) (emphasis added).

³²¹ See 2 L. LOSS, *supra* note 48, at 849.

³²² RESTATEMENT OF TORTS §§ 525, 537 (1938); RESTATEMENT OF CONTRACTS § 479 (1932).

based upon a defective statement of record or property report.³²³ Instead of requiring proof of reliance (*i.e.*, that the buyer believed and acted upon the statements of the developer), section 1410(a)³²⁴ shifts the burden, allowing the developer a defense by way of proof that, at the time of the acquisition, the purchaser knew of the untruth or omission.³²⁵ This is certainly equitable, since it insulates developers from liability for false statements of record where the truth is revealed to a purchaser prior to the sale. However, as noted below, section 1410(b)(2),³²⁶ regarding false or misleading property reports, affords no such defense.

An interesting question arises with respect to the situation where a false property report, which is part of the statement of record, is provided to the purchaser, and, during the time prior to the sale, the defect is corrected in the statement of record by amendment. If the developer fails to inform the purchaser of the error or to provide him with an updated property report, would the lot acquired be "covered by such statement of record,"³²⁷ if the amended statement of record became effective prior to sale? If not, then recovery may not be had under section 1410(a), and one must resort to section 1410(b)(2), which permits recovery where the sale is "by means of a [false] property report."³²⁸

Some significant differences between sections 1410(a) and 1410(b)(2) ought to be elaborated. Section 1410(a) refers to the statement of record, while section 1410(b)(2) extends liability to any case where the purchaser is provided with a false *property report*. Section 1410(b)(2) deviates from section 1410(a) and its counterpart in the Securities Act, section 12(2),³²⁹ in one important respect — the purchaser's knowledge of the truth is not expressly made a bar to recovery. And it is clear that actions under subparagraphs (a) and (b) of section 1410 are separate and distinct, since subparagraph (c) allows recovery for the "suit authorized under

³²³ The element of reliance was also deleted from analogous provisions in the Securities Act. Sections 11(a) and 12(2), 15 U.S.C. §§ 77k(a), 1(2) (1964), require that the purchaser not know of the untruth or omission at the time of purchase. Section 11(a) puts the burden on the defendant to show that plaintiff had such knowledge, whereas section 12(2) requires the plaintiff to show he did not know. *See generally* 3 L. LOSS, *supra* note 48, at 1702-04, 1725-26, 1729.

³²⁴ 15 U.S.C.A. § 1709(a) (Supp. 1969).

³²⁵ *Id.*

³²⁶ *Id.* § 1709(b)(2).

³²⁷ *Id.* § 1709(a).

³²⁸ *Id.* § 1709(b)(2).

³²⁹ 15 U.S.C. § 77l(2) (1964).

subsection (a) or (b).”³³⁰ Thus, a literal reading of section 1410(b)(2) could result in liability where the purchaser is provided with a false property report and is informed of the error, even though such knowledge would bar recovery under subsection (a). The omission of the “purchaser’s knowledge” defense from subsection (b) is incongruous. The statement of record is in two parts: The first is identical to the property report, and the second contains additional information on file at HUD. Unless the purchaser knows the truth, a material error in either of these parts results in liability for the developer. However, if the error is in the property report, and even if the purchaser knows the truth, subsection (b) would allow the purchaser to recover. This is an absurd result to say the least. The purchaser’s knowledge should be a uniform bar to recovery. A possible method of achieving this result would be to read this defense into the “by means of” language of subparagraph (b) — the argument being that the sale was not “by means of” the false property report if the purchaser knew the truth. Alternatively, it might be urged that the purchaser is estopped from asserting the error since he knew the truth. However, such a reading of the statute would import a reliance requirement which, in light of the interpretation of identical language in the Securities Act, was not the intent of Congress.³³¹

Although the omission of the “buyer’s knowledge” defense from subsection (b) may lead to anomolous results, a developer can avoid liability under either section by ensuring that the statement of record and property report are both complete and accurate. The stringency of sections 1410(a) and 1410(b)(2) — even, perhaps, the latter’s lack of a “purchaser’s knowledge” defense — is a function of Congress’ intent to force developers (and their agents, since section 1410(b)(2) applies to both) to make accurate and full disclosure by way of a formal statement of record and property report.

The common law deceit element of damage-causation appears to be missing from sections 1410(a) and 1410(b)(2). This is quite understandable if one is seeking rescission. However, when damages are sought, the absence of the causation requirement would be a bit more puzzling, were it not for the fact that section 12(2) of the Securities Act,³³² the counterpart of section 1410(b)(2), stands

³³⁰ 15 U.S.C.A. § 1709(c) (Supp. 1969) (emphasis added).

³³¹ See *DeMarco v. Edens*, 390 F.2d 836 (2d Cir. 1968) (no reliance required in Securities Act § 12(2)). See also 3 L. LOSS, *supra* note 48, at 1702-03.

³³² 15 U.S.C. § 771(2) (1964).

as a legislative precedent for damage relief without causation. Section 11 of the Securities Act, the congener of section 1410(a), does contain a "no causation" defense,³³³ but the language underlying the defense was not included in section 1410(a).

Finally, privity of contract appears to be a requisite element of both section 1410(a), where recovery may be had by a "person acquiring . . . from the developer or his agent,"³³⁴ and section 1410(b)(2), where the plaintiff may recover against the "developer or agent, who sells" to him.³³⁵

4. *Fraudulent Practices.*— Sections 1410(a) and 1410(b)(2) are expressly limited to misleading statements of record and property reports. They do not afford a basis for relief when misrepresentations are made to prospective purchasers by means other than these two documents. Since the Act allows the dissemination of selling literature at any time (including that period prior to the effective date of the statement of record³³⁶) it is apparent that a developer can fully condition his prospects by flooding the market with selling literature, making speeches, showing movies, and utilizing high pressure sales tactics. By the time the statement of record becomes effective, or at least when the property report is furnished, the prospect may be psychologically committed to purchase land. Even if the developer takes the utmost care in fully disclosing the transaction in the property report and furnishes the document at least 48 hours before the purchaser signs the contract, the policies of the Act may be thwarted if there are no restraints on the developer's informal promotional campaign. This is particularly true if the format of the securities prospectus is adopted for the property report, in which case the latter may never be read. Even if the property report is read, the gullible purchaser may already be persuaded by the illusions of paradise created by seemingly honest salesmen.³³⁷

To a certain extent this problem is dealt with by section 1404(a)(2)(B), which makes it unlawful "to obtain money or property by means of a material misrepresentation with respect to any infor-

³³³ *Id.* § 77k(e).

³³⁴ 15 U.S.C.A. § 1709(a) (Supp. 1969).

³³⁵ *Id.* § 1709(b)(2).

³³⁶ See text accompanying notes 169-83 *supra*.

³³⁷ In 1967, even before the earlier versions of the Act had been amended to allow offers during the preeffective period, Manuel Cohen asked for the power to promulgate rules controlling the seller's informal promotional materials. 1967 *Hearings* 52-53. The power was never specifically given.

mation contained in the statement of record or the property report or with respect to *any other information* pertinent to the lot or the subdivision and upon which the purchaser relies."³³⁸ So far as the reference to statements of record and property reports is concerned, it appears that this section overlaps section 1410(a) and section 1410(b)(2). Moreover, because proof of reliance is required for a recovery under this section, it is unlikely that resort will be made to it in such cases. However, this provision furnishes the only source of recovery for fraudulent information transmitted by means other than the statement of record and property report. Since it prohibits *misrepresentations*, it is presumably broad enough to include half-truths as well as patent falsehoods, at least as this term is used in its common law sense.

It is questionable whether section 1404(a)(2)(B) imposes an affirmative duty of disclosure beyond avoidance of half-truths. It appears that this provision was not directed toward pure omissions, because of the incongruity of requiring proof of reliance upon an unstated fact. It is unfortunate that the susceptibility of purchasers may lead them to base their decisions on the advertising campaign of the developer, completely disregarding the property report. However, it must be recalled that the property report is specifically styled as a full disclosure-type document. This is clearly not the function of advertisements. Indeed, it is difficult to imagine that Congress intended that each piece of selling literature and every promotional speech should contain a full description and analysis of all the material aspects of the development. It is the developer's duty to supply the prospective purchaser with full, complete, and accurate information. This he accomplishes by delivering the property report to the prospect. So long as he does not provide misleading information by way of his own informal selling literature, the developer has fulfilled his responsibilities. It is at this juncture that the responsibility shifts to the purchaser. Congress intended only that the purchaser should have ready access to the property report information; there is no reason to believe that it intended that the developer should force feed him. Had it meant to do so, Congress could have followed the pattern set forth in the Securities Act which prohibits all advertising during the prefiling period and requires that only prospectus-type written material be used prior to effective date.³³⁹

³³⁸ 15 U.S.C.A. § 1703(a)(2)(B) (Supp. 1969) (emphasis added).

³³⁹ Securities Act § 5, 15 U.S.C. § 77e (1964).

This does not mean, however, that there are no additional restraints on the developer beyond meeting the formal disclosure requirements of the Act and being truthful in his own materials. Although an unscrupulous developer may find consolation in the belief that purchasers may not read the property report, he must still contend with state legislation, which, in some jurisdictions, grants administrative officials authority to prohibit offerings of lots if they are deemed unfair.³⁴⁰ It is a fair guess that *state administrators* will read the property report with care.

Section 1404(a)(2)(B), aside from prohibiting the use of misleading sales literature, may depart from the common law by imposing additional restraints on the promotional campaign.

The fine art of "puffing" continues to be firmly protected by the common law. The notion that one may freely express his "opinion" in business dealings finds its genesis in the age old concept of "caveat emptor."³⁴¹ Rather than subdue the zeal of salesmen, the common law allowed puffing as an established and accepted commercial practice which purchasers ought to recognize and disregard. Not being entitled to rely upon such statements, purchasers at common law were denied recovery.³⁴² The only exception is where one "fraudulently makes a misrepresentation of fact, opinion or law for the purpose of inducing another to act or refrain from acting in reliance thereon."³⁴³ In such cases, the purchaser is entitled to relief, but the problems of proving the seller's knowledge and intent are burdensome.

Modern developments under the Securities Act, which will probably serve as precedent for interpretation of section 1404(a)(2)(B), have gone a considerable distance in watering down this vestige of "caveat emptor." The SEC and the courts have shown a significant intolerance for predictions about future market prices or the profitability of operations. Liability for such predictions (if false), even where they are identified as opinions, is almost assured.³⁴⁴ Such things as valuations and geological reports are regarded by the SEC as based on implied representations that appropriate standards of investigation have been followed. Failure to adhere to such standards by one who purports to be an expert in-

³⁴⁰ See, e.g., OHIO REV. CODE ANN. § 1707.33(G) (Page 1964).

³⁴¹ See Note, *supra* note 83, at 717 & authorities cited n.21.

³⁴² W. PROSSER, *supra* note 282, at 736-47.

³⁴³ RESTATEMENT OF TORTS § 525 (1938).

³⁴⁴ See 2 L. LOSS, *supra* note 48, at 1437-38.

volves a misrepresentation of fact.³⁴⁵ Along those same lines, a developer's statement that lots in a subdivision will increase in value may be equally prohibited under the Land Sales Act.³⁴⁶

It is submitted that in administering a disclosure-type statute like the Land Sales Act no greater latitude should be allowed. Common law permissiveness assumed that buyers were possessed of an unrealistic degree of sophistication. The fact of the matter is that people are influenced by puffing, and it is consistent with the disclosure policies of the Act that purchasers should be entitled to rely on the truth of such claims. Furthermore, it is safe to assume that puffing is done with the hope that such statements will have an effect on the purchaser's decision; otherwise, why puff? In short, puffing is an essential tool of the artful salesman — the antithesis of full and accurate disclosure. Thus, when an affirmative claim is made, such statement should be regarded as "fact."

In addition, a developer who actively discourages prospects from reading the property report may well violate clauses (A) or (C) of section 1404(a)(2), which generally prohibit deceptive business practices.³⁴⁷ These provisions may be even more encompassing, and might impose restraints on the use of some types of high pressure sales tactics which compel the purchaser to make a hurried decision. The exact dimensions of the duties imposed by this language are not clear.³⁴⁸ As a theoretical matter, clauses (A) and (C) amount to antifraud weapons when relief is not available under other provisions. Translated, they mean: "Thou shalt not devise any other cunning devices,"³⁴⁹ and their potential scope is limited only by the ingenuity of scoundrels.

³⁴⁵ *Id.* at 1437.

³⁴⁶ *Cf.* SEC Rule 14a-9, 17 C.F.R. § 240.14a-9 (1969), wherein the SEC cautions that "predictions as to specific future market values, earnings, or dividends" in proxy solicitations may be misleading depending on particular facts and circumstances.

³⁴⁷ Section 1404(a)(2), 15 U.S.C.A. § 1703(a)(2) (Supp. 1969), makes it unlawful for any developer or agent "in selling or leasing, or offering to sell or lease, any lot in a subdivision —

(A) To employ any device, scheme, or artifice to defraud, or . . .

(C) To engage in any transaction, practice, or course of business which operates or would operate as a fraud or as a deceit upon a purchaser."

³⁴⁸ Although substantially similar language is contained in section 17(a) of the Securities Act, 15 U.S.C. § 77q(a) (1964), and SEC Rule 10b-5, 17 C.F.R. § 240.10b-5 (1969), the cases under these provisions have been directed toward limiting, rather than prohibiting, certain types of noninformational conduct. For example, some securities brokers engage in a practice of "churning," whereby customers are encouraged to feverishly buy and sell securities. Of course, such activities generate substantial commissions. However, a broker is not required to forbear such conduct; he is merely required to disclose its effect. *See generally* 3 L. LOSS, *supra* note 48, at 1479-81.

³⁴⁹ *Hearings on Stock Exchange Regulation, Before House Comm. on Internal and*

The disadvantage of having to resort to clauses (A) or (C) of section 1404(a)(2) is that, by their terms, they bear a close resemblance to common law deceit,³⁵⁰ raising the possibility that the purchaser will have to offer proof of the developer's intent. This requirement is absent from the remainder of the Act, including (arguably) clause (B). To what extent will the common law elements of scienter (or, for that matter, the elements of reliance and damage-causation) be grafted onto section 1404(a)(2)?

Perhaps the twin functions of section 1404(a)(2) have some relevance. First, the section serves as the basis for administratively prosecuted injunctive proceedings.³⁵¹ It is highly unlikely that HUD, when seeking a preventive remedy, will have to show old-fashioned scienter. Some watered-down notion of guilt, such as negligent misstatement, may be sufficient.³⁵² Nor will the Secretary have to show the elements of damage, damage-causation, or reliance (except to the extent that he bases his claim on clause (B), which expressly mentions reliance).³⁵³

Second, section 1404(a)(2) serves as the basis of a purchaser's *express* private civil remedy in the form of either rescission or damages.³⁵⁴ As the source of a damage action, section 1404(a)(2) might well be read to include the common law fraud elements of old-fashioned scienter (actual knowledge plus specific intent to defraud), damage-causation, and reliance. If securities law precedent is observed, this will certainly be the case. Working with language very much like that of section 1404(a)(2), the courts first inferred private civil claims where *none were expressly given*,³⁵⁵ and have

Foreign Commerce, 73d Cong., 2d Sess. 115 (1934), quoted in 3 L. LOSS, *supra* note 48, at 1424.

³⁵⁰ See text accompanying notes 280-86 *supra*.

³⁵¹ 15 U.S.C.A. § 1714(a) (Supp. 1969).

³⁵² The same question has arisen under similarly worded statutes and regulations in the federal securities context. *Cf., e.g.*, SEC v. Capital Gains Research Bureau, 375 U.S. 180, 193 (1963); SEC v. Texas Gulf Sulphur Co., 401 F.2d 833 (2d Cir. 1968), *cert. denied*, 394 U.S. 976 (1969).

³⁵³ *Cf., e.g.*, Mutual Shares Corp. v. Genesco, Inc., 384 F.2d 540 (2d Cir. 1967) (dictum). If the Secretary attempts to state a claim based on clause (B), he will face the specific requirement that purchasers rely (or be about to rely) on false or misleading statements. Reliance, however, will probably be limited to the "actual," rather than the "justifiable," variety.

³⁵⁴ See 15 U.S.C.A. §§ 1709(b)(1), (c) (Supp. 1969). Rescission is impliedly available because of the permissive language in section 1410(c), *id.* § 1709(c).

³⁵⁵ The language in section 1404(a)(2), *id.* § 1703(a)(2), bears a marked resemblance to the language of Securities Act section 17(a) and SEC Rule 10b-5, among other securities fraud provisions. These were enacted originally for the purpose of defining the grounds for equitable administrative actions, administrative proceedings, and criminal actions. However, the courts have taken the initiative to allow private civil reme-

since engaged in a seemingly endless struggle to explicate the elements of those claims.³⁵⁶ The question of scienter alone has spawned untold pages of judicial and scholarly commentary.³⁵⁷ Should section 1404(a)(2) of the Land Sales Act lead to the same imbroglio? The courts, if they choose, can avoid becoming embroiled in a discussion over the elements of a 1404(a)(2) action. The way around the bramble bush requires an appreciation of the fact that the troublesome private rights under the securities laws are *not express*, but *judicially inferred* (statutorily implied). Once the courts had breathed life into rights which Congress did not explicitly create, they were left with the task of fashioning the dimensions of those claims — a chore which they performed partially by looking to common law notions. Not so with section 1404(a)(2). It is the basis of an *express* claim. The courts needn't go beyond the face of the statute. If Congress had meant to include particular common law elements, it could have done so. Indeed, it did in one instance by requiring actual purchaser reliance in clause (B). Under this interpretation, the issues of scienter, damage-causation, and reliance fade away, and the limitless embellishment process is skirted. For clause (B), this easy course appears rational enough. But how, in applying clauses (A) and (C), is a court to determine, without reference to general fraud notions, whether there is a "device," "scheme," "artifice to defraud," or "transaction, practice, or course of business which operates or would operate as a fraud or deceit"?³⁵⁸ A dilemma, to be sure; but a court faced with the choice should think twice before it enters a labyrinth of statutory elaboration such as that which lies beyond the portals of the securities fraud provisions.³⁵⁹ A court opting to require a scienter element need not, in view of the ambivalence of the statute itself, call for the strictest kind of specific intent to defraud. Instead, such a court could exercise a degree of creativity and allow recovery upon

dies based on these provisions. *E.g.*, *Globus v. Law Research Serv., Inc.*, 287 F. Supp. 188 (S.D.N.Y. 1968), *aff'd in part, rev'd in part*, 38 U.S.L.W. 2175 (2d Cir. Sept. 9, 1969) (§ 17(a)); *Fischman v. Raytheon Mfg. Co.*, 188 F.2d 783 (2d Cir. 1951) (Rule 10b-5).

³⁵⁶ For enlightening judicial comment on the extent to which common law notions are to be incorporated into the so-called "implied" fraud remedies, see *SEC v. Texas Gulf Sulphur Co.*, 401 F.2d 883 (2d Cir. 1968), *cert. denied*, 394 U.S. 976 (1969); *Mutual Shares Corp. v. Genesco, Inc.*, 384 F.2d 540 (2d Cir. 1967).

³⁵⁷ Compare *Ellis v. Carter*, 291 F.2d 270 (9th Cir. 1961), with *Fischman v. Raytheon Mfg. Co.*, 188 F.2d 783 (2d Cir. 1951). See also Note, *Scienter and Rule 10b-5*, 69 COLUM. L. REV. 1057 (1969).

³⁵⁸ 15 U.S.C.A. §§ 1703(a)(2)(A), (a)(2)(C) (Supp. 1969).

³⁵⁹ See generally 3 L. LOSS, *supra* note 48, at 1430-42, 1763-77, 1778-96.

a showing that the developer or his agent perpetrated a negligently fraudulent act. In view of the developer's right to conduct an all out selling effort prior to the effective date of the statement of record, a modified "fault" element, couched in terms of due care, seems quite proper (*i.e.*, if the decision is made to require such factor at all).

When section 1404(a)(2) is used as the basis of a rescission action, damage-causation is no problem. But what of scienter? If the courts look to traditional doctrines of equitable rescission, which they might easily do under clause (B) (in which there is no deceit terminology), the issue palls.³⁶⁰ Under clauses (A) and (C), however, where language of deceit abounds, the question is more difficult.³⁶¹ The case is reversed on the issue of reliance. Clause (B), like the traditional action for equitable rescission, clearly specifies a reliance element, while (A) and (C) do not. Since the function of rescission is to restore the status quo where possible, a wise court might, on a *carpe diem* rationale, choose its weapons from history, requiring reliance (actual, if not justifiable) but ignoring scienter, no matter which clause of section 1404(a)(2) is invoked by the purchaser.

Finally, it appears that privity will be required as part of the purchaser's case under any clause of section 1404(a)(2), since the suit must be brought by a "purchaser" against the "developer or agent who sells" in violation of that section.³⁶² Indeed, newspaper advertisements taken and paid for by the developer may well result in liability for the publisher, since section 1404(a)(2) applies to materials other than a property report and the term "agent" is defined to include "any person who . . . acts for or on behalf of, a developer in . . . offering . . . lots."³⁶³

5. *Measure of Damages in Private Actions.*— At common law the purchaser could recover for deceit only if he could establish a causal connection between the misrepresentation and his losses. To the extent that the losses were due to other facts not misrepresented, the purchaser's right of recovery was limited.³⁶⁴ The Land Sales Act has seemingly eliminated the damage-causation requirement, making material misrepresentations actionable *per se*, similar to

³⁶⁰ See text accompanying notes 280-82 *supra*.

³⁶¹ See text accompanying notes 279-81 *supra*.

³⁶² 15 U.S.C.A. § 1709(b)(1) (Supp. 1969).

³⁶³ *Id.* § 1701(5). The agent, however, has a right over against the developer for contribution. *Id.* § 1709(d).

³⁶⁴ W. PROSSER, *supra* note 282, at 747-53.

the remedy of rescission.³⁶⁵ However, the measure of recovery is still similar to that for deceit. Unlike rescission, where the plaintiff is entitled to his purchase price only,³⁶⁶ when the action is one for deceit, there are two popular measures of recovery: "loss of bargain" and "out of pocket." The former gives the purchaser the benefit of his bargain, based on the difference between the value of the land as represented and the value of the land at delivery.³⁶⁷ This appears to be the rule in a majority of state courts. This measure of recovery, however, entails a heavy burden of proof in the lot sales context, because of the speculative value of undeveloped land "as represented."³⁶⁸ Congress chose to pattern the Act's damage provision after the "out of pocket" rule, which permits recovery for the difference between the purchase price and the value of the land at delivery.³⁶⁹ Unlike a tort action,³⁷⁰ the Land Sales Act does not authorize recovery of interest or punitive and consequential damages.³⁷¹ The most that can be recovered is the purchase price of the lot, the reasonable cost of the improvements, and court costs. Offset against this figure is the lesser of the value of the land at the time suit is brought or the price at which the land is sold before judgment.³⁷² In a declining market, the developer is in a precarious position. If the land was purchased for \$10,000, and two years later when suit was filed it was worth only \$8,000, and possibly a year or two later before judgment is rendered the land is sold for \$6,000, the plaintiff recovers \$4,000. On the other hand, if during the pendency of the suit the land should rise in value to \$12,000, the purchaser can sell it, take his \$2,000 profit, and still recover the \$2,000 decline in value from the time of purchase to the time of suit. The purchaser could recover \$14,000 — not bad on an initial investment of \$10,000. Whether such a fluctuation will ever occur remains to be seen, but at least the possibility of reaping such a

³⁶⁵ Neither proof of loss nor causation of damage are required for rescission. 3 J. POMEROY, *supra* note 284, at § 898a (1941). Here again, however, where a damage action is based on section 1404(a)(2), 15 U.S.C.A. § 1703(a)(2) (Supp. 1969), especially clauses (A) and (B), a court might hark back to the common law and require a showing of causation.

³⁶⁶ C. MCCORMICK, HANDBOOK OF THE LAW OF DAMAGES § 121 (1935).

³⁶⁷ W. PROSSER, *supra* note 282, 750-53.

³⁶⁸ The extent of the loss must be ascertainable, not speculative or contingent, in order to recover for deceit. *Id.* at 748.

³⁶⁹ *Id.* at 750-51.

³⁷⁰ C. MCCORMICK, *supra* note 366, at § 121.

³⁷¹ 15 U.S.C.A. § 1709(e) (Supp. 1969).

³⁷² *Id.* § 1709(c).

profit exists, and the purchaser can speculate at the developer's risk.³⁷³

6. *Miscellaneous Provisions Affecting Remedies.*— The foregoing excursus on the remedy aspects of the Act does not augur well for developers who are caught in its web. Still less encouraging to the developer (and his agent) will be the knowledge that he cannot "contract around" the potential nightmare.³⁷⁴ Moreover, all remedies outside the Act, at law or equity, are preserved.³⁷⁵

A ray of hope, perhaps, is the peculiarly worded statute of limitations which is divided into two categories. Actions based on false or misleading statements of record or property reports must be brought within one year after the untruth or omission was or should have been discovered, but in no event later than three years after sale or lease.³⁷⁶ Oddly enough, however, a two year period of limitations runs from the date of *violation* with respect to actions based on noneffectiveness of a statement of record at the time of sale or lease, failure to use a property report before the purchaser or lessee signs, and use of fraudulent selling literature and methods.³⁷⁷ Thus, to take an extreme case, if a developer makes a false or misleading offer (and completes an oral gentlemen's agreement) two years before the buyer receives the property report and signs a contract, the statute may have run on the fraudulent act before the purchaser has a chance to read the property report and learn of the deception.

VII. CONCLUSION

Perhaps, as some practicing lawyers have said only half-jokingly, the Land Sales Act has been the best kept secret of the century. The absence of fanfare, however, should not be interpreted as an indication that this new law lacks scope or muscle. Even if exemptions are freely allowed by HUD and the courts, the Act represents a factor to be reckoned with on a day-to-day basis by counsel for real estate clients. It may be some time before HUD develops sufficient internal procedures and know-how to become an active force in the

³⁷³ All of this results from an unfortunate garbling of the language of Securities Act section 11(e), 15 U.S.C. § 77k(e) (1964), which the drafters of the Land Sales Act were apparently attempting to follow. Section 11(e) requires the use of price after commencement of suit but before judgment if it *reduces* the amount of damages computed using value or price of disposal before suit.

³⁷⁴ Section 1413, 15 U.S.C.A. § 1712 (Supp. 1969), voids all waivers of compliance with the Act or Regulations.

³⁷⁵ *Id.* § 1713.

³⁷⁶ *Id.* § 1711.

³⁷⁷ *Id.*

administration of the Act, but the private civil remedies have, since the Act became effective on April 28, 1969, posed a real threat to the seller of lots.

There may be a tendency to dismiss the Act as a congressional aberration which represents a significant problem only for those developers who peddle wasteland in eastern Oregon to little old ladies in Wayland, Massachusetts.³⁷⁸ This is not the case. It may also apply to the developer who creates a subdivision just outside Los Angeles and then sells a substantial majority of the lots to residents of that city. The following words of Senators Tower, Bennett, and Hickenlooper will no doubt haunt many a developer:

We want to point out our concern . . . that the bill still deals with promotional plans not for the purpose of selling land interstate.³⁷⁹

Is this the lull before the storm?

³⁷⁸ Certainly, it was this type of deal which originally stimulated congressional interest in the land sales industry. This article would be incomplete without the following bit of humor which came to light in the 1966 Hearings. A newspaper reporter told the story of a New England lady who had written to a district attorney in Oregon to find out about the land she had purchased sight-unseen. The district attorney replied, in part:

"You asked me if I can dispose of your land. I cannot and do not think I could give it away. I am not in the real estate business, but have practiced law in Oregon for about 40 years and while lawyers are often accused of crimes and misdemeanors and practices not consistent with good morals, justly or otherwise, yet I have never known a lawyer who has been guilty of selling such land as yours, even to an enemy; this, for two reasons, first the honor that every lawyer possesses would deter him from an act of this kind, and, secondly, he could not sell it.

If the gambling microbe has entered in your system and you must gamble, hunt up a poker game at home and sit in but leave Western land games to the people of the West * * * Your land has no present value * * * It is very hard, rough, rocky and destitute of vegetation of any kind and the whole section would not support more than a jackrabbit and his wife, and, if there were any children, they would be compelled to go to Nevada to keep from starving to death. Your land is about 111 miles from a road and not more than 20 from Hades and owing to the roads and the nearness of the latter place, few people go to the railroad." 1966 *Hearings* 20.

³⁷⁹ S. REP. NO. 1123, 90th Cong., 2d Sess. 199 (1968).