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New York Housing Merchant Warranty Statute: Analysis and Proposals

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THE NEW YORK HOUSING MERCHANT WARRANTY STATUTE: ANALYSIS AND PROPOSALS

For centuries, courts applied the doctrine of *caveat emptor*, or "let the buyer beware," to all sales transactions.[1] Although courts ceased applying this ancient maxim to personal property sales during the nineteenth century, they continued to apply the rule in sales of real property.[2] This doctrine traditionally left home buyers without an effective remedy for defects resulting from poor workmanship. In recent decades, however, courts in many states, recognizing the harsh effects of *caveat emptor*, have extended the concept of implied warranties to housing sales.[3] Last year, the New York State Legislature followed the lead of these courts by enacting a statutory housing merchant warranty.[4]

Although the New York housing merchant warranty provides substantial consumer protection, it does not completely fulfill the goals which inspired its adoption. The statute neither adequately protects reasonable consumer expectations and reliance nor sufficiently encourages the construction of safe and habitable homes.

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1 Note, *Minnesota Statutory Warranties on New Homes—An Examination and Proposal*, 64 MINN. L. REV. 413 (1980).

2 *See* Leo Bearman, Jr., *Caveat Emptor in Sales of Realty—Recent Assaults upon the Rule*, 14 VAND. L. REV. 541, 541-42 (1961); *see also infra* text accompanying notes 32-62.

3 As the New York Court of Appeals noted recently in Caceci v. Di Canio Constr. Corp., 72 N.Y.2d 52, 58, 526 N.E.2d 266, 268, 530 N.Y.S.2d 771, 773 (1988), "[o]ver 25 States now recognize some form of an implied warranty of habitability or skillful construction in connection with the sale of homes." (citing Cochran v. Keeton, 287 Ala. 439, 252 So. 2d 313 (1971)); *accord* Richards v. Powercraft Homes, Inc., 139 Ariz. 242, 678 P.2d 427 (1984); Coney v. Stewart, 263 Ark. 148, 562 S.W.2d 619 (1978); Pollard v. Saxe & Yolles Dev. Co., 12 Cal. 3d 374, 525 P.2d 88, 115 Cal. Rptr. 648 (1974); Cosmopolitan Homes v. Weller, 663 P.2d 1041 (Colo. 1983); Greentree Condominium Ass'n v. RSP Corp., 36 Conn. Supp. 160, 415 A.2d 248 (1980); Gable v. Silver, 264 So. 2d 418 (Fla. 1972); Bethlahmy v. Bechtel, 91 Idaho 55, 415 P.2d 698 (1966); Park v. Sohn, 89 Ill. 2d 453, 433 N.E.2d 651 (1982); Theis v. Heuer, 264 Ind. 1, 280 N.E.2d 300 (1972); Kirk v. Ridgway, 373 N.W.2d 491 (Iowa 1985); Gosselin v. Better Homes, Inc., 256 A.2d 629 (Me. 1969); Weeks v. Slavick Bldrs., Inc., 24 Mich. App. 621, 180 N.W.2d 503, *aff'd*, 384 Mich. 257, 181 N.W.2d 271 (1970); Allison v. Home Sav. Ass'n, 643 S.W.2d 847 (Mo. App. 1982); Chandler v. Madsen, 197 Mont. 234, 642 P.2d 1028 (1982); Norton v. Burleaud, 115 N.H. 435, 342 A.2d 629 (1975); McDonald v. Mianecki, 79 N.J. 275, 398 A.2d 1283 (1979); Earls v. Link, Inc., 38 N.C. App. 204, 247 S.E.2d 617 (1978); Yepsen v. Burgess, 269 Ore. 635, 525 P.2d 1019 (1974); Elderkin v. Gaster, 447 Pa. 118, 288 A.2d 771 (1972); Rutledge v. Dodenhoff, 254 S.C. 407, 175 S.E.2d 792 (1970); Sedlmajer v. Jones, 275 N.W.2d 631 (S.D. 1979); Hollen v. Leadership Homes, Inc., 502 S.W.2d 837 (Tex. Civ. App. 1973); Bolkum v. Staab, 133 Vt. 467, 346 A.2d 210 (1975); Klos v. Gockel, 87 Wash. 2d 567, 554 P.2d 1349 (1976); Tavares v. Horstman, 542 P.2d 1275 (Wyo. 1975).

4 Housing Merchant Implied Warranty, N.Y. GEN. BUS. LAW § 777 (McKinney Supp. 1990).

Consequently, the New York legislature should amend the statute by raising the warranty standards of "skillful manner" and "material defects," and by extending builder liability to all significant housing defects, regardless of fault. Furthermore, the warranty should cover all defects, patent or latent, that a builder does not explicitly disclaim.

After explaining the application and effects of traditional doctrines governing sales, this Note will survey both the demise of these doctrines and the concurrent rise of implied warranties in the sales of goods. In particular, this Note will examine the policies leading to the development of implied warranties and their recent application to the sales of new homes. Finally, after outlining the basic provisions of the New York statutory warranty, this Note will discuss the problems created by the warranty's limited scope and will propose several corrective amendments.

I
BACKGROUND

Home sales, unlike sales of goods, usually take place in a two-stage transaction, with the seller giving the buyer an opportunity to verify the seller's title and to arrange for financing.[5] Typically, the parties first sign a sales contract committing themselves to the bargain.[6] The seller often will require the buyer to deposit "earnest money" when the parties sign the sales contract.[7] If the buyer takes the initiative, then the parties can bargain for covenants in the sales contract or the deed during contract negotiations. Subsequently, once the purchaser has verified the vendor's title, the sale of the home ends in a closing, during which the vendor delivers a deed of title to the purchaser in exchange for the purchase price.[8]

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5 REPORT AND RECOMMENDATION OF LAW REVISION COMMISSION FOR 1968, 1968 Legis. Doc. No. 65(A) at 76 [hereinafter REPORT]. If the buyer purchases the home without verifying that the seller actually owns the home, the true owner may eject the buyer from the premises even though the buyer purchased the home. Furthermore, the buyer must research the title of the land in the local recording office to ensure that the seller acquired the land from someone who held good title. If a thorough search reveals that the seller acquired the land through a valid chain of title, the buyer can purchase the land with the assurance that the sale will effectively transfer all ownership rights to the buyer.

6 *Id.*

7 *Id.* Earnest money refers to a sum of money (often 10% of the selling price) deposited with the seller to ensure that the buyer is "earnest" in his desire to purchase the property. In modern practice, real estate brokers generally place these funds in an escrow account.

8 *Id.*

A. Traditional Doctrines Governing Sales of Homes

1. *Merger*

Traditionally, once the buyer accepted the deed, he absolved the vendor of all duties under the sales contract. Under the merger doctrine, all contract obligations "merged" into the deed when the seller delivered it to the buyer.[9] If the vendor intended to fulfill additional obligations, the parties had to list the obligations in the deed.[10]

Although the merger doctrine produces an equitable result in many commercial transactions, it unfairly prejudices the purchaser in sales of residential homes.[11] The doctrine presumes an arm's length bargain by individuals capable of safeguarding their own interests.[12] In a typical housing sale, however, purchasers lack the sophistication necessary to protect these interests adequately, and often fail to inspect homes in more than a cursory fashion prior to closing.[13]

In this century, courts increasingly have recognized the doctrine's potentially harsh effects in housing sales and have moved to limit its scope. For example, they have broadened the application of the "collateral promises" exception. Originally, obligations that builders typically accepted merged into the deed, but any unusual promises did not; courts deemed the latter "collateral" to the deed.[14] Significantly, modern courts commonly have characterized *all* written warranties in the sales contract as collateral.[15] These

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9 *See, e.g.*, Cox v. Wilson, 109 Ga. App. 652, 137 S.E.2d 47 (1964) (holding that all prior agreements merged in the deed); Coutrakon v. Adams, 39 Ill. App. 2d 290, 188 N.E.2d 780 (1963) (following the traditional rule that the vendor gives no implied warranties since a deed merges the provisions of the contract), *aff'd on other grounds*, 31 Ill. 2d 189, 201 N.E.2d 100 (1964).

10 *See, e.g., Coutrakon*, 39 Ill. App. 2d 290, 188 N.E.2d 780; Disbrow v. Harris, 122 N.Y. 362, 25 N.E. 356 (1890) (although the builder agreed to convey a home "in good condition," the buyer could not recover for defects in the home because he had accepted the deed); *see also* REPORT, *supra* note 5, at 55.

11 REPORT, *supra* note 5, at 76-77. For a discussion of the evolution of the merger doctrine, see generally Ernest F. Roberts, *The Case of the Unwary Home Buyer: The Housing Merchant Did It*, 52 CORNELL L.Q. 835, 857 (1967).

12 REPORT, *supra* note 5, at 76.

13 *See infra* note 77 for a discussion of the unequal bargaining power of parties to a housing sale.

14 *E.g.*, Duncan v. McAdams, 222 Ark. 143, 257 S.W.2d 568 (1953); Bull v. Willard, 9 Barb. 641 (N.Y. App. Div. 1850). *See also* Bearman, *supra* note 2, at 548 (discussing the collateral promise exception); REPORT, *supra* note 5, at 77 (explaining the early meaning of "collateral promises"); Annotation, 38 A.L.R.2d 1307 (1954) (discussing whether deed merges or supersedes antecedent contract obligations of the vendor); Bull v. Willard, 9 Barb. 641 (N.Y. App. Div. 1850)

15 *E.g.*, Re v. Magness Constr. Co., 49 Del. 377, 117 A.2d 78 (Super. Ct. 1955); Russ v. Lakeview Dev., Inc., 133 N.Y.S.2d 641 (City Ct. 1954). One court reasoned that warranties, which are never aimed at conveying the property, are by their nature collat-

courts have reasoned that a deed's purpose is to convey the property, nothing more. Warranties contained in the sales contract do not pertain to the conveyance of property, and therefore they are necessarily collateral to the main purpose of the deed.[16]

New York courts generally have held that the parties' intent determines whether the vendor's obligations merge into the deed.[17] Therefore, if parties intend for a warranty to survive the closing, then the court will give effect to that intent.[18] Some courts have inferred the parties' intent. For example, in *Price v. Woodward-Brown Realty Co.*,[19] a supreme court held that the parties did not intend merger when a seller delivered the deed to an incomplete house because the seller had not completed his performance of the contract.[20] Another early court held, in *Staff v. Lido Dunes, Inc.*,[21] that the parties did not intend for warranties concerning latent defects to merge in the deed.[22] In yet another case, *Gomes v. Ern-Roc Homes, Inc.*,[23] the builder offered a one-year guaranty regarding leakage to induce the purchaser to accept title. Because the builder had given the guaranty in order to pass title to the buyer, the supreme court reasoned that the parties had intended the guaranty to survive the closing.[24] Because of New York's focus on the parties' intent, the merger doctrine seldom has barred breach of warranty claims.

2. *Caveat Emptor*

The merger doctrine denied recovery for breaches of express covenants in housing sales contracts, and, correspondingly, *caveat emptor* denied recovery for breaches of implied warranties.[25] *Caveat*

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eral to the main purpose of the deed. Greenfield v. Liberty Constr. Corp., 81 N.Y.S.2d 550 (Sup. Ct. 1948); *see also* Bearman, *supra* note 2, at 548 (citing *Greenfield* and explaining the collateral purpose doctrine).

16 *See, e.g.*, *Greenfield*, 81 N.Y.S.2d 550.

17 REPORT, *supra* note 5, at 58 (citing *Russ*, 133 N.Y.S.2d 641).

18 *See, e.g.*, *Russ*, 133 N.Y.S.2d 641; *see also* Roberts, *supra* note 11, at 858 ("The conventional technique of keeping the merger rule within the bounds of reason is illustrated in New York, where it is said that whether a vendor's obligation has merged into the deed is a question of intent.").

19 190 N.Y.S. 561 (Sup. Ct. 1921), *aff'd mem.*, 201 A.D. 837, 192 N.Y.S. 947 (1922).

20 *Id.*

21 47 Misc. 2d 322, 262 N.Y.S.2d 544 (Sup. Ct. 1965).

22 *Id.*

23 70 Misc. 2d 658, 334 N.Y.S.2d 732 (Civ. Ct. 1972).

24 *Id.*

25 *Caveat emptor* traditionally applied to the sale of goods as well. Swett v. Colgate, 20 Johns. 196 (N.Y. 1822) (holding that the buyer who bought by description exercised his own judgment and bought at his own risk); Seixas and Seixas v. Woods, 2 Cai. R. 48 (N.Y. 1804) (dismissing the suit based on *caveat emptor* because the plaintiff (a servant) and the defendant both had opportunity to examine the cargo, and neither determined it to be worthless). *See* Walton H. Hamilton, *The Ancient Maxim Caveat Emptor*, 40 YALE L.J. 1133, 1179 (1931).

emptor,[26] or "let the buyer beware," placed the risk of defective housing on the buyer.[27] Buyers without express warranties had no claim against the builder for defects discovered after closing.[28] For this reason, *caveat emptor* required the buyer to inspect his purchase carefully. If his inspection revealed a defect, the purchaser could either reject the item or renegotiate the price. Purchasers less confident in their ability to inspect adequately could bargain for an express warranty.[29]

New York Real Property Law section 251, enacted in 1909, codified the doctrine of *caveat emptor* in sales of real property. According to the statute, "[a] covenant is not implied in a conveyance of real property, whether the conveyance contains any special covenant or not."[30] In applying the statute, New York courts have held that a buyer of real estate received no promises, warranties, or covenants other than those expressly made by the seller.[31]

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26 The judicial doctrine of *caveat emptor* originated in the fifteenth century and has gained importance through the years. DEP'T OF THE ATTORNEY GENERAL OF ONTARIO, REPORT OF THE ONTARIO LAW REFORM COMM'N ON TRADE SALES OF NEW HOUSES 6 (1968). Law reports in the 1600's referred to the doctrine directly, and, in 1628, Sir Edward Coke declared that *caveat emptor* was the general law in sales situations. *See* Bearman, *supra* note 2, at 542. The doctrine gained importance during the late 16th and 17th centuries with the rise of English trade society and became even more prevalent during the early 1800's when laissez faire developed. This political philosophy led judges to look upon the purchase of land as a "game of chance," and for this reason, judges readily accepted the effects of *caveat emptor* on sales of land. Hamilton, *supra* note 25, at 1187. Hamilton's survey of the history of *caveat emptor* is still regarded as "the classic work on the subject." McDonald v. Mianecki, 79 N.J. 275, 398 A.2d 1283, 1287 (1979); *see also* Roberts, *supra* note 11, at 836 n.1 ("Hamilton's survey of the lineage of caveat emptor is such a classic that there is no need to footnote in detail—the article speaks for itself.").

27 The doctrine of *caveat emptor* does not apply to intentional misrepresentations. For a discussion of the effect of fraud on *caveat emptor*, see Bearman, *supra* note 2, at 561-66.

28 *E.g.*, Eastman v. Britton, 175 A.D. 476, 162 N.Y.S. 587 (App. Div. 1916) (per curiam) (reversing a judgment based on an oral promise that the foundation was sound because of the parol evidence rule, and noting that no implied warranty existed).

29 Roberts, *supra* note 11, at 836-37.

30 N.Y. REAL PROP. LAW § 251 (McKinney 1989).

31 *E.g.*, *Eastman*, 175 A.D. 476, 162 N.Y.S. 587 (no implied warranty regarding outside wall); Garlock v. Lane, 15 Barb. 359 (N.Y. Sup. Ct. 1853) (covenants not implied in a warranty deed); Bradt v. Church, 39 N.Y. Sup. Ct. 262 (App. Div. 1886) (covenants not implied in quitclaim deed), *aff'd*, 110 N.Y. 537, 18 N.E. 357 (1888); Pierce v. Fuller, 36 N.Y. Sup. Ct. 179 (App. Div. 1885) (no covenants implied in quitclaim deed); Spano v. Perry, 59 Misc. 2d 1062, 301 N.Y.S.2d 836 (Sup. Ct. 1969) (section 251 excludes an implied warranty of fitness in the sale of a completed home); McDermott v. Books, 128 Misc. 17, 217 N.Y.S. 181 (Sup. Ct.), *aff'd*, 218 A.D. 849, 218 N.Y.S. 809 (App. Div. 1926) (no implied covenant arises from conveyance of realty); Lewy v. Clark Ave., Inc., 128 Misc. 16, 217 N.Y.S. 185 (Sup. Ct. 1926) (no implied covenant arises from a conveyance of real estate).

B. The Rise of Consumerism in the Sale of Goods

The Industrial Revolution introduced mass production to consumers, who in turn demanded both higher quality goods from merchants and judicial protection of their interests.[32] In response to these growing consumer demands, courts gradually relaxed the rigid application of the *caveat emptor* doctrine. First, courts began to infer an implied warranty of merchantability if the seller customarily dealt in the goods in question, and if the buyer had no opportunity to inspect.[33] During the nineteenth century, courts extended this implied warranty of merchantability to sales of personal property regardless of the buyer's opportunity to inspect.[34]

Several policies guided the development of a warranty of merchantability in sales of personal property. In particular, a number of nineteenth century judges circumvented *caveat emptor* in cases in which the buyer had relied on the seller's skill and judgment in making the purchase.[35] For example, in *Brown v. Edgington*,[36] the seller, a rope dealer, sold the buyer, a wine merchant, a crane rope to lift wine from his cellar. The rope broke while the wine merchant's servant hauled wine to the street.[37] The court refused to apply *caveat emptor* because the buyer had relied on the seller's judgment.[38]

Today, all states except Louisiana have adopted the Uniform Commercial Code (U.C.C.), which implies a warranty of merchantability in sales of goods,[39] but not in sales of real estate.[40]

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32 Bearman, *supra* note 2, at 542.

33 Gardiner v. Gray, 4 Campb. 144, 171 Eng. Rep. 46 (K.B. 1815); Laing v. Fidgeon, 6 Taunt. 108, 4 Campb. 169, 128 Eng. Rep. 974 (C.P. 1815). *See also* Paul G. Haskell, *The Case for an Implied Warranty of Quality in Sales of Real Property*, 53 GEO. L.J. 633, 636 (1965) (discussing the nineteenth century origin of the warranty); William L. Prosser, *The Implied Warranty of Merchantable Quality*, 27 MINN. L. REV. 117, 123-25 (1943) (noting the limited nature of the early warranty).

34 For a discussion of the history of the warranty of merchantability, see Ingrid M. Hillinger, *The Merchant of Section 2-314: Who Needs Him?*, 34 HASTINGS L.J. 747, 788 (1983).

35 *See id.* at 790. The U.S. Supreme Court had imposed warranty liability on a manufacturer in 1883, holding that "upon clearer grounds of justice, the fundamental inquiry must always be whether, under the circumstances of the particular case, the buyer had the right to rely and necessarily relied on the judgment of the seller and not upon his own." Kellogg Bridge Co. v. Hamilton, 110 U.S. 108, 116 (1884).

36 133 Eng. Rep. 751 (C.P. 1841).

37 *Id.* at 753.

38 *Id.* at 756-57; *accord* Jones v. Just, 3 L.R.-Q.B. 197 (1868); Bigge v. Parkinson, 158 Eng. Rep. 758 (1862).

39 U.C.C. § 2-314 reads in full:

> (1) Unless excluded or modified (Section 2-316), a warranty that the goods shall be merchantable is implied in a contract for their sale if the seller is a merchant with respect to goods of that kind. Under this section the serving for value of food or drink to be consumed either on the premises or elsewhere is a sale.

The U.C.C. warranty of merchantability applies whether or not the buyer actually relied on the seller's skills.[41] It presumes that merchants understand the manufacturing process better than the consumer. Because of the sellers' presumed knowledge, the U.C.C. imposes responsibility on them regardless of their actual knowledge or skills.[42]

Consumer expectations also influenced the adoption of the warranty of merchantability.[43] The U.C.C. drafters recognized that consumers often have reasonable expectations about the goods they purchase, but do not insist on listing their expectations in a written contract.[44] For example, car buyers expect that a car will steer properly, but few require the seller to expressly promise adequate steering. In contrast to the doctrine of *caveat emptor*, the warranty of merchantability protects the buyer's reasonable expectations about the quality of the car's steering.[45] The warranty of merchantability does not require the seller to deliver higher quality goods than the

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(2) Goods to be merchantable must be at least such as
  (a) pass without objection in the trade under the contract description; and
  (b) in the case of fungible goods, are of fair average quality within the description; and
  (c) are fit for the ordinary purposes for which such goods are used; and
  (d) run, within the variations permitted by the agreement, of even kind, quality and quantity within each unit and among all units involved; and
  (e) are adequately contained, packaged, and labeled as the agreement may require; and
  (f) conform to the promises or affirmations of fact made on the container or label if any.
(3) Unless excluded or modified (Section 2-316) other implied warranties may arise from course of dealing or usage of trade.

See generally Haskell, *supra* note 33, at 634-35 (explaining U.C.C. § 2-314).

40 Courts could construe housing as a kind of "good" to bring it within the scope of the U.C.C., but most have declined to do so. *See, e.g.*, Fink v. Denbeck, 206 Neb. 462, 293 N.W.2d 398 (1980); G-W-L, Inc. v. Robichaux, 643 S.W.2d 392 (Tex. 1982) (overruled on other grounds by Melody Home Mfg. Co. v. Barnes, 741 S.W.2d 349 (Tex. 1987)); Sponseller v. Meltebeke, 280 Or. 361, 570 P.2d 974 (1977).

41 *See* Note, *Washington's New Home Implied Warranty of Habitability—Explanation and Model Statute*, 54 WASH. L. REV. 185, 211 (1978) (authored by Holly Keesling Towle). Today's warranty of merchantability also applies regardless of the special knowledge of the seller. Hillinger, *supra* note 34, at 799. *See generally* Haskell, *supra* note 33, at 649 (discussing no-fault liability and sellers' lack of expertise).

42 *See* Hillinger, *supra* note 34, at 795-96 (citing Kellogg Bridge Co. v. Hamilton, 110 U.S. 108, 116 (1883)).

43 Homer Kripke, *The Principles Underlying the Drafting of the Uniform Commercial Code*, 1962 U. ILL. L.F. 321, 323.

44 U.C.C. § 2-313 comment 1 (1987). For further discussion, see Friedrich Kessler, *The Protection of the Consumer Under Modern Sales Law*, 74 YALE L.J. 262, 278 (1964); Prosser, *supra* note 33, at 123-25.

45 Haskell, *supra* note 33, at 634-35.

buyer reasonably expects,[46] but gives effect to the parties' unarticulated contractual agreements about quality,[47] and responds to common perceptions of fairness and justice.[48]

Concern for public safety also led to the warranty of merchantability. Courts have responded to this concern for safety in sales of food,[49] as well as in sales of other goods.[50] Implying a warranty of merchantability promotes safety by encouraging merchants to sell only safe goods to the public. Courts recognized that retailers are in a better position than consumers to determine which manufacturers reliably and responsibly manufacture safe goods, and to purchase supplies only from them.[51]

Many courts view the warranty of merchantability primarily as a policing device,[52] holding the merchant liable for unmerchantable goods, regardless of fault.[53] Because the merchant can sue suppliers who actually cause the defect, the warranty ultimately places the loss on the party responsible for it.[54] When sellers are unable to

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46 The warranty requires only average or medium quality. *Id.* at 634. To approximate buyer expectations, the warranty imposes no responsibility for patent defects, those defects "which an examination ought in the circumstances to have revealed" to the buyer. U.C.C. § 2-316(3)(b); *see* Haskell, *supra* note 33, at 635.

47 Hillinger, *supra* note 34, at 756. Dean Prosser analyzed implied warranty of merchantability cases up to 1945 and argued that most courts found an "implied agreement in fact." Prosser, *supra* note 33, at 125. The view that the warranty protects buyers' "reasonable, unarticulated quality expectations finds support in the comments to section 2-314, judicial interpretations of that section, and Dean Prosser's comments." Hillinger, *supra* note 34, at 757 (citations omitted).

48 Professor Kirgis explains that a law that responds solely to common perceptions of fairness or justice would "protect the weaker party when a loss arises from a private transaction or occurrence, unless the weaker party caused the loss through some fault of his own." Frederic L. Kirgis, *Frances Lewis Law Center Project: A Statutory Approach to Implied Warranties on New Residential Construction*, 36 WASH. & LEE L. REV. 1075, 1075 (1979). Kirgis' thesis is that a fairness-oriented approach is compatible with an efficiency-oriented approach to warranties in the sales of new homes.

49 In holding a manufacturer of contaminated sausage liable for the death of a child, a court said the "implied warranty was not based on any reliance by the buyer upon the representations of the seller, or upon his skill and judgment, but was grounded squarely upon the public policy of protecting the public health." Jacob E. Decker & Sons, Inc. v. Capps, 139 Tex. 609, 616, 164 S.W.2d 828, 831 (1942); *accord* Wiedeman v. Keller, 171 Ill. 93, 49 N.E. 210 (1887); Hoover v. Peters, 18 Mich. 51 (1869); Griggs Canning Co. v. Josey, 139 Tex. 623, 164 S.W.2d 835 (1942).

50 *See, e.g.*, Henningsen v. Bloomfield Motors, Inc., 32 N.J. 358, 161 A.2d 69 (1960).

51 *See* Hillinger, *supra* note 34, at 799 (citing *Griggs Canning Co.*, 139 Tex. 623, 633, 164 S.W.2d 835, 840 (1942)). "[I]t is the duty of the court . . . to make it in the best interest of manufacturers and those who sell, to furnish the best article that can be supplied." Jones v. Bright, 130 Eng. Rep. 1167, 1171 (C.P. 1829).

52 *See, e.g.*, Ward v. Great Atl. & Pac. Tea Co., 231 Mass. 90, 120 N.E. 225 (1918); Ryan v. Progressive Grocery Stores, 255 N.Y. 388, 175 N.E. 105 (1931); Swift & Co. v. Wells, 201 Va. 213, 110 S.E.2d 203 (1959).

53 Hillinger, *supra* note 34, at 800.

54 *Id.* at 800 (citing *Ward*, 231 Mass. 90, 120 N.E. 225; *Ryan*, 255 N.Y. 388, 175 N.E. 105; *Swift*, 201 Va. 213, 110 S.E.2d 203).

recoup losses from the supplier at fault, courts today justify this seemingly unjust result as placing the burden on the party better able to bear the loss, the seller.[55]

Summarizing all of these policies, Professor Llewellyn observed, "[w]arranty is a civil obligation. Its purpose, like that of any civil obligation, is at once to police, to prevent, and to remedy."[56]

C. Housing as a Consumer Good

In the nineteenth century, home buyers assured quality by paying the builder, a skilled artisan, in stages for the work that he had done.[57] After World War II, however, the demand for housing soared, and the building industry produced houses in large quantities, inevitably using lower quality materials and often questionable workmanship.[58] Because buyers often paid for the homes at closing, they no longer could control quality effectively. One critic noted, "the building industry outgrew the notion that the builder was an artisan and took on all the color of a manufacturing enterprise, with acres of land being cleared by heavy machinery and prefabricated houses being put up almost overnight."[59] Confronted with these changes, courts continued to apply *caveat emptor* to housing sales.[60] Many critics, however, pointed out the irony of a system that offered more protection to a buyer of a defective two-dollar pen than to a buyer of a million dollar house.[61] Reacting to pressures to mitigate the effects of *caveat emptor*, courts in many jurisdictions implied warranties of workmanlike construction or habitability in sales contracts

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55 It makes sense to place the risk of loss on the seller because his goods caused the loss. This comports with the policy of imposing strict liability on sellers who sell unreasonably dangerous products. RESTATEMENT (SECOND) OF TORTS § 402A(1)(a) (1965); *see* Hillinger, *supra* note 34, at 802. Furthermore, the seller can pass along the losses. First, the seller is better equipped to recoup any loss from the person (his supplier) who actually caused the loss. *Id.* Second, the seller can pass on his losses through price adjustments. *Id.* at 803. Finally, the seller can spread the loss by insuring against it. *Id.* at 801-02. Justice Cardozo imposed liability on the merchant, reasoning that merchant liability was "one of the hazards of the business." *Ryan*, 255 N.Y. 388, 392, 175 N.E. 105, 106 (1931). *See generally* Kripke, *supra* note 43, at 324-25 (noting that one goal of the U.C.C. draftsmen was "to put the major risk on the professional, or the institutional party.").

56 Karl Llewellyn, *On Warranty of Quality, and Society*, 36 COLUM. L. REV. 699, 712 (1936). The policies of the warranty of merchantability resemble the policies behind strict liability for product defects. *See* James A. Henderson, *Coping with the Time Dimension in Products Liability*, 69 CALIF. L. REV. 919, 931-39 (1981) (summarizing the four main objectives of strict products liability).

57 Roberts, *supra* note 11, at 837.

58 Bearman, *supra* note 2, at 542.

59 Roberts, *supra* note 11, at 837.

60 *Id.*

61 Bearman, *supra* note 2, at 541; Haskell, *supra* note 33, at 633; Roberts, *supra* note 11, at 835-36.

for new homes.[62]

New York courts also moved to ease the unfairness of *caveat emptor* by slowly narrowing its application.[63] Courts often construed unclear or unconscionable contract clauses against the builders. For example, in *Lutz v. Bayberry Huntington, Inc.*,[64] the court determined that references in the sales contract to the lender's and municipality's requirement that the builder comply with standards of workmanship constituted an implied warranty that the builder would construct the house in a workmanlike manner.[65] This expansion of liability, however, was limited, in that it depended on the specific contract language in question.[66]

Eventually, New York courts recognized an implied warranty based on a consumer theory rather than on ambignous contract language. The *De Roche v. Dame*[67] court noted that buyers' inferior bargaining position forced buyers to rely on builders' superior skill and knowledge to provide quality workmanship and materials.[68] Because of buyers' reliance, the court held that, regardless of the contract language, builders were liable for improper construction, on a theory of implied warranty of workmanlike construction and

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62 *See* cases cited *supra* note 3.

63 As Leo Bearman noted in 1961:

> Even with this rash of vendees seeking relief, the courts were understandably reluctant to overrule flatly a doctrine which had become so deeply embedded in the common law. Nevertheless with some aid from the legislatures they met the challenge, but by more devious means: they extended, reshaped and in some instances distorted other areas of the law to fit their needs. The outcome is that, while *caveat emptor* is still ostensibly the law applicable to sales of realty in every common law jurisdiction, it no longer effectively protects the builder-vendor.

Bearman, *supra* note 2, at 542-43.

64 148 N.Y.S.2d 762 (Sup. Ct. 1956).

65 *Id.* at 767-68. Another court construed a standard merger clause against the builder. The court reasoned that the parties did not intend the merger clause to apply to latent defects. Staff v. Lido Dunes, Inc., 47 Misc. 2d 322, 262 N.Y.S.2d 544 (Sup. Ct. 1965). The court indicated in dicta that despite any merger clause, contracts for the sale of homes not yet completed contained an implied warranty of workmanlike construction. *Id.* at 330, 262 N.Y.S.2d at 552. Other lower courts adhered to the distinction between contracts for the sale of completed homes and contracts for construction and sale of a home. They held that implied warranties of skillful construction existed only in contracts for sale of incomplete homes. Carter v. Cain, 112 A.D.2d 2, 490 N.Y.S.2d 472 (App. Div. 1985); Dolezel v. Fialkoff, 2 A.D.2d 642, 151 N.Y.S.2d 734 (App. Div. 1956); Spano v. Perry, 59 Misc. 2d 1062, 301 N.Y.S.2d 836 (Sup. Ct. 1969). *But see* De Roche v. Dame, 75 A.D.2d 384, 430 N.Y.S.2d 390 (App. Div. 1980); Centrella v. Holland Constr. Corp., 82 Misc. 2d 537, 370 N.Y.S.2d 832 (Sup. Ct. 1975).

66 *See, e.g., Lutz*, 148 N.Y.S.2d 762; *Centrella*, 82 Misc. 2d 537, 370 N.Y.S.2d 832. *See also* NEW YORK STATE BUILDERS ASS'N, INC., BUILDERS GUIDE TO NEW HOME WARRANTIES IN NEW YORK STATE (1989) (available by subscription from the New York State Builders Ass'n) [hereinafter GUIDE].

67 75 A.D.2d 384, 430 N.Y.S.2d 390 (1980).

68 *Id.* at 387, 430 N.Y.S.2d at 392.

habitability.[69]

Finally, in 1988, the New York Court of Appeals recognized a housing merchant warranty in the landmark case of *Caceci v. Di Canio*.[70] The defendants built the Cacecis' home on soil composed of deteriorating tree trunks, wood, and other biodegradable materials. After less than four years of occupancy, the kitchen floor began to dip, and eventually another firm had to pour a new foundation to eliminate the defect. The *Caceci* court held that the builder breached an implied warranty of skillful construction which arose by operation of law, not contract.[71]

The *Caceci* court relied on policies similar to those underlying the U.C.C. warranty of merchantability.[72] The court noted that because parties to a housing sale contract do not bargain as equals, the buyer has to rely on the builder to deliver a house reasonably fit for the purpose intended. Furthermore, the court noted that requiring a builder to construct a house free from material defects and in a skillful manner is consistent with the purchaser's reasonable expectations. In addition, the court reasoned that the builder was in a better position to prevent major defects.[73] The court placed the responsibility for defects, "as a matter of sound contract principles, policy and fairness, . . . on the party best able to prevent and bear the loss," the builder.[74]

II

ANALYSIS OF NEW YORK HOUSING MERCHANT WARRANTY STATUTE

Only five weeks after the Court of Appeals decided *Caceci v. Di Canio*, Governor Cuomo signed into law a housing merchant warranty statute.[75] The statute implies a housing merchant warranty

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69 *Id.*

70 72 N.Y.2d 52, 526 N.E.2d 266, 530 N.Y.S.2d 771 (1988).

71 *Id.* at 56-57, 526 N.E.2d at 267, 530 N.Y.S.2d at 772. The court also held that the merger clause in the contract had no legal effect on these latent defects, and that Section 251 of the *Real Property Law* applied to deeds of conveyance, not contracts for the construction and sale of new homes.

72 See *supra* text accompanying notes 41-56 for a discussion of the policies behind the warranty of merchantability in sales of goods.

73 *Caceci*, 72 N.Y.2d at 59-60, 526 N.E.2d at 269, 530 N.Y.S.2d at 774-75.

74 *Id.*

75 N.Y. GEN. BUS. LAW § 777 (McKinney Supp. 1990).

After *Caceci*, the building industry, fearing the possibly expansive scope of the common law warranty, pushed for a clearer statute to define its responsibilities. *See* Letter from Robert A. Wieboldt of the New York State Builders Association to Evan A. Davis, Counsel to the Governor (Sept. 1, 1988) (available in the Governor's Bill Jacket) [hereinafter NYSBA Letter].

One interesting question is whether a cause of action remains under the common law warranty. The statute does not claim to provide an exclusive remedy for housing

into all contracts for the sale or construction of new homes. Although supporters have hailed the statute as a significant step forward,[76] it does not completely fulfill the goals that motivated many states to adopt housing merchant warranties. To fulfill these goals, the legislature should amend the statute to impose responsibility on builders for all housing defects that consumers would not reasonably expect. The importance of fulfilling the statute's underlying policies far outweighs the initial costs of these amendments.

A. Basic Warranty Provisions

Section 777-a of the statute implies a three-part housing merchant warranty by operation of law in all contracts for sales of new homes,[77] in addition to any express warranties the builder may

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defects, although it does preempt inconsistent local laws and state statutes. N.Y. GEN. BUS. LAW § 777-b(5)(b)-(c) (McKinney Supp. 1990). The Builders Association asserts that the statutory warranty replaces the common law warranty. *See* NYSBA Letter, *supra*, at 7; GUIDE, *supra* note 66, at 51. Robert Wieboldt insists that all involved in negotiations over the statute believed that it would constitute a homeowner's exclusive remedy. Telephone Interview with Robert A. Wiebolt, New York State Builders Ass'n (Dec. 16, 1988).

On the other hand, the New York State Consumer Protection Board cites New York precedent that statutory remedies exist alongside common law remedies where the statute does not expressly state that it is an exclusive remedy. Letter from Jean Miller, General Counsel, New York State Consumer Protection Board, to Evan Davis, Governor's Counsel 2 (Sept. 1, 1988) (available in the Governor's Bill Jacket) (citing Schuster v. New York, 5 N.Y.2d 75, 154 N.E.2d 534, 180 N.Y.S.2d 265 (1958) (penal law statute, which creates an absolute liability against municipal corporations for damages for injury or death arising from aiding police at their direction in making arrests, does not nullify common law action for wrongful death)); Odom v. East Ave. Corp., 178 Misc. 363, 34 N.Y.S.2d 312, *aff'd*, 264 A.D. 985, 37 N.Y.S.2d 491 (1942) (statutory remedy granted under the Civil Rights Act to black guests at a hotel who were refused service in the hotel restaurant did not preclude the guests from maintaining a cause of action under common law innkeeper liability)). *But see* N.Y. STATUTES LAW § 34 (McKinney 1971) (statutes creating new rights are exclusive and preempt any other remedies the aggrieved party may have had).

76 Senator Paul Kehoe stated, "I believe that this legislation is extremely important to homeowners of this state, since the purchase of a new home is, in almost all instances, the largest single purchase a consumer will make." Letter from Senator L. Paul Kehoe to Evan A. Davis, Counsel to the Governor (Sept. 1, 1988) (available in the Governor's Bill Jacket); *see also* NYSBA Letter, *supra* note 75, at 11 (favoring the bill because it gives builders clear guidelines to follow). *But see* Letter from Joanne E. Jenkins, Assistant Counsel to Office of Business Permits and Regulatory Assistance, to Evan Davis (Aug. 31, 1988) (recommending disapproval because of builders' ability to escape statutory requirements) (available in the Governor's Bill Jacket) [hereinafter Jenkins' Letter].

77 N.Y. GEN. BUS. LAW § 777-a (McKinney Supp. 1989). The provision further notes that section 251 has no effect on this implied warranty, and that the warranty does not merge in the deed but instead survives the passing of title. *Id.*

Under section 777-b of the statute, a builder may exclude or modify the statutory warranty, but only if he offers a limited warranty which meets the requirements of the statute. Some of the policy concerns leading to the U.C.C. and the housing merchant warranty statute suggest that the statute should not allow builders to disclaim their war-

make.[78]

The first part of the statute imposes liability on a builder for defects that arise during the first year after the warranty date[79] caused by the builder's failure to construct a new home in a skillful manner.[80] The second part of the statute imposes a two-year period of liability on builders for any defects in the installation of a home's

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ranties so easily. In fact, some consumer advocates opposed the New York statute because of section 777-b. *See* Jenkins' Letter, *supra* note 76.

On the other hand, the U.C.C. also allows waiver if evidence suggests that the parties negotiated the waiver. Section 2-316(2) allows merchants to exclude or modify the implied warranty of merchantability if the exclusion mentions merchantability and if the writing is conspicuous. These requirements ensure that parties negotiate any disclaimers.

The housing merchant warranty also attempts to ensure that builders who disclaim warranties must bargain for a disclaimer. Limited warranties must meet numerous disclosure requirements. If they are not met, then the builder in effect will have given an express warranty in addition to the statutory housing merchant implied warranty. *See* GUIDE, *supra* note 66, at 54-55.

Because of the strong public interest in habitable homes, all houses must meet building code standards, and no exclusion can render the house unsafe or uninhabitable. N.Y. GEN. BUS. LAW § 777-b(4)(e)(i)-(ii) (McKinney Supp. 1990). Builders may, however, limit total liability under the act. *Id.* § 777-b(4)(i). If builders limit their liability to a low fixed dollar amount, perhaps only $1.00, then buyers will have no effective protection under the statute.

If such limited warranties become more common in New York than contracts with the basic statutory warranty, then the limited warranty provision may frustrate the statute's goal of protecting the consumer from a builder's defects in circumstances where the builder usually has a superior bargaining position. As a whole, the statute aims to compensate for the buyer's inferior position. Where the buyer does have enough bargaining power, section 777-a does not usually imply warranties. For example, the statute implies no warranties in contracts for the sale of buildings constructed solely for lease. If most builders decide to use limited warranties, legislators might consider eliminating the limited warranty section of the law.

78 In addition to the basic three-part warranty, the statute implies one other warranty. Stoves, refrigerators, room air conditioners, and other goods sold incidentally with a home are warranted to be free from defects caused by the builders' faulty installation. *Id.* § 777-a(3). Merchantability and fitness of these goods, however, are covered by the U.C.C., not the housing merchant warranty.

79 *Id.* § 777-a(1)(a). The warranty period begins at the "warranty date," defined as "the date of the passing of title to the first owner for occupancy by such owner or such owner's family as a residence, or the date of first occupancy of the home as a residence, whichever occurs first." *Id.* § 777(8). The home building industry's voluntary warranty-insurance program, "Home Owners Warranty" or HOW, covers defects corresponding to those in the statute for one, two, and ten year periods. NYSBA Letter, *supra* note 75, at 3. The statute follows the HOW periods, except the statute covers material defects for only six years, not ten.

80 N.Y. GEN. BUS. LAW § 777-a(1)(a) (McKinney Supp. 1990). For a discussion of the statutory definition of "skillful manner," see *infra* text accompanying notes 89-96. For example, if exterior doors warp unexpectedly during the first year and cease to be weather resistant, the builder has not constructed them in a skillful manner. GUIDE, *supra* note 66, at 111. The example is taken from the Home Owners Warranty Corporation standards. The NYSBA Builders Guide lists the standards developed by HOW and incorporated into HOW warranties. The NYSBA suggests that local associations set standards similar to the HOW standards for all local housing construction. *Id.* at 104.

major systems.[81] Finally, the statutory warranty covers material defects for six years after the warranty date.[82] Material defects[83] include, for example, the sinking floor in the Caceci's home.[84] Although some cracks and dips may result from a normal settling process,[85] the house contains a material defect when the entire foundation begins to sink.

B. Limits to the Scope of the Statute and Problems Created by the Limits

Although the statute does impose an affirmative duty on all home builders to construct homes in a skillful manner free from material defects, it also limits the scope of the warranty in several ways. First, the statute narrowly defines the terms "skillful manner" and "material defects." Second, the statute imposes no liability on the builder for defects he does not cause. Finally, the warranty does not extend to patent defects.

1. *Statutory Language*

In *Caceci*, the Court of Appeals implied a housing merchant warranty, but did not define the terms "skillful manner" and "material defects." Prior New York courts used the term "workmanlike construction," by which they meant in accordance with accepted local standards.[86] *Caceci* may have substituted the term "skillful manner" to free lower courts from their own precedent, allowing a more subjective determination of whether the builder had breached the warranty.[87] Following *Caceci*, a court could determine, for example, that a home painted in a subjectively ugly color was not constructed in a

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81 N.Y. GEN. BUS. LAW § 777-a(1)(b) (McKinney Supp. 1989). The major systems covered are "the plumbing, electrical, heating, cooling and ventilation systems of the home." The two-year warranty covers only the installation of these systems, not the quality of the materials used. For example, the warranty extends to improperly installed duct work. A ventilation system's duct work should ordinarily remain intact and securely fastened. If duct work separates or becomes unattached, the statute would hold the builder liable. GUIDE, *supra* note 66, at 129. The installation warranty, however, does not cover the goods actually installed. If a homeowner discovers that the duct material itself is substandard, the two-year installation warranty would not apply. Of course, if a homeowner discovers substandard duct work during the first year of occupancy, the one-year warranty of construction in a skillful manner would apply.

82 N.Y. GEN. BUS. LAW § 777-a(1)(c) (McKinney Supp. 1989).

83 For a detailed definition of "material defects," see *infra* text accompanying notes 97-104.

84 Caceci v. Di Canio Constr. Co., 72 N.Y.2d 52, 55, 526 N.E.2d 266, 267, 530 N.Y.S.2d 771, 772 (1988).

85 *Id.* at 56, 526 N.E.2d at 267, 530 N.Y.S.2d at 772.

86 Whitman v. Lakeside Bldrs. & Developers, 99 A.D.2d 679, 472 N.Y.S.2d 51 (App. Div. 1984); De Roche v. Dame, 75 A.D.2d 384, 430 N.Y.S.2d 390 (App. Div. 1980).

87 *See* GUIDE, *supra* note 66, at 16.

skillful manner if the buyer reasonably believed he had bargained for an aesthetically pleasing color. Similarly, the term "material defects" could include only defects that make the home unsafe or unfit for habitation,[88] or it could include practically any defect, latent or patent. By failing to define these terms, the court left the scope of the warranty unclear.

The New York statute carefully limited the scope of the housing merchant warranty. The legislators adopted the *Caceci* terms, "skillful manner" and "material defect," to describe the basic warranty coverage. Rather than defining the terms broadly to fulfill the policies underlying the statute, however, the legislature chose to limit the terms.

a. *Skillful Manner*

If a builder fails to construct a home in a "skillful manner," the statute imposes liability on him for any resulting housing defects that arise within one year after the warranty date.[89] A building is constructed in a "skillful manner" if it does not violate specific building code standards and does not deviate from locally accepted building practices in areas where the building code sets up only general standards.[90]

The statutory definition further limits the builder's duty to conform to applicable building codes by imposing no liability on a builder who violates general code standards. The New York State Builders Association explains that general code standards "are not 'relevant specific standards' of the code, and the warranty standards are established by locally accepted building practices."[91] For example, the New York State Uniform Fire Prevention and Building Code section 371 requires a safe and healthful environment. If courts were not confined by the statutory definition, they could base their interpretation of the phrase "safe and healthful environment" on reasonable consumer expectations.[92]

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88 Even that definition is not so precise: the *Caceci* house was described as not "habitable" although the Cacecis did not have to move out of it. The *Caceci* court apparently did not limit material defects to those that fail to comply with building codes or local building practices. The builder did not violate building codes by failing to do a soil test on the land, and evidence indicated that failing to do so accorded with local building practices. *Id.* at 14-15; *see infra* note 137.

89 N.Y. GEN. BUS. LAW § 777-a(1)(a) (McKinney Supp. 1990).

90 *Id.* § 777(3). *See infra* text accompanying notes 94-96.

91 NYSBA Letter, *supra* note 75, at 4.

92 For example, they could determine that narrow cracks in a finished wood floor create an unsafe environment, even if the building code does not prohibit those cracks. The HOW warranty covers only those cracks in excess of 1/8 inch in width. GUIDE, *supra* note 66, at 114. Local standards, of course, may vary, but the New York State Builders Association urges local associations to adopt the HOW standards. *Id.* at 104.

To construct a home in a "skillful manner," a builder needs to conform only to a state-wide uniform building code, not to local building codes from the definition.[93] Municipalities may adopt stricter building code standards, but builders who violate them will not incur liability for failing to construct in a "skillful manner."

Although requiring builders to construct homes in a "skillful manner" ensures a minimum safety standard, the statute defines "skillful manner" too narrowly to protect consumers' reasonable expectations. Because builders must conform to building codes under existing law,[94] consumers clearly expect builders to comply with them.[95] In addition, most consumers reasonably expect a much higher standard: they reasonably expect and rely on builders to supply houses without any significant defects.[96]

b. *Material Defect*

While builders must ensure that they build homes free from "material defects" for six years after the warranty date, again the statute limits the scope of the warranty by defining "material defects" narrowly. "Material defects" include:

> actual physical damage to the following load-bearing portions of the home caused by failure of such load-bearing portions which affects their load-bearing functions to the extent that the home becomes unsafe, unsanitary or otherwise unliveable: foundation systems and footings, beams, girders, lintels, columns, walls and partitions, floor systems, and roof framing systems.[97]

The statutory definition of "material defects" does not include many defects which courts traditionally considered material.[98] Damages to non-load-bearing portions of the home, no matter how substantial, do not constitute "material defects" under the Statute.

The narrow definition of "material defects" fails to ensure safe and habitable homes. Consumers cannot sue builders for non-

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93 The only exception is the New York City Building Code. Section 777(2) defines "building code" as:

> the uniform fire prevention and building code promulgated under section three hundred seventy-seven of the executive law, local building codes standards approved by the uniform fire prevention and building code council under section three hundred seventy-nine of the executive law, and the building code of the city of New York, as defined in title twenty-seven of the administrative code of the city of New York.

N.Y. GEN. BUS. LAW § 777(2) (McKinney 1989).

94 Jenkins' Letter, *supra* note 76.

95 Haskell, *supra* note 33, at 641.

96 *Id.* at 651-53. Of course, minor shortcomings are expected. As Professor Haskell noted, "[m]erchantability is not perfection; it is a relative concept, depending upon price and age." *Id.* at 652-53.

97 N.Y. GEN. BUS. LAW § 777(4) (McKinney Supp. 1990).

98 NYSBA Letter, *supra* note 75, at 4.

structural defects that render a home unsafe or unlivable unless they discover the defects during the one-year "skillful manner" warranty period.[99] For example, a buyer who purchases a new home built with poor insulation may not have the expertise needed to inspect for adequate insulation. He may remain unaware of the problem because the aluminum siding added to the outside walls protect the home from the wind and cold. If, during the second year of occupancy, a section of the aluminum siding falls off the house, exposing the owner to the wind and rain, he cannot recover damages for the defects. He cannot recover under the statute for lack of skillful construction because more than a year has passed. Furthermore, the defects in insulation and siding are not "material defects." The home is uninhabitable,[100] yet the statute provides the homeowner with no relief.

By defining "material defects" too narrowly, the statute also fails to fulfill reasonable consumer expectations. Although consumers generally understand that a home deteriorates over time, they nevertheless expect its parts to last a reasonable period of time.[101] For example, in *Vento v. Honeybee Homes*,[102] a home owner sued more than six years after closing, seeking damages for a leaky roof under an implied warranty theory. The court denied a motion to dismiss based on statute of limitations, reasoning that the warranty period under *Caceci* equalled "what a reasonable expectation would be that a house constructed in a workmanlike manner would be free of ma-

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99 N.Y. GEN. BUS. LAW § 777-a(1)(a) (McKinney Supp. 1990).

100 Section 777-b states that any "exception, exclusion, or standard that fails to ensure that the home is habitable, by permitting conditions to exist which render the home unsafe, shall be void as contrary to public policy." *Id.* § 777-b(4)(e)(ii). This provision appears to expand the "material defects" definition to cover our example; however, this provision applies only to limited warranties builders offer in lieu of the basic statutory warranty. Hence, no provision in the statute requires the basic statutory housing merchant to warrant that a home will be habitable.

101 *See* Robert Williams, *Development in Actions for Breach of Implied Warranties of Habitability in the Sale of New Houses*, 10 TULSA L.J. 445, 448 (1975) (rejecting a fixed statute of limitations as too inflexible and arguing for a standard of reasonableness); Note, *supra* note 41, at 214 ("[A] standard of reasonableness would provide a better method of judging how long a builder-vendor should be subject to liability than would the fixed statutory period." (footnote omitted)). *See generally* Haskell, *supra* note 33, at 652 ("Some defects in new construction might be considered to constitute breaches of merchantability although they may not appear until a number of years after the sale."); Kirgis, *supra* note 48, at 1082 ("Products are normally warranted for a specified length of time. Residences can be too; if so, the duration should reflect the relatively long expected life of residences.").

The three-tier structure of the New York statute reflects a notion that some portions of the home deteriorate faster than others. Although the point is valid, the statute restricts recovery to one year for many defects that may not arise under normal circumstances within that time.

102 141 Misc. 2d 997, 535 N.Y.S.2d 344 (Civ. Ct. 1988). The court decided the case before the effective date of the new statute.

terial defects."[103] The statute of limitations for the roof exceeded six years because a home owner "could reasonably expect that a well-made roof should last over six years."[104] The statute, however, would deny recovery for a leaky roof after the first year, despite consumer expectations.

2. *Builder Fault*

Although the statute protects consumers from many defects by imposing liability on builders for their mistakes, and in some instances for the mistakes of their subcontractors,[105] builders have no statutory duty to prevent or correct defects that other people cause. Section 777-a(2)(a) of the statute imposes liability on builders for defects that constitute: "(i) defective workmanship by the builder or by an agent, employee or subcontractor of the builder, (ii) defective materials supplied by the builder or by an agent, employee or subcontractor of the builder, or (iii) defective design provided by a design professional retained exclusively by the builder."[106] Homeowners who discover latent defects in their homes during the warranty period must prove that the builder, his agents, or his subcontractors caused the defect in order to recover under the statute.

Section 777-a(1)(b), the installation warranty provision, further limits builder liability. Builders have no statutory duty to prevent others from installing systems improperly.[107] The statute holds builders liable for improper installation only if the defect is "due to a failure *by the builder* to have installed such systems in a skillful manner . . . ."[108] Furthermore, because the statute specifically defines a "builder" as one who contracts with an owner,[109] builders have no responsibility for their subcontractors' mistakes.[110]

The provisions limiting builders' liability to instances of their own fault contravene the statute's underlying policy of protecting consumers' justified reliance in two ways.[111] First, the statute en-

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103 *Id.*, 535 N.Y.S.2d at 345.

104 *Id.*

105 Builders are liable for their subcontractors' defective workmanship, materials and design, N.Y. GEN. BUS. LAW § 777-a(2)(a) (McKinney 1989), but not for their subcontractors' faulty installation. *Id.* § 777-a(1)(b)).

106 *Id.* § 777-a(2)(a).

107 *Id.* § 777-a(1)(b).

108 *Id.* (emphasis added).

109 *Id.* § 777(1).

110 A homeowner could argue that faulty installation is a type of defective workmanship for which the builder is liable under section 777-a(2)(a). The more specific provision on installation, however, indicates that the legislature intended to treat faulty installation differently. Thus, the more accurate view is that builders are not liable for their subcontractors' faulty installation. At any rate, this provision of the statute does not provide certain protection for the home buyer.

111 Because many consumers are inexperienced in buying homes or in contracting

courages builders to avoid liability by requiring the home buyer to pay architects and suppliers directly. The statute imposes builder liability for defective materials only if the builder or his agents, employees, or subcontractors cause the defect,[112] and for defective designs only if the builder exclusively retains the design professional.[113] Builders who recommend a particular architect impliedly encourage buyers to rely on their superior knowledge about the quality of that architect's work. Nevertheless, as long as the buyer directly pays the architect, the statute exempts builders from liability for defective design.[114] Similarly, builders who want to avoid liability for faulty materials may do so by having the buyer contract directly with the major suppliers.

Second, the statute imposes no builder liability for subcontractors' faulty installation.[115] Therefore, builders can avoid liability for faulty installation by using subcontractors rather than employees to install major systems. Consumers rely on builders to construct homes free from installation defects, yet consumers normally have no interest in the identity of the installer. In effect, this provision requires buyers to ascertain who installed the faulty product to determine whether the warranty applies.[116]

3. *Patent Defects*

Section 777-a(2)(b) of the statute specifically excludes from the warranty "any patent defect which an examination ought in the circumstances to have revealed, when the buyer before taking title or accepting construction as complete has examined the home as fully as the buyer desired, or has refused to examine the home."[117]

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with a builder to have him build their home, they rely on the builder's advice in choosing suppliers and design professionals. In this sense, their reliance is much like that of the consumer who relies on the merchant to use his skills in choosing reputable manufacturers. Carving out an exception for defects the builder does not cause denies consumers a remedy for this justified reliance.

112 N.Y. GEN. BUS. LAW § 777-a(2)(a)(ii) (McKinney Supp. 1990).

113 *Id.* § 777-a(2)(a)(iii).

114 The Builders Association suggests this arrangement to its members, or in the alternative suggests that builders make sure the design professional is adequately insured. GUIDE, *supra* note 66, at 46.

115 The Builders Association recommends that "[a]s a precaution, however, builders should review their plumbing, electrical and HVAC subcontracts to assure that the subcontractors will stand behind their workmanship in the event of a warranty claim." *Id.* at 43. This precaution anticipates judicial interpretations of the provision that would broaden the coverage. Courts might determine that the plain meaning interpretation contradicts the consumer protection purposes of the statute, and thus determine that "builder" in this clause means builder and subcontractors.

116 The buyer may be able to sue the subcontractor for his negligence. Subcontractors, however, often have no insurance and few resources with which to satisfy a judgment.

117 N.Y. GEN. BUS. LAW § 777-a(2)(b) (McKinney Supp. 1990).

To justify excluding patent defects from warranty protection, courts maintain that buyers impliedly agree to purchase homes with patent defects.[118] Courts reason that buyers have the opportunity to inspect homes carefully and may want to purchase at a discount homes with defects.[119] Home buyers with enough bargaining power may negotiate a lower sales price for a defective home or require a specific repair agreement covering the defect.[120] In *Staff v. Lido Dunes*,[121] the court enforced an express merger clause as to patent defects, reasoning:

> [t]o the extent that construction defects are discoverable at the time title closes public policy is not violated by enforcement of the contract provision, because the purchaser can protect his interests by either demanding a 'specific written agreement' covering the defect or refusing to close until it has been corrected.[122]

The patent defect exception to the housing merchant warranty rests, however, on the faulty assumption that consumers can discover patent defects. Inspection of realty is much more complicated than inspection of consumer goods. The *Caceci* court recognized that "[w]hen a buyer signs a contract prior to construction of a house, inspection of premises is an impossibility . . . ."[123] Even in

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118 *See, e.g.*, Staff v. Lido Dunes, Inc., 47 Misc. 2d 322, 326, 262 N.Y.S.2d 544, 549 (Sup. Ct. 1965) (buyer has no cause of action for patent construction defects unless such defects are mentioned in the contract).

119 GUIDE, *supra* note 66, at 47.

120 The Builders Association envisions this type of bargaining. The Association suggests builders should

> require buyers to make examination (the traditional 'walk through' before closing) and to execute an affidavit or other document at the closing in which the buyer acknowledges that a reasonable inspection was made and that construction has been completed in a workmanlike manner without defects, except as specified in the document (the traditional 'punch list'). Items on the punch list can be resolved through an agreement to correct them in a specified time or through a credit to the buyer. The itemized defects will then be patent defects, excluded from the implied warranty.

Id.

121 47 Misc. 2d 322, 262 N.Y.S.2d 544.

122 *Id.* at 326, 262 N.Y.S.2d at 549. The court continued:

> [w]ith respect to latent defects, however, the provision if enforced is an absolute bar to action with respect to defects which by hypothesis are unknown at the time barred. . . . Thus, with respect to latent defects, the cause of action is extinguished at the moment it is created. . . . [A]n unreasonably short limitation period is against public policy and unenforceable.

Id. For a discussion of the court's statute of limitations approach, see REPORT, *supra* note 5, at 61.

123 *Caceci*, 72 N.Y.2d at 59, 526 N.E.2d at 269, 530 N.Y.S.2d at 774. As early as 1815, courts noted that " '[w]here there is no opportunity to inspect the commodity, the maxim of *caveat emptor* does not apply.' " Gardiner v. Gray, 171 Eng. Rep. 46, 47 (K.B. 1815).

instances where a builder completes the house before the parties sign the contract, requiring purchasers to inspect may unfairly burden them. As one critic notes, "[i]t is true that a completed home can to a limited extent be inspected for defects by the vendee before he signs the contract, but it is equally true that most potential home owners lack the competency to do their own inspecting."[124]

Despite evidence that consumers cannot competently inspect homes, New York courts often have expected them to discover defects that only experts could reasonably find. The court in *Staff v. Lido Dunes*[125] refused to allow recovery for patent defects. According to the court, the following defects were discoverable on reasonable inspection prior to closing: "the fuel gauge, fireplace support, crawl space vents, [and] absence of straps and shims between joists and girder."[126] It is difficult to believe that the average consumer has ever heard of joists and girders,[127] much less that they can discover defects concerning them.

Most homeowners cannot afford to hire expert examiners to inspect for them, either. Although expert examiners can discover little about a complete house,[128] they still may charge exorbitant fees.[129] One critic notes,

> [t]he high cost of hiring a skilled examiner would place that particular safeguard beyond the reach of most vendees, particularly the average home buyer who has very likely mortgaged heavily in order to purchase even a modest unit in a typical housing development . . . . [A]ny competent inspection after completion would usually be pecuniarily or practically impossible.[130]

C. Proposed Solution

1. *Expand the Statutory Language*

To meet consumer expectations and reliance, and to promote safety and habitability, the legislature should expand the statutory definitions of "skillful manner" and "material defects" to encom-

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124 Bearman, *supra* note 2, at 545.

125 47 Misc. 2d 322, 262 N.Y.S.2d 544 (Sup. Ct. 1965).

126 *Id.* at 329, 262 N.Y.S.2d at 551.

127 Joists are the parallel beams that hold up the planks of a floor or the laths of a ceiling. Girders are the large wooden or steel beams that support the joist. Shims are thin wedges of wood that fill in spaces. THE AMERICAN HERITAGE DICTIONARY OF THE ENGLISH LANGUAGE 706, 558, 1195 (New College ed. 1980).

128 Construction can hide most important defects, such as a sinking foundation. Many architects are reluctant to inspect houses at all unless they are called in at the beginning of construction. Bearman, *supra* note 2, at 545.

129 *Id.* In 1961, Leo Bearman did an informal survey of Boston architects who estimated their fees would run between $75 to $100 a trip, or $300 to $1000 for a complete supervision job. These figures are in 1961 dollars. *Id.*

130 *Id.* (footnote omitted).

pass defects that consumers would not ordinarily expect to manifest themselves during the warranty periods.[131] A home constructed in a "skillful manner" would show no defects during the first year. Although minor defects might manifest themselves in the next five years, defects to portions of the home "reasonably essential to the usage of the house"[132] would be considered "material defects." This amendment would not require builders to provide perfect housing, for consumers recognize that homes deteriorate over time because of ordinary wear and tear or owner neglect. These proposed definitions of the statutory terms would fulfill consumer expectations better than the current definitions do. Although consumers cannot reasonably expect a home to last forever without damage, most home buyers reasonably expect to discover no housing defects during the first year of occupancy.[133] They cannot, however, reasonably expect the warranty to extend to maintenance problems that normally occur within the first year, damage resulting from homeowner negligence, or acts of God.[134]

Most consumers expect that, for a number of years, the warranty will hold builders to higher standard than the current "material defects" definition does. Most consumers would not expect to find defects to portions of the home "reasonably essential to the use of the house"[135] during the first six years of occupancy. Thus, in the

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131 An ideal statute from the consumer's perspective would be one with no fixed statute of limitations. Some commentators have argued for this kind of "reasonableness" standard. *See* Williams, *supra* note 101, at 448 (rejecting a fixed statute of limitations as too inflexible and arguing for a standard of reasonableness); Note, *supra* note 41, at 214 ("[A] standard of reasonableness would provide a better method of judging how long a builder-vendor should be subject to liability than would the fixed statutory period." (footnote omitted)); *cf.* Note, *supra* note 1, at 435 ("The first major flaw in the Minnesota statute is the inclusion of explicit warranties within the text of the statute; this creates unnecessary rigidity in a rapidly changing area of the law.") (footnotes omitted). Other critics argue that statutes must provide the building industry with some certainty. *See, e.g.*, Bearman, *supra* note 2, at 575; Haskell, *supra* note 33, at 652.

132 Note, *supra* note 41, at 210. For further discussion of what consumers consider reasonably essential, see *supra* note 135 and accompanying text.

133 Note, *supra* note 1, at 420. Most of the one year warranty coverage can be insured. The HOW warranty covers faulty workmanship and defective materials for one year. Note, *The Home Owners Warranty Program: An Initial Analysis*, 28 STAN. L. REV. 357, 360 (1976) (authored by Jonathan L. Kempner).

134 Note, *supra* note 1, at 423-24.

135 Note, *supra* note 41, at 210 (emphasis omitted). One commentator argued for expansion to cover nonstructural defects by comparing the implied warranty of habitability that has grown out of landlord-tenant disputes.

> [A] buyer's willingness to contract is in exchange for the seller's promise to provide a livable dwelling, a package which includes not merely structural integrity, but nonstructural integrity as well, such as adequate heating, lighting, and plumbing. It is illogical to extend nonstructural protection to the $100 a month tenant, but not to the buyer of a $100,000 house.

Id. at 211 (footnote omitted). Moreover, tenants have less at stake and lower expecta-

hypothetical case where a structurally sound home no longer shelters the resident from the winter,[136] the builder has not met the consumer's reasonable expectations. Reasonable expectations will in all cases cover major structural or nonstructural defects that render the home uninhabitable.[137]

Reasonable consumer expectations also extend to other nonstructural defects that a warranty of habitability should include.[138] Consumers reasonably expect not only safe, habitable homes, but also homes free from cosmetic defects.[139] The statute should impose liability on the builder for all defects the consumer could not have anticipated, including cabinets that fall off a kitchen wall only six years after a home is built.

Expanding the statutory definitions also will protect justified consumer reliance. Purchasers rely on builders' skill and knowledge in part because they believe that the law protects them.[140] Given consumer protection laws, home purchasers assume that a guarantee, similar to the warranty on goods, exists when they purchase a new house.[141] Acting on this assumption, most home buyers will not "take risk-reducing steps beyond inspecting houses themselves and inquiring about the builders from whom they buy."[142] Furthermore, builders often encourage home buyers to rely on their skills, purposefully creating expectations that purchasers will receive not "merely liveable but truly wonderful homes."[143] Because home buyers must rely on the skill, knowledge, reputation and integrity of builders, the statute should give full effect to their reliance by expanding the definitions of "skillful manner" and "material defects."

Expanding the statutory definitions will also promote the underlying policies of safety and habitability.[144] Builders who wish to

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tions about quality than do new home purchasers. *Id.*; Note, *Housing Defects: Homeowners' Remedies—A Time For Legislative Action*, 21 WASHBURN L.J. 72, 78 (1981).

136 *See supra* notes 99-104 and accompanying text.

137 "Uninhabitable" does not mean that the residents must move out. Instead, the term means unsafe, unhealthful, or in violation of applicable building codes. *See* Note, *supra* note 1, at 422 n.45.

138 Professor Kirgis notes that a buyer of a new home expects "not only that a building is habitable, but that it meets some higher standard of functionality and durability." Kirgis, *supra* note 48, at 1078.

139 I am indebted to Gene DeSantis, counsel to the Consumer Affairs and Protection Committee, for his explanation of the effect of the statute on cosmetic defects.

140 Note, *The Implied Warranty of Habitability Doctrine in Residential Property Conveyance: Policy-Backed Change Proposals*, 62 WASH. L. REV. 743, 747 (1987) (authored by Joseph C. Brown, Jr.).

141 *Id.*

142 *Id.*

143 *Id.*; *see* Dixon v. Mountain City Constr. Co., 632 S.W.2d 538 (Tenn. 1982); Frickel v. Sunnyside Enter., 106 Wash. 2d 714, 725, 725 P.2d 422 (1986) (Pearson, J., dissenting).

144 Discovery of shoddy workmanship spurred on the current movement to require

retain good reputations have an incentive to construct quality homes, and the current definition does put some additional pressure on builders to build safe, habitable homes. Holding builders to the higher standard of the proposed amendments, however, will increase those incentives and thereby provide the best assurance to buyers that their new homes are safe and habitable.

Initially, broadening the definitions of "skillful manner" and "material defects" will have significant costs. In the short run, these broad definitions will burden the building industry.[145] Because courts must measure defects against a subjective standard, varying according to the facts of the instant case and perhaps evolving over time, builders may find it difficult to plan for future liability. Currently, only defects in the load-bearing functions of the home are insurable for the long warranty period under the HOW insurance plan.[146] Thus, builders may not be able to obtain insurance to cover liability under this expanded definition. Furthermore, the increased liability will force builders to inspect their work more carefully, increasing their costs of construction.

These increased costs will burden not only the building industry, but also consumers themselves. If builders spend more on construction of homes because they must self insure, purchase more insurance, or inspect their work more carefully, then they will attempt to pass these increased costs on to consumers. If they do so, housing prices will increase in response. Thus, consumers will bear some of the initial costs of these statutory amendments.

Although the amendment has its costs, its benefits, both for consumers and for the building industry, outweigh them. The amendments will fulfill reasonable consumer expectations and reli-

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housing merchant warranties in all new home deeds. A memorandum circulated with an early draft of the New York Assembly bill noted that several news journals "have all cited the home building industry for turning out shoddy, defective homes and failing to make repairs. They note that, while the average price of a new home is now about $63,000, the consumer gets less for his money than ever." Memorandum in Support of Legislation Assembly Bill 770-A (1988).

145 For this reason, builders might argue that only structural defects that require the owner to move out should be considered material defects:

> Under ordinary principles of contract law, unless the parties have agreed otherwise, a defect is "material" whenever it significantly impairs the purpose of the contract. Hence, a defect that makes a home unsafe or unfit for living would be a material defect under a contract for the sale of a home.

GUIDE, *supra* note 66, at 16. Although "unsafe or unfit for living" can be construed in many ways, the builders mean that the defect forces the owner to move out of the home. *Id.*

146 The Home Owner's Warranty provides protection for ten years only against "major construction defects." Major construction defects are defined as damage to the load-bearing functions of the house. *See* Note, *supra* note 1, at 361 nn.20-22 and accompanying text.

ance and encourage the construction of safe, habitable homes. By meeting the higher standards of the amended statute, builders will increase consumer confidence in the building industry. Ultimately this increased confidence should benefit the building industry as well as housing consumers. Furthermore, imposing increased responsibility on builders recognizes that they are in the best position to bear the risk of construction defects. Builders can determine which suppliers provide quality materials and which architects produce sound building designs, and the builders can work only with these reputable business people. For all of these reasons, these statutory amendments will ensure safe, habitable homes at a relatively low cost.

2. *Impose Liability Regardless of Fault*

To give full effect to consumer reliance, the legislature should also amend the law to impose liability on builders regardless of fault.[147] The statutory protection should exclude, however, damage from the following causes: owner action or neglect; action taken by a party under control of the owner; and identifiable acts of God such as lightning, floods, hurricanes, and possibly insect infestation. Although adopting a no-fault warranty will impose high initial costs on the building industry, the change should immediately benefit home buyers. Furthermore, enhanced consumer confidence in home building should benefit the building industry in the long run.

Consumers reasonably rely on builders not only to construct homes skillfully, but also to deliver homes free from any significant defects caused by anyone. Under a warranty that requires fault, consumers have no method of determining which potential defects the warranty covers. To ascertain their own potential liability, buyers would need a list of all suppliers and the supplies they provided, a list of subcontractors the builder hired to install systems together

147 If a no-fault warranty amendment is not politically feasible, a reasonable compromise would hold builders liable for all defects they could have reasonably prevented, with the understanding that they can sue for contribution or indemnification within one year of judgment. *See* N.Y. GEN. BUS. LAW § 777-a(4)(c) (McKinney Supp. 1990). Certainly a builder should be liable under the statute for his subcontractors' and other agents' work. The legislature should close the loophole that shelters builders from liability for subcontractors' faulty installation. Furthermore, builders should stand behind the materials they use regardless of who pays for them, and if they do not, the statute should require them to disclose that fact to the buyer. (Some buyers contracting for a builder to construct a home may want the builder to use inferior materials in an effort to cut costs. If that is the case, the purchaser should have to sign a waiver of some sort or the warranty should be expressly disclaimed according to the statute. As it now stands, as long as the builder does not directly contract with the supplier, no implied warranty exists.) Finally, if design professionals whom the builder recommends or requires cause defects, the builder should be liable for those defects. This compromise would serve the policies of the warranty better than the current statute does.

with a description of their work, and a list of all people who walked through the home during construction and who might have caused some damage. Only with this information can the buyer attempt to discover the limits of the builder's responsibility. The legislature must know that as a practical matter consumers cannot protect themselves in this way. Instead, consumers should be able to assume that the warranty protects them against loss from all housing defects, regardless of builder fault.

The New York State Builders Association lobbied heavily for the fault requirement of the current statute.[148] Presumably, the Association feared the high initial costs of a no-fault scheme. Under the amended statute, builders will have to pay for errors they did not cause, which will increase builders' insurance costs. Furthermore, the burden of proving causation will shift to builders. Under the current scheme, an aggrieved buyer must prove that the builder caused the housing defect to recover damages. With the amendment, courts should hold builders liable for defects unless the builder demonstrates that an enumerated exception applies. Thus, builders' litigation costs may increase under the amendment, part of which ultimately would be passed on to consumers.

The fault requirement itself, however, costs society more than its elimination would. The increase in builders' insurance costs does not represent a net drain on society. Under the current statutory scheme, the unlucky homeowner who buys a defective home bears the risk that he may not be able to prove that the builder caused the defect. The elimination of the fault requirement will spread this risk of loss throughout society. Similarly, the amendment will not increase overall litigation costs. Instead, the costs will shift to the builder, who in turn will spread the risk, either through an insurance policy or through increased housing prices.

Extending warranty coverage to defects that the builder did not cause fairly places the risk of loss on the less innocent party and on the party better able to bear the risk. Several courts have recognized the equity of imposing liability regardless of fault on builders who sell defective homes.[149] These courts reason that of the two parties, the builder can more easily guard against defects in the home and more easily protect himself against potential but unknown defects.[150] As one court noted:

> Although hindsight, it is frequently said, is 20-20 and defendants used reasonable prudence in selecting the site and designing

148 GUIDE, *supra* note 66, at 83-84.

149 *See, e.g.*, Lane v. Trenholm Building Co., 267 S.C. 497, 503, 229 S.E.2d 728, 731 (1976); House v. Thornton, 76 Wash. 2d 428, 435, 457 P.2d 199, 203-04 (1969).

150 Elderkin v. Gaster, 447 Pa. 118, 128, 288 A.2d 771, 777 (1972).

> and constructing the building, their position throughout the process of selection, planning and construction was markedly superior to that of their first purchaser-occupant. To borrow an idea from equity, of the innocent parties who suffered, it was the builder-vendor who made the harm possible. If there is a comparative standard of innocence, as well as of culpability, the defendants who built and sold the house were less innocent and more culpable than the wholly innocent and unsuspecting buyer.[151]

Extending warranty protection to all housing defects, regardless of builder fault, will give full effect to consumer reliance and more fairly allocate the risk of loss.

Ultimately, the building industry also should benefit from the no-fault warranty. As builders increase the care with which they prevent defects from all causes, home buyers' confidence in builders will increase. Responsible builders should be able to pass their increased costs on to their buyers, and the industry as a whole should benefit from the enhanced view consumers have of it. Thus, a no-fault warranty should benefit the building industry as well as consumers.

3. *Impose Liability for Patent Defects*

An exception for patent defects in the housing warranty contravenes the policies behind it. The legislature should not assume that consumers rely on their own judgment with regard to patent defects. Buyers do not observe all stages of construction, and they lack the skills needed to inspect homes for patent defects.[152] Buyers must rely on builders' expertise to deliver homes free even from patent defects. Builders, by contrast, supervise construction and have the expertise necessary to inspect the home for defects;[153] therefore, equity suggests that the builder should bear the risk of loss even for patent defects.

Some buyers may want to purchase a home with known patent defects for a discount. The statute should not allow these buyers to recover damages for defects that reduced the contract price. To solve this problem, one critic suggests that a buyer should "be held at least to the standard of competence and skill which he in fact pos-

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151 McDonald v. Mianecki, 79 N.J. 275, 297-98, 398 A.2d 1283, 1294 (1979) (citing *House*, 76 Wash. 2d at 435-36, 457 P.2d at 203-04). The *McDonald* court noted that the Washington court's sentiment was repeated by the Supreme Court of South Carolina, which stated that " 'liability is not founded upon fault, but because [the seller] has profited by receiving a fair price and, as between it and an innocent purchaser, the innocent purchaser should be protected from latent defects.' " *McDonald*, 79 N.J. at 287 n.7, 398 A.2d at 1294 n.7 (quoting *Lane*, 267 S.C. at 503, 229 S.E.2d at 731).

152 *See supra* notes 123-27 and accompanying text.

153 For a discussion of the difficulties of inspection, see *supra* notes 123-30 and accompanying text.

sesses . . . ."[154] Unfortunately, litigants will have difficulty demonstrating buyers' actual knowledge unless the defects are noted in a written contract. Another solution would exclude from the warranty all patent defects the seller disclosed to the buyer. Builders commonly disclose known defects to buyers in a "punch list," a list of defects the parties agree to leave as is.[155] Because of this common practice, builders would not be unduly burdened by a requirement that they incorporate the "punch list" within the contract. The warranty would cover all patent defects except those listed in a contract as part of a price negotiation.[156]

Although creating a "punch list" is a common practice in the building industry, some commentators maintain that requiring builders to disclose the most obvious defects is unfair and inefficient. One commentator notes, "[c]learly, if the purchaser knows of the defect, he is not entitled to the protection of the law . . . . [I]t is inappropriate to imply as a term of the contract a promise or representation against the existence of the defect."[157] Essentially, the commentator suggests that the law should equalize builders' and buyers' bargaining power, not place buyers in a dominant position. By providing a remedy for obvious defects, the law seems to allow double-dipping. If defects are obvious, sales prices may reflect them. Then, if consumers can recover under the implied warranty, they in effect recover twice.

This view, however, assumes both a high level of sophistication among home buyers and a great deal of buyer bargaining power. Even if a buyer discovers an obvious defect in a home, he may either assume the builder plans to repair it or be unable to negotiate a lower contract price. By requiring builders to incorporate their "punch lists" in the sales contract, the proposed amendment would bring the defects to the bargaining table. Builders easily could avoid the double-dipping problem by carefully including all defects

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154 Haskell, *supra* note 33, at 651.

155 GUIDE, *supra* note 66, at 84.

156 Because builders usually have a better bargaining position, courts may need to determine if the patent defects were actually part of a contract price negotiation or if the builder manifested a "take it or leave it" position. If the latter, the patent defect exclusions would violate public policy. Furthermore, the statute should require sellers to print the exclusions in bold and to show the provisions to the buyer.

Another possibility is to limit "patent defects" to those defects discoverable by a non-expert that can be seen in a walk-through with the builder. Because a walk-through would generally be done without going into the attic, looking into the crawl spaces, or lifting up carpeting, all defects in those places would be latent. Missing shims and straps would be latent because a non-expert could not discover them at all. *See supra* note 127 & accompanying text.

157 Haskell, *supra* note 33, at 651; *see also* Kirgis, *supra* note 48, at 1089 ("It is inefficient and unfair to require a seller or lessor to warrant against conditions that should be reasonably apparent to the average buyer or lessee.").

in the contract. Although this amendment initially may increase transactions costs, it eventually should decrease litigation costs. No longer will courts need to determine whether defects are latent or patent. Hence, this amendment should actually decrease overall costs. Even if costs did increase, however, coverage nevertheless should extend to all patent defects not explicitly disclosed. This extension will further the policies underlying the warranty without completely eliminating freedom of contract.

CONCLUSION

Courts, commentators, and legislators have begun to realize that the modern housing market shares more with the market for twentieth century consumer goods than the market for nineteenth century homes. Consequently, courts and legislatures in various jurisdictions have implied warranties in housing sales on policy grounds similar to those that led to the U.C.C. warranty of merchantability. New York took a significant step forward when it passed a statutory housing merchant warranty. Unfortunately, the statute does not fulfill the policy goals that shaped its enactment.

To fulfill these policy goals, the legislature should amend the statute. It should broaden the statutory definitions of "skillful manner" and "material defects" to reflect consumer expectations and reliance. The statute should impose liability on builders for all defects regardless of fault. Finally, the warranty should hold builders liable for all patent and latent defects the parties do not explicitly exclude in the contract. Although these amendments will increase builders' initial costs, in the long run they will serve the best interests of both consumers and the building industry. The amendments will better align the warranty protection with consumer expectations about homes they buy, which will increase consumer confidence in the building industry. Thus, at little cost to society, the proposed amendments will better serve all the policy goals of the housing merchant warranty.

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