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INTERSTATE LAND SALES REGULATION: THE CASE FOR AN EXPANDED FEDERAL ROLE

Public awareness of the need for protection from fraudulent vendors of undeveloped land recurs periodically and has led to brief flurries of legislative and journalistic attention since the Florida land boom of the 1920s.¹ Despite the rush of state and federal legislation enacted in recent years to combat sharp practices in the land development field, the need for stronger regulation has been revealed by testimony at public hearings held by the Office of Interstate Land Sales Registration as well as by numerous news accounts of questionable tactics employed by some land development promoters.² The recent actions of the Federal Trade Commission against deceptive advertising³ and the warnings of the Better Business Bureau⁴ and consumer publications⁵ confirm that the present land sales regulation laws have not provided the answer to abuses in the field.

The role of the federal government in regulating private sales of subdivided land is currently confined to enforcement of the disclosure requirements of the Interstate Land Sales Full Disclosure Act (Act)⁶ through the Office of Interstate Land Sales Registration (OILSR), an agency of the Department of Housing and Urban Development (HUD). The current reports of the persistence of sales practices which the Federal Act was enacted to prevent necessitate an examination of this narrow role.

¹ The Florida boom is discussed in Tindall, *The Bubble in the Sun*, 16 AM. HERITAGE, Aug. 1965, at 76. The following are representative of extensive press coverage in the early 1960s: Armbrister, *Land Frauds: Look Before You Buy*, 236 SAT. EVE. POST, Apr. 27, 1963, at 17; King, *The Great Land Swindle*, 78 COMMONWEAL 477 (1963).

² Contents of the testimony at the public hearings in Washington, D.C. is reported in Washington Post, June 1, 1972, at A1, col. 6. Tactics employed in the sales are covered in Hoffman, *About Those Land Hustlers You've Been Hearing From*, 55 SATURDAY REV., June 17, 1972, at 12, and *New American Land Rush*, 99 TIME, Feb. 28, 1972, at 72.

³ See text accompanying note 37 *infra*.

⁴ See text accompanying note 36 *infra*.

⁵ *Land Development Sales Gimmicks*, 54 CONSUMER BULL., Apr., 1971, at 21; *Land Sales Boom*, 37 CONSUMER REPORTS 606 (1972).

⁶ 15 U.S.C. §§ 1701-1720 (1970).

I. THE INTERSTATE LAND SALES FULL DISCLOSURE ACT OF 1968⁷

A. History and Provisions of the Act

Title XIV of the Housing and Urban Development Act of 1968 was enacted in response to widespread abuses in the sales of subdivided land. The legislative history reveals numerous reasons behind passage of the Act, the most important of which are: (1) the ineffectiveness of state laws in deterring fraudulent conduct in an industry that is national in scope and often operates through the mails and other means of interstate communication; (2) the need of purchasers of subdivided land for protection from the sharp sales practices of some land development companies; (3) the effect on consumers and land-use patterns of developments which are not successfully completed; and (4) the desire of the development industry for a means to enhance the image of legitimate concerns by forcing dishonest promoters either to abandon the practices which had created a scandalous image for the entire industry or to cease operations altogether.⁸

The Act is not regulatory legislation in the sense of enabling the administering agency to determine who will sell what land at what price. It is, as the name implies, a disclosure law and is patterned after the Securities Act of 1933;⁹ it also contains anti-fraud provisions similar to those in Section 17 of the Securities Act.¹⁰ It basically requires that sellers of subdivided land register with the Office of Interstate Land Sales Registration and disclose to prospective purchasers all material facts concerning the land. The registration is made in the form of a Statement of Record giving all pertinent facts concerning both the land and the seller.¹¹

⁷ *Id.*

⁸ Coffey & Welch, *Federal Regulation of Land Sales: Full Disclosure Comes Down to Earth*, 21 CASE W. RES. L. REV. 5, 7-10, 14-16 (1969). See generally *Hearings on S. 2672 Before the Subcomm. on Securities of the Senate Comm. on Banking and Currency*, 89th Cong., 2d Sess. (1966) [hereinafter cited as *1966 Hearings*]; *Hearings on S. 275 Before the Subcomm. on Securities of the Senate Comm. on Banking and Currency*, 90th Cong., 1st Sess. (1967) [hereinafter cited as *1967 Hearings*].

⁹ Coffey & Welch, *supra* note 8, at 19-21. Implications of this relationship to the Securities Act of 1933 are analyzed in Note, "Rainbow City"—*The Need for Federal Control in the Sale of Undeveloped Land*, 46 NOTRE DAME LAW. 733 (1971).

¹⁰ 15 U.S.C. § 77q (1970).

¹¹ *Id.* § 1705 prescribes the information required in the Statement of Record:

The statement of record shall contain the information and be accompanied by the documents specified hereinafter in this section—(1) the name and address of each person having an interest in the lots in the subdivision . . . ; (2) a legal description of, and a statement of the total area included in, the subdivision and a statement of the topography thereof . . . ; (3) a statement of the condition of the title to the land comprising the subdivision . . . ; (4) a

The disclosure is in the form of a Property Report including all that is in the Statement of Record except documents relating to the details of the selling organization and the subdivided land.¹² The Act applies to promotional offerings of subdivisions containing more than forty-nine lots, with some important exemptions.¹³ Any developer or agent who violates the Act¹⁴ is subject to

statement of the general terms and conditions [of sale or rental] . . . ; (5) a statement of the present condition of access to the subdivision, the existence of any unusual conditions relating to noise or safety which affect the subdivision and are known to the developer, the availability of sewage disposal facilities and other public utilities . . . in the subdivision, the proximity in miles of the subdivision to nearby municipalities, and the nature of any improvements to be installed by the developer and his estimated schedule for completion; (6) in the case of any subdivision or portion thereof against which there exists a blanket encumbrance, a statement of the consequences for an individual purchaser of a failure . . . to fulfill obligations under the instrument or instruments creating such encumbrance and the steps, if any, taken to protect the purchaser in such eventuality; (7) (A) copy of its articles of incorporation . . . if the developer is a corporation; (B) copies of all instruments by which the trust is created or declared, if the developer is a trust; (C) copies of its articles of partnership or association and all other papers pertaining to its organization, if the developer is a partnership, unincorporated association, joint stock company, or any other form of organization; and (D) if the purported holder of legal title is a person other than developer, copies of the above documents for such person; (8) copies of the deed or other instrument establishing title to the subdivision in the developer or other person and copies of any instrument creating a lien or encumbrance upon the title of developer or other person . . . ; (9) copies of all forms of conveyance to be used in selling or leasing lots to purchasers; (10) copies of instruments creating easements or other restrictions; (11) such certified and uncertified financial statements of the developer as the Secretary may require; and (12) such other information and such other documents and certifications as the Secretary may require as being reasonably necessary or appropriate for the protection of purchasers.

- ¹² A property report . . . shall contain such of the information contained in the statement of record . . . as the Secretary may deem necessary, but need not include the documents referred to in [§§ 1705(7) to 1705(11)] A property report shall also contain such other information as the Secretary may by rules or regulations require as being necessary or appropriate in the public interest or for the protection of purchasers.

Id. § 1707(a).

¹³ Exempted sale or lease transactions include: (1) lots in a subdivision, all of which are five acres or more in size; (2) improved land with a building, or on which the seller is obligated to erect a building within two years; (3) cemetery lots. *Id.* § 1702.

¹⁴ Violations of the Act are prescribed by *id.* § 1703(a):

(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 1706 of this title and a printed property report, meeting the requirements of section 1707 of this title, 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

suspension of lot sales by OILSR.¹⁵ The Act also makes any violation of its provisions the basis of an action for injunctive relief by OILSR,¹⁶ criminal proceedings brought by the Department of Justice,¹⁷ and civil action by the purchaser to recover damages resulting from the violation.¹⁸

Although a seller violates the Act by failing to meet the registration and disclosure requirements, making material misrepresentations in the Statement of Record or Property Report, or engaging in any practice or course of business which would cause the purchaser to be defrauded or deceived,¹⁹ the Office of Interstate Land Sales Registration has consistently interpreted the Act as only giving it authority to compel disclosure through the required documents.²⁰ This interpretation serves as the basis of analysis in this note.²¹ The antifraud provisions do little more than

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 *Id.* §§ 1706(d), (e).

¹⁶ *Id.* § 1714(a).

¹⁷ *Id.* §§ 1714(a), 1717. Any person convicted of willful violation of the Act is subject to a criminal penalty of a fine not exceeding \$5,000, or imprisonment not exceeding five years, or both. *Id.* § 1717.

¹⁸ *Id.* §§ 1709, 1713.

¹⁹ See note 14 *supra*.

²⁰ This conclusion is based on the following statements by Mr. Ray J. Walsh, Chief of the OILSR Complaints Section, and Mr. George K. Bernstein, Administrator of Interstate Land Sales:

The Act confers merely the authority to require a *disclosure* of any and all material facts concerning land which is being offered for sale or lease. Once an adequate disclosure has been accomplished, the Act's intent has been satisfied and compliance with the law is assured.

The *disclosure* required by the Act is accomplished by filing a Statement of Record

. . . .

Once a Statement has become effective, the Act admonishes the developer to give a copy of the Property Report to prospective purchasers

Walsh, *Consumer Protection in Land Development Sales*, 42 PENN. B. ASS'N. Q., Oct., 1970, at 38, 39.

"However [Mr. Bernstein] pointed out, his department has little other authority than to compel 'honest disclosure' of facts obtained in property reports filed with HUD." Statement attributed to Mr. George K. Bernstein, Administrator of Interstate Land Sales, at the New York City hearings, Sept. 19, 1972. N.Y. Times, Sept. 20, 1972, at 32, col. 3.

²¹ The Office has issued no rules or regulations defining a "device, scheme, or artifice to defraud" or the nature of "any transaction, practice, or course of business which operates or would operate as a fraud or deceit upon a purchaser." See 15 U.S.C. §§ 1703(a)(2)(A), (C) (1970) in note 14 *supra*. It has no specific rulemaking authority in this area; an amendment proposed by SEC Chairman Cohen that would have given it this authority was not incorporated in the Act. 1967 Hearings, *supra* note 8, at 52-53. Violations based on failure to disclose and on material misrepresentations in the required documents do not present the difficulties of proof that may exist in the antifraud provisions, as discussed in note 22 *infra*. Considering both this lack of rulemaking authority and the difficulties of proof, the interpretation of the Act by the Office which seemingly ignores the antifraud provisions appears to be justified.

state the common law,²² which is generally regarded as inadequate to provide protection for purchasers of land because of the cost, delay, and difficulties of proof inherent in actions under it.²³

Although the Act would appear to offer substantial inducements to developers to comply fully with its provisions, there is considerable evidence that this has not occurred.²⁴ This evidence also indicates that until recently the Office of Interstate Land Sales Registration did little to insure that sellers were complying with the Act.

B. Weak Enforcement of the Act by OILSR Prior to 1972

The Interstate Land Sales Act became effective as of April 30, 1969, and the *Annual Report* of the Department of Housing and Urban Development for that year stated that there were "no significant activities to report in this first year of operation,"²⁵ in referring to the administration of the Act. From all outward appearances, this comment could apply to successive years until 1972. Indeed, until the recent changes in administration at the Office of Interstate Land Sales Registration²⁶ and the announcement of public hearings, few outside of the land development industry were even aware of the existence of the Act.²⁷

²² The elements of a common-law action in deceit are:

1. A false representation made by the defendant. In the ordinary case, this representation must be one of fact.
2. Knowledge or belief on the part of the defendant that the representation is false—or, what is regarded as the equivalent, that he has not a sufficient basis of information to make it. This element is often given the technical name of "scienter."
3. An intention to induce the plaintiff to act or to refrain from action in reliance upon the misrepresentation.
4. Justifiable reliance upon the representation on the part of the plaintiff, in taking action or refraining from it.
5. Damage to the plaintiff, resulting from such reliance.

W. PROSSER, *HANDBOOK OF THE LAW OF TORTS* § 105, at 685-86 (4th ed. 1971) (footnotes omitted). The fifth element above arguably does not apply to actions under the Act, for damages recoverable by the purchaser are specified in 15 U.S.C. § 1709(c) (1970). The necessity of proving the other four elements would depend upon judicial interpretation of the antifraud provisions, and there have been no reported cases thus far. The difficulties which will confront the purchaser if the courts interpret these provisions as they have similar provisions of the Securities Act of 1933 are discussed in Coffey & Welch, *supra* note 8, at 62-68.

²³ See Note, *Regulating the Subdivided Land Market*, 81 HARV. L. REV. 1528, 1531 (1968); Coffey & Welch, *supra* note 8, at 52.

²⁴ See text accompanying note 46 *infra*.

²⁵ U.S. DEPARTMENT OF HOUSING AND URBAN DEVELOPMENT, 1969 ANNUAL REPORT 74.

²⁶ See text accompanying notes 39-42 *infra*.

²⁷ Remarks of John R. McDowell, Deputy Administrator of OILSR, at the public hearing in Detroit, Oct. 6, 1972 (tape recording on file with the *University of Michigan Journal of Law Reform*); see also Coffey & Welch, *supra* note 8, at 70.

No official reports of proceedings of the Office are available, outside of those contained in the *HUD Newsletter* and the *Annual Report* for 1969 and 1970,²⁸ and these sources report little activity in the first three years of operations. A note in the August 1, 1970 *HUD Newsletter* indicates that the first suit had just been filed under the Act.²⁹ The *1970 Annual Report* states that almost 1,700 interstate land developers were listed with the Office, and that some permanent injunctions against lot sales had been obtained.³⁰ No further actions of OILSR were reported in the *Newsletter* until April, 1972, when two suspensions of lot sales were announced.³¹

An unofficial source, *Consumer Reports*, states that the recorded actions of the Office as of May 31, 1972, included four indictments, one conviction, and eighteen lot sales suspensions.³² One reason for such a dearth of action may have been failure of OILSR to use fully the extensive investigatory powers granted to it by the Act.³³ Until this year the staff of about forty³⁴ included only two investigators, and testimony given at the recent hearings in Washington, D.C., indicated that some complainants had experienced delays of as much as two years in obtaining any substantial action by OILSR.³⁵

Either lack of action by the Office or weaknesses in the Act itself have caused other agencies to step into the breach and

²⁸ Letter from George K. Bernstein, Interstate Land Sales Administrator, to the *University of Michigan Journal of Law Reform*, Oct. 13, 1972, on file with the *University of Michigan Journal of Law Reform*.

²⁹ The suit, asking for temporary and permanent injunctions, was filed in United States District Court in Boston, Mass., against the developers of Black Horse Acres in Maine, who had allegedly failed to file a Statement of Record with OILSR or supply a Property Report to the purchasers. 1 *HUD Newsletter*, Aug. 1, 1970, at 2.

³⁰ U.S. DEPARTMENT OF HOUSING AND URBAN DEVELOPMENT, 1970 ANNUAL REPORT 79.

³¹ Lot sales by a developer may be suspended by the Office through suspension of the Statement of Record, after which the developer will be in violation of the Act if he continues to sell the property. 15 U.S.C. § 1703 (1970). After giving the developer notice and an opportunity for a hearing, this action may be taken by OILSR if it appears that the Statement of Record in effect includes an untrue statement of a material fact or omits any material fact necessary to make it not misleading. *Id.* § 1706(d).

Lot sales were suspended at the Charnita development in Pennsylvania because the Property Report failed to disclose that the Pennsylvania Department of Environmental Resources had suspended issuance of sewage permits in two townships in which it is located. Sales were also suspended at Horseshoe Bay on Lake Lyndon B. Johnson in Texas because the Property Report did not reflect a change in the developer's original promise to transfer control of an airport and stable to the property owners' association. 3 *HUD Newsletter*, Apr. 10, 1972, at 3.

³² *Land Sales Boom*, *supra* note 5, at 608.

³³ 15 U.S.C. § 1714(b) (1970).

³⁴ OILSR reported a "staff of 39 people." 1 *HUD Newsletter*, Aug. 15, 1970, at 3. Another source reported that "HUD has given OILSR forty employees," and that only two were investigators. Jones, *A Nice Piece of Desert*, 213 *NATION* 616, 624 (1971).

³⁵ *Land Sales Boom*, *supra* note 5, at 608.

attempt to remedy practices in the land development field. Warnings were recently issued by the Council of Better Business Bureaus about the practices of GAC Properties,³⁶ one of the largest land development companies in the United States, which has never been subject to a reported action of the Office. The Federal Trade Commission has just closed a case against Great Western United Corporation, which has several large developments in the western states, in which the firm consented to an order to change deceptive advertising practices concerning its developments.³⁷

The present Administrator of OILSR fully admits that the track record of the agency is poor, and in one interview said that "our office has just acted as a registration agency."³⁸

C. *The Recently Increased Activity at OILSR*

Until March 1, 1972, responsibility for administration of the Act by OILSR was assigned to the Office of the HUD Assistant Secretary for Housing Production and Mortgage Credit.³⁹ At that time the Office of Interstate Land Sales Registration was shifted to a position directly responsible to the Secretary of HUD,⁴⁰ and George K. Bernstein was appointed as the first Administrator of Interstate Land Sales.⁴¹ The new Administrator announced a "get tough" policy,⁴² and there are substantial indications that this policy is being fully implemented.

Sales in two subdivisions were suspended in April, 1972,⁴³ and the first conviction under the Act was announced in May of that year.⁴⁴ The first three of seventeen public hearings to be held in

³⁶ N.Y. Times, Feb. 13, 1972, § 8, at 4, col. 1.

³⁷ Great Western United Corp., FTC File No. 632 3062 (cited at 1 CCH CONSUMERISM 669 (1972)). An account of deceptive sales techniques employed by a salesman at Cochiti Lake, a Great Western United development in New Mexico, is given by Jones, *supra* note 34, at 616-20.

³⁸ Statement attributed to Mr. George K. Bernstein, *quoted in In Pursuit of the Second Home*, 79 NEWSWEEK, Apr. 17, 1972, at 85.

³⁹ 3 HUD Newsletter, Mar. 20, 1972, at 3.

⁴⁰ Changes in 24 C.F.R. §§ 1700.10-.20 to establish the Office of Interstate Land Sales Registration as an organizational unit of HUD and to vest authority for administering the Office in an Administrator of Interstate Land Sales are promulgated at 37 Fed. Reg. 5021-22 (1972).

⁴¹ 3 HUD Newsletter, Mar. 20, 1972, at 3.

⁴² *Land Sales Boom*, *supra* note 5, at 608.

⁴³ HUD Newsletter, *supra* note 31, at 3.

⁴⁴ A developer was convicted for selling lots in two North Carolina subdivisions, Holiday Shores and Governor's Lake Estates, without submitting a Statement of Record to OILSR or furnishing purchasers with a Property Report. *United States v. Parker*, No. 71-779-CR-CF (S.D. Fla., Mar. 23, 1972); *see also* 3 HUD Newsletter, May 15, 1972, at 3. Mr. Bernstein reported that four criminal convictions had been obtained against developers as of Sept. 20, 1972. N.Y. Times, Sept. 20, 1972, at 32, col. 3. The Act has been cited in only one reported case, *SEC v. Lake Havasu Estates*, 340 F. Supp. 1318, 1322 (D. Minn. 1972), where the court dismissed the defendant's contention that compliance

1972 by OILSR were also announced in May. The purpose of these hearings was to be

to aid the Administrator in enforcing the Interstate Land Sales Full Disclosure Act and in determining the necessity for and the basis of recommendations for further legislation or regulations or both.⁴⁵

In September, 1972, OILSR announced that 450 land developers had been notified that they were violating the Act and would face suspension of lot sales if they did not request formal hearings before the Office and succeed in disproving the charges at these hearings.⁴⁶

The public hearings were also intended to elicit consumer complaints and give publicity to the Act and the expanded enforcement policy of the Office.⁴⁷ The Office requested oral and written complaints at the hearings and promised that all complaints would be investigated if there were any possibility of relief to the consumer or a remedy against the seller under the Act. To make such investigations possible the Administrator announced in June, 1972, that the number of investigators in the Office had been increased from two to ten.⁴⁸ When the hearings began in June, complaints were coming into OILSR at the rate of 200 per week.⁴⁹

The hearings had been held in eight of the seventeen cities as of early October, 1972,⁵⁰ and although no transcripts of the proceedings at these hearings are yet available,⁵¹ some information concerning them has been published by news media in those cities.⁵²

The hearings in Washington, D.C. and New York City at

with the Interstate Land Sales Full Disclosure Act had some bearing on the issue of whether notes generated by land sales transactions were subject to registration under the Securities Act of 1933.

⁴⁵ 37 Fed. Reg. 10408 (1972).

⁴⁶ 3 HUD Newsletter, Sept. 18, 1972, at 4 (this action was pursuant to 15 U.S.C. § 1706(d) (1970)).

⁴⁷ Remarks of John R. McDowell, *supra* note 27. For examples of publicity received through news coverage of the hearings, see note 52 *infra*.

⁴⁸ Washington Post, June 2, 1972, at C2, col. 1.

⁴⁹ *Id.*, June 1, 1972, at A1, col. 6.

⁵⁰ Public hearings had been held in Washington, Kansas City, Denver, Boston, New York City, Atlanta, Columbus, and Detroit, as of October 6, 1972; further hearings are scheduled in Chicago, Seattle, San Francisco, Los Angeles, Phoenix, Houston, Little Rock, Tampa, and Miami. 37 Fed. Reg. 10408, 17773 (1972).

⁵¹ Letter from George K. Bernstein, *supra* note 28.

⁵² Washington, D.C. hearings: Washington Post, June 1, 1972, at A1, col. 6; *Id.*, June 2, 1972, at C2, col. 1.

Boston, Mass. hearings: Boston Globe, Sept. 16, 1972, at 3, col. 6.

New York City hearings: N.Y. Times, Sept. 20, 1972, at 32, col. 3; *Id.*, Sept. 21, 1972, at 26, col. 2.

Atlanta, Ga. hearings: Atlanta Const., Sept. 28, 1972, at 5-A, col. 7; Tharpe, *Licensing of Recreational Land Sellers is Urged Here*, *Id.*, Sept. 29, 1972, at 23-A, col. 1.

tracted the most participants and observers, while those in Boston, Atlanta, and Detroit were sparsely attended. Complaints from purchasers of land have been given the highest priority, although representatives of the land development industry have been encouraged to speak in their defense after complaints are heard. Complaints at any given hearing have tended to focus on one or two developments which have been extensively promoted in that area. Some witnesses have testified concerning lots that are inaccessible because of water or other natural conditions; others have cited lack of promised improvements and existence of legal restrictions on land use which render their lots unsuitable for residential purposes.⁵³ Some of the complaints have concerned land purchased before the Federal Act became effective in 1969 or land purchased by customers who later simply experienced a change of mind about the advisability of their purchase; in such cases there is no remedy under the Act.

The testimony of land development industry representatives at the hearings has been varied and sometimes highly emotional. At the Washington hearings the executive vice-president of the American Land Development Association charged that the hearings were a "farce" designed to condemn the industry publicly and he accused OILSR of refusing to help developers comply with the Act.⁵⁴ Another industry representative said that advertising and marketing practices of the industry must be controlled because nearly all land sales personnel deceive the public by creating an "atmosphere of urgency" that causes the buyer to believe that he must buy immediately or lose the opportunity.⁵⁵ At the Atlanta hearings the president of a development company recommended that a national system of examination and licensing of land salesmen be adopted to curb sales abuses in the industry.⁵⁶ At the New York City hearings a vice-president of Horizon Corporation announced that his company planned to take legal action against a witness who had testified against it.⁵⁷

⁵³ Not all of the land purchasers who have testified at the hearings are opponents of the land development industry. Two witnesses at the Detroit hearings exhibited symptoms of a condition which might be called "land fever." Both had purchased land in numerous developments in several states over the past ten years but only one of them, who referred to herself as a "land freak," was a complainant. The other witness had no complaints and testified in favor of the companies that had sold lots to him. He had not purchased any land since the Federal Act became effective but said he had difficulty in making total payments of \$297 per month on the many purchases he made before that time. Tape recording of proceedings at the Detroit hearings (on file with the *University of Michigan Journal of Law Reform*).

⁵⁴ *Washington Post*, June 1, 1972, at A-7, col. 1.

⁵⁵ *Id.*, June 2, 1972, at C2, col. 1.

⁵⁶ Tharpe, *supra* note 52.

⁵⁷ *N.Y. Times*, Sept. 21, 1972, at 26, col. 2.

The hearings appear to be accomplishing their intended purpose. The officials in the Office of Interstate Land Sales Registration are becoming more personally acquainted with the problems created by the industry which they are charged with regulating, and the public is being treated to a lively course in consumer education through the newspaper reports in the cities where the hearings are being held. However, it is too soon to judge whether the present policies of OILSR are more than a temporary reversal from its former obscure role.⁵⁸ Even if the Act is rigidly enforced, it provides for only full disclosure and not full protection for either the customer or the general public.

D. Basic Limitations on the Effectiveness of the Act

During the past year numerous changes in the regulations issued by OILSR have been made, and other recommendations for statutory amendments to the Act have been proposed by the Office.⁵⁹ One of the primary purposes of the current series of public hearings is to determine if there is a need for further regulatory and statutory amendments.⁶⁰ Nevertheless, some of the inherent limitations of the Interstate Land Sales Full Dis-

⁵⁸ "Whether or not the agency's new energy will lead to long-range correction of land sales abuses or is merely election-year rhetoric remains to be seen." *Land Sales Boom*, *supra* note 5, at 608.

⁵⁹ Regulatory changes issued by OILSR since Jan. 1, 1972, include:

1. "Intrastate or almost entirely intrastate" exemption limited to subdivisions of fewer than 300 lots, and the developer must also file a request for an "exemption order." 37 Fed. Reg. 1302, 1305 (1972). *See also* 3 HUD Newsletter, Mar. 20, 1972, at 3.
2. Requirement of fuller disclosure in the Property Report of the organization and operation of property owners' associations and of the availability of services at the development. 37 Fed. Reg. 1302, 1303, 1312-14 (1972). *See also*, 3 HUD Newsletter, Sept. 18, 1972, at 4.

Statutory amendments to the Act which have been proposed by the Office, as reported in Walsh, *The Role of the Federal Government in Land Development Sales*, 47 NOTRE DAME LAW. 267, 279-80 (1971), include:

1. Increasing the number of lots from forty-nine to ninety-nine under § 1701(3)—which defines a "subdivision" for the purposes of the Act—to relieve smaller developments from filing under the Act.
2. Deletion of § 1702(a)(2), which now exempts the sale of subdivision lots of five or more acres in size.
3. Deletion of § 1702(a)(10), exempting sales of land free of encumbrances, because of "developer confusion" over this exemption and administrative difficulties.
4. Amendment of § 1703(b) to increase the period for the right of revocation by the purchaser (if he is not shown the Property Report at least forty-eight hours before signing) from forty-eight hours to seventy-two hours and to eliminate the provision allowing the purchaser to waive this right. *See also* 2 HUD Newsletter, Sept. 6, 1971, at 1.

⁶⁰ *See* text accompanying note 45 *supra*.

closure Act will not be overcome by incremental changes such as those thus far proposed by the Office.

These weaknesses result from the nature of the Act, a full-disclosure statute which permits the Office to require only that all material facts are disclosed to the consumer in an official document. A number of important consequences flow from this basic fact. First, the official document, the Property Report, lends an unavoidable imprimatur to the seller's promotion that tends to convince potential buyers that the product has federal approval⁶¹ regardless of the disclaimer which is required in the Report itself.⁶² Second, the Act provides no viable remedies⁶³ for any sharp practices in the land sales industry which lie beyond the scope of disclosure requirements. These include all of the high-pressure tactics reported to be in common use by some land development companies⁶⁴ as well as misleading advertising by any means. Finally, the purchaser of land has no remedy under the Act if the seller fails to provide either clear title to the land or promised improvements, so long as the seller makes no assurances as to these items in the Property Report.⁶⁵ Similarly, there is no protection provided for the purchaser who buys land that cannot be used for the purpose intended or for any purpose whatever because of unsuitability or prohibitive land-use laws so long as the seller has made no untrue statements in the Property Report.⁶⁶

The hearings held by the Subcommittee on Securities of the Senate Committee on Banking and Currency in 1966 and 1967 on bills which formed the basis for the Federal Act brought forth much testimony in favor of regulatory legislation which would have provided for more consumer protection than simply full disclosure. The senators in charge of the hearings explicitly rejected the thesis of these witnesses, however; and the Chairman of the Securities Exchange Commission, which would have administered the Act as it was written at that time, agreed with the senators.⁶⁷ It was their opinion that a full-disclosure requirement

⁶¹ 1966 *Hearings*, *supra* note 8, at 195 (remarks of Mr. Kossack).

⁶² 24 C.F.R. § 1710.110 (1972).

⁶³ This statement assumes that the remedies for common-law fraud provided by § 1709(b)(1) are not viable because of the practical difficulties discussed in text accompanying notes 22-23 *supra*.

⁶⁴ Reports of the high-pressure tactics employed by some companies are discussed in Janson, *Land Hustlers in Las Vegas Thrive on Property-Hungry Vacationers*, N.Y. Times, Sept. 14, 1972, at 43, col. 1; *see also* notes 2 and 37 *supra*.

⁶⁵ This result occurs because there has been no reliance on a material misrepresentation. *See* note 63 *supra*.

⁶⁶ *See id.*

⁶⁷ 1966 *Hearings*, *supra* note 8, at 30-31, 148-49 (remarks of Sens. Williams and

was sufficient as a federal control for the land sales industry, and that true regulatory legislation was better left to the states.⁶⁸

The Act was not conceived as simply a consumer protection act, although the first impetus for some form of federal legislation came from the hearings on frauds and misrepresentations affecting the elderly held by the Senate Special Committee on Aging in 1963 and 1964.⁶⁹ A further premise behind the Act was that sale of subdivided land was a beneficial activity which was carried on primarily by legitimate enterprises in need of protection from the excesses of their few wayward brethren. For this reason, the need for consumer protection was balanced against the desire of legitimate developers for legislation which would not subject them to unduly costly and restrictive federal controls.⁷⁰

Experience, however, has proven these premises faulty. The testimony at the recent OILSR public hearings has shown that sharp practices in the industry are not limited to a few firms or the small, fly-by-night operators. Remedies for these sharp practices are available, but only a few states have enacted laws which are sufficient to curb the myriad abuses in the industry. One of these states is California, where the full-disclosure type of land sales statute was found inadequate⁷¹ and a "permit" regulatory law was enacted in 1963.⁷² Since that time the number of developments registering with the California Division of Real Estate has diminished greatly, and the Division reports that the quality of the offerings has increased.⁷³ The California statute requires the Real

Mondale); 1966 *Hearings*, *supra* note 8, at 99, 1967 *Hearings*, *supra* note 8, at 70-71 (remarks of SEC Chairman Cohen).

⁶⁸ 1966 *Hearings*, *supra* note 8, at 144, 168 (remarks of Sen. Williams); 1967 *Hearings*, *supra* note 8, at 40 (remarks of Sen. Bennett).

⁶⁹ *Hearings on Frauds and Quackery Affecting the Older Citizen Before the Senate Special Comm. on Aging*, 88th Cong., 1st Sess. (1963); *Hearings on Interstate Mail Order Land Sales Before the Subcomm. on Frauds and Misrepresentations Affecting the Elderly of the Senate Special Comm. on Aging*, 88th Cong., 2d Sess. (1964) [hereinafter cited as 1964 *Hearings*]; Coffey & Welch, *supra* note 8, at 6.

⁷⁰ 1964 *Hearings*, *supra* note 69, at 2; 1966 *Hearings*, *supra* note 8, at 1, 3, 66, 109; 1967 *Hearings*, *supra* note 8, at 2.

⁷¹ 1966 *Hearings*, *supra* note 8, at 112.

⁷² CAL. BUS. & PROF. CODE §§ 11000 to 11030 (West 1964), *as amended*, (West Supp. 1972).

⁷³ During the twenty-seven months preceding the effective date of the permit law in 1963, a total of 156 out-of-state subdivisions containing 234,195 acres and 72,131 lots was registered with the Division, and public reports were issued on the full-disclosure principle. During the twenty-eight months following that date, permits were issued to only seventy-five out-of-state developments containing 36,115 acres and 25,447 lots. The Division has deduced that the substantial decrease in the number of filings has been accompanied by an increase in the quality of the offerings because of the numerous companies which have either failed to make application for a California permit after inquiring into the high standards now in effect, or withdrawn their application after failure of the property to meet the standards. 1966 *Hearings*, *supra* note 8, at 368-73 (Appendix 3, Item No. 7—Material Submitted from California).

Estate Commissioner to pass on the quality of land offered in out-of-state subdivisions to assure that the sale price is "fair, just, and equitable" before issuing a sales permit.⁷⁴ It also requires a full-disclosure report,⁷⁵ assurances that all improvements promised will be completed,⁷⁶ and, if title to the land is encumbered, a release clause or escrow arrangement to assure that the purchaser can obtain title to the land even if the seller defaults on his obligations.⁷⁷ The Division of Real Estate also regulates the developer's advertising.⁷⁸ A law which is similar, but does not imply the "fair, just, and equitable" test, has recently been passed in Michigan.⁷⁹ The ineffectiveness of state laws in controlling nationwide promotions of land was, however, a primary reason for adoption of the Federal Act.⁸⁰ The state laws have always suffered from two basic defects: (1) lack of uniformity, causing marginal land promoters to select states with the weakest land sales laws for their operations, and (2) lack of any effective means for curbing sales promotions which are carried on by mail or telephone from points outside of any given state.

Representatives of the state regulatory bodies have consistently advocated the severest forms of federal regulation of the land sales industry, although some of their proposals would virtually eliminate the large-scale land promotions which are now commonplace. At the 1964 hearings of the Senate Subcommittee on Frauds and Misrepresentations Affecting the Elderly, an assistant attorney general of the State of California said:

Even if there is full disclosure, the sale of undeveloped lots in a premature and remote subdivision for use as home-sites or for investment is inherently fraudulent.⁸¹

At the 1966 Senate hearings on the Act, the Executive Director of the Florida Installment Land Sales Board and the counsel to the Board both recommended that the Act provide for a guarantee of promised improvements and good title by the seller, as well as regulation of the seller's advertising and licensing of sales person-

⁷⁴ "[T]he 'fair, just and equitable' test of securities regulation must be applied to pending applications for out-of-state subdivisions." 42 OP. ATT'Y GEN. 99, 104 (Cal. 1963). The Commissioner may require that the developer reduce lot prices in order to meet this test; there must be a "strong correlation" between the appraised value and the offering price. 1966 Hearings, *supra* note 8, at 120 (statement of M. G. Gordon).

⁷⁵ CAL. BUS. & PROF. CODE §§ 11018-18.1, 11025, 11027 (West Supp. 1972).

⁷⁶ *Id.* §§ 11018(d), 11018.5(a)(1), 11025(2).

⁷⁷ *Id.* §§ 11013.1-13.2 (West 1964).

⁷⁸ *Id.* § 11022. For advertising criteria used by the Division, see 10 CAL. ADM. CODE § 2799.1 (West 1971).

⁷⁹ Land Sales Act, Act of Oct. 30, 1972, Mich. P.A. No. 286 (effective Apr. 1, 1973).

⁸⁰ 1966 Hearings, *supra* note 8, at 64, 69, 76, 82, 113.

⁸¹ 1964 Hearings, *supra* note 69, at 25.

nel.⁸² More recently, at the OILSR public hearings in New York City, the Attorney General of New York, who has been prosecuting fraudulent land sellers there for many years, called for “[f]ederal laws to bar all mass-selling programs by land development companies”⁸³

There is little evidence that the Interstate Land Sales Full Disclosure Act has had any substantial salutary effect on practices in the land sales industry during the first three years of its existence. If the present policies of OILSR continue, the Act will provide the prudent purchaser with complete and reliable information on which to base his decision in buying land. Even if he does not understand the conditions set forth in the Property Report, his attorney will advise him of any pitfalls which exist.⁸⁴ But the unsophisticated customer in all likelihood will continue to purchase land which cannot fulfill his expectations for use or profit.

II. RECOMMENDATIONS FOR AMENDMENTS TO THE INTERSTATE LAND SALES FULL DISCLOSURE ACT

The sponsors of the Senate bills leading to the Interstate Land Sales Full Disclosure Act firmly rejected two concepts of federal regulation: federal preemption of the field and what has been called the “paternalistic”⁸⁵ approach. Federal preemption would have vested exclusive jurisdiction over interstate land sales in the federal government, thus precluding the individual states from applying any regulatory legislation. It was dismissed as a “political impossibility”⁸⁶ because of the expected resistance from the congressmen of those states which did not have laws comparable to the proposed federal law.

The paternalistic approach, which has also been labeled the “permit” system,⁸⁷ was rejected as unnecessary and difficult to administer on a national level.⁸⁸ This approach can be described as one involving some true regulation by the administering agency

⁸² 1966 Hearings, *supra* note 8, at 140-44.

⁸³ N.Y. Times, Sept. 21, 1972, at 26, col. 2.

⁸⁴ A common trait among the complainants at the New York City hearings was that none had consulted a lawyer before buying property. *Id.*

⁸⁵ Coffey & Welch, *supra* note 8, at 17. See also 1967 Hearings, *supra* note 8, at 52 (remarks of SEC Chairman Cohen).

⁸⁶ Coffey & Welch, *supra* note 8, at 17. See also 1966 Hearings, *supra* note 8, at 161-62, 165 (remarks of Sens. Mondale and Williams).

⁸⁷ Note, *supra* note 23, at 1533.

⁸⁸ 1966 Hearings, *supra* note 8, at 144, 168 (remarks of Sen. Williams); 1967 Hearings, *supra* note 8, at 40 (remarks of Sen. Bennett).

in that it passes on the merits of the land offering in some way, instead of merely requiring full disclosure.⁸⁹ This system sets a higher standard for the seller of land, requires a greater enforcement effort, and has had a beneficial effect on the quality of land offered for sale in California, where it has been in effect since 1963.⁹⁰

The most difficult questions concern whether such regulation on a national basis is practical or justified. True regulation by a federal agency would be more expensive than the present system. The federal government would incur significant expenses in the administration of a permit system. This cost would, however, not be prohibitive if the major portion of it were passed on to the industry regulated, as is presently done by OILSR through a system of filing fees.

The records of the hearings on the bills preceding the Federal Act show the prevailing attitude of the bills' sponsors to be that the promotional selling of subdivided land is a beneficial activity which should be encouraged,⁹¹ despite apparent abuses. This attitude simply does not square with the facts of the marketplace. Two types of buyers are present in the subdivided land market: (1) those who are purchasing land for their personal use as a homesite in the future, and (2) those who are purchasing land as a speculative investment. Both, however, are subject to the same hazards when they purchase land from a land development company that is either fundamentally dishonest or ill-equipped financially to undertake a land development project. The result in either case will be total or partial loss of the funds invested in the property.

If this were the only result of deceptive sales of subdivided land, a full-disclosure law such as the present Federal Act would arguably be sufficient protection for the buyer. At a minimum it provides him with the same type of protection that the Securities Act of 1933⁹² provides for those induced to invest in securities instead of land. Nevertheless, the sale of lots in many cases

⁸⁹ See text accompanying notes 71-79 *supra*.

⁹⁰ See note 73 *supra*.

⁹¹ 1964 Hearings, *supra* note 69, at 2; 1966 Hearings, *supra* note 8, at 1, 3, 66, 109; 1967 Hearings, *supra* note 8, at 2.

⁹² 15 U.S.C. §§ 77a-77aa (1970). The land buyer, however, deals directly with the seller and does not have the benefit of the brokerage and underwriting services, entailing professional analysis of the prospectus, which normally stand between the issuer and investor, 1966 Hearings, *supra* note 8, at 190 (remarks of Mr. Kossack). Moreover, land developments are not analyzed and rated, as are securities offerings, by private agencies. *Id.* at 425-26 (statement of Irving W. Blum). In the absence of these services, it is doubtful that the land purchaser is protected to the same degree as the securities investor. See also text accompanying note 84 *supra*.

results in detrimental environmental and economic effects reaching much further than the purchaser himself.⁹³

If the risk of such unfortunate consequences were small or the need for new communities acute, some of these evils could be tolerated. Neither is the case. Strict regulations on the sale of subdivided land will only tend to raise the standards of the industry to a level approaching that required in the Urban Growth and New Community Development Act of 1970,⁹⁴ which virtually assures that new communities sponsored jointly by the federal government and private interests will be successfully completed.

The following amendments to the Interstate Land Sales Full Disclosure Act would transform it into regulatory legislation that would more fully protect both the buyer and the region where the land is located.

⁹³ One of these effects is the creation of environmental and health problems through the sale of thousands of homesites without adequate community facilities. Such problems have prompted the Governor's Special Commission on Land Use in Michigan to recommend a comprehensive land management program to control development in the northern portion of the state. GOVERNOR'S SPECIAL COMMISSION ON LAND USE, REPORT, at 1, 6, 30 (1971).

Undeveloped land sold as an investment to residents of distant states may cause a formidable tax collection problem in the situs state. This problem was described by Mr. Keith Koske, Executive Secretary of the Colorado Real Estate Commission, at the 1964 Hearings:

Rural counties of Colorado have found some of their land to be so irresponsibly subdivided that tax assessment and collections are made difficult and costly. A county treasurer may have registered, as the owner of the land, a foreign corporation which has no intention of paying taxes. If a new owner of a lot has recorded his interest, the county treasurer may be compelled to spend \$3 preparing a tax bill of 50 cents to be mailed to a resident of New York or Hawaii. Land is the tax base of the rural county for the support of its schools and other resources. The tax base may be altered or made smaller.

1964 Hearings, *supra* note 69, at 71.

A related problem lies in the difficulty of reassembling subdivided parcels if the first developing company fails. Concerning this, Mr. Koske said:

[A new] subdivider may wish to begin a proper development of the same land. . . . [H]e may find it necessary to begin an action to quit [sic] title, but this may not be successful. Assembly of lands is difficult because of the many owners scattered all over the United States. . . . Orderly development of the land may be stopped, or delayed, or made far more costly than it should be.

Id.

The greatest problem caused by mass land sales promotions may well lie in the creation of new residential communities without any industrial base to sustain them economically. A study done at Stanford University on a projected 1,262-unit residential development financed by the Westinghouse Corporation near Half Moon Bay, California, showed that the development would require a minimum net subsidy from the town for fire protection, city services, and public schools of \$50,000 by 1977 and \$400,000 by 1982. Cited in Jones, *supra* note 34, at 623. Such communities present a double threat because, in addition to requiring a net subsidy from the surrounding region, they draw residents from older, established communities where their presence as taxpayers and consumers is vital to continued economic prosperity.

⁹⁴ 42 U.S.C. §§ 4501-4532 (1970). The standards for new communities and the developing organization are set forth at 24 C.F.R. §§ 710.5-.16 (1972).

1. A requirement of proof by the developer that the subdivision and the uses for which the lots are advertised are in full compliance with all applicable land-use and subdivision control laws before the Statement of Record becomes effective with OILSR.⁹⁵ This would prevent the purchaser from buying land which cannot be legally used for his intended purpose and would aid the situs area in enforcing its land-use laws.

2. A requirement that the seller provide every potential buyer with an opportunity to see the site of his lot, without cost, prior to the signing of the agreement to buy.⁹⁶ This would provide for fuller disclosure of the true nature of the development and lessen the fraudulent developer's present incentive to offer land that is so distant from the purchaser that he is not likely to visit it prior to purchase.

3. A requirement that the seller provide a full performance bond for all improvements promised at the development through the Property Report or advertising.⁹⁷ This would protect the purchaser from either a deliberately fraudulent developer or one whose weak financial position will cause him to default on the promised improvements.

4. A requirement of a release clause to assure that the buyer can obtain title to the property if the seller defaults on a blanket encumbrance, or an escrow arrangement for purchase monies until the title is released from the encumbrance.⁹⁸ This would assure that the purchaser can obtain either title to his property or a refund of monies paid toward the purchase price in the event that the seller defaults on his obligations.

These requirements would no doubt raise the developer's cost of doing business and increase the final price of the lots sold.⁹⁹ There are reports that some developers have run into severe cash flow problems under the present laws,¹⁰⁰ and this trend can be expected to accelerate if the initial costs of land development are increased by the regulatory laws. This might cause the demise of

⁹⁵ This amendment is substantially the same as a proposal by Mr. Robert P. McCulloch, Jr., Vice-President, McCulloch Properties. 1966 *Hearings*, *supra* note 8, at 205.

⁹⁶ This, too, was recommended by Mr. McCulloch. *Id.* at 203.

⁹⁷ See, e.g., CAL. BUS. & PROF. CODE § 11018 (West Supp. 1972).

⁹⁸ See e.g., *id.* § 11013 (West 1964).

⁹⁹ A representative of the National Association of Real Estate Boards testified in 1966 that registration alone "might result in an increase of \$500 in the price of home sites . . ." 1966 *Hearings*, *supra* note 8, at 67. The Chairman of the Securities and Exchange Commission did not agree. *Id.* at 303. However, the regulations proposed herein could have a substantial effect on lot prices in some developments.

¹⁰⁰ Land development operations accounted for \$74 million of a \$85.1 million loss by Boise Cascade in 1971. *Boise Cascade Buckles Down*, BUSINESS WEEK, Mar. 11, 1972, at 34. Similarly, negative cash flow and land sales problems caused Great Western Cities, a land development subsidiary of Great Western United Corp., to contribute substantially to the present financial problems of the Corporation. Morgenthaler, *Sic Transit Gloria*, Wall St. J., Sept. 18, 1972, at 10, col. 2.

those segments of the industry which are weakest in financial resources. Yet this result would be beneficial in view of the long-term commitments and cash reserves necessary for the creation of new communities.¹⁰¹ From the investor's point of view these requirements would raise the threshold for speculation in land and might cause him to take a closer look at an investment which is dear rather than cheap. The potential purchaser of a homesite would have much more assurance that the land is suitable for that purpose. In economic terms the higher cost of subdivided land under a federal system of full regulation would more closely reflect the true costs of the subdivision of land. Under the present system, much of this cost falls outside of the vendor-purchaser relationship.

III. CONCLUSION

There are several possible alternative solutions to the abuses currently found in the subdivided land sales industry. The proposed amendments to the Interstate Land Sales Full Disclosure Act listed above would correct many of these abuses without prohibiting mass promotions of subdivided land altogether. Although they represent a substantial expansion of federal regulation in this field, these steps appear to be necessary to bring practices in the land sales industry into harmony with consumer demands for more protection. They would have little effect on those organizations which are engaged in the bona fide business of building new communities, but would serve as harsh medicine indeed for those who are merely selling empty dreams to unwary consumers.

—*Robert R. Maxwell*

¹⁰¹ 1966 Hearings, *supra* note 8, at 297 (Appendix 2—Excerpt from Report of Special Comm. on Aging).